The role of GAARs in a post BEPS world– EU and UK perspective

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General background

- Increased mobility of profits and Global Financial Crisis/austerity—‘tax gap’ concerns
- Increasing media/public/NGO interest and corporate social responsibility pressures in some jurisdictions
- But balance pressure for competitiveness and growth.
- Rule of law concerns: legal certainty
General anti-abuse rule based on principal purposes of transactions or arrangements will be included in the OECD Model Tax Convention.

If one of the principal purposes is to obtain treaty benefits, benefits will be denied unless in accordance with object and purpose of treaty.

Nb that OECD Model Treaty commentary to Article 1 states that domestic GAARs do not generally conflict with tax treaties as they define scope of domestic tax. Confirmed BEPS Action Plan 6 final report para 26.4
Explanatory memorandum

- ‘Tax planning schemes are very elaborate and tax legislation does not usually evolve fast enough in order to include all necessary specific defences to tackle such schemes.’

- ‘This why a GAAR is useful in a tax system; it thus allows abusive tax practices to be caught despite the absence of a specific anti-avoidance rule.’

- Nb package for corporate tax only
Article 7
General anti-abuse rule

1. Non-genuine arrangements or a series thereof carried out for the essential purpose of obtaining a tax advantage that defeats the object or purpose of the otherwise applicable tax provisions shall be ignored for the purposes of calculating the corporate tax liability. An arrangement may comprise more than one step or part.

2. For the purposes of paragraph 1, an arrangement or a series thereof shall be regarded as non-genuine to the extent that they are not put into place for valid commercial reasons which reflect economic reality.

3. Where arrangements or a series thereof are ignored in accordance with paragraph 1, the tax liability shall be calculated by reference to economic substance in accordance with national law.
Compare BEPS and EU

- Purpose of treaties or of national law?
- Principal purpose or essential purpose?
- Benefits denied or economic substance taxed?
Most common law countries have a GAAR including Australia, New Zealand, Hong Kong, South Africa, Kenya and now UK

Many civil law countries have abuse of rights and/or a GAAR

USA – largely judicial rule but recent codification of economic substance

Many Asian countries have a GAAR including China. India's GAAR has been deferred until April 2017

EU: *Halifax* principle – abuse of law and proposed harmonised statutory GAAR for corporation tax. Most countries have a GAAR and others under pressure – Poland introduced a GAAR last week
Expecting too much from GAARs?

- GAARs being used as a catch all for inadequacies elsewhere. But drafting suggests linked to purpose of the underlying legislation or treaty.
- Thus not suitable where those objectives unclear or where so-called avoidance is actually the mismatching of two systems or the exploitation of international tax system (sometimes intended by at least one jurisdiction)
UK GAAR – a case study

- After prior rejection, Aaronson GAAR study November 2011– report and illustrative draft clauses

- Proposes ‘moderate rule targeted at abusive arrangements but not applying to reasonable tax planning’ NOT a broad spectrum anti-avoidance rule
Further developments

- Consultation 2012
- Interim panel appointed under Graham Aaronson as Chair to consider draft guidance
- Permanent panel chair appointed 28 March 2013 – Mr Patrick Mears retired solicitor. Further 7 members appointed June 2013 (one has since ‘resigned’).
- No case to court or panel yet
Legal position in UK prior to 2013

- No statutory general anti-avoidance rule
- No general abuse of law doctrine
- No clear judicial anti-avoidance doctrine (see next slides)
- No penalties for avoidance (unless negligence or fraud)
- No general statutory clearance (binding rulings) system (but some in individual cases)
- Extensive disclosure requirements (DOTAS since 2004)
- Restrictive rules of evidence in court
- Detailed method of legislating (not principles based). Many SAARs and TAARs
UK case law – the judicial doctrine

- *W.T. Ramsay Ltd. V IRC* [1981] as elaborated in subsequent case law to late 1990s – a judicial principle?
  - Pre-ordained series of transactions (may or may not have legitimate commercial end overall)
  - Inserted steps with no commercial purpose other than the avoidance of tax
  - No practical likelihood that the events would not take place in the order ordained
  - Pre-ordained events do take effect
Barclays Mercantile Finance Ltd v Mawson [2004] (BMBF)

Ramsay case did not introduce a new doctrine specific to revenue statutes but rescued tax law from ‘island of literal interpretation’

‘Going too far’ to say that transactions or elements of transactions with no commercial purpose should always be disregarded.

But same day, same court—IRC v Scottish Provident

applies ‘Ramsay’ principle to have regard to ‘series of transactions intended to have a commercial unity’
A very special rule of interpretation

*Collector of Stamp Revenue v Arrowtown Assets Ltd* [2003] Hong Kong case cited in BMBF) per Ribeiro PJ:

“The ultimate question is whether the relevant statutory provisions, construed purposively, were intended to apply to the transaction, viewed realistically.”

- Normal interpretation?
- Stretched interpretation?
- OR judicial doctrine?
Judges inevitably are faced with the temptation to stretch the interpretation, so far as possible, to achieve a sensible result; and this is widely regarded as producing considerable uncertainty in predicting the outcome of such disputes. In practice this uncertainty spreads from the highly abusive cases into the centre ground of responsible tax planning. A GAAR specifically targeted at abusive schemes would help reduce the risk of stretched interpretation and the uncertainty which this entails.
Key features of GAAR in UK

- Substantive overriding provision – not just interpretation
- Targets only ‘abuse’ not avoidance.
- Non-exhaustive indicators of abuse
- Objective double reasonableness test
- Burden of proof on HMRC to show abusive and counteraction just and reasonable (clarification in guidance?)
- Rules of evidence
- Advisory Panel
- Guidance – not in statute but referred to in statute
- Scope – all but VAT (EU law)
- Intended to override DTAs – express in legislation
Rules of evidence

- Court MUST take into account
  - HMRC GAAR guidance as approved by the GAAR Advisory panel at the time the arrangements were entered into
  - Opinion of Advisory Panel about arrangements

- Court MAY take into account
  - Ministerial, HMRC and other material in the public domain at time arrangements entered into.
  - Evidence of established practice at time of arrangement
Not included in proposal

- No subjective element – objective test only but narrow – no need for subjective protection
- No advance rulings provisions – why?
  - Narrowseness of test
  - Administrative and compliance burden
  - Large corporate taxpayers have informal means of discussing issues (enhanced relationship)
- Guidance not contained in statute (but must be taken into account by Court).
The Advisory Panel (AP)

- HMRC not represented on AP but appoints Chair
- HMRC designated officer must give notice to taxpayer of GAAR being applied
- Taxpayer has 45 days to respond
- If case to continue must then go to AP
- Chair of AP appoints sub-panel to give opinion on whether the arrangements are a reasonable course of action or not, or whether they cannot reach a view.
- Anonymised general reports of opinions to be published?
2013 Finance Act

207 Meaning of “tax arrangements” and “abusive”

(1) Arrangements are “tax arrangements” if, having regard to all the circumstances, it would be reasonable to conclude that the obtaining of a tax advantage was the main purpose, or one of the main purposes, of the arrangements.
(2) Tax arrangements are “abusive” if they are arrangements the entering into or carrying out of which cannot reasonably be regarded as a reasonable course of action in relation to the relevant tax provisions, having regard to all the circumstances including—

(a) whether the substantive results of the arrangements are consistent with any principles on which those provisions are based (whether express or implied) and the policy objectives of those provisions,

(b) whether the means of achieving those results involves one or more contrived or abnormal steps, and

(c) whether the arrangements are intended to exploit any shortcomings in those provisions.

(3) Where the tax arrangements form part of any other arrangements regard must also be had to those other arrangements
(4) Each of the following is an example of something which might indicate that tax arrangements are abusive—

(a) the arrangements result in an amount of income, profits or gains for tax purposes that is significantly less than the amount for economic purposes,

(b) the arrangements result in deductions or losses of an amount for tax purposes that is significantly greater than the amount for economic purposes, and

(c) the arrangements result in a claim for the repayment or crediting of tax (including foreign tax) that has not been, and is unlikely to be, paid, but in each case only if it is reasonable to assume that such a result was not the anticipated result when the relevant tax provisions were enacted.
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(c) the arrangements result in a claim for the repayment or crediting of tax (including foreign tax) that has not been, and is unlikely to be, paid, but in each case only if it is reasonable to assume that such a result was not the anticipated result when the relevant tax provisions were enacted.
Subsequent developments

- GAAR panel decision of unreasonableness as indicator of applicability of Advance Payment Notice and large business special measures
- Amendment to allow GAAR Panel decision to apply to other users (marketed schemes)
- Amendment to introduce 60% penalty
- Judicial case law continues to be applied – eg Supreme Court *UBS case* March 2016. ‘Facts construed realistically in light of statute to be applied’
- Government continues to introduce TAARS
Lessons from UK

- Revenue authority may chose to use GAAR as deterrent and not test in courts: decisions will take time
- GAAR may be appropriated for other purposes
- Panel may become quasi judicial.
- Courts could react by reducing willingness to stretch other law or
- could continue to develop their own approach, the latter especially if GAAR does not come before them
Conclusions

- GAARS must operate with the objectives of legislation or treaties
- GAARs require administrative framework to manage uncertainty within rule of law.
- Administrative mechanisms need clear purpose and structure
- GAARS not appropriate mechanism for rewriting domestic or international tax law to change tax base originally envisaged: can only protect original objectives
- GAARs do not remove need for clear principles of taxation and good drafting but can be useful back-up to prevent cat and mouse games with specific legislation
Selected sources and references

- Dourado, Aggressive Tax Planning in EU Law and in the Light of BEPS Intertax Vol43, Issue 1 42.