FINANCE COMMITTEE CALL FOR EVIDENCE
REVENUE SCOTLAND AND TAX POWERS BILL
SUBMISSION FROM HEIDI POON

Introduction

1. This is a response to the invitation by the Finance Committee to submit evidence in respect of the Bill. This submission focuses on four aspects, namely:

   - Appointment to the Tribunals;
   - The General Anti-Avoidance Rule;
   - Mediation as an option to reviews and appeals; and
   - The financial implications of the Bill as estimated in the Financial Memorandum.

The response for these areas draws on my professional experience as a chartered accountant (ICAS) and a chartered tax adviser (CIOT), and my judicial experience as a member of the Tribunal system since 2000 (of the former VAT and Duties Tribunal and then the First-Tier Tax Tribunal). It has also been informed by research undertaken in connection with an LLM course on the Principles of International Tax Law, which I have been teaching as an external lecturer at the School of Law, the University of Edinburgh.

Appointment to the Scottish tax tribunals – Part 4 of the Bill

2. The present UK system has an additional qualifier to eligibility to include ‘any person who in the Lord Chancellor’s opinion has gained experience in law which makes them as suitable for appointment as if they satisfied these criteria’. The inclusion of this qualifier must have been for good reasons. The absence of similar provisions in the current Bill needs to be examined, that it is a deliberate exclusion for good reasons and not a mere omission. Furthermore, where Sch 2 Part 1, 1(3), 2(2), 3(2a) refer to ‘the person qualifies under this sub-paragraph if … the Scottish Ministers consider appropriate’, should it not be more appropriate for the Lord President of the Scottish Judiciary to assess judicial eligibility?

3. Apart from the qualifier, it is also stated in the Bill that ‘the Scottish Ministers must appoint’ (e.g. Sch 2 Part1 2(1)). Whether these judicial offices are best to be made by the Scottish Ministers (as representatives of the legislature) deserves some scrutiny. Constitutional democracies with a presidential system, such as the United States, hold ‘the separation of powers’ of the legislature, judiciary and executive as fundamental to good government. In contrast, the UK Constitution has sometimes been described as one where there is a ‘fusion of powers’. However, in the last decade, significant policy initiatives have resulted in a more formal separation of powers of the judiciary, most notably in the passing of the Constitutional Reform Act 2005, which has led to, inter alia, the creation of an independent Supreme Court, and the Judicial Appointments Commission (JAC).

4. The JAC was set up in April 2006 as an executive non-departmental public body sponsored by the Ministry of Justice under the Constitutional Reform Act in
order ‘to maintain and strengthen the judicial independence by taking the responsibility for selecting out of the hands of the Lord Chancellor’ (per JAC’s official website). There is an emphasis on JAC’s independence in selecting office holders for courts and tribunals, including the President, legal and ordinary members of the UK Tax Tribunals.

5. The Board of JAC Commissioners is drawn from a wide range of candidates, with the selection process conducted by the JAC itself, and appointment of Commissioners is on a fixed-term basis to ensure a regular turnover in its composition. It is not clear from the Bill whether the Scottish Ministers’ responsibility for appointment of Tribunal members is intended to be delegated to an independently constituted body like the JAC. It is an aspect worth considering, as fairness (and the perception of fairness), does depend on judicial appointments being independent of the legislature and above party politics. Whether Scotland votes ‘Yes’ or ‘No’, this Bill will become the founding legislation for a tax administrative system of either a new nation or a much more devolved tax regime, and the principle of separation of powers that lies at the heart of good government, should be part of that foundation.

The General Anti-Avoidance Rule – Part 5 of the Bill

6. The UK tax code has resisted having a statutory anti-avoidance rule until recently. On balance, a statutory GAAR is probably preferable so that judges can interpret the legislation for ‘acceptable’ or ‘unacceptable’ tax avoidance within the framework of a statutory GAAR, which in turn mitigates the perception that judges are making law by creating judicial anti-avoidance doctrines. However, it is not to say that a GAAR will create greater certainty for the taxpayer or for the Revenue to know what is acceptable tax planning and what is unacceptable tax avoidance. As Brian Arnold, Professor Emeritus of Tax Law and Senior Adviser to the Canadian Tax Foundation observes: both approaches [judicial and statutory] inevitably rely on the competence of the judges to parse the tax legislation rigorously, to understand the tax system as a whole and the purpose of its constituent elements and, finally, to have an appreciation of sophisticated commercial transactions.¹

7. In comparison with the UK GAAR, the Policy Memorandum (paragraph 70) has noted a finding from the Consultation that there is ‘no support expressed for a more widely-drawn provision’; that the ‘main attractions of the narrow focus were greater certainty for businesses and maintaining Scotland's attractiveness as a location for businesses and employment’. It is not immediately obvious how a narrowly focused GAAR will necessarily confer greater certainty. From the perspective of a taxpayer or a practitioner advising clients, ‘certainty’ sits on the level of interpreting the legislation to see how it may apply to the transaction concerned. However widely or narrowly a GAAR is drawn, that process of interpretation has to be gone through. John Tiley, a member of the Advisory Committee to the Aaronson Report on the UK GAAR, has remarked: What is clear is that, once a GAAR is introduced, the players (government and taxpayers alike) are still at the mercy of the courts.² Certainty is

more an issue about interpretation of the legislation as applied to the transaction concerned, than how widely or narrowly a GAAR is drawn.

8. It may be argued that a more widely drawn GAAR may result in a reduction in the number of Targeted Anti-Avoidance Rules (TAARs) being legislated in the Scottish tax regime, and that can only be a desirable ‘trade-off’ for having a more widely drawn GAAR. The UK tax code is one of the longest (if not the longest) in the world. It has grown considerably in complexity and volume in the period of the recent Labour Government, and the current legislation carries over 300 TAARs. There is a correlation between the growth in complexity and the increased number of TAARs. The average practitioners in Scotland will have to be conversant not only with the UK tax code but the Scottish tax legislation, and it will be a welcome prospect that the Scottish tax code can develop a more encompassing approach to anti-avoidance that may lead to a significant reduction in TAARs.

9. What would appear to be a pertinent concern in relation to the UK GAAR is how it may interact with the Scottish GAAR. Will the UK and Scottish GAARs deliver the same judicial outcome on an identical tax avoidance scheme subscribed to by two different taxpayers north and south of the Anglo-Scottish border? Does the UK GAAR determination have any force of precedent on the ruling of the Scottish GAAR? If Scotland has greater devolution instead of independence, can a transaction fall under both jurisdictions? If so, how will the two jurisdictions deal with the transaction? Are these issues covered by the existing terms of the proposed Bill?

10. The legislative structure (ie: the drafting format for the provisions) of the Scottish GAAR has much in common with the UK GAAR, notwithstanding the crucial difference in focus of the Scottish GAAR being on ‘avoidance’ to give it a wider scope than the construction of ‘abuse’ under the UK GAAR. Under s206(3) FA2013, the taxes to which the UK GAAR applies is listed; it is a restrictive list that excludes taxes and duties governed by Community Law, such as VAT and alcohol and tobacco duties. Compared with the structure of the UK GAAR, the equivalent place in the Scottish GAAR is taken by s57(3) of the Bill which defines ‘authorised officer’. In terms of the current state of the devolved tax regime, it can be deduced that the Scottish GAAR can only apply to LBTT and the Landfill tax. However, clarity in respect of which taxes the GAAR is to apply to, and the basis on which further taxes will be added is a relevant consideration at this stage given the foundational nature of the Bill.

---

3 The publisher Lexis Nexis states the 2012/13 Tolley’s Orange and Yellow Handbooks at 18,634 pages, excluding preliminary pages and indexes. Compared to 1996/97, when the Handbooks were at 4,998 pages long, the UK tax code has grown exponentially in size in 15 years. According to the breakdown analysis by the Office for Tax Simplification (OTS) in early 2012:

(a) The actual number of pages in the Yellow and Orange books 2010/11 (ignoring blank pages at the start and end and introductory pages), was 17,795 pages
(b) But excluding non-statutory material this becomes 11,173 pages
(c) Further excluding duplicated and repealed legislation the length is 6,960 pages
(d) Removing further duplications and some footnotes (they explain the criteria in the paper) the "actual substantive direct and indirect UK tax legislation is about 6,102 pages, or 34.3% of the Yellow and Orange Books."

The like-for-like comparison with the Lexis Nexis figures in the OTS’ breakdown is 17,795 for 2010/11. Lexis Nexis figures do not have the breakdown to arrive at the comparable figure under (d) for 6,102 pages. Data by courtesy of Andrew Pickering, Technical Director at CIOT.
11. Another omission noted is s212 FA2013 regarding ‘Relationship between the [UK] GAAR and priority rules’. In essence, s212 provides that the UK GAAR takes priority over any other part of the legislation applying to the taxes covered by the GAAR; (hence, referential to the list of taxes under s206(3)); ‘[t]his is so even if other legislation expressly states that it takes priority over anything else.’ Are there good reasons why priority rules are not relevant for LBTT and SLfT? Even if that is the case with the two devolved taxes, priority rules will surely become relevant when it comes to interacting with other UK tax legislation and with Double Taxation Agreements (DTAs) in a more devolved tax regime.

12. It is noted that DOTAS (Disclosure of Tax Avoidance Schemes) may be discussed at Stage II of the Bill’s progress through the Parliament. It is important to note that DOTAS helps to promote a culture of transparency between the tax authorities and the taxpayers and should be encouraged. DOTAS does not, however, confer any certainty on the taxpayer as regards whether a tax-avoidance scheme entered is effective in law. The benefit of DOTAS is that if a scheme is disclosed, then it can be examined by Revenue Scotland at an early stage and that in turn will help to mitigate the consequences of late payment of tax and penalties in the event that the scheme is found ineffective. In this regard, it is worth noting that HMRC has published recently (24 January 2014) the ‘Accelerated Payments Condoc’ in relation to the new powers sought to pursue upfront payments of tax where the tax is disputed under DOTAS or where GAAR may apply. Similar powers should probably be considered in conjunction with DOTAS, whether for this Bill or at a later stage, as the two aspects are likely to become administratively connected in the UK regime.

Mediation as an option to reviews and appeals – Part 11

13. For certain disputes, resolution by mediation can be much more cost-effective than settling the dispute through the tribunal route, and should be encouraged and properly supported. It is good to see that this intermediate stage of mediation (ie: between internal review and tribunal hearing) is being formalised by the Bill, and this would appear to be a new policy direction for Revenue Scotland compared with the current practice under HMRC. The type of disputes that lend itself well to mediation and arbitration is likely to concern the quantum of an assessment rather than a point of law. The assessment can be in relation to penalties and interest, or for under-declared tax assessed to the ‘best judgement’ of the investigating officer. The ‘best-judgement’ kind of assessment often involves lengthy hearing of evidence to ascertain how the officer has based his calculations in a situation where business records are inadequate to enable the quantum of an assessment to be categorically stated.

14. When a taxpayer wants to appeal to the Tribunal against the above-mentioned type of assessment, the amount of tax in dispute can often be disproportionate to the costs involved in giving the case a tribunal hearing and the delivery of a written decision. This type of cases also have a higher tendency of a last-minute withdrawal from a scheduled hearing date, making them an administrative inconvenience for the booking of venue and members’ time.

---

15. If the mediation process is actively taken up by taxpayers for the settlement of the type of disputes mentioned, it will lead to overall savings in resolving disputes if fewer cases are dealt with at the Tribunal level. However, for the mediation process to work effectively, the independence of the mediator from Revenue Scotland is paramount. The taxpayer has to perceive mediation as a cost-effective alternative to a fair hearing at the Tribunal. In other words, the mediation process must be akin to the tribunal procedure in terms of the independence of the arbitrator, and not be perceived as a second stage of Internal Review.

16. There is little in the Bill to suggest what the criteria for selecting a mediator are. In the Policy Memorandum at paragraph 124, it is stated that, ‘The mediator will be an independent third party appointed by Revenue Scotland.’ It is not clear to what extent the appointment being made by Revenue Scotland may compromise the taxpayer’s perception of the mediator’s independence. More details on how the independence of the mediator (eligibility, criteria of selection, terms of service) is assured will give this important policy direction more weight and facilitate its promotion to the public.

17. From what I understand, there is an In-Court Adviser and Mediation Service at Edinburgh Sheriff Court, with the Mediation Service being co-ordinated by Citizens Advice Bureau. It may be appropriate to evaluate whether the existing expertise from the Mediation Service at the Sheriff Court can help to develop the mediation service envisaged by Revenue Scotland.

The financial implications of the Bill – Financial Memorandum

18. The estimated costs for the various functions in relation to the Scottish Tax Tribunals are summarised in Table 12 of the Financial Memorandum. The notes in paragraph 54 afford some indication of the various parameters used in the costing, and they are read as not meant to be exhaustive to allow a complete tallying of the components to reach the total for each category. For example, in respect of the **Set-up of Tribunals**, the total of £120K includes IT system (£18K), recruitment and training (£36K), administrative staff during the set-up phase (£26K), leaving a balance of £40K budgeted but not detailed in the notes.

19. The total cost of £730K comprises:

   (i) the initial set up costs of £120K,
   
   (ii) lead-in period of running costs at £70K (a deduced break-down, not explicitly stated in the table), and
   
   (iii) 4 years of annual costs at steady state of £135K.

The following paragraphs concern the estimate of annual running costs at £135K.

20. In terms of **fixed** annual running costs, the principal category will be administrative staff costs. Presumably, the staff costs consist of one B1 and one A3 to continue after the set-up period for the 5-year budget. It is noted that premises costs do not form part of the annual costs as the Scottish Tribunal Service will administer both Tribunals and allow their premises to be used for hearing with no fees being charged.
21. The **variable** components of the annual running costs concern the hearing and decision process related to appeals. The principal variant comes from the number of appeals that will be heard, and it is budgeted on the basis that both Tribunals will sit for two days per month. Appeals for LBTT are more likely to be on a point of law involving a scheme and determination of a lead case will settle other similar cases stayed on the outcome of the lead case. With SLfT, appeals are more likely to concern the operational aspects of assessing the tax and will probably lead to more evidence-based type of hearing to determine the quantum of tax compared with cases concerning a point of law. Evidence-based type of hearing tends to be lengthier than cases seeking determination on a point of law.

22. Averaging over 4 years, to budget for both Tribunals to sit for 2 days per month is a fair estimate. What needs to be ascertained though, is whether the budget has allowed for associated fee costs for the presiding member in relation to the budgeted hearing costs of 2 days per month:

- Case-management hearing;
- Pre-case reading time prior to the actual hearing;
- Writing time in delivering the decision.

23. It is not uncommon for case-management hearing(s) to precede the actual hearing (the 2 days per month budgeted for). Case-management hearings (CMHs) are for the purpose of ensuring the actual hearing can be conducted efficiently by delineating the scope of evidence to be admitted, narrowing down the issues to be addressed at the actual hearing, and dealing with any preliminary issues which are related to an appeal but do not form part of the appeal. Written directions are issued to the parties following each case-management hearing by the presiding member. Each CMH and the writing time for directions can cost up to a day of the presiding member’s time. Some complex cases can take more than one case management hearing, and the fee costs need to be factored into the equation in respect of CMHs. The general guideline for writing up decisions is every day of hearing is one day of writing time. For complex cases, additional time for pre-case reading and writing time of 1.5 days to a day’s sitting can be claimed with leave from the President. At the very minimum, therefore, there are the two days per month of writing time at the same rate as sitting time for the presiding member to be included in the budget.

24. Apart from the fee costs of the presiding member outwith the actual hearing days, the current system also allows for expenses incurred by tribunal members (presiding and panel) to be reimbursed in relation to travel expenses for the days of hearing, and in some circumstances, subsistence and accommodation if hearings take place at venues that involve overnight stay.

25. It is worth examining whether the costing of £135K annual running costs have covered all the necessary constituent elements, especially in respect of the variable component for the time incurred by the presiding member at the pre-hearing and post-hearing stages that will be translated into fees. Furthermore, for a 5-year budget, it may be prudent to build in an element of inflationary increase for the overall costing.