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8th August 2013

Dear Sir

CLLS Revenue Law Committee response to HMRC Consultation document on Strengthening the Code of Practice on Taxation for Banks of 31 May 2013

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 and their clients through its 19 specialist committees. This response has been prepared by the CLLS Revenue Law Committee.

1. Introduction and summary

1.1 We are grateful for the opportunity to comment on the Consultation Document of 31 May 2013 (the ***ConDoc***). We think that the ConDoc proposals are bad proposals which should either be withdrawn, or significantly amended before being pursued.

1.2 Our principal concerns are as follows:

(a) the ConDoc contemplates the imposition of a very real sanction, in that naming (either as a non-adopter or as an adopter viewed as being non-compliant) will inevitably carry some degree of shaming – i.e. deliberate damage to reputation, just as banks in the UK are working hard to rebuild reputations;

(b) the proposals are for further steps in a bad direction in that the original introduction of the Code in 2009 amounted to the introduction of a significant new element of the UK's tax code that completely sidestepped the critical parliamentary assessment that would have applied if the introduction of the Code had been subject to legislation. In our view this regrettable approach is extended

by the proposal now to legislate for enforcement of the Code without legislating the Code (and ideally the surrounding guidance) as well. The ConDoc proposals would also further the extent to which administration of the Code offends against the principle of separation of powers;

(c) the announcements proposed for the Autumn Statement are not obviously aligned with HMRC's duties of confidentiality in that they would combine publication of a test from which the identity of banks within scope can be established with publication of a list of banks who have adopted or re-adopted the Code - from which it would be straightforward to identify those who have not at that date adopted;

(d) the sanction (damage to reputation) is a blunt and potentially disproportionate instrument in at least two senses:

(i) the harm to some sorts of banks may be far greater than to others (compare the position of a bank with a large base of retail depositors who may be motivated to close or run down accounts with that of a pure investment bank), and

(ii) the sanction could not readily be applied in a manner which distinguishes between more or less innocent cases (compare a bank which deliberately chooses not to adopt because it considers that the procedures proposed would interfere with its intended approach to business with that of a bank whose adoption is delayed until just a few days after the Autumn Statement because one final internal approval took time in coming through);

(e) the proposed application of the revised regime to "potentially abusive transactions" is particularly obnoxious. The proposal is that if a single (albeit senior) HMRC officer has decided to refer a matter to the GAAR Advisory Panel, then without more a bank would be faced with a decision between self-assessing on the basis that the relevant tax planning does not work (i.e. surrendering its usual tax appeal rights) or suffering application of the coercive blunt instrument sanction of reputational damage; and

(f) the proposals for the potential imposition of a significant sanction (harm to reputation) are not balanced by any meaningful right of appeal.

1.3 We expand on these points in sections 2-7 below. In section 8 we give our responses to the specific questions raised in the ConDoc.

2. Naming and shaming: a significant sanction

2.1 The ConDoc proceeds on the basis that the naming of a bank – either as a non-adopter or as one who HMRC considers is non-compliant after adopting – is a very real sanction and we agree with that. Particularly at a time when pretty well all banks operating in the UK are concerned to rebuild or maintain their reputational standing, these issues are critically important to banks. There is undoubtedly the potential for significant financial cost to banks in harm to reputation, albeit that the cost would in many cases be hard to measure and have the potential to be of vastly different scale as between different banks and different sorts of banks. (Naming in connection with the Code would be much less of a sledgehammer if it were confined to cases where the relevant bank's name was already in the public domain – e.g. in litigation before the Tribunal.)

2.2 It is important to a transparent debate that terms be used correctly, taking into account that the proposals involve the potential for imposition of a significant sanction, and so a coercive and potentially punitive framework. If the ConDoc proposals were to be introduced, it would not be right to describe adoption of the Code as "voluntary". This is significant in that responses to many of the objections that were raised at the time of the original introduction of the Code in 2009 on the basis of the rule of law and the principle of separation of powers laid emphasis on the feature that adoption of the Code was voluntary. It would be an Orwellian misuse to persist in labelling adoption as "voluntary" if the current proposals were to be implemented, and in our view that misuse should be avoided in the interests of a clear minded debate of the merits and otherwise of the proposals.

3. Rule of law; separation of powers

3.1 We recognise that at the current time banks, and particularly banks which HMRC might view as involved in unacceptable tax avoidance, do not arouse high levels of popular sympathy. In that sense it is an opportune time to introduce proposals to make life more difficult for banks (and/or potentially less embarrassing for HMRC). But there is no necessary overlap between opportunism and doing what is right in principle and any extension of a punitive but non-legislated, or only partly legislated, part of the UK tax code can in our view only be unhelpful to the perception of those (including non-banks) appraising the UK as a place to do business.

3.2 At the time of the original introduction of the Code in 2009 a number of objections were raised on the basis of the maintenance of the rule of law and of the principle of separation of powers. One example of representations of this nature were those of the Financial Markets Law Committee, available via http://www.fmlc.org/Pages/papers.aspx, paper of 1 October 2009, which raised the question whether as "a potentially coercive framework for the relationship between a bank and HMRC" the Code should have been "subject to the same kind of critical assessment as legislation". We think that the current proposals raise the same concerns, if anything in more extreme form in that:

(a) in terms of the rule of law, the current proposals are to take the Code – itself never subjected to the parliamentary scrutiny that would have attached if it had been introduced through legislation – and to legislate only to the extent necessary to provide for a significant sanction for failure to adopt the Code, or having adopted for being viewed as non-compliant. In our view, the approach that would do least harm to the rule of law in the UK, rather than legislating for enforcement without legislating the Code itself, would be to enshrine the whole of the Code and the underlying protocol and guidance in legislation. We expect, however, that there will be a reluctance to expose the entirety of the Code framework to legislative scrutiny, not least given that central to the guidance on the Code is a notion of the "intentions of Parliament" that is avowedly different to the courts' sense of what that phrase involves; and

(b) in terms of the principle of separation of powers, the current proposals are that HMRC should have to hand a more significant sanction to persuade a bank taxpayer to self-assess in accordance with HMRC's desired view of matters. We return to this aspect in section 6 below.

3.3 Part of HMRC's response to constitutional concerns raised in 2009 was to say that the Code did not "*give HMRC a quasi legal authority. Further, it does not*

give HMRC the right to tax the bank in respect of that transaction in accordance with HMRC's view of the spirit or intention rather than the letter of the law". If the current proposals were adopted, whilst that response might remain strictly accurate, its force would be very much weakened in that the proposals are designed to give HMRC the ability to impose a potentially very significant sanction against a bank which would rather not self-assess "in accordance with HMRC's view of the spirit or intention ... of the law".

4. Taxpayer confidentiality: proposals for Autumn Statement 2013

4.1 We had assumed that HMRC had to date been operating on the basis that to identify banks which had not adopted the Code would risk a breach of the confidentiality obligation imposed by section 18 of the Commissioners for Revenue & Customs Act 2005 (***CRCA***). We had assumed that it was on that basis that when it was stated that only four of the top 15 banks had adopted the Code, no names were mentioned. We had also assumed that when the top 15 banks that had adopted the Code were named in an announcement, it was likely that all had consented to being so named, and that section 18(2)(h) CRCA therefore applied. Looking ahead, the publication in an annual report of lists of those banks that have adopted and those that have not would – if the ConDoc proposals were to be adopted – be done in accordance with specific legislation, and so within section 18(3). All of this would strike us as an admirably, and appropriately, prudent approach to the important section 18 duty.

4.2 What appears to be proposed is that by the time of the 2013 Autumn Statement (***AS***) there should be both:

(a) a clear and objective test from which it can be established (including, for example, by an interested journalist) which banks are regarded as within scope; and

(b) publication by HMRC of a list of banks who have adopted the Code.

From those two pieces of information it would be straightforward to establish a list of non-adopting banks. It is of course well established that a person can be sufficiently identified to do them harm without being explicitly named - see for example the House of Lords' decision in *Morgan v Odhams Press Limited and Another* [1971] 2 All ER 1156. Is HMRC entirely comfortable that what is proposed for the AS does not risk any breach of the section 18 duty? It would be helpful to a wider understanding of the limits on the section 18 duty if HMRC would publish or summarise the advice they have received to that effect.

5. A blunt instrument, wielded bluntly

5.1 The sanction underlying the ConDoc proposals – of harm to a bank's reputation through the shaming element of naming and shaming – would be a very unsubtle instrument. We have two concerns on this.

5.2 First, potential impact as between different sorts of banks could be of drastically varying significance. For example, the cost to a bank with a significant and potentially mobile retail deposit base (and picketable branches) might readily be vastly more significant than for a pure investment bank.

5.3 Secondly, it strikes us that it is very unlikely to be possible to name banks in a manner that achieves any widespread public appreciation of the nature or

severity of the triggering "offence". Contrast, for example, a bank which after full consideration decides not to (re-) adopt the Code because it fully intends to pursue tax planning that it expects HMRC to find objectionable with an overseas bank with only a small London operation which adopts the Code a few days after the AS solely because a final internal approval was held up. In non-compliance (as opposed to non-adoption) cases we recognise that draft clause 1(3) gives power to state details of non-compliance (itself a further deliberate inroad to taxpayer confidentiality). But even if that option was exercised by the Commissioners, there would in our view still be a risk that public appreciation of the matter might well not get beyond the headlines and into the detail.

5.4 We think that the potential for the proposed sanction to apply in such disproportionate and uncalibrated ways should be reason enough to drop proposals which have such a sanction at their core.

6. "Potentially abusive transactions" – coercion to self-assess in accordance with HMRC's position

6.1 We regard the proposed approach in cases of "potentially abusive transactions" undertaken on a bank's own account as quite wrong in principle.

6.2 The proposal is that it should be sufficient for a transaction to rank as a "potentially abusive transaction" for one officer of HMRC (albeit a senior officer) to have concluded that the matter in question should be referred to the GAAR Advisory Panel. With that status established, the following special aspect of the proposed revised Governance Protocol would apply: *"HMRC's concerns can only be resolved if the bank self-assesses or amends its self-assessment to negate the tax advantage from the transaction"*. Thus, the proposal is that the coercive threat of the sanction of harm to reputation should be used to encourage a taxpayer to self-assess in line with what HMRC would like the effect of the underlying taxing provisions to be, and to abandon the possibility of having the taxpayer's and HMRC's differing views of what the law means tested through the tribunals or courts.

6.3 To our minds, "tax" levied in such a way would no more be true taxation than the "tax" which Starbucks announced it would pay (or at any rate accelerate) when its business premises were being obstructed. Readers of the ConDoc may be forgiven for thinking that this aspect of the proposals in particular might to some extent be driven by a desire for HMRC to have an additional route to being spared the embarrassment of announcing that changes (perhaps retrospective changes) to the existing legislation might be viewed as necessary. Whatever the detail of the background to the proposal, we think it would be wrong for threat of sanction of this nature to be used to encourage taxpayers effectively to surrender what would otherwise be their normal rights of tax appeal.

6.4 In light of our concerns above, we think that this aspect of the proposals at least should be dropped altogether. Given the significant and blunt nature of the sanction, we do not think this concern would be adequately addressed merely by modifying the proposal such that "potentially abusive transaction" status would not attach at a point before there had been a finding adverse to the taxpaying bank made by an independent body such as the GAAR Advisory Panel (which is one possible modification we have heard aired). Threat of sanction of this sort should never be used to coerce taxpayers into giving up their normal rights of appeal.

7. No meaningful right of appeal

7.1 In addition to the ways in which the reputational sanction could have disproportionate impacts (5 above) it is also of concern that the proposals offer, in our view, no meaningful right of appeal against a decision to impose the sanction. On this, the ConDoc says that there will be no statutory right of appeal against "HMRC's ... decision to name ... a bank" (this is said to be on the basis that the Code will remain voluntary – see 2.2 above). The ConDoc refers to the possibility of seeking Judicial Review if a bank takes issue with an HMRC decision to name.

7.2 It seems to us that an action for Judicial Review would not offer any truly meaningful right of appeal, for three main reasons:

(a) given that the relevant draft clause would trigger the naming power if "in the opinion of the Commissioners" Code non-compliance was established, leaving to one side the (we would all hope) remote possibility of a failure to achieve *Wednesbury* reasonableness on the part of HMRC, it seems very unlikely that a taxpayer's application for Judicial Review would be successful;

(b) even if a taxpayer were successful, it is doubtful that that success would offer the bank any real redress, and certainly not financial redress. The harm complained of – publicity in connection with a dispute with HMRC over possible tax avoidance – would in many cases already have been done; and

(c) (a similar point to (b) above) it is quite possible that even pursuing a Judicial Review claim, whether or not ultimately successful, would itself involve the very harm in question, namely publicity. Even if both parties were to request a hearing *in camera*, it is entirely possible that the courts would, in view of an overriding interest in open justice, refuse such an application.

8. The ConDoc consultation questions

Set out below are our responses to the specific questions raised in the ConDoc, reflecting our wider views above.

Q.1 We welcome respondents' views on whether requiring smaller banks to only adopt Section 1 of the Code remains a tenable approach under the strengthened Code?

We think the approach remains tenable. We doubt that in practice there is a great deal in the point. We would not see the original rationale for the distinction as very much affected by the ConDoc proposals.

Q.2 Views are welcome from respondents on the proposed timetable for adoption/re-adoption.

If the proposals were to be pursued, we think that banks should have a period of at least three months after the form of the legislative wording and of the other Code framework documents are "frozen", so that a decision on adoption/re-adoption can be taken with confidence that it is the final version that is under consideration.

We would counsel against effective publication of the identities of non-adopters prior to enactment of legislation unless HMRC's advice in relation to section 18 CRCA is cast iron in nature (4 above).

We have heard some concerns expressed around the ConDoc emphasis on "unconditional" adoption/re-adoption. If there are any elements of existing side letters that are in fact acceptable to HMRC, it might ease the process if those could be published – perhaps as a standard form side letter that HMRC would be happy to exchange in connection with adoption/re-adoption.

Q.3 HMRC welcomes comments and views on the proposed approach set out to revise the Governance Protocol on Code compliance and whether the proposals provide the necessary assurance safeguards around the naming of non-compliant banks.

We do not think that the proposals provide adequate assurance safeguards. Our clearest concern is in relation to "potentially abusive transactions" – see 6 above.

Q.4 Do these proposals offer sufficient transparency for the public around how the rules will operate?

More than sufficient. We are not aware of any public clamour, or obvious case, for increased transparency around these rules.

Q.5 We also welcome views on whether any other enhancements should be considered at this time to the Governance Protocol.

In our view, the proper approach would be for the entire Code framework, including the Governance Protocol and the guidance, to be subject to parliamentary scrutiny.

Q.6 We would welcome views from respondents on whether the examples set out below provide a sufficient degree of guidance of the types of transactions, or patterns of transactions or other behaviours that would lead to HMRC concluding that a bank is not complying with its Code commitments?

AND

Q.7 Do respondents consider this to be an appropriate descriptor for transactions within the ambit of the GAAR?

We do not have detailed comments on the examples. We regard the concern raised above about the point at which "potentially abusive transaction" status attaches as a very important one.

Q.8 Do respondents agree that this definition will result in appropriate coverage by the Code?

If concerns about the nature and operation of the Code were addressed, we would have no objection to a Bank Levy based approach to establishing scope.

Q.9 Do respondents agree that the legalisation as drafted covers the issues set out in this Consultation Document appropriately?

No. See sections 1-7 above.

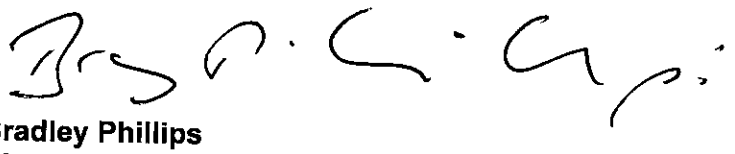
Q.10 Are there any other matters that respondents would like to see covered in the legislation?

Yes. We think that a better and more principled approach would be for the entire Code framework to be subjected to parliamentary scrutiny.

Q.11 HMRC would also be grateful for any detailed drafting points that respondents might have on the draft clauses.

We do not have detailed drafting points; we think that the underlying principles should be revisited.

Yours faithfully,



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