CHARTERED INSTITUTE OF TAXATION (CIOT) - WRITTEN EVIDENCE (DFE0017)

Draft Finance Bill 2020-2021 inquiry

1 Introduction

1.1 We are pleased to set out our comments in relation to the Committee's Inquiry into the Draft Finance Bill 2020-21. Our comments supplement the oral evidence provided by Richard Wild on 5 October 2020.

1.2 Rather than answer of each of the specific questions in the call for evidence, in the interests of brevity we have set out our comments under the specific areas within the inquiry. In the footnotes, we have also provided links to our most recent submissions to HMRC in relation to these measures, which provide further detail.

1.3 As an educational charity, our primary purpose is to promote education in taxation. One of the key aims of the CIOT is to work for a better, more efficient, tax system for all affected by it – taxpayers, their advisers and the authorities. Our comments and recommendations on tax issues are made solely in order to achieve this aim; we are a non-party-political organisation.

1.4 Our stated objectives for the tax system include:

- A legislative process which translates policy intentions into statute accurately and effectively, without unintended consequences.
- Greater simplicity and clarity, so people can understand how much tax they should be paying and why.
- Greater certainty, so businesses and individuals can plan ahead with confidence.
- A fair balance between the powers of tax collectors and the rights of taxpayers (both represented and unrepresented).
- Responsive and competent tax administration, with a minimum of bureaucracy.

2 New proposals for tackling promoters and enablers of tax avoidance schemes[1]

2.1 The Government is right to be taking a robust approach to uncooperative and unscrupulous promoters who continue to devise, promote or sell tax avoidance schemes. There should be no place for such people and their schemes in the

[1] https://www.tax.org.uk/sites/default/files/200910%20Tackling%20Promoters%20of%20Tax%20Avoidance%20-%20CIOT%20response.pdf

tax services market.

2.2 We are pleased to see HMRC recognise, both in the consultation document and more widely, the fact that today's promoters are rarely members of professional bodies, and so the extensions being proposed to HMRC's powers are not aimed at advisers adhering to high professional standards. Indeed many – perhaps a majority – of promoters are not tax advisers or tax agents at all, but rather operate in a small number of boutique firms focused mostly or entirely around such avoidance schemes, many of which are known to HMRC.

2.3 HMRC estimate that there are only around 20 to 30 active promoters currently operation, and ideally we favour HMRC targeting their resources on the activities of this small number of promoters and boutiques, rather than introducing new rules which might place additional compliance obligations on tax advisers and tax agents - even if that obligation is limited to ensuring they are not caught by those rules (which has largely been our focus).

2.4 HMRC state that around 20 promoters have left the tax avoidance market since 2014, so this line of attack (alongside other measures) is having success. But we understand that the nature of promoters' behaviour, much of which is set out in HMRC's consultation, means that existing measures can be side-stepped or frustrated. We do wonder, therefore, how successful these legislative measures will be in tackling the 'hard core' promoters who clearly do not wish to play by the rules, and whether they just move the goalposts so that this game of 'cat and mouse' with HMRC will continue.

2.5 Our two main concerns in relation to the proposed measures are:

- Lack of a right of appeal - The government proposes that there should be no right of appeal against the new information notice which forms part of the changes to DOTAS (new s310D FA 2004). We understand why HMRC is trying to limit appeal grounds (to speed up the process), but there must be strong internal governance and review of these notices before they are issued. These notices should only be used in limited and prescribed circumstances, and provisions should ensure that these notices cannot be used in the course of a standard enquiry or intervention.

- Inclusion of 'DAC 6' within the definition of 'defeated arrangements' in the POTAS regime - Under DAC6, persons are required to disclose certain cross-border tax arrangements. These are widely defined and will include many commercial arrangements. Indeed, some hallmarks in DAC6 don't require a tax avoidance motive or a tax advantage at all. We are concerned that DAC6 is to be included within the definition of a defeated arrangement and added to the POTAS threshold conditions, despite previous assurances from HMRC that DAC6 compliance would not creep into other regimes. If there is a desire to link the two then all DAC6 hallmarks that do not require a tax avoidance motive and a tax advantage (eg those that lack a main benefit test) should be excluded from scope of these proposed new rules.

2.6 Quite rightly, and as set out in their 'Promoter Strategy' published in March 2020,[2] this is just one of the steps HMRC are implementing to tackle

avoidance, which include:

- enforcing the legal obligations of promoters;
- targeted and intensive enquiries into promoters, enablers and their business entities – with HMRC doubling its resources dedicated to tackling promoters in 2019-20, and disrupting the supply chain and economics of avoidance schemes;
- using its full range of criminal powers and civil sanctions for those who fraudulently design, promote or market tax avoidance schemes;
- working closely with partner bodies, such as the Advertising Standards Authority to remove misleading advertisements, and the Insolvency Service so they can consider disqualifying directors of companies promoting and facilitating the sale of avoidance schemes;
- running an awareness campaign on tax avoidance and helping taxpayers spot avoidance, targeting sectors where promoters are particularly active;
- making it easy to report tax avoidance schemes and promoters; and
- using real-time information (RTI) and other data, making early contact with taxpayers who are potentially using an avoidance scheme, highlighting the risks and providing advice on how to leave it.

2.7 There are areas where HMRC could go further, such as:

- dealing with the issue of generic Tax Counsels' opinions supporting packaged tax avoidance schemes;
- wider communications around the risks of avoidance and the types of scheme being promoted, using non-tax-technical language – we query how effective HMRC's 'Spotlights' are at reaching end users.
- extending the requirements of Professional Conduct in Relation to Taxation (PCRT) to those parts of the market not subject to it.

3 New tax checks on licence renewal applications[3]

3.1 The CIOT does not condone any form of illegal behaviour, such as tax evasion or operating in the hidden economy. This behaviour continues to represent a significant proportion of the tax gap [hidden economy £2.6bn, evasion £4.6bn] and undermines the honest majority who pay their taxes. Conditionality, if it operates effectively, could help reduce the tax gap.

3.2 However, there is a risk of driving businesses even further into the hidden economy by operating on an unlicensed basis. This measure should be

[2] https://www.gov.uk/government/publications/tackling-promoters-of-mass-marketed-tax-avoidance-schemes
[3] https://www.tax.org.uk/sites/default/files/200910%20Tax%20checks%20on%20licence%20renewal%20applications%20-%20draft%20legislation%20-%20CIOT%20comments_0.pdf

accompanied by education of the public about the importance of using licensed businesses in the first place, as well as ensuring that licensing bodies step up their enforcement activities.

3.3 The proposal comprises two key elements:

- First time applicants – licensing bodies will be required to signpost first time applicants to HMRC guidance about their potential tax obligations, and obtain confirmation that the applicant is aware of the guidance before considering the application.
- Renewals – licensing bodies must, before considering the application, obtain confirmation from HMRC that the application has completed a 'tax check'.

3.4 Whilst the legislation seeks to set out what needs to be done, and when, it is difficult to follow and there is little detail on the 'how'. For example:

- Para 2(2) of the new schedule compels the licensing authority to draw a first time applicant's attention to various guidance specified by HMRC, and obtain confirmation that the applicant is aware of its contents. How will that two-way notification process work?
- Applicants must undertake a tax check within 120 days of a licence renewal. How will they know this, and whose obligation is it to inform them?
- Reference is made in the impact assessment to a 'new digital service'. This will need thorough advance testing before the commencement date of 4 April 2022. New digital systems, and those which span (or indeed are within) government departments are not infallible.
- What provision will be made for an applicant who may be digitally excluded? How will all parties fulfil their obligations?

3.5 Other questions arise, such as:

- If a person fails to register for tax after receiving the notification in para 2(2), will HMRC then automatically treat any subsequent failure to notify HMRC of their chargeability as deliberate for the purposes of penalties. If so then a warning to that effect should be given, including a warning setting out the consequences eg level of penalties.
- There appear to be inadequate safeguards in the event that HMRC's data is incorrect or out of date. Para 7 covers instances where HMRC failures prevent the licensing body from meeting its requirement to obtain confirmation of the completion of a tax check. It should include failures arising from inaccurate or out-of-date data held on HMRC's systems.
- The scope of the tax check includes (in effect) confirmation that the person's tax affairs are up to date. This may not be the case if someone is in the process of bringing their affairs up to date (which can take many months), who should not be denied licences in the meantime.

3.6 If the measure is, as suggested by the impact assessment, 'a simple online service' (with additional support to applicants who need it), then we are generally supportive of the measure. A post-implementation review should be carried out, certainly before extending to other taxes or jurisdictions.

4 Amendments to HMRC's civil information powers[4]

4.1 The CIOT is pleased to note that a number of the proposals that were originally put forward in HMRC's consultation document 'Amending HMRC's Civil Information Powers' are not being developed, particularly Option 1 ('Aligning with Taxpayer Notice') which would have involved removing the requirement to obtain tribunal approval in all cases. We thought this would have gone significantly further than is needed for HMRC to cope more promptly with requests for information from overseas jurisdictions.

4.2 Option 2 ('Financial Information Notice') is being progressed. The driver for change is requests for financial information from overseas tax authorities. If the new FIN was only for international information requests from other tax authorities, then we would be less concerned about the removal of the requirement for HMRC to obtain tribunal approval for issuing third party notices. However, the consultation response explains that HMRC are not able to have a different notice for international requests. UK law, and some international treaties, requires them to obtain information in the same way for both domestic and international requests. Therefore, the FIN will be available for use for both international and domestic requests for information. We are concerned about the loss of independent tribunal oversight, particularly in cases which involve requests for information about UK taxpayers.

4.3 This raises questions about how the new power will operate in practice. For example, it is likely that it will be used to obtain information about UK taxpayers and that HMRC will be using the new FIN for requests for information about UK taxpayers as well (for example during the course of a domestic tax enquiry). Under existing information gathering powers (Schedule 36 FA 2008), HMRC must obtain tribunal approval before requesting information from third parties, unless the taxpayer has given HMRC prior approval. Further, there is a right of appeal if it would be unduly onerous to comply with the notice. A number of aspects will need to be covered in guidance such as:

- Will HMRC approach the taxpayer first, for example, before issuing a FIN in cases involving UK taxpayers?
- Will cases involving domestic enquiries be dealt with differently to international requests for information?
- What type of information will HMRC use the FIN for?
- Will HMRC use the new FIN in domestic cases as a risk-assessing tool, or will

[4] https://www.tax.org.uk/sites/default/files/200910%20Amendments%20to%20HMRC%27s%20Civil%20information%20powers%20-%20draft%20legislation%20-%20CIOT%20comments.pdf

it be reserved for use during tax enquiries?

4.4 The draft legislation suggests that there is to be no right of appeal by the financial institution against the issue of a FIN, even if it would be unduly onerous for it to comply with the notice. Whilst the draft legislation does contain some other safeguards (including that the information must be reasonably required and a notice may only be issued if the information is, in the reasonable opinion of the authorised HMRC officer giving the notice, of a kind that it would not be onerous for the institution to produce or provide), we do not consider that HMRC are best placed to make that assessment.

4.5 Indeed, it appears that the first opportunity that the financial institution will have to appeal is at the point a penalty for non-compliance with the notice is imposed (although we understand that there may be some legal uncertainty over whether it is permissible to argue about the legitimacy of an information notice at a penalty appeal hearing). It is a wholly unsatisfactory position that the financial institution must first be non-compliant with the notice before it potentially has a legal route to argue against the legitimacy of the information notice.

5 New requirements for certain businesses to notify uncertain tax treatments[5]

5.1 Insofar as we understand it, the policy behind this proposal is to place an obligation on taxpayers to inform HMRC of aspects of their tax affairs where the taxpayer's interpretation of the law and how it applies to the facts in a particular case (the tax treatment) differs from HMRC's interpretation. This is the legal interpretation tax gap (defined in paragraph 3.3 of the consultation document). As per paragraph 2.7 of the consultation document: 'The measure aims to ensure that HMRC are aware of all cases where a large business has adopted a treatment with which HMRC may disagree …'

5.2 The proposal lacks clarity, both with regard to the intended outcomes and the practical implementation and impacts. As presented the requirement to notify would leave large businesses in a position of considerable uncertainty about their compliance obligations. We have encouraged the government to revisit the decision to introduce this new requirement and the policy objectives behind it.

5.3 The fundamental building block of the proposal – that is to say what is an 'uncertain tax treatment' that must be notified – is inherently uncertain and unclear on two counts. First, the wholly subjective test devised around the likelihood of an HMRC challenge. Second, the principal exclusion proposed which is intended to ensure that HMRC are not told about 'what they already know'. The lack of coherency around how this interacts with the existing tax

5 https://www.tax.org.uk/sites/default/files/200826%20Notification%20of%20uncertain%20tax%20treatment%20by%20large%20businesses%20-%20CIOT%20response.pdf

system – which already includes (a) many rules around disclosure of specific arrangements (for example DOTAS relating to tax avoidance arrangements), (b) rules relating to full and accurate disclosure in tax returns, (c) procedures for enquiries by HMRC and 'discovery' assessments to deal with issues which come to light at a later date, as well as (d) the collaborative and cooperative compliance procedures such as Business Risk Review - amplifies the flaws in the proposal.

5.4 This is compounded by the fact that a failure to comply would give rise to penalties, which should be reserved for deliberate or careless behaviour and not be applied where a compliance failure arises as a result of uncertainty or a judgement call around reporting obligations.

5.5 Our other criticisms of the proposals include:

- The proposed de minimis threshold of £1m across all taxes is far too low. The concept of materiality should be adopted, with the threshold and materiality set at different levels for different taxes.
- It is estimated to have a negligible impact on the tax gap. The maximum annual revenue increase is just £45m; less than 1% of the legal interpretation tax gap.
- It is intended to cover a wide range of taxes (corporation tax (CT), income tax (including PAYE), VAT, excise and customs duties, insurance premium tax, stamp duty land tax, stamp duty reserve tax, bank levy and petroleum revenue tax), being the taxes and duties currently in scope of the Senior Accounting Officer (SAO) regime. If the proposal is to go ahead, it should start with just one tax – probably CT – though whichever tax forms the greatest element of the legal interpretation tax gap.
- Aligned to the above, the proposed reporting deadlines do not sit comfortably with the relevant tax regimes. For example, the SAO certification is required six or nine months after the relevant company's year-end, whilst the CT return is only required to be filed 12 months after the year end. Uncertain tax treatments are likely to be unknown until very shortly before the point of filing the CT return and, therefore, determining uncertain tax treatment notifications (at least in relation to CT) by reference to the normal CT compliance process seems more appropriate.

5.6 Many of these concerns arise because the government has, without explanation, bypassed Stage 1 of the consultation process ('Setting out objectives and identifying options') and has moved straight to Stage 2 of the consultation process ('Determining the best option and developing a framework for implementation including detailed policy design'). Given the many challenges businesses are currently facing, now is not the time to add to compliance burdens unless these measures can be properly justified. We suggest that instead time could usefully be taken to explore more precisely what it is that the government wishes to achieve, and work collaboratively towards achieving it.

6 Retrospective measures in the Finance Bill

6.1 As a general rule, the CIOT opposes retrospective tax measures. The government has also stated that changes to tax legislation, where the change takes effect from a date earlier than the date of announcement, will be wholly exceptional.

6.2 The draft Finance Bill clauses published on 21 July 2020 include a measure which makes technical amendments to the Corporate Interest Restriction (CIR). This measure has retrospective effect as it backdates to 1 April 2017 (the commencement date of the CIR rules), the defence of reasonable excuse where an interest restriction return is filed late, and a penalty would otherwise arise.

6.3 As recognised in the Explanatory Note to the draft legislation, this was an unintended omission from the original rules, and introduces a safeguard which should have been there all along. In these circumstances, we accept that the measure should have retrospective effect to provide the taxpayer with the intended reasonable excuse defence from the outset of the CIR rules.

6.4 The other measure which potentially has retrospective effect are the changes proposed to the information powers in the enablers of tax avoidance regime, which it is suggested might apply from November 2017, the date the regime started. The changes are designed to make the legislation operate as originally intended to enable HMRC to obtain information from suspected enablers as soon as they become aware of a scheme. We do not think this is an exceptional circumstance, and we consider that the changes should only apply from Royal Assent.

7 Acknowledgement of submission

7.1 We would be grateful if you could acknowledge safe receipt of this submission, and ensure that the Chartered Institute of Taxation is included in the List of Respondents when any outcome of the inquiry is published.

8 The Chartered Institute of Taxation

8.1 The Chartered Institute of Taxation (CIOT) is the leading professional body in the United Kingdom concerned solely with taxation. The CIOT is an educational charity, promoting education and study of the administration and practice of taxation. One of our key aims is to work for a better, more efficient, tax system for all affected by it – taxpayers, their advisers and the authorities. The CIOT's work covers all aspects of taxation, including direct and indirect taxes and duties. Through our Low Incomes Tax Reform Group (LITRG), the CIOT has a particular focus on improving the tax system, including tax credits and

benefits, for the unrepresented taxpayer.

The CIOT draws on our members' experience in private practice, commerce and industry, government and academia to improve tax administration and propose and explain how tax policy objectives can most effectively be achieved. We also link to, and draw on, similar leading professional tax bodies in other countries. The CIOT's comments and recommendations on tax issues are made in line with our charitable objectives: we are politically neutral in our work.

The CIOT's 19,000 members have the practising title of 'Chartered Tax Adviser' and the designatory letters 'CTA', to represent the leading tax qualification.

7th October 2020