


Designing a General Anti-Abuse Rule (GAAR) for the U.K.—Issues, Benefits, and Limitations

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U.K. and General Background

- Complexity and imperfections of international and domestic tax systems
 - Global financial crisis/austerity—‘tax gap’ concerns
 - Increasing media interest
 - Rise of civil society (NGO) interest in taxation and corporate social responsibility pressures
 - But need to balance pressure for competitiveness and growth
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U.K. — History

- GAAR rejected in 1998
- Coalition Agreement 2010 includes review of GAAR
- Government appoints Graham Aaronson QC to lead study group (members of study group include three judges (one retired—Lord Hoffmann), two academics, and one tax director (BP))
- I am one of the academics—but speaking here in a personal capacity
- Aaronson GAAR study (November 2011)—report and illustrative draft clauses
- Proposes ‘moderate rule targeted at abusive arrangements, but not applying to reasonable tax planning,’ NOT a broad spectrum anti-avoidance rule

Further Developments

- Draft clauses drawn up by Parliamentary draftsman—publication June 2012
 - Revised December 2012 following consultation
 - Interim panel appointed under Graham Aaronson as Chair to consider draft guidance
 - Third version of legislation published in Finance Bill March 2013 for enactment in June 2013. Guidance awaited
 - Permanent panel chair appointed March 28, 2013—Mr. Patrick Mears
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Legal Position in U.K. Prior to 2013

- No statutory general anti-avoidance rule
 - No general abuse of law doctrine
 - No clear judicial anti-avoidance doctrine (see next slides)
 - No penalties for avoidance (unless for negligence or fraud)
 - No general statutory clearance (binding rulings) system (but some in individual cases)
 - Disclosure requirements
 - Restrictive rules of evidence in court
 - Detailed method of legislating (not principles-based)
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U.K. 'Solutions' (Pre-2013 and Continuing)

- Disclosure of Tax Avoidance Schemes (DOTAS)—legislation in Finance Act 2004 as amended
 - Disclosure provisions for selected transactions—hallmarks, etc.
 - By promoter within 5 days of making scheme available
- Specific provisions
- Over 300 'targeted anti-avoidance rules' (TAARs)—'main purpose or one of main purposes of the arrangements is to secure a tax advantage'—linked with other conditions related to specific legislation
- 'Voluntary' methods—
 - Tax law in the boardroom
 - Risk rating/enhanced relationships with business
 - Bank Code

UK Case Law – Judicial Doctrine

- *W.T. Ramsay Ltd. v. IRC* [1981] as elaborated in subsequent case law to late 1990s—a judicial principle?
 - Pre-ordained series of transactions (may or may not have legitimate commercial end overall)
 - Inserted steps with no commercial purpose other than the avoidance of tax
 - No practical likelihood that the events would not take place in the order ordained
 - Pre-ordained events do take effect

Judicial Doctrine Rejected – Only ‘Interpretation’?

- *Barclays Mercantile Finance Ltd v. Mawson* [2004] (BMBF)
 - *Ramsay* case did not introduce a new doctrine specific to revenue statutes but rescued tax law from the ‘island of literal interpretation’
 - ‘Going too far’ to say that transactions or elements of transactions with no commercial purpose should always be disregarded
- But same day, same court – *IRC v. Scottish Provident*
 - Applies ‘*Ramsay*’ principle to have regard to ‘series of transactions intended to have a commercial unity’

A Very Special Rule of Interpretation


- *Collector of Stamp Revenue v. Arrowtown Assets Ltd.* [2003] Hong Kong case cited in BMBF) per Ribeiro PJ:

“The ultimate question is whether the relevant statutory provisions, construed purposively, were intended to apply to the transaction, viewed realistically.”
- Normal interpretation ?
- Stretched or strained interpretation?
- OR Judicial doctrine?

Uncertainty Under Case Law

- *HMRC v. Tower MCashback LLP 1* [2011] decided in favor of HMRC
 - Special Commissioner and Supreme Court decided against taxpayer, BUT High Court and Court of Appeal judges would have found for taxpayer
- *Mayes Case* [2011] decided in favor of taxpayer–
 - “The Ramsay principle does not allow legal events to be deprived of their legal or fiscal effects simply because they are inserted for a tax saving purpose or can be described as ‘unreal’ or ‘artificial’”
 - Toulson LJ concurs, but it “instinctively seems wrong, because it bears no relation to commercial reality and results in a windfall which Parliament cannot have foreseen or intended”

Aaronson Report 2011

- Judges inevitably are faced with the temptation to stretch the interpretation, so far as is possible, to achieve a sensible result; and this is widely regarded as producing considerable uncertainty in predicting the outcome of such disputes. In practice this uncertainty spreads from the highly abusive cases into the center ground of responsible tax planning. **A GAAR specifically targeted at abusive schemes would help reduce the risk of stretched interpretation and the uncertainty that this entails.**
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Issues Encountered in Design of GAAR

- Aid to purposive interpretation or overriding principle?
- Drawing the line between legitimate planning and/or abuse — finding intention of legislature
- Role of factors such as commerciality, artificiality, business purpose
- Response to deliberate tax incentives
- Objective or subjective tests?
- The counterfactual (avoid Australian problem)?
- Relationship with specific provisions
- Decisions of Court of Justice of the European Union
- Double Taxation Agreements

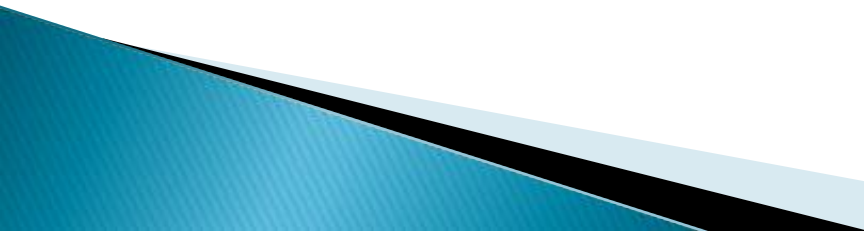
Key Features of Proposed GAAR in U.K.

- Substantive overriding provision — not just interpretation
- Targets only ‘abuse’ not avoidance.
- Non-exhaustive indicators of abuse
- Objective double reasonableness test
- Burden of proof on HMRC to show abusive and counteraction just and reasonable (clarification in guidance?)
- Rules of evidence
- Advisory Panel
- Guidance
- Scope — all but VAT (EU law)
- Intended to override DTAs — express in legislation

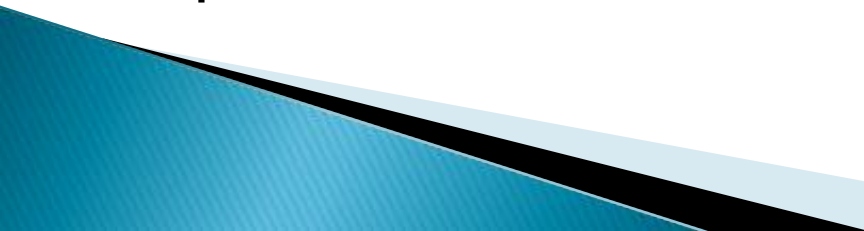
Rules of Evidence

- Court **MUST** take into account
 - HMRC GAAR guidance as approved by the GAAR Advisory panel at the time the arrangements were entered into
 - Opinion of Advisory Panel about arrangements
- Court **MAY** take into account
 - Ministerial, HMRC, and other material in the public domain at time arrangements entered into
 - Evidence of established practice at time of arrangement


Not Included in Proposal

- No subjective element—objective test only but narrow—no need for subjective protection
 - No advance rulings provisions—why?
 - Narrowness of test
 - Administrative and compliance burden
 - Large corporate taxpayers have informal means of discussing issues (enhanced relationship)
 - Guidance not contained in statute (but must be taken into account by Court)
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The Advisory Panel (AP) and Levels of Discretion

- HMRC not represented on AP
 - HMRC–designated officer must give notice to taxpayer of GAAR being applied
 - Taxpayer has 45 days to respond
 - If case to continue, must then go to AP
 - Chair of AP appoints subpanel to give opinion on whether the arrangements are a reasonable course of action or not, or whether they cannot reach a view
 - Anonymous general reports of opinions to be published?
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Process of Drafting the GAAR

- Study Group
 - Consultation (or lobbying?)
 - Political debates and confusion of different forms of avoidance leading to unrealistic expectations?
 - Agreeing on the guidance — interim panel
 - Appointment of Chair and Panel
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Effects of GAAR

- Deterrence—routine or weapon of last resort?
- (N.B. No other rules have been removed, including case law, but some new provisions considered and not introduced)
- Should reduce need for retrospective legislation and/or strengthen the argument against it (cf. *Barclays* case 2012)
- Should increase the case for underlying principled legislation; GAAR only works if taxpayer not acting reasonably with regard to policy objectives of provisions of the Tax Acts

Limitations of GAAR: What is Tax Avoidance?

- GAAR can make effective avoidance ineffective and fill obvious gaps, but cannot reform underlying faults in domestic and international tax system design
 - Thus, it cannot operate well if policy of underlying legislation is unclear or poor
 - Does GAAR increase uncertainty for law-abiding businesses? The U.K. GAAR design and panel seeks to limit this
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Limitations of GAAR– Is Risk Balance Right?

- Still requires detection and enforcement
- Requires courts to apply and uphold, so is it better than judicial approach?
 - Yes, added legitimacy and administrative framework and protection
- Should GAAR be combined with penalties?
 - No penalties in the U.K.
 - BUT new procurement rules relate to GAAR
- May be area for development once GAAR is more established—need to ensure there is a sufficient downside

Selected Sources and References

- Aaronson Study (2011) http://www.hm-treasury.gov.uk/d/gaar_final_report_111111.pdf
- J. Freedman, '[Defining Taxpayer Responsibility: In Support of a General Anti-Avoidance Principle](#)' (2004) *British Tax Review*, 332
- J. Freedman, '[Interpreting Tax Statutes: Tax Avoidance and the Intention of Parliament](#)' (2007) 123 *Law Quarterly Review* 53
- J. Freedman, '[GAAR: Challenging Assumptions](#)' (2010) *Tax Journal*, Sept. 27, 2010
- Devereux, Freedman, and Vella, *Tax Avoidance*, http://www.sbs.ox.ac.uk/centres/tax/Documents/reports/TA_3_12_12.pdf
- Ernst & Young, *GAAR Rising*, Feb. 2013.
- U.K. Finance Bill 2013: http://www.hm-treasury.gov.uk/finance_bill_2013.htm

Draft Clauses — 2013 Bill

204 Meaning of “tax arrangements” and “abusive”

(1) Arrangements are “tax arrangements” if, having regard to all the circumstances, it would be reasonable to conclude that the obtaining of a tax advantage was the main purpose, or one of the main purposes, of the arrangements

204 Cont'd — Non-Exhaustive Definition of “Abusive”

(2) Tax arrangements are “abusive” if they are arrangements the entering into or carrying out of which cannot reasonably be regarded as a reasonable course of action in relation to the relevant tax provisions, having regard to all the circumstances including—

(a) Whether the substantive results of the arrangements are consistent with any principles on which those provisions are based (whether express or implied) and the policy objectives of those provisions,

(b) Whether the means of achieving those results involves one or more contrived or abnormal steps, and

(c) Whether the arrangements are intended to exploit any shortcomings in those provisions.

(3) Where the tax arrangements form part of any other arrangements regard must also be had to those other arrangements



204 Cont'd — Non-Exhaustive Indicators

(4) Each of the following is an example of something which might indicate that tax arrangements are abusive—

- (a) the arrangements result in an amount of income, profits or gains for tax purposes that is significantly less than the amount for economic purposes,
- (b) the arrangements result in deductions or losses of an amount for tax purposes that is significantly greater than the amount for economic purposes, and
- (c) the arrangements result in a claim for the repayment or crediting of tax (including foreign tax) that has not been, and is unlikely to be, paid, but in each case only if it is reasonable to assume that such a result was not the anticipated result when the relevant tax provisions were enacted.