The City of London Law Society

4 College Hill
London EC4R 2RB
Tel +44 (0)20 7329 2173
Fax +44 (0)20 7329 2190
DX 98936 - Cheapside 2
mail@citysolicitors.org.uk
www.citysolicitors.org.uk

Attention: Chris Davidson
HM Revenue & Customs
AAG Policy
3rd Floor
100 Parliament Street
London SW1A 2BQ

13th September 2012

By post and by email (study.gaar@hmrc.gsi.gov.uk)

Dear Sir

Revenue Law Committee response to 12th June 2012 Consultation Document on A General Anti-Abuse Rule

The City of London Law Society ("CLLS") represents approximately 14,000 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 has been prepared by the CLLS Revenue Law Committee.

We are grateful for the opportunity to respond to the Consultation Document. Our response below follow the questions set out in the Consultation Document. We also make reference below to the Aaronson QC Study Group Report dated 21st November 2011 and the Study Group's Supplementary Report dated 25th June 2012. We also refer to comments made by the HMRC team and attendees at the GAAR Open Day meeting held at HM Treasury on 5th September (referred to below as "the GAAR Open Day").

1. **Do you agree that the GAAR should be limited to the taxes and duties set out in clause 1(3) of the Draft GAAR initially? Are there any particular issues relating to how the GAAR would function in relation to the taxes (including NICs) that are proposed to be included?**

   - We do not consider it workable that the GAAR should be subject to self-assessment (see further the response to Question 10 below). It would be strange for a taxpayer to undertake a scheme which it considers it needs to self assess

as ineffective. Similarly, given the high bar which it is intended must be cleared before the GAAR can be applied, we suspect that most if not all taxpayers undertaking relatively aggressive tax planning would nonetheless convince themselves that no "white space" disclosure was needed on their tax returns.

- We therefore consider that, practically, the only viable way for HMRC to force taxpayers to disclose that they have undertaken a transaction which is subject to the GAAR (and therefore, realistically, HMRC's only reliable method of identifying potential targets for attack) is via the DOTAS regime. Where a DOTAS number is included on a taxpayer's return, HMRC will know that a scheme has been implemented and will be able to identify what that scheme is. HMRC can then decide whether to seek to invoke the GAAR against it.

- It follows from this that our view is that the GAAR should only apply to those taxes to which the DOTAS regime applies (excluding VAT). It would also be necessary to amend the operation of DOTAS in relation to SDLT such that scheme numbers be included on land transaction returns. Whether or not our recommendations in relation to the interaction between the GAAR and DOTAS are accepted, we would suggest that this measure be introduced. We are genuinely puzzled as to why this is not the case already.

- We understand that the DOTAS regime has proved imperfect in a number of respects. However, it too is currently under review and subject to the consultation "Lifting the Lid on Tax Avoidance Schemes". Our view is that DOTAS and the GAAR are interlinked, and if there were to be any question of applying the GAAR to a scheme which was not required to be disclosed under DOTAS, that would indicate a serious failure of the DOTAS regime. Improvements to the DOTAS regime should be progressed alongside the GAAR, and considered with the need to identify schemes properly the subject of the GAAR in mind.

- If it is considered necessary to extend the GAAR to taxes such as PRT which are not currently subject to DOTAS, our view would be that the first step would be to extend DOTAS to those taxes.

- IHT presents particular challenges in that there are significant time differences – decades, even – between the implementation of planning and the realisation of tax savings. Furthermore, testing for avoidance by reference to the commerciality of transactions is entirely inappropriate in the context of IHT since the tax only applies to non-commercial transactions in the first place. For this reason our preliminary view is that if IHT is to be the subject of a GAAR, it will have to have a specific set of provisions to deal with it – effectively its own mini-GAAR. Given the time pressures attendant on introducing this legislation, if IHT is to be included it may be appropriate to aim for FB2014 in relation to it.

- Additionally, transactional taxes (in particular, SDLT) can be subject to avoidance of different types than taxes on profits. Many SDLT schemes operate by allowing the benefit of the use of land to pass to a buyer without at any stage giving rise to a land transaction for the purposes of the tax. In such a case how would the GAAR in its existing form operate? Could it deem there to be a substantially performed land transaction when under the basic law there is none? If so, what would the effective date of that land transaction be (the GAAR as drawn cannot

specify this)? This is not a reason not to apply the GAAR to SDLT, but, as with IHT, it may indicate that it requires SDLT specific provisions.

2. **Do you agree that the GAAR should be capable of counteracting UK tax advantages obtained under double tax agreements?**

- Subject to the Government being fully satisfied on the legality of applying the GAAR to a previously negotiated UK Double Tax Treaty, we see no reason for excluding abusive arrangements based on Treaty advantages.

- That said, it must be clear that the GAAR cannot operate to effectively amend the terms of treaties to which the UK is party but which are on terms which it would not sign up to today. In particular, if a given treaty (most notably that with Luxembourg) does not contain an anti-treaty shopping provision, the GAAR should not be able to be used effectively to imply one. If a taxpayer sets up operations in Luxembourg purely to take advantage of the treaty (and meets the requirements of the treaty, in particular in relation to the beneficial ownership of any income received), the treaty clearly allows its benefits to be available. If the Government has formed the view that the terms of a given treaty are unacceptable, the proper course of action is for it to renegotiate the treaty.

- Of course, any such application of the GAAR must also defer to the principles of EU law. As per *Cadbury Schweppes (C-196/04)*, any provision that restricts the fundamental freedoms must only apply where there are wholly artificial arrangements in place (paragraph 55).

3. **Do you agree that (1) the proposed "main purpose" rule serves as a useful filter, when coupled with the concept that arrangements must also be "abusive" and (2) a specific exclusion for arrangements without tax intent is not required? If you think a specific exclusion is required, please explain why.**

- We struggle to see what use the proposed "main purpose" rule will have in practice in acting as a meaningful filter. It is drafted very widely and the fear is that the 'main purpose' test will be of no practical benefit to taxpayers where tax has been a significant consideration in structuring arrangements, (as will frequently be the case in commercial transactions).
- As a consequence, it is really the "abusive" test alone that will govern the applicability of the GAAR. Our concerns over whether this test will operate as intended are set out in the response to Question 4 below.
- If there is to be a meaningful "purpose" test as a preliminary filter, we consider that it should be a "sole" purpose test as this would accord with the intention to catch only artificial and abusive (egregious) schemes. The fundamental problem with having a test which catches "or one of the main purposes" is that, by definition, there are other main purposes present which are commercial and not tax motivated and therefore such arrangements should not be caught by the GAAR. It may be that proposed Clause 2(2)(c) is designed to reflect this concern ultimately, although it is not entirely clear (without Guidance) what is envisaged by that clause.
- If the current formulation is to be retained, we consider that the "main purpose" test should be assessed subjectively because it would be grossly unfair to be

tainted with the GAAR unless the actual taxpayer under review intended to obtain a benefit.

- On balance, we believe it would be preferable to have a specific statutory exclusion for arrangements without tax intent. This would provide legislative comfort to the public on the point rather than requiring taxpayers to consider the detailed provisions fully or rely on Guidance (which, we note, would not have the force of law under the current HMRC formulation of the GAAR) to conclude there would be no issue in the particular circumstances.

4. **Do you agree that the proposed "double reasonableness" test operates as intended to counteract only artificial and abusive schemes (such as those described in Annex B)?**

- Although we understand that HMRC do not intend this to be the case, on a strict reading of the proposed wording, the proposed "double reasonableness" test would potentially catch much more than just "artificial and abusive" schemes and therefore there is a real concern that it would not simply operate as intended. As currently drafted it is capable of being applied widely so that it could catch a wide range of arrangements that should be regarded as "reasonable" planning. There is nothing else in the proposed legislation that clearly limits it to artificial and abusive schemes only.
- As a result, combined with the lack of any formal clearance procedure, we have real concerns that taxpayers and their advisers will not be able to ascertain with any real certainty in advance of implementing a proposed transaction whether or not a transaction could be attacked under the GAAR. It is recognised that there is likely to be a similar element of uncertainty whatever form of wording is ultimately used. If it is not possible to include specific wording in the legislation to make it clearer that the GAAR is only to counteract artificial and abusive schemes (which would be our recommendation), then we consider it vital for there to be comprehensive Guidance which makes it clear that the GAAR is only intended to operate to such schemes (for example, see the Study Group's suggested Guidance wording).
- In relation to the specific wording of the proposed "double reasonableness test", we are concerned that the reference to a "consideration of all circumstances" will require or cause judges to make moralistic assessments of the transaction which is not considered right or appropriate.
- There is a concern that HMRC may be privy to greater amounts of material than the taxpayer may have access to and therefore, the test creates an uneven playing field.
- We are also concerned over the suggestion that the "all circumstances" test would allow HMRC to place unfair weight on the fact that similar schemes or arrangements had been shut down in the past.
- We also consider it appropriate for it to be made clear that the GAAR should be applied to the tax legislation, and any other public available materials, as existed at the time that the transaction was entered into and not with the benefit of hindsight or later changes in law. In particular, in our view a taxpayer is not avoiding tax if he does something which is clearly permitted by law but which a later policy change has determined should not be permitted. In such a case it is for the government to amend the law to reflect the changed policy.
- The GAAR should not be able to be utilised as a sticking plaster for poor drafting, or to correct obvious legislative oversights. For example, in our view the GAAR should not have been able to be applied to the widely-publicised debt buy in

structure against which retrospective legislation was deployed in February. This applied highly formulaic legislation in accordance with its clear terms, in circumstances where that legislation had recently been heavily amended to close down perceived loopholes not including the structure in question (and where the structure in question had been known to HMRC for many years). In such a case the taxpayer should be able to rely on the law as it is stated on the page of the statute book.

- We also recommend a clear statement in the legislation to the effect that if there is any doubt that the GAAR applies, it should be resolved in favour of the taxpayer.
- It is also thought that where a taxpayer does something that has previously been considered acceptable (i.e. where HMRC has not previously challenged arrangements as being abusive), the GAAR should not be capable of applying. There is recognition of this in Clause 5(3)(b) in relation to the court or tribunal considering evidence of established practice but this only offers limited practical protection.

5. **Do you agree that the counteraction provision in the draft GAAR is appropriate?**

- We are content with the proposal to make a "just and reasonable" counteraction.
- We are concerned over the proposal for consequential adjustments to be made which "may affect any person (whether or not a party to the arrangements)" if such adjustments were to increase the tax liability of other parties. This seems wrong in principle and must raise questions about taxpayer confidentiality.
- If the GAAR is to be within self assessment, any consequential adjustments to be made by the taxpayer whose tax advantage is counteracted should also be self assessed. Otherwise, a taxpayer who self assesses may suffer double taxation pending HMRC making consequential adjustments. This would be unfair (see, however, our comments below on self assessment generally).

6. **The Government is continuing to develop its analysis regarding the appeals processes in relation to counteraction and consequential adjustments under the GAAR, and welcomes views which may inform detailed proposals to be published later in the year.**

- We await further details of the Government's proposals in relation to any appeals process. We agree with the proposal that a tribunal or court should be able to reach its own conclusion as to what would be the appropriate counteraction.

7. **The Government would welcome views on the options set out regarding commencement, how transitional arrangements should be dealt with, and whether there should be different rules for different taxes where appropriate.**

- There is a general concern about the GAAR applying from 1 April 2013 when the Guidance may not be final by then and the Advisory Panel will not be in place.
- Subject to the above point, we consider it fair for the GAAR to apply to new arrangements entered into on or after 1 April 2013.

- There are obvious concerns over the GAAR applying to transactions put in place before 1 April 2013 where the tax advantages may arise post that date. If complete grandfathering is not considered appropriate, as a minimum, it is thought the GAAR should not be capable of applying to any arrangement put in place before any specified date before 1 April 2013 unless that date is publicly announced in advance. We understand from the GAAR Open Day that if this option is pursued that date would be the date the draft Finance Bill is published in late November/early December.
- Our very strong preference would be for the GAAR to only apply to new arrangements post April 2013 which we understand from the GAAR Open Day is the other option being considered.

8. **The Government welcomes views on clause 5(1) of the Draft GAAR.**

- We agree that it should be for HMRC to show that the key requirements of the GAAR are met and do not see any administrative issues with what is proposed.

9. **Do you agree that it is appropriate for particular weight to be given in the Legislation to the GAAR guidance and the opinion(s) of the Advisory Panel on the arrangements?**

- Subject to our comments below in relation to the proposed Guidance and operation of the Advisory Panel, we agree with the suggestion that a court or tribunal should take into account the Guidance and any opinion of the Advisory Panel.
- We are, however, concerned over the suggestion that the Guidance and the opinion of the Advisory Panel should carry more weight than other materials. This may put the taxpayer at a unfair disadvantage where they have relied upon other materials or on what they considered as established practice.
- Opinions of the Advisory Panel should be published in anonymised form, in the same way as first tier tribunal decisions are published. We think that a digest of key principles emerging from opinions would be much less useful to practitioners seeking an insight on how the GAAR will be applied. We also agree with HMRC's view (expressed at the GAAR Open Day) that any dissenting opinions from Panel members should also be published.

10. **The Government welcomes comments on whether particular issues arise in relation to Self-Assessment (where the relevant taxes operate within a Self Assessment regime) or within the existing administrative rules for those taxes that do not operate within a Self-Assessment regime.**

- We are strongly of the view that it is inappropriate for the GAAR to be operated under the self-assessment rules. Conceptually, how can a taxpayer do this when the burden of proof on whether the GAAR applies is on HMRC?

- It is also unclear how the Government expects the GAAR will interface with the DOTAS rules. The consultation document indicates that the Government expects that the GAAR may apply in cases where DOTAS does not. As we have set out above, we think this is wrong.

- It would be strange for a taxpayer to self-assess on the basis that the GAAR applies – to do so would be entirely self defeating; there would have been no point in using a scheme unless the taxpayer was advised that it could file on the basis that it worked. Any self assessment would more likely therefore be limited in practice to a "white space" disclosure if a taxpayer thought the GAAR might apply but hoped that it would not. Of course, certain taxpayers may take the view that there is also no need to make a white space disclosure.

- In our view the key is for HMRC to be able to identify those taxpayers which have used schemes which are capable of attack. For the reasons set out above we do not believe that self assessment will enable this in any way. It is only through the DOTAS procedure and the resultant requirement to include scheme numbers on tax returns that HMRC will be able to find targets reliably.

- There may be advantages in the GAAR only being applied where HMRC direct. This may lead to greater consistency in the application of the GAAR and reduce the risk of mission creep. Requiring a taxpayer to self-assess will cause additional uncertainty for taxpayers at the time of completing their tax returns.

11. **The Government invites comments on the general proposal that the GAAR should as far as possible operate within existing administration rules for the taxes involved; and on what adaptations may be necessary to existing administrative rules to ensure that the GAAR operates with as little as possible additional administration cost and burden for taxpayers, advisers and HMRC. Is there a case for having a new type of assessment given the cross-regime range of the GAAR?**

- We, of course, favour limiting any increased burden or cost on taxpayers.

12. **The Government invites comments on whether time limits should be set for each of stages two, three and four and if so what those time limits should be.**

- We have no firm views on time limits but any proposal will need to be sensible and workable.

13. **The Government welcomes comments on the proposals relating to the Advisory Panel.**

- We have numerous concerns around the Advisory Panel proposals. As a preliminary observation, we would make the point that commenting at this stage on the Advisory Panel process is difficult in light of the fact that the Government has not published its full proposals for the Panel including likely members and procedural rules. We do, however, agree with HMRC's suggestion made at the GAAR Open Day that the Chairman will be independent and HMRC, if represented, would be outnumbered.
- A key concern regarding the operation of the Advisory Panel is around how it would assess what is "reasonable". For example, if one person on the Advisory Panel considered the planning to be reasonable, would that be enough to ensure

that the GAAR would not be applied? It seems to us that prevents the Advisory Panel from concluding that the GAAR can be applied? The Aaronson Study Group proposal sensibly seemed to provide explicit protection for a taxpayer where at least one person (other than the taxpayer) considered the planning reasonable. The detailed rules should address this issue.

- In our view, there is a strong case for HMRC not being represented on the Advisory Panel. Otherwise, the fear is that the composition of the Panel is likely to operate in HMRC's favour as HMRC will always have a representative on it. If there is to be HMRC representation, this should be a minority and a majority verdict should be necessary. HMRC should not be able to control the composition of the Panel in any individual case. We understand from the GAAR Open Day that HMRC remain strongly of the view that they should be represented. We agree with the comments made at the Open Day that if this is to be the case, the taxpayer (or its adviser) should somehow also be represented in some form when the Panel considers the taxpayer's position.
- The fact that the Panel will only receive written representations may result in decisions that are based on untested statements and possible misunderstandings of the law and facts. We have real concerns over whether the Panel is workable for complex arrangements as this would require a sophisticated level of analysis not able to be conveyed in short timespans with written representations.
- We consider that it should be the case that HMRC should be bound in practice by the decision of the Panel. If this to not to be enshrined in the legislation (our preference), then the Guidance should make it clear that only in very exceptional circumstances would HMRC pursue a GAAR assessment if the Panel has ruled against the GAAR applying. The Guidance should give examples of such exceptional circumstances.
- In terms of the Panel's role in approving the GAAR Guidance, we are keen to understand whether the entire pool of Panel members would need to consider and approve the draft or just an 'executive committee' of Panel members. What protections will there be against the Panel members merely acquiescing to the guidance produced by HMRC?
- We understand from the GAAR Open Day that consideration is being given to establishing an interim Advisory Panel solely for the purpose of approving the first iteration of the Guidance. We support such a proposal as long as the interim Panel is appropriately constituted. We agree with the comments made at the GAAR Open Day that it would not be appropriate for the interim Panel to include all or even some of the Araonson Study Group on the basis an new independent group of individuals is sensible and that the interim Panel should include persons with appropriate day to day commercial experience to be able to comment on what constitutes reasonable tax planning.
- It is unclear how the Government proposes to address the potential for conflicts of interest as between the Panel members and the scheme / arrangements being reviewed. It is possible that publishing the Advisory Panel decisions may alleviate conflict issues because no one advisor would be in an advantageous position compared to others. If Advisory Panel decisions were secret then it may be difficult to adhere to the rules of conduct which say that a solicitor has a duty to his client to tell him anything of relevance to the case (which may include an adverse GAAR ruling).

14. **The Government would welcome views on the proposals for producing and updating the guidance.**

- We consider that the guidance should be published in draft form and be separately consulted upon and ultimately be reviewed by an independent body, such as the proposed Advisory Panel or the now proposed interim Advisory Panel.
- We also consider it is imperative that the Guidance be produced as soon as possible and be finalised by 1 April 2013 (which we understand is the proposal).
- We consider it imperative that the Guidance includes examples of what may or not fall within the scope of the GAAR including examples. We understand this is proposed and we would encourage the inclusion of as many examples as possible.

15. **HMRC would welcome comments or evidence that can improve the TIA assessment of impacts, costs and yield of the GAAR proposals.**

- We are not in a position to comment.

We hope that the above responses are helpful. Our most significant concern is that as the proposed "double reasonableness" test is capable of applying to more than just artificial and abusive arrangements, there will be uncertainty for taxpayers and their advisers. We would strongly prefer if it was possible to obtain advance clearance from HMRC that the GAAR is not applicable. This could, in practice, be achieved through CRMs giving comfort, although that would not be of any assistance to those taxpayers who do not have a CRM. At the very least, we would recommend adopting the original Aaronson Study Group suggestion that clearances should be given where other statutory clearances are sought.

We also have various concerns in relation to the Advisory Panel proposals which we hope are addressed when the further detailed proposals are published.

Yours faithfully,

Bradley Phillips
Chair
The City of London Law Society Revenue Law Committee

THE CITY OF LONDON LAW SOCIETY
REVENUE LAW COMMITTEE

Individuals and firms represented on this committee are as follows.

B.S. Phillips (Herbert Smith LLP) (Chairman)

H. Barclay (Macfarlanes LLP)

C.N. Bates (Norton Rose LLP)

D. Friel (Latham & Watkins LLP)

P.D. Hale (Simmons & Simmons LLP)

M.J. Hardwick (Linklaters LLP)

C. Hargreaves (Freshfields Bruckhaus Deringer)

C. Yorke (Allen & Overy LLP)

K. Hughes (Lovells LLP)

G. Miles (Slaughter and May)

J. Scobie (Kirkland & Ellis LLP)

V. Maguire (Clifford Chance LLP)

C.G. Vanderspar (Berwin Leighton Paisner)

S. Yates (Travers Smith LLP)