

# **Strengthening Sanctions for Tax Avoidance - A Consultation on Detailed Proposals**

## **Response to consultation published 22 July 2015**

### **Introduction**

I did not comment on the initial consultation earlier this year but I welcome the opportunity to comment now on this latest consultation.

There are three distinct elements to the proposals in this document:

- The Serial Avoiders' Regime
- Penalties for the GAAR
- New POTAS threshold condition

The GAAR penalty proposal stands out slightly in that it doesn't really interact very much with the other two. It is also, I believe, a mistake at this point in time.

Whilst it is difficult to disagree in principle with the general idea of a GAAR penalty, I worry that now is far too soon after the introduction of the GAAR to be making such a change. It would be much better to allow time for the GAAR to bed-in and for its impact on behaviour to be assessed, before significant changes are made.

The Serial Avoider and POTAS proposals essentially deal with opposite sides of a similar problem. For this reason my views on issues like when a "scheme" is treated as being "defeated" are different for each of these proposals.

### **Serial Avoiders' Regime**

#### **Q1. Do you agree with a regime based on this model? If not, please outline the reasons for your view.**

The model is good in outline but I believe it needs some modification. I have no problem with the warning period starting with the first "defeat" after commencement. I do not agree, however, that a surcharge should apply for the first "defeat" of a subsequent "scheme" actually entered into during that warning period. The proposal is supposed to be dealing with "serial avoiders", I hardly think that "defeat" in 2 "schemes" qualifies the taxpayer as "serial" anything.

The surcharge should not come into play until at least two "schemes" entered into during the warning period have been "defeated". In your example in the condoc, that would be Defeat 3.

I agree that the warning period should be extended with each "defeat".

#### **Q2. What do you consider would be a suitable length for a warning period?**

I think that 5 years is adequate for the warning period.

**Q3. Would requiring serial avoiders to certify annually that they have not employed avoidance schemes, or to provide details of those they have used help discourage further avoidance?**

I fail to see where HMRC are going with this particular proposal. We already have disclosure requirements – DOTAS and VADR – do we really need another one. The “scheme” has already been disclosed under the relevant regime so what is the point in requiring a further declaration?

**Q4. Which of these approaches would best meet the five penalty principles?**

Actually, I would prefer a hybrid approach that utilised a sliding scale of surcharge. The first surcharge would be at a low rate with subsequent surcharges attracting higher rates up to a maximum. If the taxpayer came out of the warning period, the surcharge rate would reset to the minimum.

**Q5. If you believe the surcharge should be set at a high level, what should the taxpayer have to do to earn any reduction in the surcharge?**

No response.

**Q6. What other key features should form part of the surcharge to ensure it meets the five principles?**

See my answer to Q4.

**Q7. How should a reasonable excuse safeguard be structured to be fair to the taxpayer without undermining the effectiveness of the surcharge? Would excluding advice addressed to third parties, or not made by reference to the taxpayer’s circumstances, achieve this aim?**

I think that excluding reliance upon advice addressed to a third party would not only be reasonable but most logical. Advice given to a third party about a generic transaction can never, by definition, take account of any taxpayer-specific issues. Indeed, I don’t think that applies only in this scenario. I believe that HMRC should widely publicise the fact that reliance upon such advice alone is unlikely to constitute taking reasonable care. Nor, for that matter, is it sensible.

**Q8. If appealing against the surcharge on the grounds of having taken reasonable care, do you agree that putting the onus of proof on the taxpayer to demonstrate reasonable care would remove any incentive to engage in delaying tactics?**

No. This would be a step too far and would go against the principle of ‘innocent until proven guilty’.

**Q9. Do you agree that public naming of the most persistent users of tax avoidance schemes which HMRC defeats would be a fair and effective deterrent? How many schemes should be defeated before it is possible to name a serial avoider?**

No. I have a fundamental problem with this concept of “naming & shaming”. It smacks too much of the public stocks and has no place in a modern tax system.

Furthermore, what do you mean by “the most persistent users of tax avoidance schemes”? This terminology suggests some kind of ranking of all “serial avoiders” with the top (whatever number) being named. Or do you propose to have a

threshold of a specified number of defeated schemes in a set period? This does not seem to have been properly thought through.

**Q10. Do you agree that this would provide sufficient safeguards for naming serial avoiders? If not, what further safeguards do you suggest?**

My position is that I do not agree with naming, see my answer to Q9 above. On the basis that you will proceed with the proposals, however, my answer to this question is as follows.

You start by explaining that a taxpayer would have had plenty of warning of the potential naming. Fair enough but I'm not sure that is really a 'safeguard'; what happens if the taxpayer really does not understand what is happening?

You then suggest that taxpayers would have the opportunity to make representations that they should not be named. Presumably these representations will have to be made to HMRC? Is that really a safeguard?

Finally, to cap it off you state that there should be no right of appeal!

So, in summary I do not agree that you are proposing sufficient safeguards at all. If you insist on the right to publicly name "serial avoiders" then, at the very least, there should be a requirement to get approval from the Tribunal.

**Q11. Which of these options would provide the best approach to restricting access to reliefs when they have been exploited by a serial avoider as part of a defeated avoidance scheme?**

I am not in favour of these proposals to restrict access to statutory reliefs. Parliament has seen fit to introduce reliefs and to restrict access to them on this basis will be to create a two-tier tax system.

**Q12. If you favour restricting the power to restrict reliefs to certain categories, how should those categories be defined?**

As above, I am not in favour of these proposals to restrict access to statutory reliefs at all.

**Q13. Would focussing on a definition based on schemes notified or notifiable under DOTAS and VADR be sufficient to deter potential serial avoiders from entering into multiple schemes? If not, what other approach do you favour?**

Whether it deters potential avoiders or not, it seems a very sensible approach as those regimes already include a fairly wide definition of "avoidance".

**Q14. Should arrangements to which Follower Notice or GAAR have been applied be included in the definition of a scheme for these purposes? If not, please explain why you do not think this would be appropriate.**

These need to be looked at separately.

It seems reasonable to assume that the issue of a Follower Notice is indicative that the taxpayer is participating in a "scheme". It does not, however, mean that that particular taxpayer has had the scheme "defeated". The specific facts of that case may well be sufficiently different. Therefore I do not agree that the issue of a Follower Notice should be included in the definition of taking part in a "scheme".

I don't believe that arrangements that have been challenged by HMRC under the GAAR should be included. The difficulty is that it is not necessarily clear at the

time the taxpayer enters the arrangements that they will be counteracted by HMRC under the GAAR. It is unreasonable, therefore, to include them as a “scheme” for these purposes.

**Q15. Should a scheme be viewed as ‘defeated’ once a dispute is settled in HMRC’s favour, either by agreement with the taxpayer (or, as the case may be, acceptance of a Follower Notice or GAAR counteraction), or by final litigation being settled in HMRC’s favour? If not, what criteria would you apply?**

If the taxpayer is treated the same way whether they decide to agree with HMRC or whether they fight on through litigation, then I suggest that there will be little incentive to accept HMRC’s position. Why wouldn’t a taxpayer feel that litigation was worth pursuing? They might just win and face no sanction, whereas if they back down and agree with HMRC they will fall within this regime.

The only sensible trigger point is final litigation being settled in HMRC’s favour. That way there is at least some incentive for the taxpayer to settle early.

**Q16. How do you think a transitional provision should best work to encourage avoiders to withdraw from avoidance schemes they have already employed?**

If surcharges are only applied as I have suggested in my answer to Q1 and “defeat” is defined as I have argued in my answer to Q15, I’m not sure you need to worry about a transitional period. Using the diagram on page 8 of the condoc, if Scheme 3 had been entered into before the start of the warning period the taxpayer would have an incentive to settle in order to avoid the risk of a surcharge.

### **GAAR Penalties**

It is worth reiterating that, whilst the argument for a GAAR penalty makes sense in principle, I believe that it is too soon after the introduction of the GAAR to be making these changes. My answers to the specific questions must be read in that context.

**Q17. Do you agree that the proposed opportunity for taxpayers to correct their tax position is appropriate? Please explain your view.**

Yes, provided there is sufficient warning given to a taxpayer that HMRC is about to refer the arrangements to the Panel.

**Q18. Do you agree that the proposed rate for the GAAR Penalty is appropriate? If not, what penalty rate would you propose and why?**

Your reasoning as to the appropriate rate for the penalty in comparison with a penalty under Schedule 24 to FA 2007 is flawless, right up to the proposal of the actual rate. You have argued – rightly, in my opinion - that the penalty needs to be lower than that for fraudulent activity, in recognition of the important differences in behaviour. You then propose a penalty that is almost at the same level! Hardly a realistic recognition of the differences in behaviour.

The proposal to “cap” the penalty in situations where Schedule 24 to FA 2007 also applies is quite reasonable.

**Q19. Do you agree that this penalty model will act as a fair and proportionate deterrent? Please explain your view.**

The GAAR was introduced to act as a deterrent as well as to give HMRC another means of challenging “avoidance”. My concern is that you are proposing to introduce a penalty regime before allowing proper time to assess the effectiveness of the GAAR itself. If the GAAR works as a deterrent then the penalty regime is unnecessary – except as a revenue-raising tool, which is contrary to your penalty principles.

Unfortunately, without first properly assessing the effectiveness of the GAAR itself, you will never know what is providing the deterrent.

**Q20. Do you agree that this safeguard would be appropriate for the GAAR Penalty?**

Subject to my overall concerns about introducing a penalty at this stage, no I do not think this “safeguard” is appropriate. Giving discretion to HMRC is hardly a meaningful safeguard for the taxpayer.

**Q21. Do you have any views on the development of these measures?**

Allowing a Panel opinion to be used to enable counteraction against other users of the “same arrangements” appears fine in principle but ignores the fact that those users may actually have a different fact pattern.

It is clearly right that HMRC should be able to protect its position in respect of a GAAR challenge and overall enquiry time limits. On balance I feel it may be better to leave time limits alone but allow HMRC to make a “provisional” counteraction under GAAR in order to protect its position. It will be essential that this procedural matter should not have any impact on the overall GAAR process other than to protect HMRC’s position with regard to potential tax liabilities. The taxpayer’s position must remain as it would have done without such a “provisional” counteraction.

**POTAS**

**Q22. Would including the definitions listed above as triggering this threshold condition be sufficient? If not, what other approach do you favour?**

For these purposes, I do feel that the list is sufficient. In contrast to my views in respect of the Serial Avoider proposals, when dealing with promoters I do believe that it is appropriate to include situations where a taxpayer has conceded HMRC’s view and withdrawn from the “scheme” as a “defeat” for that promoter.

**Q23. What are your views on the options for the trigger for the threshold condition? Please explain your reasoning.**

The suggestion that the trigger might be based on a certain proportion of users being defeated does have much more merit. However, it suffers from the problem raised in the next question.

**Q24. At what point should a scheme that has high numbers of users count as having been defeated?**

Surely, as long as the users can be tracked, HMRC will know what proportion have either withdrawn or lost in litigation.

**Q25. What are your views on the proposed methods of counting defeated schemes that will trigger this threshold condition? Do you think that a rule regarding proportions of cases defeated would be appropriate?**

It seems to me that you really need to be looking at the “defeated” “schemes” in the context of all of the “schemes” being promoted. Is a promoter who has 3 “schemes” “defeated” out of a total of twenty (with all the others being fine) really the same as a promoter with 3 “schemes”, all of which are “defeated”?

**Q26. Do you agree that a period of up to 9 years provides sufficient time to accurately establish regularity of behaviour for this threshold condition? What are your views on the furthest date in the past the authorised officer should consider?**

The problem with this proposal is not so much the furthest date in the past, as the amount of time you are proposing to look forward. You say that “regularly” means “repeatedly, frequently, [sic] or often”. Surely this requires a relatively short period of time over which to establish the necessary behaviour, not 9 years.

Your example in the condoc describes 3 “defeats” in a period of 6<sup>1</sup>/<sub>2</sub> years. That, in itself, hardly feels like “regularly”. Of course, coming back to my answer to Q25, if those 3 “schemes” represented a significant proportion of the total “schemes” promoted by that person then maybe that would be reasonable.

Unfortunately, stretching the time period out like this seems almost designed to make it easier to shoe horn behaviour into your definition.

**Q27. What provisions should be made for cases that are already in the courts but have not yet concluded?**

Given that the relevant point seems to be the “defeat” of a “scheme”, rather than its creation per se, it seems reasonable to include the “defeat” of any “scheme”, even if it was already in the court system at the commencement date of these provisions.

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