These notes refer to the Finance Act 2010 (c.13) which received Royal Assent on 8 April 2010

FINANCE ACT 2010

EXPLANATORY NOTES

INTRODUCTION

Section 56 and Schedule 17: Disclosure of Tax Avoidance Schemes

Summary

1. Section 56 and Schedule 17 amend provisions in Part 7 of the Finance Act (FA) 2004 (Part 7), which require promoters and users of certain tax avoidance schemes to provide information about them to HM Revenue & Customs (HMRC); and section 98C of the Taxes Management Act 1970 (TMA), which provides for penalties for non-compliance with those duties. In particular, they amend the definition of "promoter" and the time at which the duty to disclose a scheme arises; require promoters of notifiable schemes periodically to provide lists of clients; empower HMRC to require intermediaries who are concerned in the marketing of a scheme, but who are not promoters, to identify the promoter; and substantially increase the penalties available to the Tribunal where a scheme is not disclosed as required.

2. Powers are also taken to vary the amounts of penalties should that appear necessary. All regulations varying penalty amounts are subject to an affirmative resolution of the House of Commons.

Details of the Schedule

3. Paragraph 1 states that Part 7, which comprises sections 306 – 319 of FA 2004 and contains the primary legislation in relation to the disclosure regime, is amended by the paragraphs which follow.

4. Paragraph 2 amends section 307 of FA 2004, which defines "promoter" so that the definition includes persons who market fully designed schemes in order to solicit clients to whom they will sell the scheme. In practice promoters often market schemes through introducers, persons whose role is to introduce potential clients to the promoter, and section 307 is also amended to include a definition of "introducer".

   a. Sub-paragraph (2) inserts a new sub-paragraph (ii) in section 307(1)(a), providing that, in addition to the existing criteria, a person ("P") is also a promoter if he has made "a firm approach" to another person ("C") relating to a scheme with a view to P making the scheme available for implementation by C or any other person. In practice C may be an introducer or a potential client.

   b. Sub-paragraph (3) makes a consequential amendment to subsection (1)(b).

   c. Sub-paragraph (4) inserts a new subsection (1A) in section 307, defining "introducer". A person is an "introducer" if he makes a "marketing contact" with another person in relation to a scheme.

   d. Sub-paragraph (5) inserts new subsections (4A) to (4C) which respectively define "makes a firm approach", "makes a marketing contact" and "substantially designed":

i. A person "makes a firm approach" if he "makes a marketing contact" at a time when the scheme has been "substantially designed";

ii. A person makes a marketing contact if he communicates to another person information about a scheme, including an explanation of the tax advantage, with a view to that person or any other person implementing the scheme. This covers communication of a general nature both to persons who may wish to use the scheme, and to intermediaries or introducers who may in turn communicate it to a potential user;

iii. A scheme is "substantially designed" if the development of its design has reached the stage where it would be reasonable to assume that the transactions a person would enter into, should the person decide to implement the scheme, would not be substantially different from those envisaged in that design.

e. Sub-paragraphs (6) and (7) make consequential amendments to subsections (5) and (6) of section 307.

5. Paragraph 3 amends section 308(2) of FA 2004, which defines the "relevant date", i.e. the beginning of the period within which a disclosure must be made, so as to insert a new trigger point for the disclosure of a fully designed scheme that a promoter markets to potential clients, in line with the revised definition of 'promoter' in section 307 as amended by paragraph 2.

a. Sub-paragraph (3) inserts a new paragraph (za) in section 308(2), corresponding to the new sub-paragraph (ii) of section 307(1)(a) of FA 2004, providing that the date on which a promoter first makes a firm approach is a "relevant date".

b. Sub-paragraph (2) makes a consequential amendment.

6. Paragraph 4 extends section 313A(1) of FA 2004 to introducers. Section 313A allows HMRC to require persons they suspect of being promoters (or, as a consequence of this amendment, introducers) of a notifiable scheme to explain why they think they are not required to disclose the scheme. This enables HMRC to seek information where it is aware that a person is marketing a scheme but is not certain if that person is the scheme promoter or merely an introducer.

7. Paragraph 5 inserts in section 318(1) of FA 2004 definitions of "introducer", "makes a firm approach" and "makes a marketing contact" which correspond to the definitions in new subsections (4A) to (4C) of section 307 of FA 2004.

8. Paragraph 6 inserts a new section 313ZA in FA 2004.

a. Subsection (1) sets out the scope of the new section. It applies where a promoter is subject to the "reference number information requirement" or would be so required had the promoter complied with section 308 of FA 2004 and got a reference number from HMRC.

b. Subsection (2) defines the "reference number information requirement". It is the requirement, in section 312 of FA 2004, to notify clients of the reference number allocated to the scheme by HMRC. Section 312 (and therefore new section 313ZA) applies once a client has implemented a scheme.

c. Subsection (3) requires promoters to provide prescribed information about clients and to do so within a prescribed period after the "relevant period" prescribed under subsection (4). "Prescribed" means prescribed by regulations made by HMRC (see section 318(1) of FA 2004). It is intended that the prescribed information will be the names and addresses of clients, the "relevant period" will be each calendar quarter, and that the "prescribed period" will be 14 days. So promoters will be required to provide to HMRC lists of clients who have implemented a scheme and

have been issued with a SRN in each calendar quarter, and to do so within 14 days of the end of the quarter.

d. Subsection (5) disapplies the obligation to provide client lists where HMRC have given notice under section 312(6) of FA 2004 that promoters are no longer required to provide clients with SRN information.

9. Paragraph 7 makes a consequential amendment to section 316 of FA 2004, adding a reference to new section 313ZA(1). Section 316 allows HMRC to specify the form and manner in which information must be provided. It is used to specify such matters as forms on which information is to be provided and the address to which the form is to be sent.

10. Paragraph 8 amends section 317(2) so that regulations may make different provision for different cases, allowing regulations to be tailored to different circumstances that may arise.

11. Paragraph 9 inserts a new section 313C in FA 2004.

a. Subsection (1) provides that HMRC may require a person whom they suspect is an introducer of a notifiable scheme to provide prescribed information about any other person who has provided him with information about a scheme. The requirement must be by written notice. The other person who has provided the introducer with information about the scheme is likely to be the promoter of the scheme, but in some circumstances may be a further intermediary.

b. Subsection (2) requires a notice under new section 313C to specify the scheme to which it relates.

c. Subsection (3) requires a person to comply with a notice within a prescribed period, or such longer period as HMRC may direct. Again, "prescribed" means prescribed in regulations made by HMRC (section 318(1) of FA 2004).

12. Paragraph 10 amends section 98C of TMA, which provides for penalties for non-compliance with duties under Part 7.

a. Sub-paragraph (2) amends subsection (1)(a) of section 98C. At present subsection (1)(a) provides for a single initial penalty of up to £5,000 for failure to comply with any of the Part 7 duties mentioned in section 98C(2). For failure to disclose a scheme, sub-paragraph (2) replaces the initial single penalty with an initial daily penalty not exceeding £600 for each day during the "initial period", which is defined in new subsection (2ZA). The initial penalty for failure to comply with other duties (duties imposed by the disclosure regime other than disclosing the scheme) mentioned in section 98C(2) remains unchanged. There is no change to the provisions (sections 100(2)(f) and 100C of TMA) which require penalties under subsection (1)(a) to be determined by the First-tier Tribunal.

b. Sub-paragraph (3) amends subsection (2) of section 98C, adding the new duties of promoters to provide client lists and of introducers to identify promoters to HMRC to the list of duties to which a penalty relates. The penalty in these cases is the existing single initial penalty not exceeding £5,000.

c. Sub-paragraph (4) inserts new subsections (2ZA) to (2ZE) in section 98C after existing subsection (2).

i. New subsection (2ZA) defines the "initial period" referred to in the amended subsection (1)(a)(i). The "initial period" begins with the "relevant day" and ends on the day the penalty is determined by the Tribunal, or the day before the person complies with the duty in question, whichever is earlier. The "relevant day" is defined in the Table in subsection (2ZA). In each case it is the day after the end of the period during which the person should have complied with the duty in question.

So the "initial period" is the period of non-compliance beginning on the day after the deadline for complying, and ending when the penalty is determined, or when the person complies if earlier.

ii. New subsection (2ZB) requires the Tribunal, in determining the level of penalty for failure to disclose a scheme, to take account of all relevant matters, including the need for the penalty to be an adequate deterrent, having regard in particular to:

1. in the case of a promoter's failure to make a disclosure within the prescribed period, to the fees received or likely to have been received in connection with the scheme; and

2. in the case of a taxpayer's failure to make a disclosure within the prescribed period, to the tax advantage obtained or sought from the scheme.

iii. New subsection (2ZC) provides that where the daily penalty determined under subsection (1)(a)(i) appears inappropriately low, then the Tribunal may increase the penalty to an amount, not exceeding £1 million.

iv. New subsection (2ZD) provides for HMRC to commence proceedings before the First-tier Tribunal for re-determination of a penalty where it appears that the "relevant day" from which a penalty has been determined is incorrect. This may occur in cases where the Tribunal has made an order under section 306A of FA 2004 that a scheme be treated as notifiable.

HMRC may apply for orders under section 306A where they have evidence to satisfy the tests in that section but cannot prove that a scheme is notifiable, and therefore cannot prove that the time limit for notifying is to be calculated from the relevant dates in section 308(2) of FA 2004. If non-compliance continues after an order is made HMRC may seek a penalty, but in the absence of further evidence the Tribunal will only be able to determine a penalty on the basis that the duty arose from the section 306A order itself, and that the time limit for compliance, and the "relevant day" for the purposes of determining the "initial period", are to be calculated from the date of the order.

However, evidence may subsequently come to light, possibly from a belated notification, that the scheme was indeed notifiable from the beginning, and that the "initial period" should start from an earlier date. Subsection (2ZD) allows HMRC to apply to the Tribunal for the daily penalty to be backdated accordingly.

v. New subsection (2ZE) provides for the Treasury to vary by secondary legislation the amounts of both the proposed initial daily penalty in subsection (1) and new subsection (2ZC) of section 98C of TMA. Such regulations are subject to an affirmative resolution of the House of Commons.

d. Sub-paragraph (5) amends subsection (2A) of section 98C of TMA.

At present subsection (2A), together with subsection (2C)(a), provides vires for the Treasury by regulations to increase the amount of the daily penalty under section 98C(1)(b) where the Tribunal has made an order under section 306A of FA 2004 that a scheme be treated as notifiable.

The amendment extends the vires to the proposed initial daily penalty, and, together with the amendment to subsection (2C)(b) (see below), also provides vires for HMRC to prescribe by regulations the period after which the increased amount is to apply.

e. Sub-paragraph (6) amends subsection (2B) of section 98C of TMA.

At present subsection (2B), together with subsection (2C), provides vires for the Treasury by regulations to increase the amount of the daily penalty under section 98C(1)(b) where the Tribunal has made an order under section 314A of FA 2004 that a scheme is notifiable, and for HMRC to prescribe by regulations the period after which the increased amount is to apply.

The amendment extends the vires to the proposed initial daily penalty.

f. Any regulations varying the amount of a penalty in section 306A or 314A cases are subject to an affirmative resolution of the House of Commons.

g. Sub-paragraph (7) amends subsection (2C)(b) of section 98C of TMA, which defines "prescribed period" in subsection (2B) in relation to orders under section 314A of FA 2004. The amendment extends the definition to cases where orders have been made under section 306A of FA 2004, and is consequential to the amendment of subsection (2A).

h. Sub-paragraphs (8) and (9) add a reference to section 306A of FA 2004 to subsections (2D) and (2E) of section 98C of TMA. Subsections (2D) and (2E) provide, respectively:

i. That the making of a disclosure order does not mean that a person either had, or did not have, reasonable excuse for non-compliance; and

ii. That after an order is made, any reasonable excuse founded on uncertainty as to notifiability ceases after the period prescribed under subsection (2B) of section 98C of TMA for the increased penalty

Under section 118(2) of TMA a person who has a reasonable excuse for failure to comply is deemed not to have defaulted, and as a consequence is not liable to a penalty. But if the reasonable excuse ceases the person must then comply without unreasonable delay

The effect of the amendment is that, where an order is made under section 306A, any reasonable excuse ceases after the period prescribed under subsection (2B), which will be 10 days. If the scheme then remains undisclosed the promoter becomes liable to a penalty at the increased rate prescribed under subsection (2A) which will be an amount not exceeding £5,000 per day. This is already the case where an order is made under section 314A.

i. Sub-paragraph (10) amends subsection (2F) of section 98C of TMA, which contains certain procedural provisions concerning secondary legislation.

i. Sub-paragraph 10(a) is consequential to the amendments described above.

ii. Sub-paragraph 10(b) amends subsection (2F)(c) to provide that regulations varying the amounts specified in section 98C(1) be subject to the affirmative parliamentary procedure, as are regulations increasing the amount in section 306A and 314A cases at present.

Background Note

13. Measures requiring the disclosure of tax avoidance schemes falling within descriptions prescribed in regulations were introduced in FA 2004. Initially the prescribed descriptions were limited in scope to income tax, corporation tax (CT) and capital gains tax (CGT), and to schemes which concerned employment or certain financial products. Stamp duty land tax, in relation to commercial property, was added with effect from 1 August 2005, and the regime was extended to the whole of income tax, CT and CGT from 1 August 2006.

14. A separate disclosure regime exists for National Insurance Contributions. Regulations mirroring, with modifications, the tax regime as it applies to income tax came into effect on 1 May 2007.

15. A separate disclosure regime also exists for VAT. That is outside the scope of this measure.

16. The purpose of disclosure is to provide HMRC with early information about tax avoidance schemes, informing risk assessment and selection of schemes for either closure by legislation or operational challenge.

17. Disclosure requires certain persons (normally promoters) to provide information about tax avoidance schemes sufficient for an officer of HMRC to understand how they are intended to work.

18. The scheme reference number (SRN) system is intended to identify the users of notifiable schemes. HMRC allocate a SRN to schemes when they are disclosed, and notify it to the person who makes the disclosure. This is normally a promoter of the scheme. Promoters are required to pass the SRN to clients who implement the scheme, who must report it back to HMRC, normally on a tax return affected by using the scheme.

19. The amendments are designed to advance the time at which information about schemes and users of schemes is to be provided, to enable HMRC to identify the promoter of schemes involving intermediary introducers, and to enhance the effectiveness of penalties as a deterrent against non-compliance.

20. HMRC issued a consultation document Disclosure of Tax Avoidance Schemes (DOTAS) containing draft Finance Bill legislation on 9 December 2009. This section and Schedule revise the draft legislation to reflect comments made by respondents and the outcome of discussions between HMRC and promoters and representative bodies.