



HM TREASURY



HM Revenue
& Customs

Tackling tax avoidance

March 2011



HM TREASURY



HM Revenue
& Customs

Tackling tax avoidance

March 2011

Printed on paper containing 75% recycled fibre content minimum.

If using an electronic version of the document, please consider the environment and only print the pages which you need and recycle them when you have finished.

© Crown copyright 2011

You may re-use this information (not including logos) free of charge in any format or medium, under the terms of the Open Government Licence. To view this licence, visit <http://www.nationalarchives.gov.uk/doc/open-government-licence/> or write to the Information Policy Team, The National Archives, Kew, London TW9 4DU, or e-mail: psi@nationalarchives.gsi.gov.uk.

ISBN 978-1-84532-854-2
PU1157

Contents

	Page
Foreword	3
Executive summary	5
Chapter 1 The strategic approach in practice	7
Chapter 2 Tackling avoidance at the root	9
Chapter 3 Tackling avoidance through challenge and litigation	13
Chapter 4 Protocol on unscheduled announcement of changes to tax law	17
Annex A Protocol consultation responses	21

Foreword

This Government has taken early action to ensure that the UK is seen as a good place to do business. We have set out our Corporate Tax Road Map, we are reforming the Controlled Foreign Companies regime and we are tackling complexity in the tax system. We have committed to improving predictability and stability through our new tax policy making process – with the emphasis on clear policy objectives, transparency and consultation. Business has welcomed our commitment to a new way of doing things.

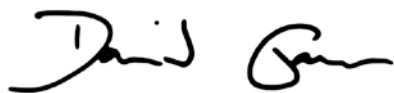
But I want to be clear that being open for business does not mean being open to tax avoidance. We are committed to creating the right tax environment for business and individuals, which encourages enterprise and minimises red tape. In return we expect everyone to pay their fair share. And where we see tax avoidance, we will crack down on it. That's particularly important at a time when the Government has had to make tough choices elsewhere.

We inherited a tax system with a 'tax gap' of around £40 billion. More than a sixth of that is due to tax evasion – that is, illegally understating tax liabilities. But a further one sixth is estimated to be due to tax avoidance – that is, reducing tax liabilities by using the tax law to get a tax advantage that Parliament never intended. And the problem is a persistent one – only this month, we have moved to close down an avoidance scheme using contrived, circular transactions claimed to generate tax relief twice for effectively the same expense.

Clearly, there is a problem we need to tackle and we are committed to tackling it differently from our predecessors. That means a more strategic approach that gets to the root of the problem, rather than treating the symptoms. This Budget unveils an ambitious package of measures to help us do that - including a new anti-avoidance strategy, the first announcements of reviews in high risk areas of the tax system, options to reduce the cash flow advantage from using avoidance schemes and targeted responses to specific avoidance risks. And to reinforce our commitment to improving stability, we are also setting out the principles we will use to decide when to announce unscheduled tax changes.

This document reports real progress in making our new strategic approach to avoidance a reality. It also reports on Her Majesty's Revenue and Customs (HMRC) challenge to avoidance risks on the ground through its compliance activities. We have underlined our commitment to HMRC with our investment of over £900 million in the Spending Review, which should bring in around £7 billion per year in additional revenue by 2014-15.

So we are tackling avoidance on all fronts. And we fully intend to keep up that pressure, to protect the Exchequer and maintain fairness in the tax system.



David Gauke MP

Exchequer Secretary to the Treasury

Executive summary

Tax avoidance represents a significant part of the UK tax gap. Unlike evasion, it is not in itself illegal, but it involves using the tax law to get a tax advantage that Parliament never intended. It frequently involves contrived, artificial transactions that serve little or no purpose other than to reduce tax liability. And it enables some taxpayers to gain an unfair advantage, undermining confidence in the tax system.

To get to grips with this problem, but in a way that does not undermine its commitment to improving the predictability and stability of the tax system, the Government launched its new strategic approach to tackling avoidance in June 2010, as part of the consultation document on tax policy making (*Tax policy making – a new approach*). The key elements of this new approach are:

- making the most of opportunities to make the tax system more watertight against avoidance, for example, as part of wider policy reform;
- reviewing areas of the tax system that have been under repeated avoidance attack, to get to the heart of the problem and develop sustainable solutions; and
- creating new generic defences against avoidance, going beyond closing identified avoidance loopholes, including considering the case for a General Anti-Avoidance Rule (GAAR).

When it is still necessary to close off specific avoidance opportunities, the Government will balance the need to change tax law against its commitment to improve stability.

Budget 2011 marks a significant advance in making the new approach a reality, as the following chapters show.

Chapter 1 introduces **HMRC's new anti-avoidance strategy**, showing how HMRC's activities will put the Government's approach into practice. It focuses on three core elements:

- preventing avoidance at the outset where possible;
- detecting it early where it persists; and
- countering it effectively through challenge by HMRC.

The HMRC strategy provides a coherent framework for all the strands of HMRC's anti-avoidance activity that together help ensure that avoidance is tackled robustly.

Chapter 2 describes action to **strengthen defences in legislation**. The Government is launching two new pieces of work.

First, as indicated in December 2010, this Budget announces new reviews of high risk areas of the tax code. These are areas that have seen repeated avoidance attack or have needed frequent amendment over recent years to close loopholes. Two areas are singled out for a complete review, starting this summer, which will draw on consultation with external interested parties to shape proposals for improving strategic defences in those areas. Later Budgets will announce further areas for review as part of a rolling programme.

Second, the Government will consult this summer on proposals to remove the cash flow advantage that tax avoiders can get by using high risk avoidance schemes. At present, a minority exploit the cash flow advantage of retaining tax during a dispute over liability, in some cases, even where the Courts have already ruled against similar transactions. The Government is

determined to address this systemic advantage to reduce the appeal of participating in high risk avoidance. Consultation will ensure that changes are properly targeted.

Chapter 3 reports progress on **HMRC's operational activities in support of the new strategic approach** to avoidance. Where opportunities for avoidance persist, HMRC will work to identify it early, using the enhanced rules requiring promoters to disclose tax avoidance schemes to HMRC and other sources of information. Based on a robust assessment of risk, HMRC will investigate cases of potential avoidance, tailoring its approach according to the characteristics of different taxpayer groups. The focus is particularly on large business cases and the wealthy, where the immediate tax at risk is greatest. HMRC aims to resolve any disputes with customers as quickly as possible, but, if necessary, will take them through to litigation.

Finally, Chapter 4 publishes **the Government's Protocol on unscheduled announcements** of tax changes. This reinforces the Government's commitment to improve the stability of the tax system, at the same time as allowing decisive action when risks to the Exchequer are identified. The Protocol provides a set of criteria that Ministers will observe when deciding whether to announce a change to tax law that has immediate effect. The Protocol reflects views from consultation on a draft text published in December 2010 and the Forum of Tax Professionals will monitor how the Protocol is applied in practice.

1

The strategic approach in practice

1.1 HMRC's latest estimate of the tax gap (for 2008-09) is £42 billion.¹ Avoidance by using the tax law to get a tax advantage that Parliament never intended is estimated to account for 17.5 per cent of the overall tax gap. Others have suggested that both the overall tax gap and the amount attributable to avoidance are a lot higher. The Government believes that those higher estimates are based on flawed methodology. Calculating the tax gap is not an exact science, but HMRC's estimates are based on detailed taxpayer information, are in line with international comparators and make allowance for use of tax reliefs as intended by Parliament. What is clear, even allowing for a degree of caution about the estimates, is that tax avoidance is one of the biggest elements of the tax gap and needs to be tackled.

1.2 To illustrate the problem of avoidance in practice, two recent examples show its persistence and range:

- in the first example, a highly artificial scheme was disclosed to HMRC aiming at generating artificial tax deductions for individuals. The scheme involved contrived employment arrangements under which the individual deliberately triggered a payment of damages and claimed a tax deduction. In reality, the individual had not suffered a financial loss; and
- in the second example, HMRC became aware of a widely marketed and implemented scheme whereby large businesses entered into contrived, circular transactions over a period of three or four weeks involving leased plant and machinery. The aim was to claim tax relief twice on one amount of expenditure.

Both schemes were closed down by changes in legislation.

1.3 Tax avoidance is not a new problem. But this Government has made clear that it proposes a new approach to tackling it, putting the emphasis on strategic measures. In that way, avoidance can be tackled effectively without undermining predictability and stability in the tax system. Work to improve the robustness of policy and legislation for the longer term is complemented by targeted measures to tackle specific risks in the short term and effective challenge by HMRC.

1.4 HMRC supports all the elements of the Government's strategic approach to tackling avoidance. Its **new anti-avoidance strategy** shows how HMRC will focus its work on implementing the Government's new approach. The strategy provides a coherent framework for HMRC's activities under three core elements:

- preventing avoidance at the outset where possible;
- detecting it early where it persists; and
- countering it effectively through legislative change or challenge by HMRC.

¹ *Measuring Tax Gaps 2010*, an Official Statistics release, 16 September 2010. Available on HMRC website at <http://www.hmrc.gov.uk/stats/measuring-tax-gaps-2010.htm.pdf>

1.5 This reflects HMRC's wider corporate strategy of tailoring its approach to different groups of taxpayers according to their needs and risk profile. HMRC will use the anti-avoidance strategy as a basis for decisions on priorities and allocation of resource and to enable the right decisions to be made about how to respond to avoidance risk. Chapter 3 provides more detail of the detection, investigation and litigation work HMRC undertakes to tackle avoidance risks on the ground.

Figure 1.A: HMRC's anti-avoidance strategy

	We will	We are
Prevention	minimise opportunities for avoidance through policy design and effective legislation	developing strategic defences against avoidance, including 'principles based' legislation where appropriate
	engage with our customers to provide certainty on our approach and to influence avoidance behaviours	responding rapidly and proportionately where our legislation is vulnerable
Detection	identify, analyse and respond promptly to avoidance risks	risk assessing new legislation and rigorously testing it where appropriate
	prioritise our resource on the most significant risks	raising awareness of the risks and costs of avoidance activity
Counteraction	challenge avoidance through project managed enquiries that are cost-effective and consistent	working with intermediaries to promote voluntary disclosure and compliance
	engage in litigation where that is the most appropriate solution, after considering alternative options	improving the clarity of our guidance material
		building relationships with our largest and most complex businesses and our high net worth customers based on transparency and 'real time' resolution to encourage them to adopt lower risk tax strategies
		maintaining the effectiveness of the rules on disclosing avoidance schemes (DOTAS)
		optimising our use of avoidance intelligence through DOTAS and other sources
		ensuring that our response to our customers is proportionate to risk
		maintaining a dynamic picture of avoidance risk, with a clear focus on resourcing the highest risks to revenue and regimes
		programme managing interventions across technical themes with clear internal governance, transparency and accountability
		exploring options for collaborative dispute resolution
		resolving cases in accordance with our Litigation and Settlement Strategy

2

Tackling avoidance at the root

2.1 The best way to protect the Exchequer from avoidance, provide certainty for taxpayers and simplify the tax system is to eliminate avoidance opportunities at the outset, rather than tackling risks once they have materialised. That is at the heart of the Government's new strategic approach. Wherever possible, this Government will prioritise robust design of policy and legislation, underpinned by clearly stated policy objectives. The aim is to maximise prevention of avoidance, reducing the need for immediate changes to legislation once an avoidance risk has arisen, or for HMRC to challenge avoidance once it has happened. This chapter outlines progress with strengthening defences in tax legislation.

2.2 The June 2010 tax policy making document identified two key elements of the new strategic approach to tackling avoidance: ¹

- identifying new generic defences against avoidance, including considering the case for a General Anti-Avoidance Rule (GAAR); and
- reviewing areas of the tax system that have seen repeated avoidance attack with a view to developing sustainable solutions.

2.3 This chapter sets out four strands of work on legislative defences:

- a new proposal to reduce the cash flow benefits that taxpayers can gain from using high risk avoidance schemes;
- a new rolling programme of reviews on high risk areas of the tax code;
- work in hand on a GAAR; and
- the targeted tax measures that sit alongside this strategic work to address specific avoidance risks that have emerged.

High risk avoidance schemes

2.4 There is a market for tax avoidance schemes, even where HMRC believes they do not deliver the advertised tax advantages – comprising both promoters willing to sell them and taxpayers willing to buy. Some taxpayers are prepared to enter into high risk schemes to exploit a cash flow advantage of retaining tax whilst continuing to dispute a liability, in some cases even where the courts have ruled against similar transactions. This advantage results from tax and interest only becoming payable under some tax regimes once HMRC has proven each use of a scheme to fail.

2.5 The Government intends to address this behaviour by the minority by removing the cash flow advantage of using such avoidance schemes. It will bring forward proposals to list specific schemes in regulations, with a range of options to ensure that users of the listed schemes do not benefit from retaining the tax in dispute. Users of schemes will be encouraged to pay the disputed tax earlier than is currently required or will face an additional charge for late payment of the tax when it is found to be due.

¹ *Tax policy making: a new approach*, HM Treasury and HMRC, June 2010

2.6 The schemes proposed for listing will be subject to Parliamentary scrutiny to ensure schemes are only listed where there is a strong case for doing so, including independent advice to support HMRC's assessment of the strength of its arguments. The proposed additional charge will be expected to remove any cash flow advantages from using the scheme.

2.7 A consultation document on these proposals will be published in May 2011 with a view to developing legislation for inclusion in Finance Bill 2012, in accordance with the new approach to tax policy making.²

Programme of reviews of high risk areas

2.8 This Budget announces the first reviews in the programme of work to strengthen the legislative framework in areas of the tax code that have repeatedly been subject to avoidance attack. These will comprise complete reviews which will draw on consultation with external interested parties to shape proposals for improving strategic defences in those areas. There will be a rolling programme of work, identifying the areas of greatest risk where policy reform is not already providing the opportunity for review.

2.9 The first two areas to be considered are:

Income tax losses

2.10 Reliefs for income tax losses, particularly where losses can be used to reduce tax due on other income of the same or a previous year, have frequently been exploited as a mechanism for tax avoidance. The legislation for the reliefs has frequently been changed to close off avoidance opportunities, but schemes exploiting these reliefs continue to be marketed and used. The review will examine how the underlying policy objectives for the relief can be maintained whilst ensuring that it is effectively targeted on those who were meant to benefit from it.

Unauthorised Unit Trusts

2.11 The legislation governing Unauthorised Unit Trusts is complex and such trusts are used by companies to create tax advantages. The review of the legislation will aim to ensure that commercial use of these structures is not disadvantaged, whilst minimising the scope to use them for avoidance. It will also cover the mechanics of the legislation which currently imposes burdens on both commercial users of Unauthorised Unit Trusts and HMRC.

Timing

2.12 The reviews will be carried out in accordance with the new approach to tax policy making, with consultation on both the approach to tackling avoidance risk and the detailed legislation to effect any change.

² As above.; *Tax policy making: a new approach*, HM Treasury and HMRC, June 2010; *The new approach to tax policy making: a response to the consultation*, HM Treasury and HMRC, December 2010

Table 2.A: Timetable for programme of reviews of high risk areas

Summer 2011	• Publish consultation paper on income tax losses • Publish consultation paper on Unauthorised Unit Trusts
Budget 2012	• Interim announcement on progress • Announce new reviews of high risk areas
Autumn 2012	• Publish draft legislation on income tax losses • Publish draft legislation on Unauthorised Unit Trusts
Finance Bill 2013	• Introduce legislation on income tax losses • Introduce legislation on Unauthorised Unit Trusts

Future reviews

2.13 Subsequent Budgets will announce further areas for review. HM Treasury and HMRC would welcome suggestions from interested parties for areas of the tax code that may be candidates for review under this programme. HMRC will also invite input through its regular engagement with businesses and representative bodies.

General Anti-Avoidance Rule (GAAR)

2.14 The Government announced in December 2010 that a study group led by Graham Aaronson QC would be set up to explore the case for a GAAR in the UK.³ Graham Aaronson's study group will consider the scope and design of a GAAR capable of meeting the following objectives:

- providing the Government with an effective means of deterring and countering tax avoidance;
- ensuring that the rules work fairly and would not erode the UK tax regime's attractiveness to business;
- ensuring that certainty about the tax treatment of transactions could be provided without undue compliance costs for businesses and individuals; and
- keeping any increase in resource costs for HMRC to an acceptable level and ensuring that there would be a minimal need for resource to be diverted from other priorities.

2.15 The terms of reference were published on 6 December 2010.⁴ The study group will complete its work by 31 October 2011 and will report its conclusions to the Exchequer Secretary. The Government has committed to further, formal consultation if the proposal is taken forward.

Specific anti-avoidance measures

2.16 The Government's commitment to strengthening strategic defences against avoidance will reduce the need for frequent changes to legislation and contribute to simplifying the tax system.

³ Available on the HM Treasury website: http://www.hm-treasury.gov.uk/d/wms_antiavoidance_061210.pdf

⁴ Available on HMRC website: <http://www.hmrc.gov.uk/budget-updates/gaar.htm>

In addition to the work outlined above, specific changes included in Finance Bill 2011 will address a long-standing area of risk where payments through intermediary arrangements have been used to avoid PAYE and National Insurance Contributions (NICs). Avoidance using corporate finance tax rules is also being tackled through measures on mismatches between the accounting and tax treatment of transactions.

2.17 The Budget also announces strategic measures for consultation and potential legislation in Finance Bill 2012. These include improvements to tax legislation in areas such as capital allowances, the use of double taxation treaties and contributions to pension schemes in non-cash form. The Government will also consult further on extending the hallmarks that describe avoidance schemes required to be disclosed to HMRC.

2.18 Alongside the work to improve strategic defences, there is still a need to address specific avoidance risks as they arise. Finance Bill 2011 will include three measures to tackle Stamp Duty Land Tax avoidance and further measures on avoidance in the corporate sector which take immediate effect.

2.19 In addition, on 9 March 2011 legislation was introduced with immediate effect by Written Ministerial Statement to counter an aggressive avoidance scheme seeking to claim capital allowances twice on leased plant and machinery.⁵ The announcement was made in accordance with the criteria in the Protocol discussed in Chapter 4.

2.20 Measures introduced in Finance Bill 2011 will increase tax receipts by around £4 billion over the course of this Parliament.

⁵ Available on the HM Treasury website: http://www.hm-treasury.gov.uk/d/wms_antiavoidance090311.pdf

3

Tackling avoidance through challenge and litigation

3.1 Earlier chapters have explained the Government's strategic approach, aiming to tackle avoidance at its root, and have set out how this is being put into action through policy and legislative design. Robust legislation, delivering clear policy objectives, provides certainty for taxpayers and minimises the opportunity and the incentive to avoid tax. Targeted legislative changes also play a part in countering avoidance activity, and have a deterrent effect.

3.2 But important as it is, legislative change is only one aspect of countering tax avoidance. This chapter looks at the operational effort by HMRC in support of the anti-avoidance strategy. That effort is framed by HMRC's customer-centric business strategy, which identifies levels of risk in different taxpayer groups and sets out the strategic choices for managing the risks effectively.

3.3 The following sections identify HMRC's activities under the three core elements of the anti-avoidance strategy: prevention, detection and counteraction, and demonstrate how HMRC is addressing risk within and across the large business and wealthy individual customer groups, including by taking appropriate action through litigation.

3.4 The Government recognises HMRC's significant progress in developing its operational approach to tackling avoidance and other aspects of the tax gap. Underlining its backing for HMRC's operational activities, the Government announced investment of over £900 million in the Spending Review to tackle avoidance, evasion and criminal attack with the objective of bringing in around £7 billion per year in additional revenue by 2014-15.

Box 3.A: Prevention

Reducing opportunities for avoidance and deterring businesses and individuals from engaging in it are the most effective ways to maximise revenues to the Exchequer whilst reducing costs for both taxpayers and HMRC. Key activities include:

- working with banks to implement the Code of Practice on Taxation, which commits banks to operate within the spirit as well as the letter of the law. 200 banks have now adopted the code, including the top 15;
- HMRC's *Spotlights* internet publication which provides a consumer protection message to customers offered tax avoidance schemes which HMRC will actively challenge.^a *Spotlights* features articles on thirteen specific schemes and covers generic indicators of avoidance that are likely to invite a challenge from HMRC. It also now identifies areas of avoidance in which taxpayers are conceding that HMRC's arguments are right;
- providing formal and informal views on proposed transactions to identify avoidance risk and provide certainty to businesses undertaking commercial transactions; and
- improving the design of policy and legislation by building up expertise and commercial understanding in HMRC, including investing in expertise through the Spending Review settlement.

^a Available on the HMRC website: <http://www.hmrc.gov.uk/avoidance/spotlights.htm>

Box 3.B: Detection

Where avoidance opportunities persist, HMRC aims to identify them as early as possible so that an effective response can quickly be put in place. Current activities to enhance HMRC's detection capability are:

- improving the rules on disclosure of tax avoidance schemes:
 - bringing in the bank levy and Inheritance Tax on transfers into trusts;
 - working with scheme promoters on a smooth introduction of the new requirement to provide lists of clients who have taken up avoidance schemes, with the first lists being due by 30 April 2011; and
 - improving coverage by developing new hallmarks (descriptions of schemes required to be disclosed).
- monitoring compliance with the disclosure rules and challenging failure to comply, using litigation where necessary;
- monitoring and evaluating other sources of information, including using the relationship with large business and the wealthy to obtain an early insight into proposed transactions.

Box 3.C: Counteraction

Common to HMRC's approach to all customers is:

- clear assessment of risk, with resources allocated accordingly and responses project managed across multiple cases to ensure consistent outcomes;
- rigorous assessment of proposals for resolving avoidance issues through a clear governance framework, to ensure that they are settled in a way that is consistent with the potential outcome of litigation as required by HMRC's Litigation and Settlement Strategy;^a
- use of settlement initiatives, where appropriate, to publicise the terms within the Litigation and Settlement Strategy on which HMRC will be willing to resolve avoidance issues, such as the lease premium avoidance schemes initiative published by HMRC in June 2010;^b
- identification of, and action to counter, cross-border tax avoidance by working jointly with the tax administrations of Australia, Canada, China, France, Germany, Japan, the Republic of Korea and the United States through the Joint International Tax Shelter Information Centre (JITSIC), of which the UK is a founder member; and
- litigation, where necessary and without hesitation, when other approaches have been explored.

^a Available on the HMRC website: <http://www.hmrc.gov.uk/practitioners/lss.pdf>

^b Further details are on the HMRC website: <http://www.hmrc.gov.uk/news/lease-prem-sett.pdf>

Work with large businesses and wealthy individuals

3.5 HMRC's approach to managing different customers is to allocate its resource to those groups that present higher risk or need more support. For large businesses and wealthy individuals, HMRC believes active engagement with the customer is the most effective approach to manage issues such as tax avoidance, whilst improving service to customers.

3.6 With large businesses, which account for around 60 per cent of tax receipts and up to a quarter of the overall tax gap, HMRC explicitly seeks relationships based on greater openness and transparency. For the largest businesses, one-to-one Customer Relationship Managers (CRMs) ensure that HMRC has extensive understanding of tax and avoidance risks in the context of the commercial environment in which customers are operating. This supports a strong response to avoidance threats while also allowing high levels of customer service, for example, through clearances.

3.7 'Real time' working, where differences of view are settled even before the accounts are finalised, is now increasingly the norm. For customers, this provides greater certainty and reduces costs. For HMRC, it gives confidence that risks are being managed up-front, at the time when there are still opportunities to change the law if necessary.

3.8 For those customers who are low risk – judged by their internal systems and controls and attitude towards avoidance – fewer audits take place. This allows HMRC to devote most resource to cases where revenues at stake are the most significant. Since the introduction of CRMs, the number of minor issues open with Large Business Service (LBS) customers (the largest 770 businesses) has fallen by 97 per cent, and the number of issues over 18 months old by 58 per cent, while yield from interventions has risen from £3.6 billion in 2005-6 to £4.6 billion in 2009-10.

3.9 In the highest risk cases, which frequently involve multiple avoidance schemes, HMRC puts in place dedicated project teams and seeks engagement with the customer at Board level through its High Risk Corporate Programme (HRCP) and the more recently introduced Managing Complex Risks (MCR) programme. The HRCP Board governs decisions on litigation and settlement where tax involved is more than £100 million for LBS Customers. Since it began HRCP has generated additional tax yield of over £8 billion. MCR provides a similar multi-tax approach outside the LBS.

3.10 For the wealthiest individual customers, HMRC has extended its relationship-managed approach by appointing CRMs, with the aim of building knowledge of complex financial arrangements for high-value personal tax affairs. This enables areas of uncertainty to be identified and resolved at an earlier stage, with a focus on the areas of greatest risk.

Litigation

3.11 HMRC aims to prevent disputes from building up as far as possible. However, where necessary, HMRC does not hesitate to litigate, particularly on avoidance transactions which have a read-across to similar transactions by other users. Recent litigation cases have countered:

- a complex finance transaction by a large corporate group aimed at turning a commercially profitable transaction into a loss for tax purposes;
- a tax motivated currency transaction by an international financial services group aimed at getting an increased deduction from currency swaps, producing a tax result inconsistent with the economic reality;
- a scheme used by a bank to pay bonuses in a way designed to artificially exploit tax rules to avoid PAYE and NICs;
- an attempt by a company to avoid PAYE and NICs by contending that employees had agreed to be paid only the national minimum wage whilst other payments to them comprised dividends;
- a lead case for a scheme marketed across a number of individuals designed to avoid capital gains tax on disposal of an asset;
- individuals artificially creating capital losses for tax purposes where no actual loss had arisen; and
- a scheme for individuals promoted by a large accountancy firm which was intended to create artificial losses, for use against taxable income, from pre-agreed investment and sale transactions which would not leave the users out of pocket.

4

Protocol on unscheduled announcement of changes to tax law

4.1 Making legislation more robust is key to both preventing avoidance opportunities and countering avoidance when it does arise. This Government is committed to developing strategic defences against avoidance so as to minimise the need for frequent changes in tax law designed to address specific avoidance loopholes. But there will still be a need for such changes to protect the Exchequer from risk – as illustrated by the Written Ministerial Statement issued on 9 March 2011. So there is a balance to be struck between improving stability and predictability in the tax system and moving quickly to reduce risk to the Exchequer.

4.2 In December 2010, HMRC published a discussion document setting out a draft Protocol on announcements outside scheduled fiscal events,¹ fulfilling the commitment in the June 2010 tax policy making document.² To emphasise the Government's commitment to a more stable tax system, the draft Protocol sets out the criteria that Ministers undertake to use in deciding whether an announcement of immediate change to tax legislation is justified, and the process that will be followed for announcements.

Government response

4.3 Ministers and officials are grateful to all those bodies who responded to the consultation. A summary of points raised by respondents is set out in Annex A. In response, the Protocol has been amended in the following key respects:

- the Protocol will explicitly recognise that changes to tax legislation where the change is effective from a date earlier than the date of announcement will be wholly exceptional (this will not prevent such announcements if their effect is solely to reduce tax liabilities);
- legislative changes announced by Ministerial Statement will be confined to addressing the specific risk to the Exchequer that has been identified, with any wider changes being considered on a slower timetable;
- a change in HMRC's interpretation of the law (unless prompted by a Court ruling) will not be regarded as 'significant new information' in the terms of the Protocol;
- Written Ministerial Statements announcing changes to tax legislation will be made before 2pm;
- any announcement will be accompanied by a detailed technical explanation of the proposed change;
- consideration will be given to consulting informally in confidence before an announcement is made, subject to the risk of forestalling; and

¹ Available on HMRC website: <http://www.hmrc.gov.uk/budget-updates/autumn-tax/tax-policy-other-6655.pdf>

² *Tax policy making: a new approach*, HM Treasury and HMRC, June 2010

- the Protocol makes clear the role of the Office for Budget Responsibility in scrutinising estimates of Exchequer impact associated with policy changes.³

4.4 The final version of the Protocol is below and it will also be available on the HM Treasury and HMRC websites. The operation of the Protocol will be monitored by the Forum for Tax Professionals (FTP)⁴ who will recommend changes where appropriate.

4.5 The Government has committed, wherever possible, to publishing clauses for the Finance Bill in draft each year to allow time for comment. This may include draft clauses for anti-avoidance measures that have been announced earlier to help ensure that changes are properly targeted. Publishing draft clauses may occasionally mean it is necessary to introduce provisions which have effect from the date when clauses are published for comment, in order to prevent attempts to forestall planned changes, and the Protocol is not intended to prevent changes of this kind.

³ The Office for Budget Responsibility was formed in May 2010. Further details can be found on their website: <http://budgetresponsibility.independent.gov.uk/index.html>

⁴ The Forum for Tax Professionals was established in July 2010. More detail can be found on the HM Treasury website at: http://www.hm-treasury.gov.uk/tax_forums_tax_professionals.htm

Box 4.A: Protocol on unscheduled announcements of changes in tax law

The Government has made clear its aim to strike the right balance between restoring the UK tax system's reputation for predictability, stability and simplicity and preserving its ability to protect the Exchequer by making changes where necessary. In particular, changes to tax legislation where the change takes effect from a date earlier than the date of announcement will be wholly exceptional.

- 1 Ministers undertake to observe the following criteria when considering a change to tax law which will:
 - be announced other than at Budget; and
 - take effect before the legislation implementing the change is enacted.
- 2 Such changes to tax law will normally only be announced other than at Budget where:
 - there would otherwise be a significant risk to the Exchequer;
 - significant new information has emerged to identify the risk or indicate its scale; and
 - changing the law immediately is expected to prevent significant losses to the Exchequer.

Announcements will usually take the form of a Written Ministerial Statement to Parliament before 2pm.

- 3 Legislative changes announced in this way will be confined to addressing the risk to the Exchequer that has been identified. A change in HMRC's interpretation of the law (unless prompted by a Court ruling) will not be regarded as 'significant new information'.
- 4 Where Ministers believe that such a change is justified, the process will be as follows:
 - a Minister will make a public announcement of the intention to change the law and make clear that the change will take effect before the legislation is enacted;
 - the public announcement will be accompanied by the technical detail necessary to amount to a sufficiently clear warning of the nature of the change and its timing;
 - HM Revenue & Customs (HMRC) will publish the Written Ministerial Statement and draft clauses on the HMRC website as soon as practicable after the announcement to Parliament. If, exceptionally, draft clauses cannot be published on the day of the announcement, a detailed technical note explaining the nature of the proposed change and the reasons for it will accompany the announcement; and
 - legislation to give the measure effect will be included in the next available Finance Bill.

- 5 Whilst the Government will not invite comment on the intention to legislate, the nature of the change or on its timing, it will consult after the announcement to establish whether the draft legislation would achieve its objective and change the law as intended. Subject to the risk of forestalling, consideration will be given to consulting informally in confidence before an announcement is made.
- 6 As part of the normal Budget process, the Office for Budget Responsibility will scrutinise the estimates of Exchequer impact associated with any change to tax policy.

To ensure that this undertaking is put into practice effectively, the Forum of Tax Professionals will review announcements as a standing agenda item at its regular meetings and provide Ministers with a view on how the Protocol is being observed in practice. The Forum may recommend changes to the Protocol.

A Protocol consultation responses

A.1 The discussion document published by HMRC in December 2010 set out a draft Protocol on announcements outside scheduled fiscal events with the criteria that changes in tax legislation taking effect before the legislation was enacted would normally only be announced by Written Ministerial Statement outside a scheduled fiscal event where:

- there would otherwise be significant risk to the Exchequer;
- significant new information has emerged to identify the risk or indicate its scale; and
- changing the law immediately would prevent significant losses to the Exchequer.

A.2 Comments were invited on the following questions:

- will the criteria set out [above] enable the Government to strike the right balance between stability in the tax system and protection of the Exchequer? Should other criteria be considered?
- whether the Protocol should be more specific about the nature of the risks for which an immediate change of legislation might be appropriate.
- whether sufficient guidance on what 'significant' would mean in practice could be given by way of illustrative examples or whether more guidance should be included in the Protocol.
- are there suggestions for improvements to the process for making and publicising announcements described in paragraphs 5, 6 and 7 of the draft Protocol, recognising that key elements of the process are dictated by the need to provide legal certainty?

Summary of responses

A.3 Formal responses were received from the Society of Trust & Estate Practitioners (STEP), PricewaterhouseCoopers (PwC), the Institute of Chartered Accountants in England and Wales (ICAEW), the Low Income Tax Reform Group (LITRG), the Chartered Institute of Taxation (CIOT), The Law Society, the Institute of Chartered Accountants of Scotland (ICAS), and The City of London Law Society.

A.4 The draft Protocol was welcomed as a positive contribution to improving the stability of the tax system, with most respondents thinking that it generally struck the right balance between improving stability and retaining freedom to make changes to protect the Exchequer. Some respondents suggested that the scope for making announcements could be narrowed and that the criteria on when an announcement would be made could be drawn more tightly.

A.5 Key points raised by respondents to the consultation were:

- support for the commitment that a change in legislation taking effect from a date before the date of its announcement would be 'wholly exceptional';

- acknowledgement that the Forum for Tax Professionals (FTP) is the right body to monitor the application of the Protocol in practice and to recommend changes where necessary;
- recognition that it would be difficult to define the term 'significant' when describing the nature and size of a risk to the Exchequer. While a minority thought that a tighter definition was appropriate, the majority were content to leave this as a matter of judgement for Ministers subject to scrutiny by the FTP.
- the need for detailed technical information with the announcement, irrespective of whether draft legislation is published alongside the Ministerial statement, so that taxpayers have clarity about the nature of the change and who is likely to be affected; and
- if possible, proposed changes should be subject to informal consultation with interested parties before the announcement.

A.6 In addition to the key points above, some points of clarification were raised and some respondents had suggestions on the timing of announcements and ways of communicating changes to those affected.

A.7 On timing, it was suggested that Ministerial statements should be made before a certain time of day, providing certainty after that time that no announcement was planned.

A.8 On communication, respondents suggested that the routes for publicising announcements could be broadened at relatively low cost to include such things as targeted e-mails to representative bodies, as well as the use of Twitter and RSS feeds.

HM Treasury contacts

This document can be found in full on our website at:
hm-treasury.gov.uk

If you require this information in another language, format or have general enquiries about HM Treasury and its work, contact:

Correspondence Team
HM Treasury
1 Horse Guards Road
London
SW1A 2HQ

Tel: 020 7270 4558

Fax: 020 7270 4861

E-mail: public.enquiries@hm-treasury.gov.uk

ISBN 978-1-84532-854-2



9 781845 328542 >