



TAXREP 22/12

(ICAEW REP 86/12)

ICAEW TAX REPRESENTATION

Possible changes to income tax rules on interest

Comments submitted on 22 June 2012 by ICAEW Tax Faculty in response to HM Revenue & Customs Consultation Document published on 27 March 2012

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INTRODUCTION

1. ICAEW welcomes the opportunity to comment on the Consultation Document *Possible changes to income tax rules on interest* published by HM Revenue & Customs (HMRC) on 27 March 2012.
2. Information about the Tax Faculty and ICAEW is given below. We have also set out, in Appendix 1, the Tax Faculty's Ten Tenets for a Better Tax System by which we benchmark proposals to change the tax system.

WHO WE ARE

3. ICAEW is a world-leading professional accountancy body. We operate under a Royal Charter which obliges us to work in the public interest. ICAEW's regulation of its members, in particular its responsibilities in respect of auditors, is overseen by the UK Financial Reporting Council. We provide leadership and practical support to over 138,000 member chartered accountants in more than 160 countries, working with governments, regulators and industry in order to ensure that the highest standards are maintained.
4. ICAEW members operate across a wide range of areas in business, practice and the public sector. They provide financial expertise and guidance based on the highest professional, technical and ethical standards. They are trained to provide clarity and apply rigour, and so help create long-term sustainable economic value.
5. The Tax Faculty is the voice of tax within ICAEW and is a leading authority on taxation. Internationally recognised as a source of expertise, the faculty is responsible for submissions to tax authorities on behalf of ICAEW as a whole. It also provides a range of tax services, including TAXline, a monthly journal sent to more than 8,000 members, a weekly newswire and a referral scheme.

OUR COMMENTS

Overview

6. The coalition government has announced its policy of making the UK 'Open for business' and a key element of this is to have the most competitive tax system amongst the G20 countries. A key feature of the UK tax regime has been the generous nature of the interest provisions which we believe make the UK tax regime competitive and encourages investment into the UK. Any proposed changes to the interest regime need to ensure that the competitiveness of the tax regime is not impaired.

Interest include in compensation payments

7. We believe that the proposed changes to s 380A Income Tax (Trading and Other Income) Act 2005 (ITTOIA) and Part 15 Income Tax Act 2007 (ITA) should provide greater clarity for UK taxpayers and, as a result, are to be welcomed.
8. We believe that the extension of the requirement to deduct income tax to parties other than deposit takers and building societies is likely to add to their administrative burdens despite the statement to the contrary in paragraph 3.15 of the Consultation Document.

Yearly interest arising in the UK

9. We believe that the distinction between 'short' and 'yearly' interest is well established by case law and is widely understood.
10. There is a requirement in the market place for short term movements of cash and the extension of withholding tax to the resultant short interest would, in our view, be anti-competitive as many EU countries have no withholding tax on interest at all, administratively

burdensome and so would not be sensible. Not least because there is a considerable level of bureaucracy involved in the withholding tax regime which makes the UK current treaty exemption system rather onerous and burdensome compared with many other European jurisdictions.

11. There are several commercial situations where the proposed change would create significant difficulties. It would seriously impede if not destroy the commercial paper market and would make cash pooling arrangements within UK groups of companies more arduous and would almost certainly cause those groups to reconsider the way they manage their treasury functions with the possibility of moving them offshore.
12. In relation to the proposed change to s 874 ITA we do not object to the removal of 'location of the agreement of deed evidencing the debt' from the criteria establishing whether or not the payment of interest arises in the UK as long as it is clear that the other existing criteria will continue to apply.

Quoted Eurobonds

13. We think that taxpayers have a number of options available to them in terms of structuring their funding requirements without incurring withholding tax and the Eurobond method is often chosen because it is the most simple of the options. If the rules are changed then the alternatives will be chosen and the level of tax revenue anticipated in the Consultation Document may not be achieved.
14. If changes are to be made then we recommend that existing arrangements are properly grandfathered.

Interest in kind and funding bonds

15. We would urge the government to exercise caution in relation to the proposed funding bond changes which will have an adverse impact on those UK business who are using such bonds because they are already in a difficult financial situation. If the decision is taken to make the change then we recommend that there should also be generous grandfathering provisions to ensure that existing arrangements are not adversely affected.

Disguised interest

16. We support the introduction of a rule in the income tax code to tax amounts that are 'economically equivalent to interest' as if they were interest which reflects the corporation tax rule in s 486N Corporation Tax Act 2009.

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ICAEW TAX FACULTY'S TEN TENETS FOR A BETTER TAX SYSTEM

The tax system should be:

1. **Statutory:** tax legislation should be enacted by statute and subject to proper democratic scrutiny by Parliament.
2. **Certain:** in virtually all circumstances the application of the tax rules should be certain. It should not normally be necessary for anyone to resort to the courts in order to resolve how the rules operate in relation to his or her tax affairs.
3. **Simple:** the tax rules should aim to be simple, understandable and clear in their objectives.
4. **Easy to collect and to calculate:** a person's tax liability should be easy to calculate and straightforward and cheap to collect.
5. **Properly targeted:** when anti-avoidance legislation is passed, due regard should be had to maintaining the simplicity and certainty of the tax system by targeting it to close specific loopholes.
6. **Constant:** Changes to the underlying rules should be kept to a minimum. There should be a justifiable economic and/or social basis for any change to the tax rules and this justification should be made public and the underlying policy made clear.
7. **Subject to proper consultation:** other than in exceptional circumstances, the Government should allow adequate time for both the drafting of tax legislation and full consultation on it.
8. **Regularly reviewed:** the tax rules should be subject to a regular public review to determine their continuing relevance and whether their original justification has been realised. If a tax rule is no longer relevant, then it should be repealed.
9. **Fair and reasonable:** the revenue authorities have a duty to exercise their powers reasonably. There should be a right of appeal to an independent tribunal against all their decisions.
10. **Competitive:** tax rules and rates should be framed so as to encourage investment, capital and trade in and with the UK.

These are explained in more detail in our discussion document published in October 1999 as TAXGUIDE 4/99 (see icaew.com/en/technical/tax/tax-faculty/~media/Files/Technical/Tax/Tax%20news/TaxGuides/TAXGUIDE-4-99-Towards-a-Better-tax-system.ashx)