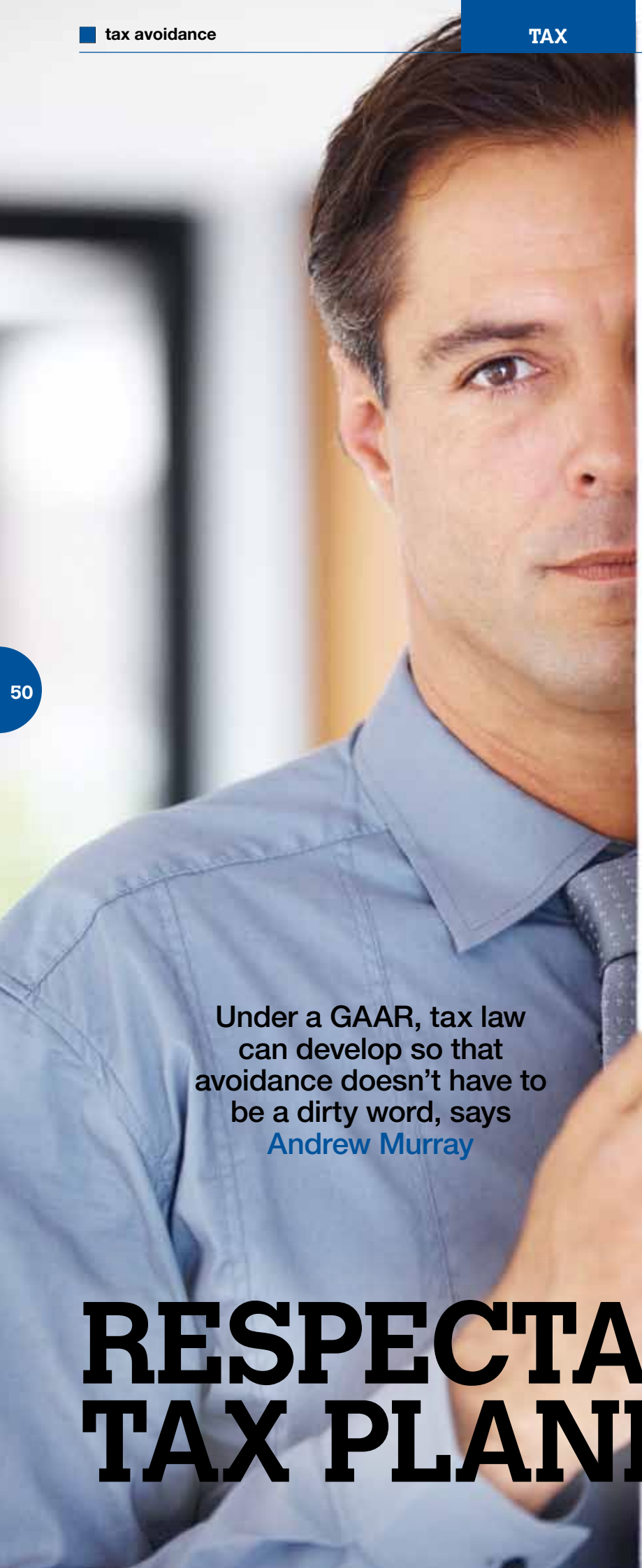

RESPECTABLE TAX PLANNING?

Under a GAAR, tax law can develop so that avoidance doesn't have to be a dirty word, says Andrew Murray

The recent Budget announcement that the government has accepted the recommendations of the Aaronson Report on the introduction of a General Anti-Abuse Rule (GAAR) to the UK statute book comes as little surprise. That said, it raises the question of whether the GAAR and the Disclosure of Tax Avoidance Schemes (DOTAS) regime will make comfortable bedfellows or ought to be mutually exclusive. For the foreseeable future, both the GAAR and DOTAS need to co-exist because they approach tax avoidance from different policy perspectives and are a response to a tax avoidance 'industry' that is a uniquely UK phenomenon.

The development of tax planning in the UK and, as its by-product, a rampantly active avoidance industry, is due in main or part to a literal interpretation of the governing legislation. This 'letter of the law' approach has witnessed the development of aggressive planning that is tax effective but, more often than not, lacking commercial substance. The DOTAS regime was introduced as one means of attempting to counter this approach to tax 'schemes'. The government insisted that DOTAS was intended to 'shift business and professional perceptions about tax… ensuring that tax avoidance is understood as unproductive, generating risk and costs that most businesses will not want to incur.'

The success of the various scheme providers in promoting their wares has meant that DOTAS is a necessary ex post facto tool in keeping HMRC informed of the various arrangements circulating in the market. For the more 'costly' or successful schemes (eg, land trading partnerships), countering legislation (often drafted in increasingly complex and lengthy terms, sometimes in retrospective form) follows.

INTERPRETATION

Yet, while DOTAS attaches to the more egregious schemes it does not necessarily result in a greater tax take or alter attitudes to tax planning. The recent *Mayes ([2011]*

ECWACiv 407) decision is an excellent illustration of the ineffectiveness of a purely prescriptive approach and ex post facto correction. Mayes involved a seven-step process that was designed to give income tax and capital gains tax relief with no actual economic loss. The Court of Appeal judgment, while holding that the scheme was effective, also attacked the rationale of the underlying planning stating their 'reluctant concurrence in a result which instinctively seems wrong, because it bears no relation to commercial reality and results in a windfall which parliament cannot have foreseen or intended'.

The difficulty with a prescriptive approach to taxation is that the draftsman attempts to anticipate all of the adverse ploys to which it might be put. The result is legislation that is overly complex, voluminous and riddled with exceptions to exceptions – rendering it virtually unintelligible. The recent disguised remuneration provisions and the new controlled foreign companies (CFC) rules are a great example of this methodology. When viewed in this light, it seems clear that the current policy rationale has lost its way.

It is under this pretext that a GAAR has been hailed as a solution to the current ills. This is because, assuming the approach by Graham Aaranson QC is appropriately adopted, a GAAR ought, over time, to introduce a significant shift in the development and interpretation of UK tax law.

A GAAR focuses on the 'principles' of the enacting legislation rather than the black and white letter of the law. It is an attempt to understand what parliament intended (perhaps in and of itself a dangerous task) in enacting tax legislation. Taxpayers should then be guided by these principles in planning their tax affairs. Without a strong line of thought or adequately drafted principles espoused in either the legislation itself or in accompanying documents, the GAAR itself becomes redundant. This ought to encourage legislators and policymakers to consider the broad aspects of tax policy and to ensure these principles are clearly considered. Unfortunately this is almost entirely obfuscated in the current legislative process.

THE JUDICIARY

The courts too have a critical role to play. Unlike under the current system of prescriptive legislation and DOTAS, where courts are, at times, forced to judicially 'stretch' legislative language to prevent abuses, interpretation under a GAAR is likely to be less restrictive. Undoubtedly, there will be an adjustment period (as there was in the 'early adopter' jurisdictions of Canada, Australia and New Zealand) as the Courts familiarise themselves with the overlay of a GAAR. The courts in the early adopter jurisdictions tended to 'read down' the scope of the GAAR. However, the passage of time and an increased understanding of what constitutes 'acceptable' or 'reasonable' tax planning has resulted in considerable impetus for courts in those jurisdictions to give full effect to the GAAR rationale.

The contractual disclosure facility gives HMRC more legal clout to take tax avoiders to court

Is HMRC showing its teeth?

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Aaronson's vision of the UK GAAR attempts to address some of the problems encountered by those 'early adopters'. Rather than a broad spectrum anti-avoidance provision, the GAAR is intended to focus on abusive arrangements that violate the 'will of parliament' – Aaronson uses the words 'a reasonable exercise of choice… without a tax intent'. The focus, therefore, is likely to be similar to DOTAS. However, while DOTAS allows a scheme a nine to 12 month shelf life before being closed by countering legislation, highly artificial and speculative schemes are unlikely to find market appetite under a GAAR.

Yet a GAAR is unlikely to be a panacea for HMRC. It is likely to take a considerable time for the UK's approach to tax planning to alter. Thus, in the interim at least, DOTAS and a GAAR will need to co-exist because of the different approaches to tax avoidance they represent. DOTAS as a means of providing information to enact stop-gap legislation for particularly egregious tax schemes and a GAAR to combat tax planning that steps beyond the bounds of reasonableness.

It is not just tax advisers that will need to adopt a different approach. HMRC views most forms of tax planning as inherently 'bad' or unlawful. While undoubtedly some schemes push the boundary beyond reasonable limits, UK tax legislation includes numerous provisions that actively encourage taxpayers to seek a reduction in their effective tax rate. HMRC will need to acclimatise to an environment that allows 'respectable' tax planning within the principles established by the governing legislation and in an environment where the burden of proof rests with them to prove otherwise.

The difficulty with a prescriptive tax approach is that the draftsman attempts to anticipate all of the adverse ploys to which it might be put

It is no doubt the hope of Aaronson, parliament, HMRC and perhaps the majority of tax advisers that a GAAR will signal a 'new approach' to tax avoidance in the UK. Recent legislation is unnecessarily complex and is the result of the historically prescriptive approach adopted in the UK. While DOTAS is currently necessary, it is hoped that with the introduction of the GAAR and the attitudinal shift it ought to bring, DOTAS can be consigned to the annals of legislative history.

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