

# LABOUR'S TAX TRANSPARENCY AND ENFORCEMENT PROGRAMME

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Labour's Tax Transparency and Enforcement Programme will be the most comprehensive effort ever made by any UK government to end the social scourge of tax avoidance and ensure that those super-rich individuals and minority of giant corporations seeking to duck their responsibilities to society will pay their fair share.

By its nature, tax avoidance is difficult to quantify. Estimates of the wealth hoarded globally in tax havens range from \$4-\$20 trillion. Even HMRC estimates that the "tax gap", some of which is due to tax avoidance and evasion, comes to £36 billion.<sup>1</sup>

To meet the scale of avoidance, we will reverse the cuts at HMRC, restoring staffing numbers with an additional £200 million of funding, which will enable HMRC to properly investigate avoidance and bring in more revenue.<sup>2</sup> Under a Labour government committed to closing the loopholes and ending tax avoidance through our Tax Transparency and Enforcement Programme, we are confident that **at least an additional £6.5-8.5 billion a year can be raised.**

## COSTED MEASURES

### *Preferred creditor status for HMRC*

Prior to 2002, HMRC was a preferential creditor for insolvent businesses and individuals. The insolvency regime introduced by the 2002 Enterprise Act meant that HMRC ceased to be a preferential creditor in the pecking order of claims and ranked alongside unsecured creditors.

The idea was to dissuade HMRC from launching insolvency proceedings. It was argued that this would somehow prolong the life of distressed businesses. There is little evidence of that, but there is some evidence to show that the law has been abused and it is too easy for directors and major shareholders to avoid debts due to HMRC. For example, in the case of Swiss Rock Limited (a vehicle owned by Dominic Chappell of BHS fame), its directors extracted as much cash as possible and avoided paying £733,000 of VAT and corporation tax to HMRC after being placed in liquidation by directors. In the insolvency of Bernard Matthews Limited, banks and directors sold assets from the company to repay debts due to themselves, but dumped a £1.38 million tax liability to HMRC.

Write-offs by HMRC are significant and do not form part of its usual estimate of the "tax gap". The table below shows the amount written off for financial years since 2010. The value written off will be counter-cyclical: as the economy recovered from the crash and recession, fewer and fewer businesses would need to write off their taxes for any purpose.

## Taxes written-off by HMRC (£bn)

Year	Total	Income tax	VAT	Corp Tax	Alcohol duty	Tobacco duty	CGT	NIC	Fines	Other
2015-16	4.0	0.868	1.562	0.326	0.035	0.014	0.041	0.391	0.724	0.024
2014-15	4.2	1.049	1.436	0.585	0.073	0.003	0.040	0.462	0.434	0.155
2013-14	5.1	1.668	1.681	0.440	0.044	0.005	0.040	0.679	0.540	0.037
2012-13	5.3	1.285	2.004	0.608	0.072	0.001	0.038	0.734	0.534	0.031
2011-12	5.2	1.499	1.920	0.503	0.064	0.001	0.042	0.653	0.403	0.086
2010-11	5.9	1.346	1.989	0.635	0.010	0.003	0.039	0.823	0.369	0.647

*Restoring the pre-2002 preferred creditor status of HMRC would allow less tax to be written off, and remove the scope for some avoidance that has opened up. On a conservative assumption that, over the cycle, an average of around 25 per cent of the tax written off could then be collected, around £1-1.5 billion annually could be collected.*

### *Incorporation avoidance*

With the sharp reductions in headline Corporation Tax since 2010, the difference between CT and headline tax rates on personal income (including NICs) has become wider in successive years. There is now a clear tax incentive for individuals to self-incorporate. The Office for Budget Responsibility has begun modelling the impact of this form of tax avoidance, and losses to the Exchequer are substantial. Small gains in CT receipts are overwhelmed by losses in income tax and NICs.

### Losses from excess incorporation

	2017-18	2018-19	2019-20	2020-2021
Incorporations loss	1.1	1.7	2.0	2.5

*Source: OBR, Economic and Fiscal Outlook (November 2016), Box 4.1*

Increasing the headline rate of Corporation Tax (on OBR forecasts) would bring in revenues. *The amount raised would be around £1.7 billion for 2018-19, rising to £2.5 billion by 2020-21.*

### *Closing the "Mayfair Tax" loophole*

The "Mayfair Tax" loophole is a scheme used by managers of private equity companies. It depends on treating carried interest as a capital gain rather than as income, which means that the income tax rate faced by the equity fund manager on much of their income could be as low as 28 per cent. It is possible to drag even this low rate further through other avoidance schemes, and a zero rate can apply to a fund manager who can claim to be non-domiciled in the UK. *Independent estimates have put the loss from the loophole at £0.7 billion p.a.<sup>3</sup>*

### ***Closing the Eurobond loophole***

The basis of the loophole is that the Channel Island Stock Exchange is a recognized stock exchange under Section 841 of the UK Income and Corporation Taxes Act 1988 and securities listed at that Exchange enjoy exemptions from withholding tax even though the securities may be held by opaque companies. So the UK company makes interest payments gross i.e. without any withholding tax. The recipient usually arranges his/her tax affairs in such a way s/he escapes tax altogether. *Independent estimates put the tax lost at £0.5 billion per year.*<sup>4</sup>

### ***Umbrella agencies clampdown***

Aggressive tax avoidance schemes are used by temp recruitment agencies to significantly reduce tax liabilities. The schemes being marketed depend on workers' contracts being transferred from a single employment agency into thousands of tiny companies, each one of which claims a tax break, and whose directors are claimed to be based overseas. By structuring themselves in this way, *independently estimated losses run to at least £0.1 billion a year.*<sup>5</sup>

### ***Advanced Thin Capitalisation Agreements***

Advanced Thin Capitalisation Agreements (ATCA) were introduced in 2007 to grant large, multi-group companies some certainty about their future tax liabilities, by setting out well in advanced the expected scale of losses that can be claimed for the cost of capital within the group. Until the present government seemingly discontinued publishing statistics on their use, official figures suggested they were becoming increasingly popular. The government has not directly answered questions in the House as to when the statistics will be published again, stating only that it intends to.<sup>6</sup>

### **ATCA agreements**

	2010 to 2011	2011 to 2012	2012 to 2013	2013 to 2014
ATCAs agreed	127	160	144	198
Agreements in force	231	279	414	510
Average time to reach agreement (months)	9.8	10.1	11.7	11.4
50% agreed within (months)	6.9	7.7	9.7	10.4

However, news reports of Formula One's very significant reduction in their tax liability over the last five years (\$192 million on \$5 billion of profits) through the use of an ATCA suggest that there has been considerable scope for avoidance. Formula One had generated significant losses by making huge loans between different groups, charged at exceptional (10 per cent) rates of interest, and which were allowed as a loss under an existing ATCA with HMRC. Had the tax been levied at the more usual level, Formula One would have been liable for a further £400 million.

Changes to the HMRC guidelines, in force from April 2017, now limit the amount of interest loss relief that can be claimed to 30 per cent of UK earnings. This would increase F1's tax bill to £52 million annually, rather than £5 million as today. But with a comprehensive investigation of existing ATCA agreements, and a general presumption against offering such deals, the scope of losses could be further reduced. Whilst it is unlikely that the 510 ATCAs in force will be of the same scale as Formula One, it is reasonable to presume that at least some of those currently produce significant and unwarranted losses. *In the absence of data, presenting an estimate for additional taxes raised is challenging. On reasonable assumptions about the scale of ATCA agreements in force, we have been advised to estimate that an investigation of ATCA and clampdown on their use could raise £0.5-1 billion in additional revenue.*

## OTHER MEASURES

Labour's Tax Transparency and Enforcement Programme also includes a range of measures that, by their nature, are harder to directly cost. We have drawn up this list in consultation with tax experts and specialists in avoidance measures so that it is comprehensive in its scope and application. Taken together, we have taken expert advice to conservatively estimate that the additional revenue raised from these measures will come to £2-3bn per year.

- 1. An immediate public inquiry into avoidance.** The Labour Party wants to see an immediate public inquiry launched into the revelations in the Panama Papers, to establish the harm done to the UK's tax revenue and consider detailed proposals for reform including, if necessary, amendments to UK company law and/or trust law to increase transparency.
- 2. Greater scrutiny of MPs.** Labour will change the register of House of Commons Members' Interests to include mandatory publication of all offshore holdings.
- 3. Create a specialised Tax Enforcement Unit.** Labour wants HMRC to be properly resourced to investigate any potential illegality whether in relation to tax law or conflicts of interest for legislators. We would double the number of staff scrutinising the tax affairs of High Net Worth individuals and companies and increase the number of prosecutions.
- 4. A Withholding Tax for abusive tax havens.** Labour will draw up a list of abusive tax havens and introduce sanctions against them. We will consult on the introduction of a withholding tax levied against any dividend, interest and related payments to individuals or companies in abusive tax havens. This will be deducted at source before any payment is made and remitted to HMRC.
- 5. Public filing of large company tax returns.** Labour will require all large companies to publicly file their tax returns and related documents at Companies House. This will not only inform the public of novel tax avoidance tactics used by companies but also empower parliamentary committees to ask searching questions of the companies and HMRC. Currently, it is all too easy for companies to avoid this as they hide behind the veil of confidentiality.
- 6. Public filing of the tax returns of wealthy individuals earning more than £1 million.** The Panama Papers, the HSBC leaks and others have shown that many wealthy individuals have used offshore tax havens to avoid taxes. Labour will erode the secrecy by the tax returns of wealthy individuals publicly available.

- 7. No public contracts for tax avoiders.** Labour will legislate to ensure that those involved in tax avoidance are unable to secure public contracts from central government, local government and public bodies. Taxpayers should not fund contractors engaged in tax avoidance. All bidders will be required to make a public declaration of their profits from UK sources and corporation tax paid in each of the last five years. No contractor will be permitted to relocate public contracts in a tax haven entity.
- 8. Repatriate contracts parked in tax havens.** Many public contracts for building schools, hospitals, care homes and other public facilities awarded to contractors under the Private Finance Initiative (PFI) have subsequently been relocated to tax havens. This has enabled contractors to avoid UK taxes on profits funded by taxpayers. Labour would require repatriation of all such contracts.
- 9. Public contract transparency.** Overseas companies wanting to tender for public sector contracts must have all of their beneficial owners and directors listed publicly. Labour will establish a register of companies bidding for public sector contracts and procurement which will show their shareholders, directors, control and full disclosure of beneficial ownership listed publicly. The companies must establish a permanent establishment in the UK and pay taxes on the profits made in the UK.
- 10. A register of beneficial ownership of companies.** Labour will require disclosure of all shareholders above a minimal value, instead of only those holding over 25%. It will not permit the real owners and beneficiaries to hide behind nominee shareholders and directors. No overseas company will be permitted to be a director of any UK company without meeting the UK transparency standards.
- 11. A register of trusts.** Trusts are a key vehicle for tax avoidance and illicit financial flows. Labour will create a public register of all trusts showing their assets and beneficiaries. We will look particularly at trusts which transfer the residence of their trustees offshore, and those tax avoidance schemes involving trusts which are disclosed to the HMRC under the current law.
- 12. Enforce our programme by working with the banking sector.** A Labour government will work with banks to promote good corporate governance and provide further information over beneficial ownership for all companies and trusts that they work for.

**13. A General Anti-Avoidance Rule.** The government currently has what it calls a General Anti-Abuse Rule. This is inadequate as it does not challenge the abuses already established. It requires HMRC to seek permission from an business advisory panel before taking any legal action to stamp out abuses. Unsurprisingly, so far no action has been taken to deal with abuses. Labour will instead introduce a General Anti-Avoidance Rule (GAAR) designed to end sham transactions. Any transaction lacking economic substance will be considered to be a sham and thus not allowed for tax purposes. Oversight and guidance will be provided by a broader panel of experts.

**14. Strict minimum standards for Crown Dependencies and Overseas Territories.** This minimum standard will include a public register of owners, directors, major shareholders and beneficial owners for all companies and trusts and requirement for companies and limited liability partnerships to publish accounts.

**15. Create an offshore companies levy.** This will capture purchases of UK property from offshore trusts located in tax havens.

**16. Full country-by-country reporting.** Co-operating internationally to introduce full country-by-country reporting across the tax jurisdictions.

## REFERENCES

- 1 HMRC (20 October 2016), "Measuring Tax Gaps 2016 edition"
- 2 The data released by HMRC shows that the financial returns from investigations into large businesses for 2013/14 have jumped to £97 in extra tax for every £1 invested in the last year, up from £87 during the previous year. Both the local compliance (which investigates individual taxpayers and small businesses) and high net worth units collected approximately £18 for every £1 invested in 2013/14, up from £16 over 2012/13. Pinsent Masons, "HMRC investigations into large companies now yielding £97 for every £1 invested", available at: <https://www.pinsentmasons.com/en/media/press-releases/2015/hmrc-investigations-into-large-companies-now-yielding-97-for-every-1-invested/>
- 3 Upper estimate from: Independent (19 February 2015), "Private equity bosses using £700m tax loophole...", available at: <http://www.independent.co.uk/news/uk/politics/private-equity-bosses-using-700m-tax-loophole-and-donating-to-the-tories-10054911.html>
- 4 Estimate reported in Independent (23 October 2013), "Eurobonds scandal: the high street giants avoiding millions in tax", available at: <http://www.independent.co.uk/news/uk/politics/eurobonds-scandal-the-high-street-giants-avoiding-millions-in-tax-8897591.html>
- 5 Guardian (15 November 2016), "Revealed: temp agencies tax avoidance schemes cost 'hundreds of millions'", available at: <https://www.theguardian.com/uk-news/2016/nov/15/revealed-temp-agencies-avoidance-scheme-costs-taxpayers-hundreds-of-millions>
- 6 Guardian (15 November 2016), "Revealed: temp agencies tax avoidance schemes cost 'hundreds of millions'", available at: <https://www.theguardian.com/uk-news/2016/nov/15/revealed-temp-agencies-avoidance-scheme-costs-taxpayers-hundreds-of-millions>
- 6 See Written Questions from Lord Harries of Prentregrath: <http://www.parliament.uk/business/publications/written-questions-answers-statements/written-questions-answers/?page=1&max=20&questiontype=AllQuestions&house=commons%2clords&member=3813>

