

TAX ADMINISTRATION AND THE RULE OF LAW

On Wednesday 20 November 2013, the Bingham Centre for the Rule of Law held a one-day conference entitled 'Do our tax systems meet rule of law standards?' This was the second of two conferences focusing on tax and the rule of law principles set out in the late Lord Bingham's book on the subject.

Anthony Thomas was among the speakers in the afternoon session, in his capacity as former president of the CIOT and chairman of LITRG. His theme was the need for the tax administration to recognise and uphold the rights and safeguards due to all taxpayers equally, whether large corporate or unrepresented individual.

The text of Anthony's speech is below. A summary of the day's proceedings appears on the Bingham Centre website at <http://www.biicl.org/binghamcentre/>.

Selective enforcement and equal treatment

For the UK tax system to operate efficiently and effectively there must be mutual trust between taxpayers, the tax profession and the fiscal authority. There must also be confidence that the law is applied equally to all sectors of society. Complex laws applied in an oppressive manner results in lower, not higher tax revenues and the US is probably a good example of that.

The rule of law is the foundation of everything we do in tax. In particular there are three of the Lord Bingham principles which apply.

Firstly, the laws of the land should apply equally to all save to the extent that objective differences justify differentiation.

Secondly, ministers and public officers at all levels must exercise the powers conferred upon them in good faith, fairly, for the purposes for which the powers were conferred without exceeding the limit of such powers and not unreasonably.

And thirdly, questions of legal right and liability should ordinarily be resolved by the application of the law and not by the exercise of some discretion of some official, in effect giving them quasi legislative powers.

It is clear that equality before the law is a cornerstone of our society. There cannot be one rule for the rich and powerful and another for the poor. There is though an important but related issue – inequality in administration gives rise

to unequal treatment and hence unfairness. It is this which has to a large extent been the focus of much criticism of HMRC, their supposed “special relationship” with big business, the Public Accounts Committee, and much of the ill-informed and ill-considered media attention.

It is quite astonishing really that the unthinkable has actually happened. The world is in turmoil, I suppose the recent earthquake is a good example; there are more sex pests being unearthed every week; yet tax is topping the news agenda for the first time in living memory. The debate over how much an individual or company should pay in tax will rumble on for months. Companies cannot win. The trouble is the letter of the law has been replaced by the spirit of the law and big companies, and little ones for that matter do not know what to do about it. For a company to operate well within the law and minimise their tax liability has become as unacceptable as a banking boss pocketing a bonus that was earned legally under an incentive plan agreed some years earlier.

The “Starbucks” incident demonstrates that the tail is wagging the dog. What was presented as a climb-down by the coffee chain has only managed to inflame. By offering to pay £20m over two years to make up for a long period of rarely troubling HMRC is exactly the wrong way round. If we have not got a tax system fit for purpose it really is for the government to change it, not for foreign companies to offer a donation. I suppose it does not help that rather than taking a broader view HMRC is obsessive about the minutiae, as anyone who completes a self-assessment tax return knows. It is not an organisation that has improved that much since it was created by the merger some years ago, although under its new leadership there are clear signs of some improvement.

Let us be perfectly clear, politicians and HMRC are a major part of the problem. For almost two decades each year they have enacted reams of badly worded and highly complex legislation with totally inadequate parliamentary scrutiny. No-one seriously believes that politicians understand the legislation they are enacting in anything more than a superficial way—they have neither the time nor training to do so. HMRC suggests the problem and then proposes the legislation that purports to solve it. Then when shortcomings inevitably appear,

the fault is attributed to those who identify them and not those who conceive them.

The most important lesson coming out of the Goldman Sachs saga is that it is in political hands to allow the tax office to fulfil its mission. The seeming leniency of the deal and cosiness between HMRC and taxpayer caused controversy. It is hard to avoid the conclusion that HMRC let political face saving as well as merit count. This is a flaw in which HMRC work – an unholy trinity of an overly complex tax code, a desire for negotiated settlements, and good relationships with big business combined with a confidentiality that prevents public scrutiny. Running a fair and efficient tax system requires will and resource. Both have been lacking and HMRC's political masters are to blame. Policy makers have improved the situation in recent years and an overhaul of the tax system has closed many loopholes. It will be interesting to see how the GAAR helps but it will some while before its impact is capable of being assessed.

I will quote from a FT editorial dated 14 October 2013 which is telling.

“Politicians of all parties also hound business to pay their fair share of tax, whatever that means. Lawmakers should set the legal framework while accepting that companies will always seek to pay no more tax than they can get away with – legally or in terms of reputation”. The editor went on to conclude:

“Taxation should not be a question of moral exhortation”. How right – at least the editor of the FT “gets it” and it is very disappointing that other newspapers seem more interested in a memorable headline which does nothing for a better understanding of tax avoidance and the complexities of tax.

HMRC has moved to a more aggressive strategy of litigating as least as long as there is an even chance of winning. Settlements are now vetted by at least two Commissioners not involved in the negotiations who should at least not be susceptible to capture. HMRC needs resources and backing to fight big battles but it must be seen to be impartial when it negotiates. For citizens to trust that HMRC is impartial when it negotiates there must be transparency that big companies are not getting sweetheart deals, so lawmakers must find ways for settlements to be more open to public scrutiny and the first report of the Tax Assurance Commissioner is an excellent start.

Should you, though, get a better service because you pay more tax? It would be a novel way to encourage growth but not one that sits comfortably with the rule of law.

HMRC are responsible for the collection of tax and must apply the law correctly. The Commissioners should not move away from this position merely because the result seems unfair or unreasonable. To do so would be contrary to the will of parliament as interpreted by the courts. There may though be circumstances where applying discretion would result in better management and in such circumstances the Commissioners can choose to apply discretion.

The current public perception is a belief that big business and the wealthy have access to “corridors of power” not available to the poor and smaller business that gives them a better deal when interacting with HMRC.

Government departments are entitled to make laws under powers delegated to them by Parliament, but laws sometimes conflict with one another. Where a regulation or a piece of tertiary legislation conflicts with the wider rule of law then clearly the latter must prevail. I will give an example:

Very recently the First-Tier Tribunal decided that HMRC had acted illegally when it issued a notice requiring three taxpayers to file their VAT returns online. The judge found that HMRC has breached their human rights and acted unlawfully under EU law, because HMRC failed to make exemptions for the elderly, the disabled or persons living too remotely for reliable internet access.

Two of the appellants had disabilities, all three ran businesses and filed their VAT returns on paper and on time for years and the third lived in a part of the country with no broadband. All three were aged and so learning to use a computer was difficult. Any decision as closely argued as this one must be persuasive and influential even if not technically binding. In essence what it says is that government departments cannot when exercising their functions simply disregard the laws of the land or the human rights of the taxpayer. They must obey the rule of law. Digital mandation was on the point of being forced through without regard for the needs of older or disabled people or those unable to access broadband. Fortunately in this country the courts provide a mechanism for correcting such abuses.

This case does though have lessons for us all, and not just HMRC, who I am hoping will sit around a table with the likes of LITRG and other interested parties to agree a sensible and workable solution and way forward. The alternative would be further expensive and hugely time consuming litigation the outcome of which would be uncertainty for a number of years.

Finally in the words of Edmund Burke “It is not what a lawyer tells me I may do; it is what humanity and reason and justice tell me I must do”.