INSTITUTE OF CHARTERED ACCOUNTANTS SCOTLAND (ICAS) - WRITTEN EVIDENCE (DFE0008)

Draft Finance Bill 2020-2021 inquiry

Question 1: How effective are the existing powers of HMRC in tackling promoters and enablers of tax avoidance schemes?

1. The government and HMRC have taken extensive action over the last two decades to tackle tax avoidance – with considerable success. The introduction of DOTAS in 2004 followed by various targeted anti-avoidance rules and the general anti-abuse rule had a significant impact.

2. The professional bodes have also played their part – culminating in the introduction of the revised Professional Conduct in Relation to Taxation (PRCT), which includes Standard 4 on tax planning. The version of PCRT in force since 2017 makes clear that any advice given on tax planning should be in line with the spirit of the legislation and should not seek to exploit loopholes.

3. HMRC's Measuring Tax Gaps 2020 edition (Tax gap estimates for 2018 to 2019) indicates that avoidance only accounts for £1.7 billion (5%) – down from £3.7 billion in 2005 to 2006. Far more is accounted for by criminal attacks (£4.5 billion -14%), evasion (£4.6 billion – 15%) and the hidden economy (£2.6 billion – 9%).

4. However, limited numbers of promoters still promote and sell aggressive tax avoidance schemes – one particularly worrying aspect is the 'mass market' nature of loan schemes, noted by Sir Amyas Morse in his report on the loan charge. These promoters are unlikely to belong to professional bodies and are usually not giving tax advice at all in the normal sense. Instead they promote arrangements to taxpayers who often do not realise that they are being sold tax avoidance arrangements that will be challenged by HMRC. Scheme users, particularly users of loan schemes, often do not (or cannot afford to) take independent advice, so only see the promoter's account of the scheme.

5. It is clear from HMRC's recent consultation document on the new proposals for tackling promoters of tax avoidance that these promoters frequently do not comply with DOTAS and have found ways to sidestep the application of the Promoters of Tax Avoidance Schemes (POTAS) rules and the enablers rules – which were specifically intended to tackle the ongoing marketing and supply of tax avoidance schemes.

Question 2: What has been your experience of the Promoters of Tax Avoidance Schemes (POTAS) rules and the enablers rules in practice?

6. Our direct experience of the rules is limited. As recognised in paragraph 2.9 of the recent HMRC consultation, promoters of tax avoidance are rarely members of professional bodies. ICAS members are required to comply with PCRT, so should not be within the scope of the POTAS rules. PCRT guidance on tax planning also makes clear that it would be difficult to envisage any circumstances in which it would be appropriate to introduce a client to another adviser's planning arrangement, where the other adviser is subject to a monitoring notice within POTAS.

7. HMRC's guidance on the enablers legislation specifically notes that if a person conducts their business in accordance with PCRT and acts wholly within the spirt of the standards for tax planning it is unlikely that they will come within the scope of the legislation.

Question 3: Are HMRC's communications likely to be effective in informing potential scheme users about schemes, and so deter them from participating?

8. To date we do not consider that HMRC's communications have generally been effective in informing potential scheme users and deterring them from participating. HMRC's approach has relied heavily on Spotlights and whilst agents and advisers belonging to the main professional bodies will generally be aware of these (and they are referenced in PCRT) we believe that awareness amongst taxpayers in general is very low. We have made some suggestions for strategies HMRC could adopt, which we discuss in our response to Question 4.

Question 4: How effective will the proposed measures be against those who promote aggressive tax avoidance schemes, and in informing and deterring potential scheme users? What else could HMRC be doing in this area?

9. We broadly support the proposed measures. However, we believe that their effect may be limited because promoters (particularly those based offshore) are likely to continue to make determined efforts to sidestep the regimes.

10. We believe that more could be done by HMRC to deter users from taking up schemes. As noted in our response to Question 3 we do not consider that HMRC's Spotlights have been very effective to date, due to low awareness amongst taxpayers. We have suggested that HMRC could consider more use of social media and mainstream media for campaigns which would make information about schemes more accessible.

11. We also support the development of more targeted approaches by HMRC, to counter information provided by promoters. Many scheme users (particularly those who do not take independent professional advice) have little understanding that the scheme they have been sold is unlikely to work and will be challenged by HMRC.

12. The loan charge review recommended that HMRC should consider enhancing its usage of PAYE real time information (RTI) to communicate directly with taxpayers it suspects may be engaging in tax avoidance and proactively put them on notice of its view. We are aware that HMRC is looking into the development of an avoidance advisory service which would allow taxpayers to seek a view from HMRC on whether the employment arrangements they are considering using are likely to involve avoidance. This is a promising development which (subject to the outcome of a pilot which is currently in progress) we hope can be expanded in future.

13. RTI data helps HMRC to identify possible users of employment related schemes in order to make direct contact. However, HMRC could investigate the use of other data which would allow direct communication about other types of schemes; for example, in the context of SDLT and LBTT we understand that house purchasers are being contacted by firms (who obtain their details from the Land Registry/Registers of Scotland) telling them they have paid too much tax – HMRC could counter this by providing warnings and information about SDLT/LBTT avoidance schemes.

14. As the recent promoters' consultation notes, promoters "*are often deliberately silent in their marketing to taxpayers about the risks of successful challenge by HMRC*". Some advertising by promoters is also actively misleading. HMRC has had some success in tackling this by referring cases to the Advertising Standards Authority. We welcome the fact that HMRC is now working with the ASA to develop a joint enforcement notice covering the advertising of tax avoidance schemes.

15. Imposition of a monitoring notice under the POTAS regime would allow information about the promoter to be published by HMRC and would require the promoter to tell clients that it is a monitored promoter. With appropriate publicity from HMRC this would act as a clear warning to compliant taxpayers and to agents. No monitoring notices have yet been imposed – probably because of promoters sidestepping the regime – but could be helpful in future if the proposed measures allow HMRC to impose monitoring notices.

16. In addition to action by HMRC, we consider that both the Scottish and UK Governments could take action to prevent some employees (particularly lower paid ones) being pushed into disguised remuneration schemes. Government departments and public sector bodies taking on workers could be required either to employ them through the official payroll or,

where employment agencies are used, to ensure that those agencies are not using any type of disguised remuneration scheme. For instance, as part of procurement procedures all government departments and public sector bodies could insist on a written confirmation from employment agencies providing staff that they will not use any disguised remuneration scheme.

Question 5: Are the safeguards being proposed sufficient to ensure an appropriate balance is struck between HMRC and taxpayer?

17. In general, we consider that the safeguards are appropriate, subject to two concerns.

18. Firstly, in the POTAS regime, we do not believe that the addition of DAC 6 arrangements to FA 2014 Schedule 34A (defeated arrangements) is appropriate. Unlike the other provisions referenced (for example GAAR), some of the DAC 6 Hallmarks are very broad (and do not include a 'main benefit' test) so will catch some commercial arrangements where there is no tax avoidance intention.

19. Secondly, the enablers' proposals include changes designed to address issues HMRC has encountered with suspected enablers who claim "that client confidentiality prevented them from voluntarily providing client information without an information notice". Whilst we understand the difficulties, it is important that HMRC appreciates that client confidentiality is a fundamental principle in professional standards and should not be discounted. We accept that it is not HMRC's intention to 'get round' client confidentiality rules but a recent case reported to us demonstrated that some HMRC officers do not respect the importance of client confidentiality. A robust approach from HMRC, to monitoring implementation of the revised powers, will be required.

New tax checks on licence renewal applications

Question 6: Are the proposals for tax checks on licence renewal applications fair and proportionate? How effective is the legislation likely to be, and is any amendment needed?

20. We have no comments on this question; we have not received any feedback from ICAS members on these proposals.

Question 7: What is your view of the principle of conditionality and its use in the tax system?

21. As a general principle we believe that conditionality can be useful in a tax system that relies heavily on voluntary compliance. It can be an effective way of ensuring compliance and is particularly useful where the tax liability arises from a one-off transaction that HMRC or Revenue Scotland may otherwise not be immediately aware of.

22. There is already one area of tax where it is helpful; in Scotland the purchaser of property cannot register ownership of that property with Registers of Scotland without first paying Land and Buildings Transaction Tax.

23. In the context of the draft Finance Bill clauses, conditionality may assist HMRC in identifying those who have been operating in the hidden economy. However, there may be a risk that some of those affected will choose not to renew their licences to avoid the tax check. We have no evidence which would allow us to assess whether this is likely to be a significant issue in any of the sectors covered by the proposals.

Question 8: How do you view the Government's stated intention to extend conditionality to Scotland and Northern Ireland, as well as to other trades?

24. We have no comments on the specific proposal to work with the devolved administrations to extend this measure to Scotland and Northern Ireland, beyond noting that liaison is important when putting in place conditionality, where one of the elements is a reserved matter and the other is devolved (or where both elements are devolved). In the case of the current proposals, notifying HMRC of chargeability to corporation tax is a reserved matter, whereas renewing a private hire licence is devolved. For an unincorporated business, Scottish income tax receipts are devolved, although the tax collection is administered by HMRC.

25. This is part of a wider issue of ensuring that UK tax decisions take account of the consequences for devolved taxes. In our view the UK government and the devolved administrations should work more closely together to develop processes for developing and implementing new tax policies which take account of the overlap between devolved and reserved matters and the possible consequences of UK tax decisions for devolved taxes (and other devolved matters).

Question 9: Could the problems this measure is designed to address have been tackled effectively by other means? If so, what are they?

26. We have no comments on this question.

Amendments to HMRC's civil information powers

Question 10: What is your view of the removal of the requirement to obtain tax tribunal approval before issuing a Financial Institution Notice? Are the safeguards promised instead adequate and, if not, what more should be done?

27. The key driver behind the introduction of the Financial Institution Notice (FIN) is the international standards for exchange of information on request; specifically, HMRC should reply to a request for information from an overseas tax authority within 6 months. Where HMRC has to use a

third party information notice it currently takes, on average, 12 months. Whilst we support HMRC having appropriate information powers to enable it to check tax compliance and to comply with international obligations, we do not believe that what is essentially an administrative and timing problem provides sufficient justification for removing an essential safeguard.

28. If a distinction could be made between overseas and domestic FINs – with the requirement for tribunal approval being retained for domestic FINs but not for FINs arising from requests made by overseas tax authorities – that might be acceptable. However, the response to the 2018 consultation stated that it is not possible to treat overseas requests differently, so the draft legislation removes tribunal approval in all cases. In our view this is unacceptable; taxpayers need to have confidence that HMRC's powers are being exercised proportionately and that an appropriate balance is being struck. In the case of FINs, independent scrutiny by the Tribunal is the only effective taxpayer safeguard to ensure that HMRC is only seeking information that is reasonably required.

29. Approaching a bank or other financial institution for information about a taxpayer, without the taxpayer's agreement, is highly intrusive; there appears to be no recognition of the potential adverse effects on taxpayers of a FIN being issued to their bank. Risk averse institutions might decide to withdraw banking facilities from a customer if they assumed that the issue of the notice indicated wrongdoing. Given the intrusive nature of the proposed FIN, we do not believe that the proposed safeguards are sufficient for domestic cases. No internal HMRC process would be an adequate replacement for the independent scrutiny of the tribunal.

30. The taxpayer will receive a copy of the FIN from HMRC (unless HMRC has obtained tribunal approval to waive this requirement) but does not have any right of appeal. The taxpayer could seek judicial review of the FIN but this is unlikely to be a viable option in most cases because of the time constraints and cost – even if the review succeeded it would be too late to prevent any damage to the taxpayer's relationship with the financial institution.

31. We have reports from members of cases where the relationship between HMRC and the taxpayer has completely broken down. We also understand that far more taxpayer information notices are already being issued, often at an unduly early stage of an enquiry (where the taxpayer and their agent are cooperating) - some of which appear to be inappropriate 'fishing' expeditions on the part of HMRC. In the absence of any requirement to obtain tribunal approval for FINs, we are concerned that HMRC will make increasing use of these in domestic cases – in some cases inappropriately.

Question 11: Is the scope of the new power in terms of the information to be reported to HMRC appropriate and sufficiently clear?

32. We have no comments on this question.

Question 12: How can the need for adequate taxpayer safeguards and timely international exchange of information be balanced? What steps should be taken to ensure that taxpayer safeguards are not treated as dispensable when they make it more difficult to meet other obligations?

33. It is not acceptable to dispense with taxpayer safeguards. If no distinction can be made between overseas and domestic cases, we believe that independent external oversight of FINs should be retained in all cases because it is essential to maintain taxpayer confidence in the tax system and ensure that HMRC exercises its powers proportionately.

34. The administrative and timing problem of responding to overseas information requests within 6 months should be tackled by ensuring that both HMRC and tribunals have adequate resources to allow them to deal with applications in a timely manner.

Notification of uncertain tax treatments by large businesses

The sub-committee welcomes general views on this proposal

35. The proposal will require large businesses to notify HMRC where they have adopted an uncertain tax treatment. The stated intention is to improve HMRC's ability to identify where businesses have adopted a different legal interpretation to HMRC's view and to help to reduce tax losses caused by businesses adopting tax treatments that do not stand up to legal scrutiny.

36. We do not believe that the proposed notification requirement is proportionate or workable in its current form – or that it will achieve the stated aim. It will impose disproportionate additional costs and administrative burdens on the compliant majority of large businesses, due to the subjective and unclear nature of the definition of uncertain tax treatment and the resulting risk of inadvertently failing to notify.

37. As currently proposed, there could apparently be a breach of the notification requirement (and a penalty) even in cases where the courts ultimately uphold the approach adopted. Combined with other aspects of the proposals this will lead to notifications HMRC do not want (and/or multiple requests for confirmation that sufficient information has been disclosed) from compliant businesses erring on the side of caution. This will tie up HMRC resources and the requirement is therefore unlikely to assist HMRC in identifying cases which do require close scrutiny,

particularly as non-compliant businesses will be less likely to make notifications.

38. Feedback from our members working for large corporates, or advising them, indicates that HMRC's Business Risk Review (BRR) process and associated collaborative working with HMRC, mean that these companies already proactively disclose any areas of uncertainty to their Customer Compliance Manager (CCM). Most want to engage constructively with HMRC in real time to address uncertainty – but HMRC resource constraints already mean this is not always possible. We are concerned that the impact of the proposed requirement on HMRC resources could adversely affect collaborative working and make it harder for some large businesses to achieve the real time engagement they would like.

39. HMRC time would be better spent concentrating on the small number of higher-risk businesses which do not want to adopt collaborative working, rather than sifting through disclosures from compliant companies or providing them with confirmations that sufficient information has been disclosed.

40. If the notification requirement is implemented it should therefore be revised to target the minority of large businesses which do not already engage constructively with HMRC. This could be achieved by providing that businesses would only be within the notification regime where they receive a high risk rating under HMRC's BRR process and/or providing that businesses will only be within the regime where HMRC issues a notice or direction.

41. If a more targeted approach is not adopted, it will be essential to change the definition of uncertain tax treatment to something clearer and more objective and to introduce some form of materiality threshold. HMRC should also considerably improve its guidance (to provide clear indications of its views), keep that guidance up to date and make VAT rulings more readily available. The number of taxes in scope should also be reduced to make it easier to devise a workable regime. HMRC will require additional CCM resource to ensure it can operate the regime without reducing its ability to engage with large businesses more generally.

42. As currently proposed one individual would be responsible for making the notification and subject to penalties for any failure to notify; this is not appropriate. Determining the tax treatment to be adopted is the responsibility of the company – not any one individual. In large groups this will involve many people and discussions at different levels of the organisation. The notification requirement should therefore be placed on the company.

Corporate Interest Restriction (CIR) – technical amendments

The sub-committee is interested in views on the impact and appropriateness of proposed retrospective measures in the Finance Bill, in relation to uncertainty within the tax system.

43. The retrospective amendment is a minor technical one, which provides that a reporting company (in the CIR regime) is not liable to a late filing penalty where the company has a reasonable excuse for the failure and the return is submitted as soon as possible once the reasonable excuse ceases. It applies from 1 April 2017 (the date the interest restriction was introduced).

44. As a broad policy principle, we do not agree with retrospection. However, it would normally be the case that penalties for late filing would not be applied where the taxpayer has a reasonable excuse; companies within the CIR regime would have expected this to be the case, in line with the wider corporation tax filing regime. The omission of a reasonable excuse provision from the original legislation was unintended. We believe it is appropriate to correct this mistake to ensure that the regime works as expected and intended.

Tuesday 6th October 2020