CONFEDERATION OF BRITISH INDUSTRY (CBI) – WRITTEN EVIDENCE
Draft Finance Bill 2020-2021 inquiry

1. Background

1.1. As the UK's leading business organisation, the CBI speaks for some 190,000 businesses that together employ around a third of the private sector workforce, covering the full spectrum of business interests both by sector and by size.

1.2. We welcome the opportunity to submit evidence for the Sub-committee's inquiry and will be commenting on the notification of uncertain tax treatments consultation as a priority. We have also attached out responses to the notification of uncertain tax treatments consultation as an appendix.

2. Introduction

2.1. Whilst the CBI welcomes any proposal that seeks to strengthens HMRC's ability to seek out and change the behaviours of those involved in the promoting and enabling of tax avoidance schemes, we consider it of paramount importance that any measures are appropriately targeted, proportionate and practical to apply.

2.2. Our members are very concerned in particular with the scope of the current proposal which, if not withdrawn or modified significantly, will represent a significant and disproportionate compliance burden for large businesses, the majority of whom HMRC acknowledge are within the "compliant majority".

2.3. We believe that any new measures should be considered in light of the existing tax compliance frameworks to ensure they do not duplicate/overlap with the already extensive existing requirements, DOTAS, DAC6 SAO and IMOC to name a few. HMRC notes that some taxpayers will be familiar with the notification of uncertain corporate tax positions regimes operated in the USA and Australia; we would note that the notification regime pre-dated the Cooperative Compliance regime in Australia (and indeed the USA does not have a similar cooperative compliance regime), while the UK's recent introduction of the Framework for Co-operative Compliance (Framework), is clear in its expectations of large businesses/banks in relation to transparency over significant tax risks and uncertainties. For example, the Framework requires discussion (and therefore disclosure) in relation to "significant risks" and "transactions with significant tax implications". HMRC should consider this apparent duplication as part of any implementation of the proposals.

2.4. Parliament should instead introduce legislation designed to specifically target the minority of Large Business customers who continue to use aggressive tax planning, rather than introduce a broad disclosure regime

which will impact, and have compliance costs for, all businesses at a time when the UK should instead be focussing on recovery and growth.

3. Notification of Uncertain Tax Treatments by large businesses

3.1. The proposal seems to be aimed at closing the "legal interpretation" part of the overall tax gap, and yet there is no clear explanation, either in the recent Uncertain Tax Treatments Consultation Document or in HMRC's tax gap publications, of how the figures for the legal interpretation tax gap are arrived at.

3.2. The significant variations in the figures imply a lack of robustness in the estimates. We note that the £6.2bn referred to in 2.2[1] of the ConDoc has since been revised down to £5.4bn and the figure for 2020 is £4.9bn. 1.2[2] of the ConDoc indicates that the gap relates to situations where business adopt tax treatments that do not stand up to legal scrutiny; so our assumption is that the tax gap relating to legal interpretation must relate to positions taken by taxpayers that wouldn't stand up to legal scrutiny but that HMRC are unaware of. It would be helpful if this were confirmed and, if so, how the estimates have been arrived at.

Scope of the proposals

3.3. The purpose of the proposal is stated as being to "improve HMRC's ability to identify issues where businesses have adopted a different legal interpretation to HMRC's view. This requirement will help to reduce tax losses caused by businesses adopting tax treatments that do not stand up to legal scrutiny" (paragraph 1.2). The document then goes on to define "legal interpretation" at paragraph 3.3[3] of the consultation document, which understandably refers to different interpretations of legislation, case law and guidelines, however then provides examples which are not examples of legal interpretation differences, such as the accounting treatment of a transaction, or a methodology used for transfer pricing or VAT partial exemption purposes. In addition, we are also aware that some of our members understand that HMRC has indicated that a key target of this proposal from their perspective is a small minority of Large Business customers whom HMRC view as perpetually non-compliant.

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1 "The legal interpretation tax gap (defined in Chapter 3) in the 2019 edition of 'Measuring tax gaps' is £6.2bn (18% of the overall tax gap). Although not exclusive to large business, the majority of the legal interpretation tax gap is attributable to that customer group."

2 "The proposal is designed to improve HMRC's ability to identify issues where businesses have adopted a different legal interpretation to HMRC's view. This requirement will help to reduce tax losses caused by businesses adopting tax treatments that do not stand up to legal scrutiny."

3 'Legal interpretation' 6 is defined as: "Legal interpretation losses arise where the customer's and HMRC's interpretation of the law and how it applies to the facts in a particular case result in a different tax outcome, and there is no avoidance. Specifically, this includes the interpretation of legislation, case-law, or guidelines relating to the application of legislation or case-law. Examples include categorisation such as an asset for allowances or VAT liability of a supply, the accounting treatment of a transaction, or the methodology used to calculate the amount of tax due as in transfer pricing, or VAT partial exemption."

3.4. Our concern is that the approach to disclosure should be very different depending on the precise target of the proposals and we consider that this should be clarified as a crucial first step. This will be critical to ensuring the disclosure regime is fit-for-purpose and does not unnecessarily increase compliance requirements for businesses who are not the target of the proposals (and as a result, reduce the usefulness of the disclosures for HMRC).

Meaning of uncertain tax treatment

3.5. Defining an uncertain tax treatment as "one where the business believes that HMRC may not agree with their interpretation of the legislation, case law or guidance" is excessively vague and would result in taxpayers having to second guess the approach HMRC may take on a whole range of issues.

3.6. While aligning the financial thresholds for determining which taxpayers would be subject to a UTTs disclosure regime to those in the Senior Accounting Officer (SAO) and Publication of Tax Strategies (PoTS) regimes, as suggested in HMRC's proposal, seems to appropriately target large businesses, applying the regime to all taxes currently in scope of the SAO regime seems excessively broad.

3.7. We would encourage HMRC to either reduce the scope of the proposal to corporation tax (which would align the compliance requirements to work undertaken as part of existing financial reporting processes) or, if there is a desire to apply the notification requirement beyond corporation tax, we would encourage HMRC to consider carefully which of the more material taxes contributing to the "legal interpretation tax gap" it would be appropriate to include in the scope of the notification requirement, while not creating an undue compliance burden for the majority of compliant businesses.

Reporting threshold

3.8. It is currently proposed that UTTs which, individually or combined (depending on whether, using the principles set out in IFRIC23, the entity considers tax treatments separately or on a combined basis), amount to a tax outcome of greater than £1m will be notifiable. Setting the threshold in this way presents several challenges to large businesses.

3.9. Where a large business views UTTs on a combined basis, the proposal would seem to reduce the materiality threshold such that, for example, ten issues with a tax outcome of £100,000 each would be reportable. We would expect that many large businesses would view UTTs on such a combined basis such that reporting of individual issues down to such a low level of materiality would be unnecessarily burdensome and provide less meaningful information on UTTs to HMRC.

3.10. We would suggest that an approach which employs a suitable, flexible, materiality threshold, along the lines of that adopted by the Australian Tax Office, would be more appropriate, and that this should be applied on a separate UTT by UTT basis (rather than on a combined basis) to better allow HMRC to identify higher risk UTTs.

Requirement to notify

3.11. We would note that the quantification requirement proposed would be unique globally and goes far beyond the requirements of the regimes in the US and Australia, where the entry condition to the rules is a question of materiality or accounts treatment, but where no quantification is required. Given the difficulty with quantification as noted below, we would encourage HMRC to revisit this aspect of the proposal.

3.12. UTTs and their appraisal may arise as a result of tax advice received which is subject to Legal Privilege. The interaction between the notification requirements in the current proposal and Legal Privilege must be addressed to ensure HMRC is not unacceptably restricting taxpayers rights.

Final Comments

3.13. As noted above, we understand from discussions HMRC has had subsequent to the publication of the consultation document that a key target of this proposal is the continued aggressive, and often undisclosed, tax planning activity undertaken by a minority of Large Business customers.

3.14. It is vital to take into account that it is indeed Parliament's role to set the law (preferably with clear policy and intent) and the Courts' role to uncover, in cases of disagreement, what Parliament's intention in setting that law was – in other words, the meaning of the law in any particular case. Neither business nor HMRC are final arbiter in this regard and therefore, to implement a regime whereby business is required to guess the mind of HMRC, as to what they may or may not believe the mind of Parliament to have been when making the law, is in our view a highly uncertain exercise which will be fraught with disagreement, inefficiency and error. Given additionally that HMRC guidance has no force of law and HMRC are clear that they are free to depart from it in many cases, this is of no assistance to the taxpayer. The result of these points is, in short, likely to be no improvement on the current situation, including from HMRC's perspective, but nonetheless will entail a concomitantly large increase in compliance time and expense on both sides. This does not seem to be a viable or desirable outcome for any of the interested parties.

4. Appendix: Consultation question responses

Q1 Do you think the suggested threshold criteria are suitable for the requirement to notify?

4.1. In short, yes. However, the consultation refers to both the SAO and tax strategy thresholds which differ slightly. This may cause confusion as to which thresholds apply and must be clarified in any legislation.

Q2 Do you think that there are any other areas which should be excluded from the notification regime?

4.2. Yes, the area of pre-transaction clearance should be widened, particularly also by the use/ acceptance of unilateral APAs as an instrument to confirm the tax treatment in the UK more quickly. We do not understand why in 2.16, there will be no formal exception for instances where a UTT has been the subject of a clearance request to HMRC. Further, any case where the tax treatment has already been the subject of discussion or other notification to HMRC (for example, white-space disclosure on a tax return) should be considered for exclusion – we elaborate further below.

4.3. In addition, it is noted that there will be significant difficulties in determining whether to exclude UTT's that are part of an ongoing compliance review and more clarity is needed when defining "formal discussions" in point 2.14. For example, does formal discussion include formal audit enquiries and regular meetings with HMRC where topics are discussed and minuted, or not?

4.4. Notification should not be required where the taxpayer applies an interpretation that HMRC has accepted, or even taken itself, in relation to the same or a different taxpayer). Similarly where a position has been outlined to a group's CCM it should not need to be notified in this regime. This is on the basis that the assessment of likelihood of HMRC challenge will be impacted by this.

4.5. An additional point of concern in the proposals is the lack of any grandfathering provisions. Absent these, the first year of introduction would require an impracticable retrospective assessment of all positions that might still be having tax effects. Consider the example of a large retailer with thousands of product lines – it would be required to reassess each of these individually to determine whether the currently adopted tax treatment (particularly VAT treatment) might be something that HMRC could disagree with. This is simply unfeasible, and it is therefore essential that whatever proposals are finally brought forward include effective grandfathering provisions, such that only positions adopted after the provisions take effect are reportable.

Q3 Do you think the definition and principles in IFRIC23 are appropriate to be used for the requirement to notify?

4.6. The principles of IFRIC23 only apply to businesses adopting IFRS or FRS 101 in some cases. Many large businesses /entities use FRS 102 and therefore there are differing levels of base alignment. IFRISC23 may be a logical starting point, however, it currently only applies to corporate income taxes and not other taxes such as VAT and Income tax. If this scope is to be significantly broadened, a great deal of additional work would need to be done along with the consideration of alternatives.

4.7. Further clarity on what a UTT is would also need to be provided. Under IFRIC23 the requirement is that an assessment is made on whether it is probable the tax authority (including court) would accept an uncertain tax treatment. It looks to the ultimate outcome, and not solely the likelihood of a HMRC challenge. The consultation remarks however guide us towards a

separate and distinct circumstance where it is likely that HMRC might take a different view. Businesses are unable to determine what HMRC is 'likely' to challenge and to further compound this issue, some HMRC interpretations are ultimately unsuccessful.

4.8. HMRC should consider reducing the scope of the proposal to corporation tax, which would align to work undertaken as part of existing financial reporting processes, or if there is a desire to apply the notification requirement beyond CT, should consider carefully which of the more material taxes contributing to the 'legal interpretation gap' it would be appropriate to include whilst not creating an undue compliance burden

Q5. Do you think the proposed de minimis threshold of £1m is reasonable for the notification of uncertain tax treatment?

4.9. There is a definite need to assess the impact of a large volume of smaller value interactions which cumulatively breach the de minimis threshold, however the current proposals miss this point, as many businesses which would not fall into the regime under any other circumstance, would have uncertain tax transactions with £1m at stake. For many large businesses, the viewing of UTT's on such a combined basis, such that reporting of individual issues results in the capturing of transactions down to low levels of materiality, would create unnecessary burden and provide little meaningful information to HMRC on uncertain tax treatments.

4.10. There is also a question on time period, does the threshold apply per issue or is it an entity aggregation for each tax. An approach which mirrors that of the Australian tax office's, which employs a suitable flexible materiality threshold, would be more appropriate, and this should be applied to separate UTT's by UTT basis, rather than on a combined basis.

Q6. Do you believe there are strong arguments for a materiality threshold?

4.11. If the calculation period could be retrospective, then a materiality threshold would be required.

Q7. Do you envisage problems determining the £1m threshold for indirect taxes, particular VAT?

4.12. Care needs to be taken in defining the £1m threshold. With VAT in particular, the netting of input VAT and output VAT may mean that there is no incremental tax payable. Reporting in this case should be on net tax payable rather than gross basis.

Q9. Do you consider that it would be beneficial to supplement the main requirement with a specific list of indicators of uncertainty?

4.13. In practice a 'list' may be unworkable as in some cases, particularly within the scope of VAT, a new product may be VAT exempt rather than taxable. This treatment may not be considered to be an uncertain one by a business,

however, HMRC may later take a different stance. Clearly, this creates great uncertainty for business, with the associated impacts on both business and HMRC as discussed earlier. Additionally to this is the point, also raised earlier, that HMRC Guidance is simply no substitute for clarity in legislation, for the very reason that HMRC may, at any point, change its mind. . It is for these primary reasons that focus should be kept on narrowing the scope of law rather than utilising guidance for this purpose. If guidance must be used, we suggest that the law for the regime creates a statutory legitimate expectation that any business following the relevant version of the guidance in force at the time it took the tax position in question, can rely on that or any later version of the guidance.

Q11 Do you think the SAO certification process is appropriate for the notification requirement

4.14. The SAO is responsible for financial accounting arrangements, and a tax reporting regime that sits outside of those responsibilities should not be part of the SAO regime. The company should be accountable for notification and reporting in the same way that it is for the completeness and accuracy of its tax return.

4.15. The intention here is to reduce additional compliance burdens by combining both notifications however this requires further thought. Taking corporation tax compliance processes as an example. The SAO certification is typically required 6/9 months after the relevant company's year-end whilst the corporation tax return is only required to be filed 12 months after the relevant company's year end. It may therefore be the case that uncertain tax treatments are unknown until the point of filing the corporation tax return and therefore aligning uncertain tax treatment notifications with the normal compliance process seems more appropriate. This would avoid extending SAO responsibilities into particularly judgmental tax areas and unnecessarily increasing SAO's compliance burdens.

Q12 Would reporting VAT and PAYE issues occurring in the tax year, rather than in the accounting period for the company cause any significant difficulties?

4.16. The reporting requirement should be driven by the company's tax returns. Until a company has submitted its return, there can be no UTT. The same principle applies to VAT and other taxes.

4.17. Looking at VAT in more detail, there is a concern that the requirement to notify in instances where transactions arise at short notice and need to be executed swiftly for commercial reasons, will be challenging. Quite often there can be more than one view of the tax treatment and each transaction may be highly fact specific. The typical values of such transactions would immediately bring them into scope and cause businesses further administrative burdens and uncertainty. Reporting in the year after relevant transactions have been undertaken would make the reporting requirement more manageable.

Q16 Do you think there are any common disputes, that due to the complex nature of such disputes, where specific documents or information should be provided alongside the notification?

4.18. The nature of uncertain tax treatments is such that it is unlikely that there will be commonality due to a diverse group of facts and circumstances. The disclosure should contain a concise description and any associated amounts. HMRC should then request any additional documentation or evidence (to the extent that they are entitled to) on a case by case basis.

Q18 Regarding the penalty in 6.3.2, who do you think should be liable to a penalty, the person liable to notify or the entity, and, if more than one (legal) person, in what circumstances, and to what quantum, would these persons be culpable/liable?

4.19. Unless uncertainty is clearly defined, the imposition of penalties for failure to notify is deeply troubling. Penalising an individual should be reserved for deliberate failure to disclose as opposed to a failure based on an oversight/ uncertainty around obligations. A better alternative is that the liability should fall upon the entity, but again, the penalty regime must account for the fact that, if uncertainty is not clearly defined, many innocent mistakes are likely to occur.

22nd October 2020