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Section 161 and Schedule 19: large businesses: tax strategies and sanctions for persistently unco-operative behaviour: further commentary

Introduction

In their note[1] in this Issue, Kevin Costello and Richard Stratton explain how the Finance Act 2016 (FA 2016) introduces the latest in a growing list of creative measures intended to address tax avoidance by large businesses.[2] This note seeks to add some further context to these provisions as part of the framework for governance of large business taxation in the UK. As set out by Costello and Stratton in their note, section 161 and Schedule 19 FA 2016 impose a requirement on large businesses to publish a tax strategy and introduce a "special measures" regime for persistently uncooperative behaviour. These measures were first proposed in a Consultation Document of 22 July 2015 (Consultation Document),[3] together with a proposal for a voluntary "Code of Practice on Taxation for Large Business". Following the consultation, the latter proposal was transformed into a proposal for a "Framework for Cooperative Compliance",[4] intended for a soft launch in April 2016, though the launch has been delayed.[5] The FA 2016 measures rely heavily on reputational pressures as a mechanism but backing these soft pressures by legal sanctions prior to any non-compliance is not entirely consistent with a co-operative compliance model. To the extent that these provisions escalate counteraction for persistent non-compliance through special measures, however, they do utilise the standard regulatory compliance pyramid.[6] One of the writers' key criticisms is that the measures backed by sanctions may not be narrowly enough targeted, despite Government reassurances to the contrary. Furthermore, the special measures raise some concerns. Whilst unlikely in practice, technically they could result in meaningful consequences being imposed on a business as a result of activity which is ultimately found by a court to be in line with the law.

Background

The measures are presented as part of the fight against tax avoidance, incentivising the "right behaviour" and ensuring that "aggressive tax planners" are tackled in order to create and maintain

[1] K. Costello and R. Stratton, "Section 161 and Schedule 19: large businesses: tax strategies and sanctions for persistently unco-operative behaviour" [2016] BTR 646.

[2] The Large Business Directorate includes the largest 2,000 or so businesses.

[3] HMRC, *Improving Large Business Tax Compliance* (22 July 2015) (Consultation Document), available at: *https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/447313/Improving_Large_Business_Tax_Compliance.pdf* [Accessed 26 November 2016]. Part of the analysis in this note was first presented as a response to the Consultation Document in J. Vella and J. Freedman, *Response to Consultation Document "Improving Large Business Tax Compliance" published by HMRC on July 22, 2015* (Oxford University Centre for Business Taxation, November 2015), available at: *http://www.sbs.ox.ac.uk/sites/default/files/Business_Taxation/Docs/Publications/Policy_Papers/response-to-hmrc-consultation-a.pdf* [Accessed 23 November 2016].

[4] HMRC, *Improving Large Business Tax Compliance* (9 December 2015) (Summary of Responses).

[5] The writers do not discuss the proposal for a "Code of Practice on Taxation for Large Business" in this note. The writers discuss the expected Framework for Cooperative Compliance briefly in the last section.

[6] I. Ayres and J. Braithwaite, *Responsive Regulation: Transcending the Deregulation Debate* (Oxford: OUP, 1992).

a level playing field for the vast majority of businesses.[7] They were put forward as a continuation of the co-operative compliance mode of working. These objectives chime with the current political climate and have been presented carefully in such a way as to appear beneficial both to the public and to the majority of businesses. It is necessary, however, to examine the detail of the measures to evaluate whether they achieve their objectives in the long term. A system based on trust, such as the co-operative compliance programme, can be undermined by the introduction of certain types and levels of sanction: the balance and dynamic is a complex one.[8] Tax morale amongst business, but also more generally, could suffer in the long run from taking a short-term view. It is on good tax morale that all tax systems rely to achieve high levels of voluntary compliance from the vast majority of taxpayers, so that threats to that relationship would be to the detriment of long-term revenue collection.

Much good work has been done to establish the existing co-operative compliance regime and this is a positive development for business, HMRC and the wider public, in that it increases the ability of the tax administration to collect revenue efficiently. Surveys and analysis undertaken by the writers suggest that this regime has on the whole worked well to improve transparency, speed of resolution and understanding of commercial issues amongst the population covered by the Large Business Service.[9] However the current climate of public lack of trust in business and intense criticism of HMRC handling of large business tax administrations arguably threatens the relationship. Indeed some critics would argue that the relationship between HMRC and large business is too cosy and this might be a trigger for these measures. There is a risk that this reaction could lead to provisions that undermine the concept of relationships based on trust, which could actually reduce the amount of information coming to HMRC.

Tax strategies

Businesses are required by FA 2016 to publish a tax strategy on the internet[10] if in their previous tax year they have either a turnover above £200 million or a balance sheet over £2 billion.[11] The content that must be included in the published strategy is prescribed by FA 2016[12] and failure to comply results in a penalty.[13]

[7] D. Gauke, "Foreword to Consultation Document", above fn.3, and D. Gauke's speech at the HMRC annual stakeholder conference, 16 July 2015, available at: *https://www.gov.uk/government/speeches/david-gaukes-speech-at-hmrcs-annual-stakeholder-conference* [Accessed 26 November 2016]. See also Summary of Responses, above fn.4, 4.

[8] K. Gangl, E. Hofmann, M. Pollai and E. Kirchler, "The Dynamics of Power and Trust in the 'Slippery Slope Framework' and its Impact on the Tax Climate" (2012), available at: *http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2024946* [Accessed 26 November 2016].

[9] See J. Freedman, F. Ng and J. Vella, *HMRC's relationship with large business* (2014) Oxford University Centre for Business Taxation Report, available at: *http://www.sbs.ox.ac.uk/sites/default/files/Business_Taxation/Docs/Publications/Reports/HMRCs-relationship-with-business.pdf* [Accessed 26 November 2016].

[10] The strategy must be available free of charge until the following year's strategy has been published. For groups and sub-groups, the combined totals of all the relevant bodies are taken into account: FA 2016 Sch.19, paras 16, 19, 22, 25.

[11] FA 2016 Sch.19, paras 2–15. The writers here focus on the broad policy objectives of this measure. The writers refer to "business" throughout and do not distinguish between cases where the entity which is subject to the legislation is a company, partnership, a group or a sub-group. Technical considerations surrounding this aspect of the measure are discussed by Costello and Stratton, above fn.1.

[12] FA 2016 Sch.19, paras 17, 20, 23, 25.

[13] FA 2016 Sch.19, paras.18, 21, 24, 25.

Value in having a tax strategy

There could be some benefits in companies adopting a formal tax strategy. In a survey undertaken by the writers in 2008[14] a number of tax directors expressed the view that such strategies could focus the mind on how tax and tax risk is managed within a company. Clearly, such strategies, if approved by the Board of Directors, could also ensure that tax issues are discussed at the highest governance levels within the company. The Consultation Document had suggested making a member of the Board of Directors "responsible for owning and signing off the tax strategy".[15] This has now been abandoned as the Government accepted that accountability should rest with the Executive Board as a whole.[16]

On the other hand, the discussion of strategy does not, of course, determine the outcome of those deliberations. In the current climate one would expect many directors to be keen to avoid reputational risk, but this will depend on the type of firm concerned. In our 2008 survey we reported that

> "… a few interviewees noted that board engagement can have the opposite effect [that is, can encourage tax minimization attempts] as a result of the so-called 'golf course syndrome'".[17]

In other words, in some cases the Board of Directors has been keener to minimise tax than the tax advisers and directors were. This could be partly driven by investor preference on these issues. A recent survey by Allen & Overy in fact explained that

> "[w]hile some investors are most focused on transparency, reputation and ensuring stability of the tax position, for many it is simply a question of minimising leakage on their returns".[18]

Nevertheless, it does seem likely that the publication of a tax strategy will focus the minds of the Board on reputational issues and advisers will no doubt seek to take the opportunities this exercise offers to make sure issues have been full considered. Indeed, no doubt advisers will be using this as an opportunity to advise on tax matters more generally.[19]

The content of the tax strategy

A clear weakness with tax strategies is that they can be drafted in carefully selected vague language that is open to interpretation. Schedule 19 FA 2016 partly seeks to address this concern by prescribing the following content, which is then further elaborated in HMRC's June 2016 Guidance, *Large businesses: publish your tax strategy* (HMRC Guidance): the approach to tax

[14] J. Freedman, G. Loomer and J. Vella, "Corporate Tax Risk and Tax Avoidance: New Approaches" [2009] BTR 74.
[15] Consultation Document, above fn.3, para.2.24.
[16] Summary of Responses, above fn.4, paras 3.6 and 3.10.
[17] Freedman, Loomer and Vella, above fn.14, 85.
[18] Allen & Overy, *Negotiating the minefield: challenges facing the corporate tax function* (October 2015), available at: *http://www.allenovery.com/SiteCollectionDocuments/Global_Tax_Challenges%20facing%20the%20corporate%20tax%20function.pdf* [Accessed 26 November 2016].
[19] See for example Ernst & Young LLP (EY), *Tax strategy publication: Are you ready?* (2016), available at: *http://www.ey.com/Publication/vwLUAssets/EY-tax-news-2016-07-05-01/$FILE/EY-tax-news-2016-07-05-01.pdf* [Accessed 26 November 2016]; Deloitte, *Tax strategies in the spotlight* (2016), available at: *https://www2.deloitte.com/uk/en/pages/tax/articles/tax-transparency.html* [Accessed 26 November 2016].

risk management and governance in relation to UK taxation[20]; attitude to tax planning so far as it affects UK taxation[21]; the level of risk in relation to UK taxation the business is prepared to accept[22]; and the business's approach towards its dealing with HMRC.[23]

Prescribing the content of the strategies in this way may not have the effect of turning strategies into meaningful documents which open up their tax modus operandi to the world at large. The information on tax risk management and governance might be useful and one would expect some interesting information to be gleaned from that, but information under the other three headings is likely to become standardised and, to some extent, uniform.[24] One can expect many large businesses to fulfil their requirement to provide information on their attitude to tax planning by including statements along the following lines: "we do not undertake artificial tax planning which is devoid of commercial reality", "we aim to pay taxes where value is created as due under the national law and international tax treaties" and "we respect both the letter and the spirit of the law". Each of these statements can allow behaviour of varying degrees of aggressiveness depending on the interpreter's particular interpretation. Such statements disclose very little of interest to readers and the companies adopting them will not necessarily feel any more constrained in their tax planning behaviour with these statements than without them. For this reason, this measure may well not produce its desired effect, particularly with the most recalcitrant firms which are those the Government is concerned to target. It may be that the Government is relying on pressure from the media and NGOs, and the influence of advisers, to put pressure on business to make this exercise more meaningful. Again, this may be effective with some businesses, but these are likely to be those that are already complaint. The most recalcitrant firms will be those that also resist such pressures.

The Consultation Document had suggested a stronger mechanism to ensure that the statements included in the strategies "are seen to be meaningful".[25] Tax strategies could include factual information to demonstrate how the tax strategy was being applied in practice. This has been dropped as a result of the consultation, partly in response to concern that it would lead to the publication of commercially sensitive information.[26]

The Consultation Document had proposed a fifth area to be covered by the tax strategy

[20] HMRC, *Guidance: Large businesses: publish your tax strategy* (HMRC Guidance) (24 June 2016), available at: *https://www.gov.uk/guidance/large-businesses-publish-your-tax-strategy* [Accessed 26 November 2016] explains that this should include the tax risks linked to the business's size, complexity and any changes to the business. Information on governance arrangements should include details on how the business's tax risk is managed, a high level description of key roles and their responsibilities, information on the systems and controls in place to manage tax risk, and details on the levels of oversight of the business's board and its involvement.

[21] HMRC Guidance, above fn.20, explains that if a business has a code of conduct it should include details of it. It should also include information about why a business might seek external tax advice, if any; an outline of its tax planning motives and the importance of each to its tax strategy.

[22] HMRC Guidance, above fn.20, explains that this should include if the business's internal governance has rigid levels of acceptable tax risk and, if so, it should explain how it is influenced by stakeholders.

[23] HMRC Guidance, above fn.20, explains that this should include how the business meets their requirement to work with HMRC and how it works with HMRC on: current, future and past tax risks; tax events; and interpreting the law.

[24] See Ernst & Young LLP (EY), above fn.19, 4: "Our approach will help to ensure that … you benchmark well to what your peers publish".

[25] Consultation Document, above fn.3, para.2.29.

[26] Summary of Responses, above fn.4, para.3.19.

> "[w]hether the UK Group has a target Effective Tax Rates (ETR), what it is, and what measures the business is taking to maintain or reach this target ETR".[27]

Respondents to the consultation were "in general agreement" with the Government on the contents of the tax strategy, except for this item, which was thus dropped.[28] This was sensible as it would have been very problematic partly because such measures are particularly open to misunderstanding as there may be many different reasons for the ETR in any given year. As it turned out, the majority of business respondents to the consultation did not have such targets and where they existed it was noted that they may be commercially sensitive information and they would rarely be UK specific.[29] Therefore this was unlikely to be workable or useful. However there is a new provision, inserted as an amendment that, most unusually, was accepted by the Government, that the Treasury may by regulations require a country-by-country report to be included in the group tax strategy.[30]

Publication of the strategy and the reputational mechanism

The new tax strategy provisions go beyond co-operative compliance in the relationship between the revenue authority and the tax payer, by requiring public disclosure of the strategy. This will include country-by-country reporting if the Treasury makes regulations under paragraph 17(6) of Schedule 19 FA 2016. The Consultation Document sets out the underlying thinking behind this measure. It is based on the optimistic view that not only will businesses write meaningful strategies which the public will be able to successfully decode but also that this will trigger a reputational mechanism through which a change in corporate behaviour will be achieved:

> "Our most recent research into large businesses (also published today) tells us that the degree of codification and content of a tax strategy are 'clear indicators of aggressiveness' in tax planning. The research found that 'businesses with a greater appetite for risk tend[ed] not to have written (or published) tax strategies, while those with lower risk-appetite tended to have more formalised strategies.' This research also shows that reputational concerns can influence the attitudes of large businesses and encourage them to pursue less aggressive tax planning arrangements."[31]

[27] Consultation Document, above fn.3, para.2.28.
[28] Summary of Responses, above fn.4, paras 3.2 and 3.12.
[29] Summary of Responses, above fn.4, para.3.12.
[30] FA 2016 Sch.19, para.17(6). FA 2016 Sch.19 para.17(7) gives "country-by-country report" the meaning it has in the Taxes (Base Erosion and Profit Shifting) (Country-by-Country Reporting) Regulations 2016 (SI 2016/237). This is a strange place to find this provision, since its proponents argue that it is accounting data and not tax data. R.J. Murphy, *European Union: Country-by-Country Reporting Data—Accounting or Tax Information?* (2016), available at: *http://www.taxresearch.org.uk/Blog/2016/11/18/european-union-country-by-country-reporting-data-accounting-or-tax-information/* [Accessed 26 November 2016].
[31] TNS, *Exploring Large Business Tax Strategy Behaviour*, TNS BMRB Final Report HMRC Research Report 363 (July 2015), available at: *https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/444898/HMRC_Research_Report_363_-_Exploring_Large_Business_Tax_Behaviours.pdf* [Accessed 26 November 2016]. This was a survey from a sample drawn by HMRC of 35 individuals with a strategic decision making role in tax in large companies from the LBS population. 12 were higher risk, seven medium risk and 16 lower risk. This is a small and not necessarily representative sample upon which to base a new legislative requirement.

This appears to confuse correlation with causation. It may be true that companies that have a lower risk appetite tend to have formalised tax strategies, however, it does not follow, as a matter of logic, that requiring companies with a higher risk appetite to adopt formal tax strategies, without more, will induce them to reduce their risk appetite. Setting this to one side and even assuming that the public will glean meaningful information from the strategies, it remains unclear whether the reputational mechanism at the heart of this measure will be effective. For this mechanism to work consumers and investors should change their consumption or investment behaviour in response to concerns about the companies' tax affairs. It is not clear that they will, or more precisely, whether a number sufficient to make a difference will. Furthermore, even if such reputational mechanisms did work they would apply differentially across sectors. In particular, they can be expected to be even less effective in sectors which are not consumer facing.

It may be that the process of discussing the strategy is helpful, particularly at a board level, and revealing it to HMRC could then be a requirement to ensure that this discussion had taken place, but this does not of itself demand publication to the public. It is not clear that such a requirement will result in the development of a serious strategy rather than a public relations document. An important point to note is that the publication requirement could even reduce the usefulness of this document by inhibiting inclusion of certain material. Transparency does not always increase understanding and trust.[32] Since, as we have seen, many businesses will employ experts to advise on content and presentation, it seems that this measure will create work for tax advisers and PR firms, but the likely impact on the amount of tax collected is less clear.[33]

Consequences

Failure to publish a tax strategy correctly and in time will be met with a penalty.[34] Businesses are also liable to penalties if their strategies do not remain accessible free of charge until publication of their next strategy. The application of the tax strategy cannot lead to a penalty. It merely forms part of the business risk review process between HMRC and the large business.[35] One can only hope that this or future governments do not fall into the temptation of reversing this decision. It would be very worrying indeed if businesses could be penalised if in HMRC's view they do not adhere to their strategy. Given that HMRC have in the recent past used the fact that a bank had signed up to the Bank Code of Conduct as justification for the introduction of retrospective legislation,[36] one also hopes that tax strategies are not used in the same misguided manner.

[32] J. Freedman, "Restoring Trust", *Tax Adviser*, 22 June 2016, available at: *http://www.taxadvisermagazine.com/article/restoring-trust* [Accessed 26 November 2016].
[33] See above fn.19.
[34] The penalties are: up to £7,500 for the first six months, a further penalty of up to £7,500 for six to 12 months and £7,500 every additional month for periods over 12 months.
[35] Consultation Document, above fn.3, paras 2.33 and 2.34. Summary of Responses, above fn.4, para.3.22.
[36] See J. Treanor, "Barclays £500m tax loophole closed by Treasury in rare retrospective action", *Guardian*, 28 February 2012, available at: *http://www.guardian.co.uk/business/2012/feb/28/treasury-closes-barclays-tax-schemes* [Accessed 26 November 2016]; and "Barclays Bank told by Treasury to pay £500m avoided tax", *BBC News*, 29 February 2012, available at: *http://www.bbc.co.uk/news/business-17181213* [Accessed 26 November 2016].

Special measures

Intended scope

Although it probably received the least attention in the debates around the consultation, the "special measures" regime may be the most worrying measure in concept because it involves the most serious sanctions. The Consultation Document and surrounding discussion were at pains to emphasise that this measure narrowly targets the "very small"[37] number of large businesses, even a "handful",[38] that persistently undertake aggressive tax planning, or refuse to engage with HMRC in an open and collaborative manner. This suggests, as predicted by these writers in previous work,[39] that the benefits of being "low risk" would not suffice to make some of the most recalcitrant companies change their tax planning behaviour. It is consistent with responsive regulation theory to target those recalcitrant taxpayers with a stick rather than a carrot. It is reassuring to the majority of companies, which are broadly compliant in any event, to be told that these measures are aimed only at the more extreme end of the spectrum. But these measures are on the statute book and the underlying assumptions give rise to concerns. Provisions intended to apply narrowly can be found to affect taxpayers beyond their original intended scope and can also be used more extensively in the future, when their origins might have been forgotten.[40] This is one reason why designing safeguards which strike the right balance is of critical importance.

The special measures regime in outline

HMRC's December 2015 policy paper *Tax administration: large business special measures regime* sums up the mechanics of this rather tortuous regime in the following terms:

> "where a designated HMRC officer determines that a business is at risk of entering special measures, they will be notified of the specific behaviours putting them at risk of entry into special measures, and have twelve months to make improvements.
>
> After twelve months the position will be reviewed and the designated HMRC officer may recommend that the business has improved behaviours and is no longer at risk of special measures. Equally HMRC's designated officer may notify the business that no improvement has been made and for reasons of the behaviours set out in the notice, the business will enter special measures. No sanctions apply at this stage.
>
> A business will remain in special measures for a twenty four month period before a review. If any further examples of the evidence for entry into special measures occur then sanctions may be triggered. The review period can be brought to a conclusion earlier with the agreement of both parties.

[37] Consultation Document, above fn.3, para.4.3. See also para.4.5.
[38] Summary of Responses, above fn.4, para.5.1.
[39] Freedman, Loomer and Vella, above fn.14, 88–89.
[40] Similar reassurances were given in respect of the diverted profits tax, but anecdotal evidence suggests that that provision is being used more widely than was anticipated.

> Sanctions may include removing the defence of reasonable care in relation to behaviours previously notified of, and/or withdrawing certainty by removing access to non-statutory clearances.
>
> Following the twenty four months, after a review, if there is no further evidence of the behaviours set out on entry, the business will exit special measures. If the behaviours causing original entry still exist, the special measures period will be extended for a further twenty four months and the business may be considered for being named as being in special measures."[41]

Warning notices

The mechanics set out in outline here are covered in greater detail in the note by Costello and Stratton.[42] The regime is set in motion when a designated officer[43] issues a warning notice to a business.[44] This is done if the officer considers the business[45] to have satisfied the following three criteria (three criteria): 1. it has "persistently"[46] engaged in uncooperative behaviour; 2. "some or all of that uncooperative behaviour has caused there to be, or contributed to there being, two or more significant tax issues … which are unresolved"; and 3. "there is a reasonable likelihood of further instances of the group engaging in uncooperative behaviour in a manner which causes there to be, or contributes to there being, significant tax issues".[47,48]

The key concept in this regime is that of "uncooperative behaviour". A business is deemed to have engaged in "uncooperative behaviour" in one of two situations.[49] The first situation is if the business "has delayed or otherwise hindered HMRC in the exercise of their functions" (the behaviour condition).[50] The legislation lists factors which may indicate behaviour of this kind, including the extent to which HMRC have had to use their statutory powers to obtain information from the business, the accuracy of the documents submitted to HMRC, and, worryingly, the extent to which the business "relied on interpretations of legislation relating to UK taxation which, at the time, are speculative". Such interpretations arise "if it is likely that a court or tribunal would disagree with it".[51] The designated officer thus not only has to take a view on the

[41] HMRC, *policy paper: Tax administration: large business special measures regime* (9 December 2015), available at: *https://www.gov.uk/government/publications/tax-administration-large-business-special-measures-regime/tax-administration-large-business-special-measures-regime* [Accessed 26 November 2016].
[42] Costello and Stratton, above fn.1.
[43] Defined in FA 2016 Sch.19, para.53.
[44] FA 2016 Sch.19, para.41.
[45] The regime applies to groups, sub-groups, companies and partnerships with the necessary modifications. To keep the discussion simple the writers here consider the basics mechanics of the regime as it applies to these different types of entities.
[46] FA 2016 Sch.19, para.36(4) explains that references to "doing something 'persistently' include doing it on a sufficient number of occasions for it to be clear that it represents a pattern of behaviour". Beyond the subjectivity inherent in this test, it is unclear why, by adding the word "include" in this definition, the legislation leaves the door open for persistent behaviour to arise even beyond the circumstances set out in the definition.
[47] A significant tax issue is defined as one where there is a disagreement or there is likely to be a disagreement about an issue affecting the tax due, which has or could be referred to a court or tribunal and the difference in the view of HMRC and the taxpayer is or is likely to be not less than £2 million: FA 2016 Sch.19, para.39.
[48] FA 2016 Sch.19, para.35.
[49] FA 2016 Sch.19, para.36.
[50] FA 2016 Sch.19, para.37.
[51] FA 2016 Sch.19, para.37(3).

interpretation of the law, but he also has to take a view on the likelihood that the interpretation offered by the business will be accepted by the court or tribunal. He need not believe (subjectively) that this is "almost certain" or "highly likely". He need only believe that this is "likely"—not a high threshold at all. Independently of this issue, for the purpose of the argument set out below the writers need only note that this undoubtedly allows the criterion to be engaged in situations where the view taken by the business is eventually accepted by the court or tribunal.

The second situation is where a tax avoidance scheme is used that either a designated officer is seeking to counteract using the general anti-abuse rule (GAAR) or is disclosable under the disclosure of tax avoidance schemes (DOTAS) regime.[52] These triggers could operate in situations where a scheme is eventually found to be compliant with the law by a court or tribunal. Indeed, HMRC's guidance on DOTAS explicitly states that "[o]n its own the disclosure of a tax arrangement has no effect on the tax position of any person who uses it"[53] and "[u]nder the rules, a tax arrangement may need to be disclosed even if HMRC is already aware of it or it is not considered to be avoidance".[54] It is a matter of some concern that both the GAAR and DOTAS regimes are being used here (and elsewhere in this and other legislation) for purposes for which they were not designed. By overstretching these provisions for these new purposes, they may end up being narrowly construed to protect a taxpayer or otherwise constrained, so that this could become counter-productive. It is worrying that a company could find itself on notice for entering into a number of tax arrangements that eventually are upheld as effective by the courts. However, as the legislation stands, this is a possibility, however unlikely it may be in practice.

Special measures regime, confirmation notices and sanctions

The behaviour and expected behaviour described above, only puts the company in question on notice. It then has 12 months to improve its behaviour.[55] If it has not improved by then, it will enter the special measures regime, after which it will be at risk of triggering sanctions.[56]

A designated officer can serve a business with a special measure notice 12 months after a warning notice was given and not later than 15 months from such notice, if it continues to fulfil the three criteria mentioned above. The special measures notice must set out the officer's reasons for this decision.[57] The same points continue to apply about the nature of those criteria, and at this stage the consequences become very serious. Once in the regime, in specific circumstances, the company will lose its ability to rely on the defence of "reasonable care" within Schedule 24 to the Finance Act 2007. Inter alia this means that the company cannot fall back on reliance on

[52] FA 2016 Sch.19, para.38.
[53] HMRC, *Guidance: Disclosure of tax avoidance schemes (DOTAS)*, available at: *https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/560047/dotas-guidance.pdf* [Accessed 26 November 2016], para.2.2.
[54] HMRC, DOTAS, above fn.53, para.2.3.2.
[55] The warning notice may also be withdrawn at any time by the officer, and, in any event expires after 15 months. FA 2016 Sch.19, para.41(3).
[56] FA 2016 Sch.19, para.42.
[57] FA 2016 Sch.19, para.42(5).

tax advice.[58] The taxpayer may then be charged penalties on the basis that the behaviour was at least careless, if not deliberate, meaning that this status has serious consequences.[59]

The removal of a reasonable care defence[60] shows a mistrust in the courts, which can hear all the evidence and decide whether there was reasonable care taken or not. If the problem at the root of this relates to the use of legal advice as a shield, then this needs to be tackled for all taxpayers rather than removing the entire defence from a class of taxpayers.

Businesses can also be named and shamed if they continue to fulfil the three criteria mentioned above 24 months after the special measures notice is issued but not later than 27 months from this date[61] and the officer issues a confirmation notice.[62] One can doubt, as mentioned above, whether the reputational mechanisms at the heart of the naming and shaming sanction will work as expected, particularly with the small group of hardened businesses the measure is meant to target. However, as the law is drafted, there is a possibility that these measures will in time be employed beyond this narrow group and the reputational mechanisms might work in some cases, particularly with customer facing businesses. This would again mean that the special measures regime can lead to meaningful consequences for persistent behaviour which clashes with HMRC but which is eventually found to be compliant with the law by a court or tribunal.

Conclusion

As mentioned above, these provisions follow the prescriptions of the standard regulatory compliance pyramid to the extent that they escalate counteraction for persistent non-compliance. However, concern remains as to whether they will be employed beyond the most recalcitrant group of non-compliers right at the top of the pyramid. More troubling, this is a further measure which technically allows the boundary drawn by law to be replaced by the boundary drawn by HMRC, albeit in limited and controlled circumstances. As shown, businesses might be subject to meaningful consequences under the regime on the basis of persistent adoption of schemes which are disclosable or based on an interpretation of the law which is deemed by HMRC as "speculative", even if a court might find the scheme to be in line with the law. The writers do not expect this to be a real danger in practice at present for many companies, but they do believe that the notion that special treatment can be aimed at those entering into schemes—even persistently—that might still be upheld by the courts, could be in tension with the rule of law.

Framework for Cooperative Compliance

As seen, the Consultation Document put forward a third proposal, that for a voluntary Code of Practice on Taxation for Large Business. The "overwhelming theme of responses received"

[58] This aspect of the FA 2007 Sch.24 reasonable care defence is perceived as a problem by HMRC—see too HMRC consultation document, *Strengthening Tax Avoidance Sanctions and Deterrents* (17 August 2016), available at: *https://www.gov.uk/government/consultations/strengthening-tax-avoidance-sanctions-and-deterrents-discussion-document* [Accessed 26 November 2016], para.3.5 and following.
[59] FA 2016 Sch.19, para.47.
[60] Respondents to the consultation "generally raised concerns" about this sanction, but this did not alter the Government's view on the matter. Summary of Responses, above fn.4, paras 5.39 and 5.41.
[61] FA 2016 Sch.19, paras 43 and 44(1).
[62] FA 2016 Sch.19, para.44(2). The officer must set out the reasons for his decision: FA 2016 Sch.19 para.44(5).

during the consultation was that it lacked mutuality,[63] in that it spelled out HMRC's expectations of large businesses but not large businesses' expectations of HMRC. HMRC have now made it clear that the Code was merely meant to codify the characteristics of a "low-risk" co-operative relationship. The proposal is now for a "Framework for Cooperative Compliance" which will

> "set out a common set of principles and ways in which large businesses and HMRC can work together to ensure that the right tax is paid at the right time".[64]

The framework is expected to be launched soon. The concept of a framework that is imposed on businesses is different from the operation of co-operative compliance in other jurisdictions, where there is usually an agreement between the company and the revenue authority, tailored to the particular situation.[65] Nevertheless this reflects the way in which risk rating works in the UK. A major issue for respondents to the consultation was the reference in the proposed Code, now a Framework, to "intentions of parliament" and "spirit of the law". Respondents felt that they should be able to follow the legislation, which should be "clear in and of itself".[66] Updated guidance on the Bank Code published in November 2016,[67] explains that HMRC view the spirit of the law as being synonymous with following the intentions of Parliament and sets out HMRC's understanding of the intention of Parliament in more subtle terms than in the past. This may help to make the proposed Framework more acceptable, despite the fact that it still goes beyond the law in its expectations, thus giving discretion to HMRC officials to require a company to refrain from making what HMRC see as speculative arguments, which are nevertheless arguments that could be upheld by the courts.

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[63] Summary of Responses, above fn.4, para.4.3.
[64] Summary of Responses, above fn.4, para.4.5.
[65] See E. van der Enden, et al., "Netherlands" in A. Bakker and S. Kloosterhof (eds), *Tax Risk Management* (Amsterdam: IBFD, 2010) and other chapters in that book.
[66] Summary of responses, above fn.4, para.4.16.
[67] *The Code of Practice on Taxation for Banks—consolidated guidance*, available at: *https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/566119/The_Code_of_Practice_on_Taxation_for_Banks___HMRC_consolidated_guidance.pdf* [Accessed 26 November 2016].

Disclosure; Large businesses; Penalties; Reporting requirements; Tax avoidance

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