Tax Intermediaries Disincentives: Discrimination on the Basis of Profession?

Kluwer International Tax Blog
March 6, 2017

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Please refer tot his post as: Piergiorgio Valente and Ian Hayes, 'Tax Intermediaries Disincentives: Discrimination on the Basis of Profession?', Kluwer International Tax Blog, March 6 2017, http://kluwertaxblog.com/2017/03/06/tax-intermediaries-disincentives-discrimination-basis-profession/

On 16 February 2017 the Public Consultation on the proposed introduction of rules at EU level to disincentivize promotion of aggressive tax planning schemes was closed. The rules under consideration focus on a Mandatory Disclosure Regime (MDR) – referred to also as a Disclosure of Tax Avoidance Schemes (DOTAS) regime. Under such rules, tax advisers and tax intermediaries would be required to notify tax authorities on tax structures which could be considered aggressive or abusive, howsoever such terms may be defined.

For this purpose intermediaries may include, consultants, lawyers, financial and investment advisers, accountants, financial institutions, insurance intermediaries, agents establishing companies or any other type of person involved in the design of structures potentially leading to tax avoidance.

In this article, reference to tax advisers encompasses specifically professionally established and regulated individuals while, reference to intermediaries implies the wider definition and it is accepted that some of these categories may not be regulated or subject to ethical and professional constraint. This article is concerned with the position of tax advisers.

The measures have been proposed in haste as a response to and in the wake of the "Panama Papers" disclosures, with a view to preventing future abuse. The European Commission underlined that "the Panama Papers have highlighted how certain intermediaries appear to have actively helped their clients to conceal money offshore". From an international perspective, the European initiative towards tax intermediaries' mandatory disclosure is neither the first nor the last in this direction.

The UK has been active in this respect since early this century. The DOTAS regime came into force in 2004, and in 2016 Her Majesty's Revenue and Customs (HMRC) put forward a proposal for the introduction of sanctions for enablers and users of tax avoidance, more of which later.

Action 12 of OECD's BEPS Project outlines a template to facilitate the introduction of MDR in countries without equivalent measures; and, following this lead the Australian Budget 2016/2017 Law makes provision for disclosure of potential tax avoidance.

Mandatory disclosure by tax advisers and tax intermediaries is seen as a mechanism to increase tax transparency and to give legislators time to react to and block new market schemes which have the potential to facilitate tax avoidance.

It is expected to have four important and interconnected advantages. Firstly, it would remedy the lack of taxpayer information available to tax authorities. At the same time, it would allow more efficient targeting of tax audits by identifying both the tax professionals promoting suspicious schemes as well as the users. Thirdly, the imposition of obligatory disclosure would itself function as a disincentive to promoting and implementing such schemes. Finally, the risk of early detection and counteraction undermines the viability of schemes and acts as a major impediment to the commercial development of the market.

Nevertheless, MDR cannot be perceived as flawless. It has a negative side. The introduction of mandatory disclosure seriously undermines the continuous development of a fair, effective and efficient tax system in the EU. Moreover, it is not a "magic bullet" and there are real limits to its potential.

In the UK, there has been a sharp fall off in the number of disclosures made under DOTAS and its parallel regime for indirect taxes (VATDR). This is seen by HMRC as indicating that avoidance planners, far from being dissuaded from their business, have amended it to avoid the requirements for disclosure and is one of the main driving forces behind HMRC's attack on avoidance enablers.

The Commission's proposal is underpinned by the assumption that all tax advisers and tax intermediaries facilitate avoidance, which is an outrageous simplification casting a shadow on tax professionals as a whole. Because some intermediaries have been and, apparently, continue to be involved with aggressive tax planning structures, and to prevent such phenomena in the future, all tax intermediaries, without distinction, are to bear additional legal and professional obligations.

The vast majority of tax advisers fully, ethically and comprehensively apply tax legislation and by such application empower their clients to comply as well. The generalization on which MDR is to be founded is reason enough to question both its legitimacy and proportionality with respect to its purpose. In this regard, it should be considered that the EU proposal, not for the first time, exceeds OECD recommendations and amounts to gold plating.

An MDR entails risk to the effectiveness of the overall tax system. The mere proposal of the regime, irrespective of its final adoption, engenders a negative perception of tax professionals by the general public. Such an adverse view undermines the client/professional relationship between taxpayers and tax advisers, questions the professional ethics of practitioners and undermines the confidence which is an essential part of a client/professional relationship.

It is these tax same advisers who are the very professionals qualified to enable taxpayers to understand correctly and fulfill properly their tax obligations. The complexity of modern tax law, the uncertainty prevailing in the international tax area and the wave of new obligations currently being introduced to update the current tax framework, render ethical and professional tax advice essential for the system's smooth function. Under these circumstances, actions discouraging taxpayers from seeking advice from professionally regulated tax advisers and shifting the burden from tax administrations, undermine all parties' mutual trust and do not seem a good idea.

Furthermore, it is arguable that the proposed MDR targets tax advisers and tax intermediaries in order to address problems originating either from the inadequate functioning of tax administrations or from unadvised choices made by the taxpayer. In particular, its primary goal is to supply tax administrations with information to combat tax avoidance however meretricious that may be.

Tax avoidance is generated by deficient tax legislation, as has been widely recognized in the framework of the BEPS Project. It is the responsibility of tax authorities to gather information on taxpayers' activities and, to this effect, they are provided with several instruments, e.g. tax returns, administrative cooperation, and technologies to extract conclusions.

Failure of legislators and administrations to fulfill their role efficiently, whether by lack of resource or determination, does not suffice to justify imposition of burdens, pregnant with penalty, on specific categories of professionals in an attempt to rectify a situation which is, in large part, of their own making. Politicians should be pilloried for failure to provide adequate funds, whilst administrations are to be criticized for failure to speak truth to power.

Implementation of aggressive tax planning constitutes an informed decision of the taxpayer. Therefore any action which shifts the burden of compliance to a tax adviser or a tax intermediary away from the taxpayer is misplaced and raises doubts as to allocation of responsibility and respective liability within the EU tax system.

Performance of tax advisers in compliance with their professional obligations is regulated by professional codes of conduct and ethical boundaries. In the UK those tax advisers who are professionally regulated are, from 1 March 2017, required to

comply with a revised and enhanced regulatory document, Professional Conduct in Relation to Taxation (PCRT). This makes involvement with aggressive tax planning a disciplinary offence and, because of compliance with it, HMRC have intimated that such regulated professionals are not the target of the enablers legislation, which will come into force on receipt of royal assent to Finance Act 2017.

Regulated compliance is the case in most comparable professions. In this light, it should be considered whether measures targeted directly to taxpayers, i.e. mandatory reporting by the users of suspicious tax structures, would be more appropriate for the purposes pursued by the Commission. This option would not prejudice the taxpayer/tax adviser relationship, indeed it would enhance it since the taxpayer will, in all probability, look to the tax adviser to oversee the compliance requirements he is tasked with. It would convey a more just message to the tax community: choice implies liability and (tax) advantages sanctions.

The proposed introduction of the MDR is trivial for a series of other reasons, detailed in the CFE Opinion Statement submitted to the Public Consultation. It is not clear how such a regime would be reconciled with the privilege, granted under the national legislation of some member states, to communications between taxpayers and tax consultants. It is also moot how under the proposed scheme, taxpayers' fundamental rights to representation and fair dispute resolution will be weighted and safeguarded.

Moreover, it is remarkable that sanctions are currently being considered for introduction to deal with behavior currently considered entirely lawful. Finally, the effectiveness of disclosure regimes is far from guaranteed, exemplified by the UK National Audit Office in its 2012 Report to HMRC for the evaluation of the corresponding UK DOTAS regime.

The concerns raised with respect to the EU proposal for MDR clearly point out the need for careful elaboration of any legislation to such end. Even more strongly, they indicate that it is rather risky – at this stage at least – to proceed with an EU-wide initiative. Existence of EU legislation would effectively limit the margin of national legislators to tailor a – by definition – burdensome regime to national needs, challenging respect for the principle of proportionality.

A number of measures have been and are still being introduced worldwide to fight tax avoidance, e.g. enhanced exchange of information and country-by-country reporting. The international tax arena is transforming. It would be both wise and prudent to postpone complex compliance measures of questionable effect until the shape of the new tax framework can be clarified and the effects of the new measures assessed. It is highly likely that MDR will prove to be unnecessary under the new circumstances. Abstaining from enactment of the proposal would also reinforce tax advisers' fair and just position in the tax system, as enablers of compliance – not aggressive avoidance – and giving positive support and impetus to more effective taxation.