THE CITY OF LONDON LAW SOCIETY

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Susan O'Hara
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By email: susan.o'hara@hmrc.gsi.gov.uk

Dear Ms O'Hara

Re: Comments on HM Revenue & Customs' Consultation Document "A Code of Practice on Taxation for Banks"

The City of London Law Society ("CLLS") represents approximately 13,000 City lawyers through individual and corporate membership including some of the largest international law firms in the world. These law firms advise a variety of clients from multinational companies and financial institutions to Government departments, often in relation to complex, multi jurisdictional legal issues.

The CLLS responds to a variety of consultations on issues of importance to its members through its 17 specialist committees. This response in respect of "A Code of Practice on Taxation for Banks" (the **Code**) has been prepared by the CLLS Revenue Committee. We are grateful for the opportunity to comment on the Consultation Document dated 29 June 2009 relating to the Code. .

You have included in that document at Chapter 5 the questions for consultation. We set out below our comments in relation to questions 1 and 3.

1. What issues are likely to arise in introducing and complying with the Code and how can these issues be overcome?

We are concerned that there will be many situations in which the spirit of the tax law and/or the intentions of Parliament will not be clear. In particular, there are likely to be circumstances where the transaction or arrangements being entered into and their tax treatment would never realistically have been considered by Parliament at the time the applicable legislation was enacted. This may be of particular concern when considering whether the interaction of different parts of the tax code together produces a result which was never intended by Parliament. In such circumstances it will be very difficult for an officer of a bank (even one who is professionally advised) to be certain that a bank's activities are within the spirit of the tax law and not contrary to the intentions of Parliament.

The Code seeks to prevent banks "promoting" transactions that would give rise to a tax result contrary to the intentions of Parliament. We understand that the intention is not to prevent banks "facilitating"

transactions involving third parties. We are concerned that the distinction between the promotion and facilitation of transactions is not clear. Is it intended that this will be elaborated upon in guidance? We are concerned that, unless it is made clear in what circumstances banks will not be regarded as a promoter, banks may be reluctant to facilitate transactions involving third parties except in circumstances where they fully understand the tax implications not only of the transaction in question but to each of the parties entering into that transaction. In such circumstances the level of tax due diligence carried out by a bank is likely to be greater than is currently the case where the main purpose of such due diligence is to be sufficiently certain that funds advanced will be repaid. If banks feel unable to lend money to third parties without having first carried out extensive tax due diligence on the transaction in question and the parties involved, this may lead to banks refusing to lend to borrowers engaged in legitimate tax planning and could act as a fetter on lending. This would obviously be contrary to HM Government's objective of freeing up lending to business.

In Section 1 of the Code (at paragraph 3.9) HM Government makes clear its intention that banks will apply the Code in all their dealings, "throughout their commercial operations, including in their subsidiaries and other vehicles". It would be helpful if guidance could be given as to what is meant by the term "other vehicles" in this context. For example, is it intended that entities in which a bank has less than a controlling interest will be included, such as certain joint venture vehicles? Although a bank may have an economic and/or legal interest in an entity, the nature of that interest may be such that the bank is not in a position to control that entity and therefore ensure that the entity applies the Code in its commercial operations.

It is unclear to us when it is intended the Code will enter into force. We assume it is not intended that transactions or arrangements entered into before the Code comes into force will be affected by it. However, clarification on this point would be welcome.

We note that the Code is intended to apply to banks. We would be interested to know if HMRC proposes to extend the Code to other types of taxpayer in the future e.g. large business.

3. What support should banks expect from HMRC to help them implement and abide by the Code?

It is clear that HM Government wants to encourage open dialogue with the banks and to promote a discussion between the banks and HMRC about any potential uncertainties regarding the tax treatment of transactions which a bank is considering entering into. The Code envisages that a bank will consult HMRC when it is uncertain whether a proposed transaction is within the spirit of the tax law or in accordance with the intentions of Parliament and that doubts will be resolved through discussions with HMRC.

HMRC will be aware that many transactions entered into by banks involve complex tax issues and short timescales for implementation. In order to achieve HM Government's objective we think HMRC will need to be prepared to dedicate considerable resource and expertise to its discussions with banks regarding their commercial operations. Such discussions will often have to take place in "real time" so that issues can be resolved quickly. It would be helpful to understand how such resource and expertise will be made available in practice to the banks.

In Section 4 of the Code (at paragraph 3.24) a key aspect of the desired relationship between HMRC and the banks is described as involving full disclosure by the banks of issues that the banks consider HMRC would want to know about and might want to discuss. We would be concerned if such discussions are used by HMRC as a means of obtaining early disclosure of arrangements or schemes which are subsequently closed down at short notice. Such action on the part of HMRC would not, in our opinion, encourage transparent and constructive relationships with the banks. In our view the proper means by which HMRC should obtain early disclosure of tax avoidance schemes is through the 2004 Disclosure of Tax Avoidance Schemes legislation. The Code should not be used as a means to circumvent or make up for any perceived inadequacies in that legislation.

We note HM Government's objective that relationships between the banks and HMRC should, wherever possible, be transparent and constructive and based on mutual trust. To this end, we hope that HMRC will also adopt the same principles and behaviours when interpreting and applying tax legislation as it expects from the banks i.e. that HMRC will interpret and apply tax legislation having regard to the spirit of the law and the intentions of Parliament. We would not expect that it is only the banks that are intended to interpret and apply the law this way. In our view this should be a two-way process.

Whether HMRC achieves an open dialogue with the banks is, in our view, likely to depend to a large extent upon how HMRC responds to what it is told by the banks. If the banks' impression of their discussions with HMRC is that HMRC is acting reasonably, providing objective interpretations of the law and giving the banks some direction as to whether a particular type of transaction or arrangement might be challenged or legislated against, then such discussions are likely to be considered by the banks as useful and constructive. If, however, banks think that HMRC is simply using its discussions with the banks as an information gathering exercise with a view to dissuading them from carrying out any tax planning and/or attempting to influence or regulate the way in which the banks carry on their business then this is likely to result in the banks being less inclined to be open and candid in their discussions with HMRC.

Yours sincerely

Bradley Phillips

Chair
Revenue Law Committee

THE CITY OF LONDON LAW SOCIETY
REVENUE LAW COMMITTEE

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