

Tax planning in the public sector is an ethical non-sta...

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I may be a little quite on the blogging front this morning as I am driving to Northampton to take part in a debate at RSM Tenon's Public Sector Tax & VAT Annual Conference.

The motion I'm debating is:

This house holds that tax planning and avoidance by public sector bodies is unethical

I'll be saying this:

I was delighted to be asked to discuss the motion put before you today, because as those who asked me noted, whilst I've written a great deal about the ethics of tax planning and avoidance in the private sector I have never engaged in debate on this issue with regard to the public sector. This, therefore, is the first outing for some new ideas. I hope that some of you will agree with them, but let me assure you, my conclusion is radical.

In that case, and given that I know that when discussing tax abuse language can be a massive obstacle to progress, let me very clearly define the terms that I'll be using this morning.

First of all, I am sure that we can all agree that tax evasion is a criminal act of deception to understate a source of taxable income or to claim a tax deduction for which there is no justification. I am sincerely hoping that no public sector body in the UK is knowingly involved in such activity, so let us now leave that issue behind us and go to the other extreme next.

I use the term tax compliance to describe the polar opposite of tax evasion. In the language of this debate it is not, as some of you might think, completing documentation for submission to HM Revenue and Customs. Tax compliance is instead, in my view, 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.

That is not only what I would hope the public sector bodies of the UK set out to do, it is also what I expect every single taxpayer in this country to do and that is precisely why I wrote the recent General Anti-Tax Avoidance Principle Bill presented to the House of Commons by Michael Meacher MP.

What then is tax avoidance? Let me be clear. Tax avoidance is about seeking to get round the law. In that case tax avoidance has nothing to do with exercising those options that are available to a tax payer within the law. So, for example, the option to tax a property for the purposes of VAT is one that is provided by law. As a result, deciding whether or not to exercise that option is to undertake what I would call tax planning. The law intended this choice; you are required to make that choice. The outcome, unless a series of other steps were put into the transaction to secure a tax advantage that would otherwise not be available, is always going to be tax compliant in that case. So let us put aside straight away the absurd notion that anything from claiming a personal allowance onwards is tax avoidance. That's sophistry by those seeking to exonerate their own abusive behaviour.

What might that abusive, tax avoiding, behaviour be? Well if you want an example choosing to pay an employee who has been engaged by a public body through a personal service company when they are clearly undertaking tasks for which no substitute can be provided, to which no risk is attached, and where they are very clearly a public servant and not a supplier of services to a public body is, in my opinion, an action seeking to get round the due provisions of law to secure a tax advantage by not paying employers National Insurance contributions. That is tax avoidance, and everyone from the Parliamentary Accounts Committee and the Daily Mail onwards can spot it a mile off.

I hope in that case that the distinction between tax avoidance and tax planning is now apparent. It comes down to motive. What is the person making the choice seeking to do? Are they trying to comply with the law, or are they trying to get around the law? My contention is a simple one. If you are trying to comply with the law then your actions are ethical. If you're trying to get around the law then your actions are unethical.

And let me be clear that when saying this I believe the motive can usually be clearly identified in actions. It is claimed that tax law is complex and to some degree I agree. But it is nothing like as complex as it would need to be but for the actions of those who seek to avoid tax. That's because tax avoidance almost invariably involves putting some step into a transaction that can only be explained by a desire to reduce a tax bill. Using a personal service company is such a step. So too would be the use of a special purpose vehicle solely to exclude a transaction from group VAT registration to secure a tax benefit. Whilst law must be specified in words, actions speak more loudly when it

comes to identifying motive and that is why the purposive approach that I've included in the General Anti-Tax Avoidance Principle Bill now before Parliament is so important.

There is, however, an inevitable conclusion from these observations and that is that there is no way that morality can be excluded from taxation. Indeed, to claim, as I know my opponent in this debate has done in his paper, that morality should be taken out of the debate is to put forward what is in itself a moral judgment. I lay the paradox before you.

You are, each and every one of you, an ethical being, like it or not. And each and every one of you has to make ethical decisions in the course of your work. That does not change when you come to tax. To pretend it does is just that, a pretence.

In that case, what should the guidance for those decisions on tax be? I'm well aware that my opponent will argue that a review of case law decided by our learned friends in the House of Lords and Supreme Court is sufficient for this purpose, and that as a result we can rely upon the construction of contracts to give us the guidance we need. Such is, broadly speaking, the current state of that law.

I have to tell you, my opponent is as wrong on this, as he was on his argument on morality. I have looked for the motivation for his belief in the paper that he has presented, which I've had the advantage of seeing, and have found it in his claim that "the directors of a listed company have an implicit imperative imposed upon them under company law to do everything legally tenable to mitigate the company's tax liability in the interests of its shareholders." This, he seems to think, is the basis for the actions on tax he thinks public authorities must also take, and this seems to be his justification that all judgments can be reduced to an appraisal of the contracts entered into as the basis for determination of what is right and wrong.

Unfortunately for the purposes of his argument there is absolutely no such implicit or explicit obligation imposed upon the directors of any company, public or otherwise, in section 172 of the Companies Act 2006 which lays out the duties directors have to the shareholders and to other parties. That section actually says:

A director of a company must act in the way he considers, in good faith, would be most likely to promote the success of the company for the benefit of its members as a whole, and in doing so have regard (amongst other matters) to-

(a) the likely consequences of any decision in the long term,

(b) the interests of the company's employees,

(c) the need to foster the company's business relationships with suppliers, customers and others,

(d) the impact of the company's operations on the community and the environment,

(e) the desirability of the company maintaining a reputation for high standards of business conduct, and

(f) the need to act fairly as between members of the company.

There is, as you will note, nothing absolute about that. The exercise of judgment is required, and the exercise of good faith is essential. There is of course a duty of care to the shareholders, but remember that they have no way of enforcing it: they cannot sue the director if he or she fails in their opinion to maximise profit or minimise tax. No shareholder has that right. As a result it is very clear that there is no absolute guidance to behaviour, whether in contract law, or as my opponent has claimed, in statute law: such simple guidance simply does not exist. The claim that such guidance does exist is then but an excuse, and it is wrong.

That though has serious implications. If such claims have no substance in law, as is clearly the case, then those suggesting to the contrary are not offering a moral opinion when doing so, for that would presuppose in this case that there was law to interpret when there is none, but they are instead offering a political judgment, since they are actually offering an opinion on what they would like the law to be when at present it is very clearly otherwise. And as we know, for a public official to offer political opinion puts them on dangerous ground.

I therefore think that those offering advice on tax in the public sector, and how such decisions should be made, should look for their guidance elsewhere. So I looked, for example, at the guidance of the Local Government Association and I quickly found that there are standards and ethics with which councillors must comply, and codes of conduct too. All do, of course, imply that morality is an essential part of the decision-making process that they must embrace. And I learned from the code of conduct that councillors must:

- * not bring their office or authority into disrepute
- * not seek to improperly influence decisions to the advantage or disadvantage of themselves or anyone else
- * only use the resources of the authority in accordance with its requirements
- * use the authority's resources for proper purposes only. It is not appropriate to use the resources for political or party political purposes, unless it is lawful and in accordance with their authority's requirements

So let's look at this more appropriate guidance through the eyes of the reasonable person: let's call them a voter. What do they think the local authority might be? I'd suggest they think it a part of government. And I think they'd be right. Indeed, it is not only a part of government, it is a government.

And I wonder what that voter might think governments should do? My suggestion to you is this. They expect that it should pass good laws. But more than that, they expect it to uphold the law. That's one thing they rely on government to do: that's its job. And so they would expect those who serve it to be exemplars of good practice in upholding the law, reinforcing the law, and making clear that the rule of law is the basis on which our society is founded. And as such they would expect a local authority — or indeed any public body - to work in close harmony with other public bodies, including central government.

Would they, in that case, expect their local authority to spend money, not just a little money, but substantial amounts of money, challenging laws created by central government? Or would they think that an example of local authority waste?

And do you think they would they ever expect the judgement criteria used by those in office in a local authority, and all those who advise them, to be the same as those lowest common denominator level criteria found in some of our largest multinational corporations, that very clearly set out to exploit and abuse the principles on which our society is built by denying their role in it and the contribution that they should make so it?

The very obvious answer to all these questions is, of course, no. I put it to you as simply as this: for a public authority to be seen to be challenging central government on the application of law to enrich itself is quite simply ethically wrong, not just to me, but I think to all people of common sense in this country.

And yet that is what local authorities have been doing. The perfect example is the Isle of Wight car parking case. Just a moment's thought makes clear that there is no way that every person who paid VAT to the Isle of Wight Council will, if that decision goes through, be reimbursed the tax they have paid to it since 1973. There will, instead, be an unjust enrichment of the Isle of Wight Council.

Except, yet again, any person of common sense will realise that will not happen. Isn't it obvious that if £1 billion in VAT had to be repaid that the government would straightaway claim this back from the payments to be made to local authorities which fund 80% of their activities?

Isn't it then also glaringly obvious to anyone that this activity is at best a zero-sum game?

Except, again, isn't it obvious to anyone that it is not even that? This can only be a negative sum game where the only people who actually gain are the tax profession, who are the people who advise on the construction of these claims which merely reallocate money from one pot within government to another pot within government, bringing discredit upon all involved in the process.

Is that ethical? No, clearly it is not. It's not ethical that the main beneficiary of tax revenue be the accountancy and legal professions.

Nor is it even useful because there is never a net gain to society from it.

And in that case I suggest there is no way that any councillor or director of a public body should be engaged in such activity if they are to comply with the standards of conduct that are demanded of them. That some do so is a sad indication of the current state of local government.

Once upon a time, in the real glory days of local authorities in this country, they built housing, they provided public transport systems, they delivered public sanitation, they provided electricity and gas. They transformed lives.

And now here we are, apparently thinking it is the job of local authorities to challenge government through innovative tax planning. How far have our ethics fallen, and how far has the contribution of the accountancy profession in the public sector — once dedicated to financing the real contribution those authorities could make to society — fallen with it.

That's a sorry tale, so let me finish with a suggestion, because it's not my style to identify problems and not suggest solutions to them. In this case the obvious answer is actually a very simple one. We just need one clause in next year's Finance Bill to solve this problem once and for all. It would say:

Public authorities in the UK shall be barred from litigating on any taxation matter bar the recovery of council taxes, fees and other charges owing to them.

That should make clear where the duty of councils and other bodies lies on this issue, once and for all. And then all the effort now wasted on this issue could be put to so much better use. For that the public would be truly grateful.

It's just sad that we'd need a law to say what is so obviously right.

I move the motion.