

Why the UK needs a general anti-avoidance principle (GAntiP)

and why

Graham Aaranson's General Anti-Avoidance Rule (GAAR) won't work

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Background – and what the government is proposing

In December 2010 the Governmentⁱ asked Graham Aaronson QC to lead a study that would consider whether General Anti-Avoidance Rule (GAAR) could deter and counter tax avoidance, whilst providing certainty, retaining a tax regime that is attractive to businesses, and minimising costs for businesses and HMRC.

Aaranson reported in November 2011. He, to use his own wordsⁱⁱ “strongly recommended the introduction of a GAAR specifically targeted at highly artificial and abusive tax schemes”. But he did at the same time in his reportⁱⁱⁱ say “I have concluded that introducing a broad spectrum general anti-avoidance rule would not be beneficial for the UK tax system. This would carry a real risk of undermining the ability of business and individuals to carry out sensible and responsible tax planning. Such tax planning is an entirely appropriate response to the complexities of a tax system such as the UK’s.” The inherent conflict within his report is readily apparent.

As the Exchequer Secretary to the Treasury (David Gauke MP) noted in his response^{iv} to the report “Mr Aaronson has recommended a narrowly focused GAAR which should initially apply to the main direct taxes – income tax, capital gains tax, corporation tax, and petroleum revenue tax, as well as national insurance contributions”. That is a fair summary: what is being proposed is a narrowly focussed GAAR that has the sole, and very limited aim, of tackling what it calls “the most egregious tax avoidance schemes [that] focus on prescriptive tax rules which are not susceptible to contextual interpretation”.

What's wrong with the government's proposal

The government appears to have endorsed Aaranson's GAAR, making claim in the process that it is serious about tackling tax avoidance. Unfortunately the two claims are not really compatible. Aaranson's GAAR will not tackle almost any of the recent high profile tax avoidance issues that have reached the press and rightly attracted outrage including:

- The recent problem at the Student Loan Company^v
- The abuse of Channel Island's VAT^{vi}

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- The use of offshore, such as Google billing all its sales in the UK from Ireland to avoid maybe £100 million in tax a year^{vii}

The reality is that this GAAR will stop a handful of the most extreme tax planning cases a year, and that is it. It has to be said this is not surprising. One of those on the committee advising on this GAAR was Lord Hoffman. As a House of Lords judge he was instrumental in reversing the impact of the 1982 House of Lords decision known as Ramsey^{viii} which effectively gave the UK a GAntiP because as Lord Diplock subsequently noted when applying the decision^{ix} in order for the Ramsay principle to apply, there had to be:

- 1) a series of transactions; which are
- 2) pre-ordained; and
- 3) into which there are inserted steps that have no commercial purpose apart from tax avoidance.

Under Ramsey the artificial step inserted for tax avoidance was ignored when calculating the tax due—effectively delivering a general anti-avoidance principle.

Lord Hoffman overturned this logic in the 2001 House of Lords case called Westmoreland Investments^x. He did two things in so doing. First, he ignored principles and reinforced the right of a person to be taxed in accordance with the strict wording of the law, whether the result was desirable or otherwise. As such he reinforced the power of prescriptive tax rules and downplayed the importance of contextual interpretation. In other words he created the problem the currently proposed GAAR is supposed to address, which is, no doubt, why it does it so half-heartedly. Secondly, he reinforced the legal right to tax plan within those strictly prescriptive tax rules. This is the favourite game of the tax avoider. As such he was the last person who should have been engaged in the process of producing a GAAR and the GAAR we are being presented with has minimal impact, precisely because that is what he has sought to achieve as a judge.

There is an alternative

The GAAR we are being presented with will not work. What we need is a legal embodiment of the Ramsey principle as noted above. I drafted such a proposal, which was tabled in debate on the Finance Bill 2009 by John Pugh MP and Michael Meacher MP. It was a general anti-avoidance principle in two clauses that said:

"1 If when determining the liability of a person to taxation, duty or similar charge due under statute in the UK it shall be established that a step or steps have been included in a transaction giving rise to that liability or to any claim for an allowance, deduction or relief, with such steps having been included for the sole or one of the main purposes of securing a reduction in that liability to taxation, duty or similar charge with no other material economic purpose for the inclusion of such a step being capable of demonstration by the taxpayer, then subject to the sole exception that the step or steps in question are specifically permitted under the term of any legislation promoted for the specific purpose of permitting such use, such step or steps shall be ignored when calculating the resulting liability to taxation, duty or similar charge.

2 In the interpretation of this provision a construction that would promote the purpose or object underlying the provision shall preferred to a construction that would not promote that purpose or object".

I believe that this would deliver the Ramsey principle into law. That's not what Hoffman and Aaranson wanted, but it is what the UK needs.

And I happen to believe that this also delivers a tax regime “that is attractive to businesses, [whilst] minimising costs for businesses and HMRC” to quote the government’s objectives, noted above. That is because such a general anti-avoidance principle would:

1. Provide certainty because anyone would know that artificial steps in transactions will not work;
2. Will create a level playing field for all business and people because those, to quote the Prime Minister^{xi}, “who have the fancy corporate lawyers and the rest of it” will be subject to “a tougher approach” so that “very wealthy individuals and ... bigger companies pay their fair share” by being denied access to loopholes;
3. Will ensure business and its advisers focuses on making money and not on avoiding tax, to the benefit of the economy at large;
4. Will reduce HMRC’s costs by letting them tackle abuse directly.

Examples

To give examples of how the GAAR would work, using the cases noted above:

1. In the case of the Student Loan Company, the inclusion of the personal service company in the transaction would be the artificial step to reduce tax. The result would be that it would be ignored and PAYE would have been operated, as was obviously necessary. The same would be true of all the other similar arrangements now in force throughout the civil service. If a case had to be made for a general anti-avoidance principle then this is it.
2. In the case of Channel Island’s VAT abuse, shipping the goods to and from the Channel Islands for no reason but tax saving would have been the artificial step and would have been ignored for VAT purposes. Hundreds of millions of pounds would have been saved as a result.
3. In the case of billing sales from Ireland when those sales are arranged in the UK, the billing from Ireland would be the artificial step and the sale would be deemed to have been made in the UK.

In other words, this general anti-avoidance principle works where the GAAR will not.

The result is that tax compliance would be promoted by this general anti-avoidance principle where tax compliance is seeking to pay the right amount of tax (but no more) in the right place at the right time where right means that the economic substance of the transactions undertaken coincides with the place and form in which they are reported for taxation purposes. And that is why it is exactly what the UK needs right now and Aaranson’s GAAR is not.

ⁱ http://www.hm-treasury.gov.uk/tax_avoidance_gaar.htm

ⁱⁱ http://www.hm-treasury.gov.uk/d/letter_grahamaaronsonqc_to_xst_111111.pdf

ⁱⁱⁱ http://www.hm-treasury.gov.uk/d/gaar_final_report_111111.pdf

^{iv} http://www.hm-treasury.gov.uk/d/written_ministerial_statement_211111.pdf

^v <http://www.guardian.co.uk/education/2012/feb/01/student-loans-company-tax-row>

^{vi} http://www.hm-treasury.gov.uk/press_122_11.htm

^{vii} <http://www.pcpro.co.uk/news/354286/google-accused-of-uk-tax-dodging>

^{viii} http://en.wikipedia.org/wiki/The_Ramsay_Principle

^{ix} <http://www.taxationweb.co.uk/tax-articles/general/the-ramsay-principle.html>

^x <http://www.tax.org.uk/tax-policy/tax-adviser-articles/2001/case-analysis-westmoreland-ramsay-reconstructed>

^{xi} <http://www.bbc.co.uk/news/uk-politics-16422437>