PLB 2014 3 34

THE GENERAL ANTI-ABUSE RULE (THE GAAR)

INTRODUCTION

The general anti-abuse rule (the GAAR) is contained in FA 2013 s.206 et seq and came into effect on the 17th July 2013.

The HMRC material is in the HMRC's GAAR Guidance, approved by the Advisory GAAR Guidance Panel (Parts A, B, C and E) with effect from 15 April 2013.

AMBIT

The rule has effect for the purpose of counteracting:-

tax advantages arising from

tax arrangements that are

abusive.

TAX

The rule applies to the full range of taxes i.e. income tax, corporation tax, capital gains tax, PRT, IHT and even the ATED. Stamp duty land tax is also included but not stamp duty (the rate of stamp duty is only ½ per cent so it may not be considered to be worth the effort).

THERE MUST BE A TAX ARRANGEMENT

For the provision to apply there must be a tax arrangement.

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 arrangement (s.207(1)).

Example

X Lid is for sale. It holds valuable investment property. Z Lid buys it and immediately puts it into liquidation in case it has unknown creditors. This is not a tax arrangement. One of the main purposes of the arrangement (purchase and liquidation) was not to avoid tax.

THE TAX ARRANGEMENT MUST BE ABUSIVE

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 provision 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 and the policy objectives of those provisions (i.e. the intention of the legislation) and

(b) whether the means of achieving those results involves one or more "contrived or abnormal" (what is contrived or abnormal to one person may not be to another: subjective judgements rule here) steps and

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

The following "*might*" (importantly s207 (4) uses the word "might" and not "shall") indicate that an arrangement is abusive:-

(1) the results of the arrangement cause the amount taxable to be less than the amount which has been economically obtained; or

(2) the arrangement results in a deduction or a loss of an amount for tax purposes that is significantly greater than the amount for economic purposes (this is directed at artificial tax loss schemes); or

(3) the arrangement results in a claim for the repayment or crediting of tax that has not been, or is unlikely to be, paid.

HMRC PRACTICE AND ABUSE

FA 2013 s207(5) states that the fact that arrangements accord with established practice, and HMRC had, at the time the arrangements were entered into, indicated its acceptance of that practice, is an example of something which might indicate that the arrangements are not abusive.

Practices extant before 17 July 2013 can also be taken into account.

HMRC in their guidance approved by the Advisory Panel with effect from 15th April 2013 at C5.12.7 states:-

> "... the nature of HMRC's acceptance may be relevant. For example, the acceptance may take the form of a statement to the effect that HMRC considers that certain practices fall within the intended scope of particular legislative provisions; in which case such statement would carry considerable weight in showing that the arrangements were not abusive. By contrast, however, the statement might indicate no more than a grudging acceptance that the tax rules as drafted could not prevent arrangements of that sort achieving their tax objective even though in HMRC's opinion such arrangements were contrived and were not in accordance with the underlying policy of the legislation. In such a case, HMRC's acceptance would carry little or no weight, in determining whether the arrangement in question was abusive."

THE TAXPAYER MUST OBTAIN A TAX ADVANTAGE

A tax advantage would include an increase or relief from tax or the avoidance of a charge to tax or the avoidance of a possible assessment to tax. See s.208.

Example

Under the CGT rules which apply to overseas trusts which make capital gains, gains are matched to benefits under TCGA 1992 s87A and if payments of £X are made offshore in year 2 being a year a gain of £X is made there is no matching with earlier benefits made over to beneficiaries in year 1. This gives the taxpayer a tax advantage. There is scope for making the best of the matching rules. However this is using the matching rules within the intention of Parliament and *there is no abuse*. On the other hand if the settlor added funds to the settlement so a payment could be made to him to wash the gains there would be an abuse: the added funds have gone round in a circle. See the HMRC guidance D21.

COUNTERACTION IN A JUST AND REASONABLE MANNER

If the provision applies then the tax advantage is to be counteracted in a just and reasonable manner under s.209.

THE GAAR AND OTHER TAX PROVISIONS

The GAAR does not displace any other tax provisions which may be used by HMRC to assess tax on the taxpayer such as specific anti-avoidance provisions.

It does not displace the Ramsay approach to statutory interpretation.

Furthermore, there is no restriction on the same with regards to double tax treaties.

Example

Mr X who is resident in the UK arranges for interest to arise to his Liechtenstein company relying on the interest article in the new DTT to protect the interest from a UK tax charge. HMRC may seek to asses Mr X on the interest under ITA 2007 s720 or if needs be under the GAAR.

THE GUIDANCE

The guidance in Part D sets out a number of examples where it is considered the GAAR may apply and may not apply and this gives practitioners a feel for how the provisions are likely to operate.

THE KEY

The key to the operation of the provision is whether the arrangements are abusive and this as mentioned above involves a double reasonableness test. Arrangements are abusive if entering into or carrying out the same cannot reasonably be regarded as a reasonable course of action to take in relation to the relevant tax provisions having regard to circumstances set out in s.207(2).

As to whether one can say that the carrying out of the course of action cannot reasonably be regarded as a reasonable course of action is a question which is ultimately left to the judges but practitioners may also be called upon to exercise their judgements.

Example

If a company sold at market value a let property to its subsidiary (both being foreign companies) in order to increase the amount of deductible interest against the rent, on an intra-group lending (known as "step-ups"), the question may be raised as to whether the GAAR could apply to that. The transaction is carried out because the property has gone up in value so there is nothing artificial in that respect. It may, however, be looked upon as a contrivance and the real economic effect of the two companies is unchanged but the tax bill overall is reduced. One could, however, take the view that it is a reasonable course of action and should be reasonably regarded as such, in relation to the interest relief provisions and the writer inclines to that view. The key may, however, be s.207 (5). The Revenue/HMRC has accepted such transactions in the past and the question is whether the correspondence, which the taxpayer has, shows HMRC accept the principle that provided the sale consideration properly equated with the market value of the property there was nothing objectionable under the then legislation (i.e., pre-GAAR) to the transaction being effective and HMRC had not "grudgingly" accepted the position. See also HMRC's acceptance of the position re SDLT: see the HMRC statement of 10/2/2006 and SDLTM23040. It may also be that if there is a counteraction than any counteraction would simply, on a just and reasonable basis, limit the amount of interest relief to that which would have been available had the transfer not taken place. There is thus no down side to the transaction: the GAAR does not punish but counteracts in a just and reasonable manner.

APPEALS

The appeals procedure requires the taxpayer to take the case before a tribunal or court and in determining whether the rule applies the tribunal or court must take account of HMRC's guidance about the general anti-avoidance rules approved by the GAAR Advisory Panel and any opinion of the GAAR Advisory Panel on the particular arrangement (which they will have been called upon to opine on in advance as part of the unique GAAR appeals procedure).

SAFE ARRANGEMENTS

HMRC in their guidance give examples of arrangements which they consider to be safe such as the taxpayer choosing to trade on his own account or trading through a company or deciding to invest in an ISA or make gifts of assets for IHT purposes, avoiding the reservation of benefit provisions.

Also making use of specific statutory incentives and reliefs would not involve the GAAR unless the same were used or abused in an unusual fashion (see paras B4.3 and B4.4 of the guidance).

CONCLUSIONS

It is difficult to tell whether the GAAR will be restricted to wholly artificial tax arrangements or whether it will gradually be extended to apply to many types of arrangements like the one mentioned above concerning interest relief.

Practitioners may well have to apply the double reasonable test in particular cases taking into account their experience over the years as to what intuitively they feel is abusive.

There is no doubt the provision is widely drafted but the courts must ultimately apply the double reasonable test where there is a dispute with HMRC and this will depend on the economic and political circumstances at the time and how tax avoidance is viewed by the courts and indeed Parliament and the Newspapers and the general body of taxpayers at the time. If tax rates are high and public money is not being properly expended "reasonable" may have a narrow meaning. If the economic circumstances are difficult and the government seem to be genuinely wrestling with the same at a time of general austerity reasonable may have a wider interpretation.

The word is elastic and subjective and dangerous to have at the heart of a tax code where certainty is the natural guiding principle.

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