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1. Overview

On 17 March 2004, the Chancellor of the Exchequer announced new rules which introduce a new obligation on promoters and users of certain tax schemes and arrangements to disclose details to the Inland Revenue.

The new rules will give the Inland Revenue earlier and better intelligence on the various schemes being used. This will enable the Government to make swifter and more targeted responses to certain tax avoidance arrangements, if it considers that any action is desirable.

i) Summary of the Rules

The rules require disclosure of transactions or arrangements which:

- are expected to obtain a tax advantage
- as a main benefit and
- involve certain employment or financial products.

The person responsible for making the disclosure is normally the person who designed or marketed the scheme (the promoter) but in some circumstances can be the scheme user. For more details click here.

In general, disclosure must be made within five working days of the scheme being made available for implementation or when the transaction takes place. For more details click here.

Only one disclosure per scheme is required. For more details click here.

The Revenue will issue a reference number for each disclosable scheme. Promoters must provide this number to clients.

Taxpayers who use the scheme must enter that number on their tax returns For more details click here.

ii) What is covered

The rules apply to arrangements which have as a main benefit the gaining of a tax advantage. The tax advantage referred to must be in respect of Income Tax, Corporation Tax or Capital Gains Tax. There are separate disclosure rules concerning VAT avoidance. These are not covered by this guidance.

Only arrangements that involve certain products require disclosure. These are:

- Financial Products and
- Employment Products

The rules are designed to target schemes or arrangements where there is a high risk of tax avoidance.

iii) Summary of How to Comply

a) Scheme Disclosure Forms

There are separate forms for promoters, users with offshore promoters and in-house teams where there is no promoter. Click here for more details

b) Where to Send Completed Forms

Promoters and scheme users with offshore promoters

Completed forms should be sent to the Avoidance Intelligence Unit

Schemes with no promoter (in-house)

Completed forms should be sent to the tax office dealing with the scheme user's relevant returns.

c) Reference Numbers

On receipt of a disclosure, the Revenue may issue a reference number. If the Revenue decide not to issue a reference number then a letter confirming this will be issued.

Where the number is issued to a promoter, the promoter must pass that number to any clients who have used the scheme or arrangement. The user of the scheme must then enter the number on their tax return for the year(s) or period(s) for which the tax advantage arises.

Where the reference number is issued to a scheme user because the promoter is overseas, the user must enter the number on their tax return.

Where the disclosure is in respect of a scheme or arrangement devised and implemented without a promoter (in-house schemes) then, as the disclosure of the scheme details is only due at the normal filing date for the return, the Revenue will not normally issue a reference number.

2. Detailed Guidance

A) Disclosure of Scheme Details

i) Summary

The schemes and arrangements subject to the disclosure rules are those which meet all three of the following conditions:

- The arrangements give rise to a tax advantage.
- The advantage is the main benefit, or one of the main benefits, which might be expected to arise from the arrangements.
- The arrangements fall within any description prescribed in Regulations. The regulations limit the scope of any tax advantage to income tax, corporation tax and capital gains tax.

The new disclosure rules will require promoters to provide a description of the scheme or arrangement, including any details of the types of transactions involved, the expected tax consequences and the tax law provisions which they rely upon. The Inland Revenue will register these schemes and allocate a reference number to each disclosable scheme.

Promoters will be required to provide this number to all their clients who use the scheme or arrangements. A promoter who advises a client to use a disclosable scheme will either give the client an existing reference number for that scheme or disclose it as a new scheme.

Taxpayers will be required to provide details of the scheme or arrangement to the Inland Revenue in two circumstances:

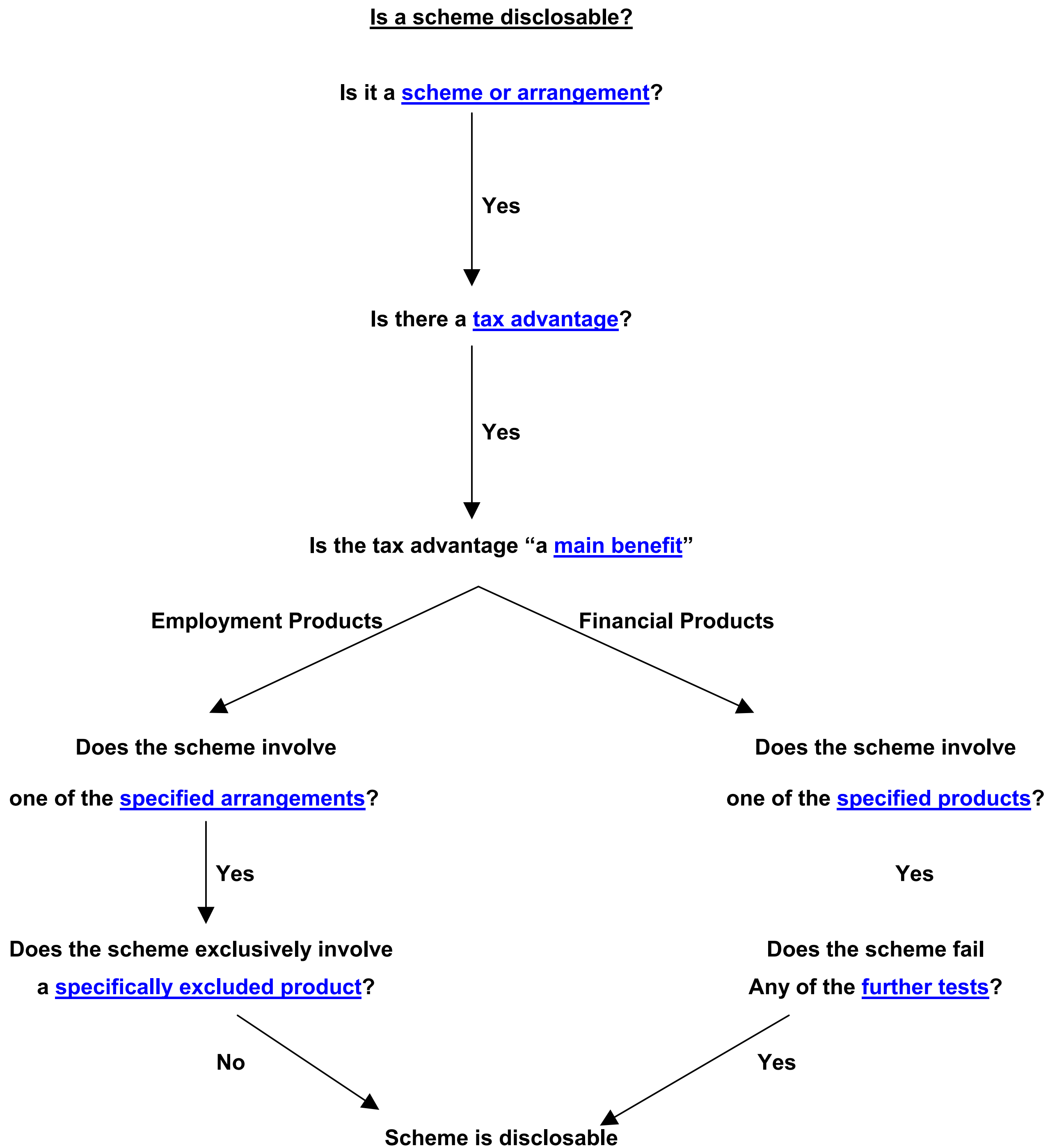
- Where they have used a scheme or arrangements which was provided by a promoter based offshore who has not registered it with the Inland Revenue. In these circumstances, taxpayers will be required to disclose details of schemes five working days after the scheme was implemented
- Where they have used a scheme or arrangements which they have devised themselves. In these circumstances, taxpayers will be required to disclose details of the scheme together with the relevant tax return.

ii) When do the Rules Operate from?

The rules apply generally from 1 August 2004. There are transitional provisions that apply to arrangements involving employment products from 18 March 2004 and financial products from 22 June 2004.

iii) Is it a Disclosable Scheme?

a) Flow Chart



b) Meaning of Scheme or Arrangement

This is widely defined as "any scheme, transaction or series of transactions". We do not intend that this should catch everyday tax advice and in our view the overall disclosure rules will filter such advice out. We will be updating our guidance regularly to ensure that unnecessary disclosures are not made.

However, much everyday advice involves transactions that do give rise to tax advantages that are within the definition of tax advantage in S318(1) FA 2004.

c) Meaning of Tax Advantage

Tax advantage is defined as relief or increased relief from tax, for example:

- obtaining a relief or deduction in computing profits or gains or relief for a loss against profits, or
- repayment or increased repayment of tax, or
- the avoidance or reduction of a charge to tax or an assessment to that tax or the avoidance of a possible assessment to that tax - a simple example would be a scheme whereby income was received in a capital form, or
- the deferral of any payment of tax, for example by the creation of a timing mismatch between the receipt of income or the payment of an expense and its recognition for tax purposes, or
- the avoidance of any obligation to deduct or account for any tax.

d) Meaning of Main Benefit

The main benefit test is an objective test. If a tax advantage as defined by the legislation arises from the arrangement there will be a benefit. Whether it is a main benefit is a question of fact.

e) Financial Products

Summary

The Tax Avoidance Schemes (Prescribed Descriptions of Arrangements) Regulations 2004 set out a number of conditions, all of which must be met for the arrangement to be a prescribed financial product.

The financial products which are included in arrangements which need to be disclosed are:

- Those which are included in the list of financial products at paragraph 7(1) of the Regulations.
- Are not excluded by paragraph 7(2) (this covers PEPs and ISAs) or paragraph 7(4) (this covers finance leasing).
- Are not incidental to the obtaining of the tax advantage; and
- Fail one of the three tests in paragraph 8.

Any arrangements which do not contain such a financial product are not disclosable by virtue of part 2 of the Tax Avoidance Schemes (Prescribed Descriptions of Arrangements) Regulations 2004.

Products Included

The financial products which are specified are as follows:

- A loan.
- A derivative.
- A repo.
- A stock loan.
- A share.
- Anything which in accordance with UK accounting practice is in substance a loan or lending of money.

Products Excluded

The financial products which are excluded by paragraph 7(2) and (4) are as follows:

- Assets held within an ISA account.
- Assets held within a PEP.
- Anything which is accounted for as a finance lease.

Under paragraph 6(2), arrangements are only disclosable if the expected tax advantage, which is a main benefit of the arrangements arises, to a significant degree, from the inclusion of the financial product in the arrangements. Whether the tax advantage arises "to a significant degree" from a particular financial product is a question of fact. If the connection between the inclusion of the financial product and the obtaining of the tax advantage is minor and trivial, then that linkage is ignored and the financial product does not lead to disclosure. "Arises from" requires a direct connection. It is not sufficient that the scheme would not be entered into without, for example, borrowing money. (But disclosure may still be required by reference to the inclusion of other financial products which are not incidental.)

Further Tests

Arrangements are not disclosable unless they fail at least one of the three tests in paragraph 8. These tests are:

- Paragraph 8(2), the premium fee test;
- Paragraph 8(3), the confidentiality test;
- Paragraph 8(4), the off-market terms test.

Arrangements which pass all three of these tests are excluded arrangements and disclosure is not required.

f) Employment Products

Summary

The Tax Avoidance Schemes (Prescribed Descriptions of Arrangements) Regulations 2004 define arrangements connected with employment which must be disclosed unless specifically excluded

Notifiable proposals or arrangements connected with employment arise where there might be expected to be:

- a reduction in tax (income tax, capital gains tax or corporation tax), or
- a deferment of liability to such tax, of an employer, employee, or any other person
- which arises by virtue of the employee's employment and the arrangement involves securities or associated rights, payments to trustees and intermediaries or loans.

Arrangements Included

Notifiable proposals or arrangements will involve one or more of the following:

- securities or associated rights;
- payments to trustees and intermediaries; or
- loans.

Arrangements are notifiable even if any payments within them are to a person other than the employee. Payments for this purpose have a wide definition and include transfers of assets and anything which increases the value of an asset or reduces a liability.

'Securities and associated rights' include :

- securities;
- interests in securities;
- securities options;
- any right derived from securities; and

- anything whose value or amount is calculated by reference to one or more of the above.

Specific Exclusions

- Approved share schemes and EMI
- Payments to trusts established for the purpose of
  - an approved pension scheme
  - an approved share incentive plan
  - an approved SAYE scheme
  - an approved CSOP

iv) Who Needs to Disclose a Scheme's Details?

a) Promoters

A promoter is any person who conducts a relevant business and:

- has any responsibility for designing any notifiable proposal or arrangements except in excluded circumstances; or
- makes a notifiable proposal available to another person (for example by marketing or promoting arrangements designed by another person); or
- has any responsibility for the organisation or management of the notifiable arrangements, but only if they are connected with the designer of the arrangements.

Each of these activities is distinct; for example, making available is a separate activity from design and is not simply a question of communicating a bespoke design to a client. Consequently, bespoke advice would generally involve design but not making available. Marketing would always be making available and would be entirely separate from design, which could either be done by the same person or by another.

In this context, the design requires the application of thought to a problem. Merely documenting or pricing a financial product to someone else's design is not itself design. But developing a solution to a requirement is.

A relevant business is any trade, profession or business which involves the provision to others of services relating to taxation, or is carried on by a bank or company in a banking group.

However, in some circumstances, a person is not treated as a promoter. These circumstances relate to: in-house teams within groups, employees, and peripheral designers. Click here for more information

A person can be a promoter whether or not he is resident in the UK.

Multiple Promoters

If more than one person is a promoter in relation to the same scheme, responsibility for making the disclosure to the Inland Revenue may be discharged by one promoter only. If a promoter in respect of a notifiable scheme or arrangement is unable to establish whether the scheme has already been notified by another promoter, they should disclose the scheme.

b) Scheme Users with Offshore Promoters

Where a scheme or arrangements which fall within the requirements described in Section 3 has been designed or made available by a promoter based overseas, the user should establish whether the promoter has disclosed the scheme to the Inland Revenue. If they have, the user will be able to give a reference number to include on the relevant tax return. If they have not, then the responsibility for making the disclosure falls to the user.

c) When there is no Promoter (in-house)

Where there is no promoter involved, the obligation to disclose the scheme details falls on the user of the scheme.

v) When is a Disclosure Required?

a) By Promoters

A promoter is required to notify the Inland Revenue of the scheme or arrangements within five working days of whichever is the earlier of:

- for a promoter who makes the scheme available for implementation by another; the date on which he does so; or

- for other promoters, the date on which he first becomes aware of any transaction forming part of the notifiable arrangements.

  Click here for more information

b) By Users with Offshore Promoters

A user of a scheme with an offshore promoter is required to notify the Inland Revenue of the scheme or arrangements which meet the criteria for disclosure within five working days of the first step of the arrangements being taken.

c) When there is no Promoter

Where there is no promoter, users are required to disclose the scheme by the date on which they would otherwise have had to notify the Inland Revenue of the scheme reference number. In other words:

- For a tax advantage arising in relation to income tax or capital gains tax, users should disclose the scheme by 31 January following the end of the tax year in which they entered into any transaction forming part of the scheme.
- For a tax advantage arising in relation to corporation tax, users should disclose the scheme by the earlier of the following:
  - if the company's period of account is not longer than 18 months, not later than 12 months from the end of the period of account in which a user entered into any transaction forming part of the scheme.
  - if the company's period of account is longer than 18 months, not later than 30 months from the beginning of the period of account in which a user entered into any transaction forming part of the scheme.
- For a tax advantage arising in relation to PAYE, users should disclose the scheme to the Inland Revenue not later than 19 May following the end of the tax year in which they entered into any transaction forming part of the scheme.

vi) Transitional Rules

The new rules commence on the 1 August 2004 but, in order to prevent forestalling, they operate from 18 March 2004 for on-shore promoters of employment products, 23 April 2004 for

off-shore promoters of employment products and in-house users, and from 22 June 2004 for financial products.

a) Financial Products

Schemes involving financial products which were made available for implementation by a promoter or where any transaction forming part of the notifiable proposal or notifiable arrangements occurred between 22 June 2004 and 31 July 2004 must be disclosed by 31 October 2004. The same time limit applies where the first step taken to implement a financial product scheme notifiable by a user (where schemes are provided by an offshore promoter) takes place between 22 June and 31 July.

Where either a promoter makes a financial product available for implementation or any transaction forming part of the notifiable proposal or notifiable arrangements occurs between 1 August 2004 and 24 September 2004, disclosure must be made by 30 September.

b) Employment Products

Schemes involving employment products made available for implementation by a promoter, or where any transaction forming part of the notifiable proposal or notifiable arrangements occurs, between 18 March 2004 and 31 July 2004 must be disclosed by 31 October 2004. Where the first step taken to implement an employment product scheme notifiable by a user (where schemes are provided by an offshore promoter or devised in-house) takes place between 23 April 2004 and 31 July 2004, disclosure should also be made by 31 October 2004.

Where either a promoter makes an employment product available for implementation or a user takes the first step to implement an employment product scheme between 1 August 2004 and 24 September 2004, disclosure must be made by 30 September.

vii) What Needs to be Disclosed

The Inland Revenue will require sufficient detail to be able to understand the operation of the scheme. This should be a straightforward description highlighting the aim of the scheme, the steps involved and the tax law which the scheme relies on. The following information should be included:

- the name and address of the promoter and, if different, the person giving the notification;
- details of the provision of the disclosure rules under which the scheme is notifiable;
- name or title of the scheme (if any);
- a summary of the scheme; and
- an explanation of the tax avoidance element of the arrangements and the tax law provisions on which it is based.

There is no requirement to disclose:

- the name or other details of the client(s)
- the arguments the Revenue may be able to use to counter the scheme, or
- anything covered by Legal Professional Privilege

viii) How Many Disclosures are Required per Scheme?

a) General

Where a number of different clients implement the same scheme, the promoter should only disclose the scheme once. This is the case even if the scheme is tailored in a particular way to suit a specific client. However, the scheme should be disclosed separately where there has been a substantial change in the way in which it operates.

The transitional rules ensure that if the relevant date for disclosure falls before 18 March 2004, 23 April 2004 or 22 June 2004 (as appropriate) a notifiable proposal or arrangement does not need to be disclosed. When a new client is advised after these dates to implement the same scheme as one which was not disclosed because it fell before it, and hence the scheme has not been disclosed, the promoter must disclose in relation to the new client.

b) Meaning of "Substantially the Same"

What constitutes a change in a scheme or arrangement so that it is no longer substantially the same is a matter which will need to be considered on each occasion. However, the Inland Revenue would generally consider a scheme to be no longer substantially the same if the effect of any change was to make any previous disclosure misleading in relation to the second (or subsequent) client. This includes changes in the tax analysis.

We will regard arrangements as substantially the same where the only change is:

- a different taxpayer
- a different company in the same group

as long as these changes do not lead to a different tax analysis.

We will not regard arrangements as substantially the same where there are changes to deal with:

- changes in the law
- changes in accounting treatment
- changes in the tax attributes (eg. trading losses vs capital losses)
- other legal/commercial issues if these could have an effect on the tax analysis

ix) How do I Disclose?

a) Avoidance Intelligence Unit

The Inland Revenue has created a new Avoidance Intelligence Unit (AIU) to monitor the avoidance industry. As part of that role this unit is responsible for handling and policing the new disclosure rules.

b) Scheme Disclosure Forms

There are three alternative forms available for completion in the following circumstances:

- Form AIU1 – completion by a scheme promoter
- Form AIU2 – completion by a scheme user when the promoter is overseas
- Form AIU3 – completion by a scheme user where there is no promoter (in-house schemes)

If further space is required on any of the forms then the continuation sheet, AIU5, should be used.

All forms are available from the IR web site at www.inlandrevenue.gov.uk/aiu/index.htm in either pdf or word format, or from the order line (Tel: 08459 000 404 ; Fax: 08459 000 604)

c) Where to Send Completed Forms

Promoters and scheme users with offshore promoters

Completed forms should be sent to the Avoidance Intelligence Unit, 22 Kingsway, London WC2B 6NR. Disclosures will be accepted by post, fax [020 7438 4409] or by email to Jack.Young@ir.gsi.gov.uk.

It is important to note that the email channel is not a secure line.

Completed disclosure forms being sent by email should be in either word or pdf format.

Schemes with no promoter (in-house)

Completed forms should be sent to the office dealing with the scheme user's relevant returns.

d) Contacting AIU

The AIU can be contacted either by writing to:
The Avoidance Intelligence Unit
22 Kingsway
London
WC2B 6NR

Or by telephoning:
General enquiries 020 7438 6733
Head of Unit 020 7438 9145

x) Interaction with Clearance Applications

a) General

Promoters and taxpayers who are required to make disclosures may do so at the same time as submitting a statutory clearance application under any of sections 215, 225, 444A or 707 of the Income and Corporation Taxes Act 1988, or 138, 139, 140B or 140D of the Taxation of Chargeable Gains Act 1992; providing:

- The taxpayer is eligible to make the clearance application relating to a transaction which forms part of a disclosable scheme, or
- The promoter is submitting the clearance application on behalf of a taxpayer who is eligible to make the clearance application relating to a transaction which forms part of a disclosable scheme; and
- The clearance application is made before the transaction is entered into; and
- The clearance application contains all of the information required to be disclosed; and
- The clearance application is accompanied by (for promoters) or includes (for scheme users) a prominent statement signed by the person *required to make the disclosure* to the effect that the application should be treated as fulfilling their disclosure obligation.

b) Time limits

Clearance applications will usually (and in most cases must) be made pre-transaction. Therefore, in most cases the time within which the disclosure must be made is unaffected.

However, if you are a promoter with a reasonable intention of submitting a clearance application and you would otherwise be required to disclose within five working days of the day on which you made the scheme available (that is, the 'relevant date' is the date specified in section 308(2)(a) FA04), you should make the disclosure with the clearance application and not later than the date on which the first transaction forming part of the disclosable scheme occurs.

If the promoter held a reasonable intention to submit a statutory clearance application, but changes that intention, the period within which disclosure must be made is five working days following the day on which the reasonable intention ceased.

c) Procedural guidance

Disclosure of the scheme details can be made to the relevant clearance section at the same time as the clearance application either separately on the appropriate scheme disclosure forms or by clearly stating on the covering letter seeking the clearance that the application is intended to be a scheme disclosure as well. In the latter circumstances, the letter must be signed by both the person seeking the clearance (taxpayer) and, if different, the person required to make the disclosure (promoter or scheme user).

xi) Interaction with COP10

It is the Department's policy, as set out in Code of Practice 10, not to provide advice on transactions designed to avoid tax. The introduction of the disclosure rules does not alter this policy in any way and does not affect our existing CoP 10 procedures. The Inland Revenue will operate the disclosure rules in an entirely non-judgemental way: the allocation of a reference number to a scheme which has been disclosed should not be interpreted as giving any view on whether the scheme is effective in law in achieving its intended tax effect.

Equally, the fact that a disclosure has been made will not be taken as any admission by the promoter or user that the arrangements constitute tax avoidance.

xii) Legal Professional Privilege

Lawyers are subject to the disclosure rules in the same way as other professional advisers. The rules do not require the disclosure of any information which would be subject to legal professional privilege (in Scotland, confidentiality of communications) in legal proceedings. The ambit of legal professional privilege is under discussion with the Law Society following which we shall add further guidance.

xiii) Penalties for Failing to Comply with Disclosure Rules

There are penalties for promoters who fail to comply with their obligations under the disclosure rules. These are described in Section 98C(1) of the Taxes Management Act 1970.

An initial penalty can be imposed up to a maximum of £5,000 for each failure. The Special Commissioners will determine whether a penalty should be imposed in specific cases and if so at what the level. There is a right of appeal to the High Court or the Court of Session in Scotland against any penalty.

Where a promoter continues to fail to comply with their obligations after a penalty has been imposed, an authorised officer of the Board can impose a further penalty or penalties of up to a maximum of £600 for each day that the failure continues. There is a right of appeal against such a penalty to the General or Special Commissioners, with a further appeal to the High Court or the Court of Session in Scotland.

There are also penalties for users of schemes which do not involve an external promoter or where the promoter is based outside the UK. These operate in the same way and are set at the same level as those for promoters described above.

How the Revenue will apply the penalties

The Inland Revenue will seek to impose a penalty in all cases of non-compliance. However, there are a number of circumstances where we will not seek to impose a penalty on promoters who fail to meet their obligations. In particular, the Revenue will not impose a penalty where we can be satisfied that:

- a promoter has made a judgement on a reasonable basis in determining whether or not a disclosure is required; or
- the promoter can demonstrate there is a reasonable excuse for the failure to comply.

There is no statutory definition of what constitutes a reasonable excuse, but we will consider the circumstances of each case where a failure occurred. This is in line with our existing approach to penalties as described in Section 118(2) of the Taxes Management Act 1970.

xiv) Revenue to Issue a Reference Number

When a scheme has been disclosed, the Inland Revenue will issue the promoter a reference number within 30 days of receipt. The issue of this reference number does not indicate any judgement or assessment on the part of the Revenue of the scheme itself.

A promoter is then required to provide all clients who use the scheme with the reference number by 30 days from the later of the following dates:

- when they first become aware that the client has taken the first step to implement the scheme; or
- the receipt of the scheme reference number from the Inland Revenue.

Promoters are not required to give the reference number to clients who used the scheme before 18 March 2004.

B) Disclosure of Reference Numbers

i) General

Users of schemes and arrangements are required to inform the Inland Revenue that they have used a registered scheme or arrangement, normally when submitting the income tax, corporation tax or P35 return. Users should provide both the scheme reference number and the year in which the tax advantage is expected to arise. There is no obligation on a user if the promoter does not inform them of a reference number.

There are different rules for users who are not required to submit any of the returns mentioned above

In practice, this means that:

- where the tax advantage relates to income tax or capital gains tax, users should put the required information on their income tax return;
- where the tax advantage relates to corporation tax, users should put the required information on their corporation tax return; and
- employers using qualifying employment products should include the information on their P35 return rather than on either the income tax or corporation tax return. There is no need for employees to enter a number on their own tax return in this circumstance.

The returns on which the information should be included are those covering the year of assessment, accounting period or tax year in which the scheme reference number is received, or in which the expected tax advantage arises, whichever is the earlier.

Where the tax advantage covers more than one tax year or accounting period, the information must be provided on each return in which the tax advantage arises until it has been exhausted or until it is clear that no further tax advantage will arise.

Employees are not required to disclose scheme reference numbers on their personal tax returns if the scheme number has been notified to their employer. In these circumstances, the employer is responsible for declaring the required information on the P35 return or separately (see paragraph iv below).

ii) Individuals

Income tax returns will be amended to accommodate the additional information for the tax year 2004/05 onwards.

If the reference number is to be notified to the Inland Revenue on the separate form, this will be due by the normal return filing dates, that is the earlier of:

- by 31 January following the end of the tax year in which the scheme reference number is received; or
- by 31 January following the end of the tax year in which the tax advantage arises.

iii) Companies

Amended corporation tax returns will be issued from 1st October 2004. Users who receive a return which has not been amended should notify the scheme reference number and the year in which the tax advantage arises in a letter accompanying the return.

If the reference number is to be notified to the Inland Revenue on the separate form, this will be due by the normal return filing date, that is:

- where the company's period of account is 18 months or less, no later than 12 months from the end of the period in which the scheme reference number is received or in which the tax advantage arises, whichever is earlier;
- where the company's period of account is greater than 18 months, not later than 30 months from the beginning of the period of account in which the scheme number is received, or in which the tax advantage arises, whichever is the earlier.

iv) Employers

The P35 return will not be amended until the tax year 2006/07. Until this time, transitional arrangements are in place under which employers must notify the Inland Revenue separately. Disclosure of the scheme reference number and the year in which the tax advantage arises should be provided by 19 May after the end of the tax year in which the scheme reference number is received, or in which the expected tax advantage arises, whichever is the earlier. This information should be provided annually until the tax advantage has been exhausted.

If the reference number is to be notified to the Inland Revenue on the separate form this will be due by the normal return filing date, that is:

- by 19 May following the end of the tax year in which the scheme reference number is received; or
- by 19 May following the end of the tax year in which the tax advantage arises, if that is earlier.

v) What to do if revised return not available or if a return is not otherwise due.

Separate forms are available if disclosure is required for persons who otherwise do not have to make a return or where a revised return is not available. Form AIU4 is available from the IR web site (www.inlandrevenue.gov.uk/aiu/index.htm) or from the order line (Tel: 08459 000 404; Fax: 08459 000 604).

vi) Penalties for Non-Compliance

There are penalties for users of schemes who fail to notify the Inland Revenue of the scheme number that a promoter has provided them with. These are described in Section 98C(3) of the Taxes Management Act 1970.

The amount of the penalty increases for each instance of failure to notify the Inland Revenue:

- a penalty of £100 for the first failure;
- a penalty of £500 for a second failure;
- a penalty of £1,000 for a third and all subsequent failures.

These penalties are determined by an authorised officer of the Board with a right of appeal to the General or Special Commissioners, and a further appeal to the High Court or Court of Session in Scotland.

The Inland Revenue will seek to impose a penalty in all cases of non-compliance. However, we will not seek a penalty on users of schemes who fail to meet their obligations where we can be satisfied that:

- they have made a judgement on a reasonable basis in determining whether or not he is required to make a disclosure; or
- they have a reasonable excuse for the failure to comply.

There is no statutory definition of what constitutes a reasonable excuse, but we will consider the circumstances of each case where a failure occurred. This is in line with our existing approach to penalties as described in Section 118(2) of the Taxes Management Act 1970.

Appendices

1. Detailed meaning of specified financial product

Loans

This includes all forms of borrowing and lending, including all securities (e.g. a qualifying corporate bond (QCB)).

The draft Regulations which were published on 17 May excluded simple loans. The final Regulations do not contain this exclusion and therefore all loans are potentially disclosable as financial products. However, simple loans may be excluded by virtue of paragraph 6(2) or paragraph 8.

Derivative contracts

The definition of a derivative is anything which is within the very broad definition of derivative in Schedule 26, FA 2002. Under Schedule 26, certain derivatives are not taxed as income, but this exclusion does not apply for disclosure purposes and hence any derivative described in Schedule 26 is a potentially disclosable financial product. This applies whether or not the user of the scheme is liable to corporation tax.

Repos

This is an agreement for the sale and repurchase of securities of the kind described in paragraphs (a) to (c) of subsection (1) of section 730A of the Income and Corporation Taxes Act 1988.

Stock lending agreements

Stock lending arrangements within the meaning of section 263B(1) of the Taxation of Chargeable Gains Act 1992.

Shares

The draft regulations published on 17 May excluded ordinary shares. This exclusion has not been carried through to the final Regulations and therefore an ordinary share is a potentially disclosable financial product. However, ordinary shares may be excluded by paragraph 6(2) or paragraph 8.

Contracts which are in substance a loan

Under UK generally accepted accounting practice (UK GAAP), certain contracts, or combinations of contracts, which are not in legal form loans or financing contracts are required to be accounted for as though they were loans or other similar financing arrangements. This involves the application of accounting substance over legal form and is manifest in particular in Financial Reporting Standard 5 (FRS5) issued by the Accounting Standards Board. This approach is also present in Statement of Standard Accounting Practice 21 relating to leases, but for the purposes of paragraph 7 anything which is a finance lease for the purpose of UK GAAP (SSAP 21) is not treated as being accounted for as a loan.

UK GAAP here means generally accepted accounting practice as applicable to companies to which the Companies Act 1985 applies (section 836A ICTA 1988). Where the person to whom the test is to be applied is not a company, that person will be treated as if he is nonetheless subject to the requirements of the 1985 Act in accounting for the transaction. For periods beginning on or after 1 January 2005, the definition of UK GAAP will be in section 50 Finance Act 2004. The effect of this is that, for such periods, a company which uses International Accounting Standards (IAS) to draw up its accounts will apply those Standards to determine whether a contract or combination of contracts is accounted for as a loan etc. IAS does not contain any direct equivalent to FRS 5 but, in drawing up accounts, companies are nonetheless required to have regard to the substance of the matters concerned. There would not seem to be any material difference between UK GAAP and IAS on the question of accounting for particular contracts in accordance with their substance.

The following are examples of transactions that are not within any of the products listed in paragraph 7(1)(a)-(e) but which may nevertheless be financial products within paragraph 7(1)(f) and hence form, or form part of, disclosable arrangements because, in substance, they may represent the making of a loan:

- A rent factoring transaction – see section 43A to 43G ICTA
- A financial reinsurance contract
- A sale of receivables, e.g. as part of a securitisation exercise

The tests for a prescribed financial product will be applied to individuals (including members of a partnership), companies and trustees.

Premium Fee Test

The premium fee test is failed if a promoter would be able to obtain a premium fee for the arrangements. But if "no promoter, and no person connected with a promoter, might reasonably be expected to obtain a premium fee", the test is satisfied. This is therefore a hypothetical test which focuses on whether any promoter could charge a premium fee if he chose to do so. Whether or not the actual promoter charges a premium fee is not sufficient, although the test will be failed if the promoter does so.

The definition of a premium fee is set out in paragraph 8(5). There are two limbs, both of which must be present. Firstly, the premium fee is a fee which is chargeable by virtue of the tax avoidance element of the arrangements. Secondly, the premium fee is attributable to, or contingent on the obtaining of, the tax advantage. This test is therefore looking for tax advice which is in some sense innovative and valuable, which the adviser can use to obtain an abnormal fee from a client who cannot obtain similar advice from a variety of other advisers.

The fact that the actual promoter is not charging a premium fee is not sufficient. The question is whether it might reasonably be expected that another promoter could charge a premium fee if he wished to do so.

The test should be applied from the perspective of a client who is experienced in receiving tax advice or other services of the type being provided. If such a client would regard the advice as valuable and not generally available, he would be prepared to pay a premium for it; by contrast, if such a client could obtain similar advice elsewhere, he would be unwilling to pay more than a normal fee for it.

Premium fee definition

The first limb of the definition is that a premium fee is a fee chargeable by virtue of the tax avoidance element of the arrangements. A fee will only be by virtue of the tax avoidance element if the ability to obtain it derives from this element. The question is whether the tax avoidance element is such that a promoter who wished to do so would be able to charge a premium fee. A fee will not be classed as a premium fee solely on account of factors such as:

- The adviser's location – fees in some parts of the country are higher than in others, but this is not by virtue of the tax avoidance element.
- The urgency of the advice – in some commercial deals, the advice is needed urgently and a higher fee may be charged, but this is not by virtue of the tax avoidance element.

- The size of the transaction – if a large amount is at stake on a deal, the tax adviser may wish to increase his fee to reflect the greater level of exposure in the event that the client should sue for negligence, but this is not by virtue of the tax avoidance element.
- The adviser's skills – some advisers normally charge more for advice than others to reflect the perceived higher quality of advice provided, but this is not necessarily by virtue of the tax avoidance element.
- The scarcity of appropriately skilled staff – some areas of tax advice are more complex than others and fees may be higher to reflect this, but this is not necessarily by virtue of the tax avoidance element.
- General fee-charging arrangements – there may be tax advisers whose normal approach is to charge a fee linked to the tax saved or repayment obtained, or contingent on the tax advice being correct, but this is not necessarily by virtue of the tax avoidance element.
- The normal variations in fee-billing arrangements – professional firms will often negotiate around their standard hourly charges to reflect the client's willingness to pay, but this is not necessarily by virtue of the tax avoidance element.

On the other hand, such factors may exist alongside other factors which mean that the fee is a premium fee chargeable by virtue of the tax avoidance element.

The second limb of the definition is that a premium fee is a fee which is either:

- To a significant extent attributable to the tax advantage. It is the amount of the fee which must be attributable to the tax advantage, not merely the existence of the fee. Such a fee may be:
  - ➢ A fee which significantly exceeds the fee which would normally be charged by the adviser for that sort of advice.
  - ➢ A fee which is calculated as a proportion of the tax advantage expected to be obtained.

  For example, take an adviser who normally charges £100 per hour and takes 10 hours to advise on a particular transaction. If he could charge a flat fee of £5,000 for the current transaction if he so wished, this may be a premium fee. The fact that he could charge a flat fee of £1,000 instead of an hourly rate would not make this a premium fee though. All tax advisers rely upon their professional reputations and it is therefore not sufficient

that the tax adviser's ability to obtain fees at his normal charge-out rate is in an indirect sense attributable to his giving advice which is regarded as satisfactory by his clients, and that his clients are likely to be satisfied if he is able to provide advice which leads to a tax advantage. Such an indirect linkage is not sufficient to constitute a fee "attributable to a significant extent" to the tax advantage expected to be obtained from the arrangements in question.

- A fee contingent on the obtaining of the tax advantage. A fee will not be classed as a premium fee solely on account of its being contingent on the transaction taking place, even though the tax advantage is indirectly dependent on this.

Confidentiality Test

The confidentiality test is whether a promoter might reasonably be expected to wish to keep the tax avoidance element confidential. It is not relevant that tax advisers are under a duty of confidentiality to clients – this is specifically ignored. Nor is it relevant that tax advisers may be under other legal obligations, for example under competition law not to engage in anti-competitive behaviour. This is because the test focuses on what a promoter might wish to keep confidential.

The test looks at what the promoter might reasonably wish to keep confidential from competitors in order to preserve the promoter's own competitive advantage. The competitive advantage arises from the adviser being aware of a tax avoidance opportunity and his ability to build this into the arrangements which he advises his client to undertake. The tax avoidance element is only capable of generating any competitive advantage for the promoter if other competitors are unaware of it and hence could not have included it in their advice to clients. Where the tax avoidance element is well-known to other tax advisers, against whom the promoter is in competition, the confidentiality test will not be failed.

Since the confidentiality test is concerned only with whether a promoter might reasonably be expected to wish to keep the tax avoidance element of the arrangements confidential, it is not concerned with whether a promoter might wish to keep other elements of the arrangements confidential, such as the deal size, the identity of the parties etc.

Off-Market Test

Paragraph 8(4) applies where a promoter (or a person connected with a promoter) becomes a party to the financial product. This will generally be a bank which becomes a party to a loan, derivative or other financial product but it could be any other promoter.

Where paragraph 8(4) applies, the test is whether any of the terms of the financial product differ significantly from the terms which the other party to the financial product could have obtained in the open market. For example, a bank would normally be prepared to lend money to a customer at LIBOR plus a margin to reflect the customer's credit-worthiness. A loan which is otherwise on normal terms and is at such a rate would not fail the test in Regulation 8(4).

The test is whether the customer could have gone to another bank and obtained an equivalent financial product, in this example a loan at a similar rate of interest and other terms. Where the financial product does not contain any tax avoidance element, or where there is no implicit premium fee for the promoter built into the pricing of the financial product, the customer would be able to go to another bank and obtain the identical financial product on similar terms. However, if the promoter has a tax avoidance idea from which he wishes to generate a profit, reflecting his competitive advantage in having identified the opportunity, the financial product will be priced at a rate which differs from the rate which the customer would be offered if he invited other banks to quote for the equivalent financial product, assuming fully competitive financial markets.

For example, assume market interest rates are such that a taxpayer could enter into an interest-rate swap at LIBOR floating for 5% fixed. A taxpayer who wanted to do so could obtain a swap at LIBOR floating (receive) for 6% fixed (pay) but would expect to receive a premium for doing so. If a bank invented an innovative interest-rate swap carrying a significant tax advantage, the taxpayer might be willing to deal without receiving any premium. The bank would have built an implicit premium fee into the terms of the swap. Applying paragraph 8(4), the question is what the open-market price would be. In an open market, the bank would be unable to obtain this premium because the taxpayer could obtain an equivalent swap from another bank, and this would drive the price down to the market-clearing level. So this innovative swap would not be on open-market terms and would fail the paragraph 8(4) test.

Tax Avoidance Element of Arrangements

The Regulations operate in various places by reference to the tax avoidance element of the arrangements. The places are as follows:

- The Information Regulations require disclosure of sufficient information as might reasonably be expected to enable an officer of the Board to comprehend the manner in which the proposal is intended to operate, including information explaining each of the tax avoidance elements.
- The Promoters Regulations prevent a person from being regarded as a promoter where

  - in the course of providing tax advice, they are not responsible for the design of any of the tax avoidance elements or
  - they are not responsible for the design of all of the tax avoidance elements and lack full knowledge:
    - ➢ of whether the arrangements (or proposal) are notifiable arrangements (or a notifiable proposal) or
    - ➢ to comply with the disclosure obligation.
- The Financial Products Regulations define the confidentiality test by reference to a promoter's reasonable wish to keep the tax avoidance element confidential, and defines the premium fee by reference to a fee which is chargeable by virtue of any tax avoidance element.

In each of these places, the tax avoidance element is "any element of the arrangements (including the way in which they are structured) from which the tax advantage expected to be obtained arises". This "element" may be

- a financial product
- a way of combining that financial product with other elements of the arrangements or
- a way of interpreting the tax legislation in relation to the financial arrangements, i.e. the tax analysis which underlies the structuring of the arrangements.

The tax advantage referred to is the one which is a main benefit of the arrangements.

2. Detailed meaning of specified arrangement

Securities and interests in securities

The list of securities is based on section 420 ITEPA 2003 as introduced by Schedule 22 FA 2003; they are:

- shares in any body corporate (wherever incorporated) or in any unincorporated body constituted under the law of a country or territory outside the United Kingdom,
- debentures, debenture stock, loan stock, bonds, certificates of deposit and other instruments creating or acknowledging indebtedness,
- warrants and other instruments entitling their holders to subscribe for securities (whether or not in existence or identifiable),
- certificates and other instruments conferring rights in respect of securities held by persons other than the persons on whom the rights are conferred and the transfer of which may be effected without the consent of those persons,
- units in a collective investment scheme, which means arrangements which are made with respect to property of any description, including money, and the purpose or effect of which is to enable persons taking part in the arrangements to participate in or receive profits or income arising from the acquisition, holding, management or disposal of the property or sums paid out of such profits or income.
- futures, which means rights under a contract for the sale of a commodity or other property under which delivery is to be made at a future date at a price agreed when the contract is made; and
- rights under contracts for differences or contracts similar to contracts for differences, the latter being a contract the purpose or pretended purpose of which is to secure a profit or avoid a loss by reference to fluctuations in the value or price of property or an index or other factor designated in the contract.

No exclusions from being securities

The exclusions from being "securities" in subsection (5) of section 420 do not apply for these purposes. This results in, for instance, cheques and other items being within the meaning of securities. This of itself does not trigger a requirement to disclose the simple act of paying an employee's salary using a cheque, because in these circumstances there will not be a tax advantage. If that employee receives £1,000 then tax of £400 (assuming a rate of 40%) will be paid.

This means that for the purposes of the regulations securities has a significantly wider meaning than it does for the purposes of the legislation in Part 7 of ITEPA 2003 dealing with employment-related securities. This ensures that if arrangements involve the provision or use of items of the sort listed in section 420(5) and those arrangements are expected to result in a tax advantage then the arrangements must be disclosed. Where, however, statute provides that the item being used benefits from a tax advantage, and the arrangements in their entirety consist of the provision of that item they do not, of themselves, need to be disclosed. Where, however, the provision of the item is part of a wider arrangement which obtains a tax advantage, or where the provision is made to exploit a perceived weakness in the legislation, then the arrangements constitute notifiable arrangements.

Approved share schemes & EMI

Securities and securities options obtained through an arrangement wholly comprising an Inland Revenue approved share/share option scheme (Share Incentive Plan, Save as You Earn, or Company Share Option Plan) which benefits from a statutory tax advantage are exempt from disclosure. This exemption also applies to any arrangements which have been submitted to the Inland Revenue during the process of considering them for approval. If approval is refused then the arrangements become disclosable.

Enterprise Management Incentives (EMI) arrangements are also exempt from the disclosure requirement where they comprise in their entirety the grant of a qualifying (tax advantaged) EMI share option, together with such steps, if any, as are reasonably necessary to facilitate the grant of such an option.

Where steps taken are clearly connected to the grant of the qualifying EMI share option and are not designed to circumvent any of the EMI qualifying rules such arrangements will not need to be disclosed.

Where however specific steps are being taken to bring a company which would not otherwise qualify within the EMI rules this will need to be disclosed. These may include:

- reducing the company’s gross assets
- restructuring the business so one of the group companies trades mainly in the UK
- reorganising the ownership of the company’s shares

The two examples below help to illustrate where steps taken do not need to be disclosed and at the other end of the spectrum where disclosure is required.

For example: Company A has two authorised and issued ordinary shares, which are held one each by Mr and Mrs A. All of the conditions for issuing an EMI share option are fulfilled, but the company cannot issue an option over shares to an employee until the capital base is reorganised. The company therefore increases the authorised share capital to 3,000 ordinary shares, and then makes a 999 for 1 bonus issue. Mr and Mrs A now hold 1,000 shares each. The company issues an EMI share option to an employee over 100 of the unissued shares. The company restructuring is clearly connected with the grant of the qualifying EMI share option. The arrangement does not need to be disclosed since the steps taken were necessary and reasonable and were not designed to circumvent any of the EMI qualifying rules.

At the other end of the spectrum, Company B which trades mainly outside the UK wants to grant an EMI share option, but fails the ‘qualifying trade’ test. An advisor suggests that the company should split the trade between UK and overseas, and devises a complex corporate structure that enables the company to meet the qualifying trade test, while the substance of the company’s activities remains unchanged. This restructuring is clearly designed to circumvent the EMI qualifying rules, and must be disclosed.

The same principle applies where a company enters into arrangements to put itself in a position to apply for approval under an approved scheme, if those arrangements are not disclosed as part of the approvals process.

<u>Taxed (unapproved) share schemes</u>

Taxed employee share schemes (often referred to as "unapproved" schemes) will only need to be disclosed where they confer a tax advantage. The test of whether there is a tax advantage is a comparative one, by reference to the principles underpinning the legislation, defined by the rules in ITEPA 2003 relating to the acquisition of employment-related securities. The principles behind those rules seek to tax value at the time it is accessed by an employee and are comparable with the position where cash of that value is paid at that time. If, on making this comparison, the tax payable using employment-related securities is the same as it would be using cash then no tax advantage exists and the arrangements do not need to be disclosed.

The application of this cash comparison test will usually be straightforward. For example, value of £1,000 is accessed by the employee on exercising a share option. The tax expected to arise by virtue of the employment-related securities option legislation in Chapter 5, Part 7, ITEPA 2003, is £400 (assuming liability at 40%) – the same amount that would be payable if £1,000 cash were given to the same employee. Provided the option is not part of a wider arrangement which gives rise to a tax advantage, it does not need to be disclosed

A similar logic applies where, for example, the value takes the form of an award of restricted employment-related securities to which Chapter 2 applies or convertible employment-related securities to which Chapter 3 of Part 7, ITEPA 2003 applies.

Elections in respect of restricted shares

When employees acquire employment-related securities that are subject to restrictions that reduce their value, payment of income tax on the proportion of the value that represents the effect of the restrictions is deferred until those restrictions are lifted or varied. In such circumstances the employee and employer can jointly elect to treat the securities as if they were not restricted. This decision to opt out of a statutory deferral does not confer a tax advantage and does not therefore need to be disclosed. The employee is paying tax on value that is treated for tax purposes as having passed at the time the securities are acquired whereas in reality that value will not pass until a later date. However, if the election in respect of those securities is a feature of arrangements to avoid tax then the disclosure is required.

Ratchets, Geared Growth and other similar arrangements

Where an employee acquires employment-related securities, those securities are treated as the employee's investment provided the employee either pays full market value for them, or pays tax on the value received in accordance with the rules in Part 7 ITEPA 2003 because a lesser amount was paid. Normal commercial growth in the value of that investment, proportionate to the underlying growth in the value of the company, is not value obtained by way of remuneration and is therefore not within the scope of Part 7 ITEPA 2003. Similarly, it will not be regarded as remuneration value for the purpose of applying the tax advantage test.

Where arrangements involving employment-related securities will pass value to an employee (or any other person by reason of that employee's employment) in excess of normal commercial growth proportionate to the employee's investment, then that bonus value is treated as passing by reason of employment and therefore by way of remuneration. It is not necessary to speculate on what normal commercial growth is in these circumstances. An appropriate comparison can be made by modelling the arrangement in their entirety on the assumption that there is no commercial growth in the shares over the period of the arrangements. If on such modelling the employee receives value on which the tax expected to be payable is less than the tax that would be payable if that value were received in cash then the arrangement will need to be disclosed.

Dividends

The payment of a normal commercial dividend to an employee shareholder out of a company's annual or retained trading profits will not generally be regarded as conferring a tax advantage in the employment product context where the dividend is chargeable under Schedule F.

Where a non-commercial transaction (which could include paying a dividend) artificially manipulates the value of employment-related securities and is part of arrangements designed to transfer value to an employee the anti-avoidance rules in Part 7 ITEPA 2003 will come into play to ensure the right amount of income tax is payable on the value transferred. If, however, a promoter takes the view that the value will not, despite the provisions in Part 7, be subject to the same amount of income tax as would be payable if that value were passed in cash, then the arrangement needs to be disclosed, since a tax advantage is expected to arise.

Cashless exercises

It is common in employee share schemes for a loan to be made to enable the employee to purchase the shares when options are exercised. Shares will then be immediately sold and the loan repaid. This is often referred to as a "cashless exercise". The making of the loan is a benefit within the rules in Chapter 7 of Part 3 of ITEPA. Where tax is properly applied in accordance with the rules in that Part then the existence of a cashless exercise does not require the arrangements to be disclosed.

Forfeitable Shares

The statutory rules recognise the fact that employment-related securities may be lost (forfeit) if certain events occur and defer the time at which the employment benefit is measured until that risk has gone. This means that the tax charge does not arise until that point. This deferral does not of itself result in the conferring of a tax advantage provided that the forfeiture condition is for sound commercial reasons and not tax-driven. However where a forfeiture condition is imposed with the intention of giving the employee all the rights, privileges and benefits of share ownership over a period without tax charge, then a tax advantage arises and the arrangements are notifiable. Similarly, where the forfeiture provision is artificially created for tax purposes the arrangement will be notifiable.

Long Term Incentive Plans (LTIPs) and Nil-cost options

There is no difference between a nil-cost option or other form of LTIP arrangement chargeable under the employment-related securities options rules and an option where the strike price is equal to the market value of the underlying securities at the time the option was granted. Therefore application of the cash comparison will show that there is no tax advantage and

unless the options are part of a wider scheme or arrangement which do convey a tax advantage then the arrangement will not be notifiable.

Memoranda of understanding on taxed share schemes

The Inland Revenue has entered into a number of memoranda of understanding (MOU) in relation to the operation of the employment-related securities' rules. Those MOUs do not contain concessions or special tax treatment. They simply set out how the rules work in relation to certain prescribed circumstances. So far as arrangements involving securities, in their entirety, fall within the scope of an MOU they will not be notifiable under the disclosure rules because no tax advantage arises. However, if the scheme or arrangements go wider than what is described in an MOU then it is a question of fact whether those arrangements, when viewed as a whole, give rise to a tax advantage within the meaning of the disclosure rules.

The Use of Offshore Employee Trusts for Employee Share Schemes

Where arrangements include the formation of a trust, the promoter of the arrangements will need to consider whether there is a tax advantage. In doing so, they should consider the tax that would be payable (including CGT payable by the trustees) and if they decide to use an offshore trust, they will need to notify the arrangement if there is a reduction in the total UK tax. However in comparing the tax that would have been paid if the trust were onshore, the promoter would need to take account of ESC D35, which removes the UK tax charge on the trustees in certain circumstances. If ESC D35 would not apply, and the use of the offshore trust will effectively extend the exemption from CGT beyond that envisaged by the ESC, then the arrangement should be notified. This will be the case even where the arrangements are an incidental feature of a share scheme (whether or not the share scheme is tax-advantaged). The tax advantages offered by the approved share schemes and EMI do not extend to the CGT liability of the trustees, and the use of an offshore trust is not an inevitable feature of a scheme.

What are payments to trustees and intermediaries?

'Payments to trustees and intermediaries' are any payments by an employer or a person connected with the employer to:

- a trust (whether established in the UK or overseas) for the benefit of an employee, a person associated with an employee, or a class of persons including an employee or an employee's associate or
- a third party entitled under the terms of an employee benefit scheme to hold or use the payment for the provision of benefits to employees or an employee's associate.

Certain employment arrangements involving payments to trusts or intermediaries are outside the disclosure rules. These are payments to trusts established for the purposes of:

- an approved pension scheme
- an approved share incentive plan
- an approved SAYE scheme
- an approved CSOP

This exemption also applies in respect of any arrangements which have been or will be submitted to the Inland Revenue for approval as an approved pension scheme.

Payments to trusts established to hold funds to which S329AA ICTA1988 applies (personal injury damages in the form of periodical payments) are also exempt from disclosure.

<u>What are loans?</u>

'Loans' are any arrangements which include the making or releasing of any loan by an employer (or a person connected with an employer) for the benefit of an employee or any other person by reason of an employee's employment.

Any arrangements, which in their entirety, are either taxable as a benefit under Part 3 Chapter 7 of ITEPA (or would be but for the exemptions in S176 to S178 and S180), or are not taxable because of the limited exemption for bridging loans under S288/289 ITEPA are outside the disclosure rules.

3. Further guidance on definition of promoters

a) Responsibility for design

A person may be "to any extent responsible for the design of" the arrangements or proposed arrangements if he contributes to the design. An adviser who is consulted on the design and gives an opinion that it achieves its intended effect, without offering any suggestions for changes, is not a designer. An adviser who is consulted and explains why the design does not work or offers suggestions for changes to it may be a designer, unless excluded by the regulations.

The Tax Avoidance Schemes (Promoters and Prescribed Circumstances) Regulations 2004 prescribe circumstances in which persons are not to be regarded as promoters by reason of being responsible for designing a notifiable proposal or arrangements. These circumstances are groups, employees, secondary designers, and those who cannot comply.

Regulation 2 - Tax Services to Companies Within the Same Group

A company which provides tax services to another company within the same group is outside the definition of a promoter. This ensures that notifiable arrangements devised within a group for its own use are notifiable in the same way as arrangements devised by a single company for its own use.

This exclusion does not extend to consortium companies or joint ventures.

In general terms, a company is classed as in the same group if it has a 51% or greater share in another company's ordinary share capital, profits or assets. Whether a company is classed as in the same group depends on whether they would, under section 170 of the Taxation of Chargeable Gains Act 1992, be members of the same group for the purposes of sections 171 to 181 of that Act if section 170 TCGA:

- substituted references to 51 per cent subsidiaries for references to 75 per cent subsidiaries; and
- subsection (3)(b) and subsections (6) and (8) were omitted.

For example, if D is a subsidiary of C, and C a subsidiary of B and B a subsidiary of A, and A, B and C each have a 51 per cent interest in the ordinary share capital, profits and assets of a directly held subsidiary.

Regulation 3 – employees

The primary legislation provides that a person is a promoter if he does certain things in the course of a relevant business. It was pointed out during consultations that it was possible to read this as including persons who are employees of tax advisory firms. It was suggested that if there is a disagreement between a professional firm which does not believe disclosure is required and an employee of the firm who has given the tax advice, the employee could be in a difficult position and might be found in default of the disclosure rules if he did not personally disclose. It was never intended that there should be any such obligation on employees

Regulation 3 makes it clear that employees (and office-holders) are not to be treated as promoters, whether they are employed by a promoter or are employees of the taxpaying user. For this purpose, any employee of a person connected with such a promoter or user is treated as though that promoter or user were themselves the promoter or user. This ensures that an employee of a connected company is able to obtain the benefit of this exclusion. For example, an employee of a professional firm might strictly be employed by a service company; or an employee in a tax department of a user might be employed by a company other than the company which obtains the tax advantage

The exclusion of employees in this way ensures that the obligation to disclose falls on the employer.

It has also been suggested that partners in a partnership (or members of an LLP) might be in a similar position. The law does not provide any protection for such partners. However, where the partner is potentially a promoter as well as the partnership, compliance with the obligation by the partnership will discharge the partner's obligation to disclose (S308(4)).

Regulation 4 – secondary designers

Regulation 4 excludes certain persons from being treated as promoters by reason of being to any extent responsible for the design of the proposal or arrangements. Such persons may still be promoters if they make the notifiable proposal or arrangements available for implementation.

There are three situations which are excluded, where the primary legislation would designate persons as promoters by reason of their being involved, to any extent, in the design of the arrangements or proposed arrangements. The three exclusions are as follows:

- The benign tax advice test.
- The non-tax adviser test.

- The ignorance test.

The benign tax adviser test is at regulation 4(2). This applies where, in the course of providing tax advice, a person is not responsible for the design of any of the tax avoidance elements. For example, if one promoter has devised the arrangements but consults another firm in relation to a particular element of those arrangements and the second firm provides tax advice. The second firm will not be a promoter, despite being involved in the design of the overall arrangements, as long as it is not involved in the design of the tax avoidance element of the arrangements. This might happen if a firm was engaged to advise on the best way to achieve a scheme and advice was given to change the design so that a quoted eurobond was used to avoid withholding tax. The use of a quoted eurobond is a well-known feature of the tax system which would not be expected to result in either a premium fee or the wish to keep the technique confidential. (Nor is the promoter usually a party to the financial product.) That law firm would be providing tax advice and would be to an extent responsible for the design of the overall arrangements but would only have provided benign tax advice.

Regulation 4(3) applies to relevant businesses other than a bank or securities house (or company in such a group). Such businesses are not treated as promoters whatever the extent of the design of the arrangements (or proposed arrangements) for which they are responsible as long as they have not provided any tax advice in carrying out their responsibilities. For example:

- if a promoter consults a law firm (which has a relevant business which includes giving tax advice) in relation to company law, the firm may give advice as to the design of the arrangements without becoming a promoter as long as it provides no tax advice in the course of carrying out its responsibilities.
- if a promoter consults an accounting firm in relation to accounting, the firm may give advice as to the design of the arrangements without becoming a promoter as long as it provides no tax advice in the course of carrying out its responsibilities.

Any “benign” tax advice of the kind mentioned above in relation to Paragraph 4(2), such as “routine” tax input into the form and terms of any documentation implementing a proposal, where any tax advice on the “design” of the proposal or arrangements has been provided by others, will not be treated as tax advice for these purposes.

Under regulation 4(4), a person is not regarded as a promoter for the purposes of the disclosure regime if they could not reasonably be expected to have either:

- Sufficient information to enable them to know whether or not the arrangements are notifiable arrangements (or the proposal is a notifiable proposal). For example, a bank may be involved in the design of a financial product but may have insufficient knowledge of the overall arrangements to know whether any of the tests at paragraph 8 of the Financial Products Regulations has been failed.
- Sufficient information as would enable that person to comply. The information regulations require the promoter to explain the tax avoidance element of the arrangements or proposed arrangements and to list the statutory provisions on which the tax advantage is based. Some persons, for example banks or law firms brought in to advise on particular aspects of the arrangements, may be unable to comply with this obligation since they do not have sufficient information about the tax advantage

For these purposes, where having the relevant "information" depends not merely upon factual knowledge, but upon the application of some particular expertise, persons will not normally be expected to have such an expertise if it falls outside their own area of professional expertise (unless the matters in question can reasonably be said to be common knowledge amongst business and professional persons generally).

However, this paragraph is only available where a person is not responsible for the design of all the tax avoidance elements. So it is only available to a secondary designer, not the primary designer.

Regulation 5

Regulation 5 prevents a person from being treated as a promoter by reason of being involved in the organisation or management of the arrangements, unless that person is connected with a person who has designed the arrangements.

b) Making a notifiable proposal available

Making available for implementation is not the same as communicating a design. Designing necessarily involves communication, but not all design can be making available.

Making available for implementation is not synonymous with making fit for purpose. The latter is part of the design process

A person will not be making a proposal "available for implementation by other persons" unless he communicates the proposal to a taxpayer who would be in a position to obtain the relevant

tax advantage. So except where the service provided is distribution or introduction, no one can make available whose client is not the end user of the "solution".

A non-designer whose client is the user will be making available.

But a designer whose client is the user will not be making available unless they have:

- marketed the scheme;
- proactively sought clients for their "solution"; or
- provided an existing solution in response to a request either for ideas generally, or for a specific commercial objective.

Except in the case of “conduit” or “agent” arrangements, a person who merely communicates a proposal to another person to enable that second person to market or circulate the proposal to others, or to incorporate the idea into their own proposal, (rather than to enable the second person to implement the proposal), will not be making the proposal available for implementation (although, of course, the second person may be making the proposal available for implementation).

In cases of mere “conduit” or “agent” arrangements – i.e. if a person communicates a proposal to a second person merely so that the second person can act as his distributor to taxpayers who would be in a position to obtain the relevant tax advantage (the second person in reality acting wholly or to a substantial degree for the benefit of the first person or a person connected with him) - the first person would himself be making the proposal available to the relevant user.

A person cannot make something available to another person if that other person already has it. So, for example, a professional adviser who is approached by a client to advise on the effects of a specific proposal which has been generated by that client or another person, and who simply provides that advice, will not be making the proposal available to his client. Similarly, a professional adviser in that situation who suggests changes to the proposal (whether of a minor or substantive nature, provided that the adviser does not merely provide what is in substance an existing solution) will not be making the proposal available to his client.

If a client approaches a professional adviser with a specific tax problem or tax issue arising from specific facts and circumstances, the professional adviser does not make a notifiable proposal available for implementation by his client merely by virtue of providing professional analysis and advice in response to that specific request (although, of course, such an

professional adviser may be a promoter by being responsible to some extent for the design of a notifiable proposal). On the other hand, a professional adviser or any other person who makes an unsolicited approach to another person with a proposal may be making that proposal available to them. In addition, a person who communicates a proposal to another person in response to a general request for ideas or proposals may be making that proposal available to them. For example, if a person receives a general request from a client or potential client for "any proposals that you might have for reducing my tax bill", and responds to that request with one or more specific proposals, he may be making those proposals available to his client or potential client. In such cases, whether the proposal is "made available for implementation" will depend on whether the communication of the proposal is sufficiently detailed and the surrounding circumstances are such that it may fairly be said that the proposal is then available for implementation by the client (see further below).

COMPARISON: DESIGN vs MAKING AVAILABLE

The following table indicates how the Inland Revenue sees the distinction between designing arrangements and making them available for implementation

Idea is brought to adviser who confirms it is effective.	*Neither designer nor making available.*
Idea is brought to adviser who identifies flaws and/or advises minor changes.	*Designer. Not making available.*
Idea is brought to adviser who advises major changes.	*Designer. Not making available unless (*) applies.*
Specific commercial objective is brought to designer who formulates or assists in formulating bespoke solution.	*Designer. Not making available unless (*) applies.*
General commercial objective is brought to designer who advises.	*Designer (unless designed by another). Making available.*
General enquiry of adviser – do you have any solutions?	*Designer (unless designed by another). Making available.*
Adviser with existing solution seeks client with relevant objective.	*Designer (unless designed by another). Making available.*
Designer of "solution" obtains adviser's client list for fee.	*Neither designer nor making available.*
Designer of "solution" obtains introduction to client from adviser for fee.	*Not designer. Making available (unless pure introduction with no marketing).*
Adviser distributes "solution" designed by another.	*Not designer. Making available.*
* Adviser incorporates what is in substance an existing solution into advice	*Designer. Making available*

4. Timing of disclosure for promoters

The timing of disclosure depends on whether the promoter has made a proposal available for implementation. If so, the guidance below applies. If not, disclosure must be made five working days after the first transaction.

A scheme or arrangement is 'available for implementation' when a promoter provides sufficient details to clients or potential clients to enable them to consider whether they should implement the scheme or arrangements. There is no requirement for the scheme to be tailored to any particular client.

A proposal is "made available for implementation" for these purposes when a promoter makes the proposal available to a taxpayer who could obtain the relevant tax advantage, at a stage when the proposal is sufficiently advanced and the proposal is communicated in sufficient detail that the taxpayer can decide whether or not to implement it. The precise time when this will occur will depend on the circumstances.

In some circumstances, whether a scheme is something that can be implemented and so in being put to a potential client amounts to making 'available for implementation' might be a matter of degree. However, schemes discussed in the following circumstances would not be liable to be disclosed:

- spontaneous discussion of new ideas which will need more research before any implementation would be possible;
- general discussions about different types of tax planning services available;
- a general outline presentation at a tax conference which does not go into any of the detailed mechanics of how the scheme would operate, or sets out an 'untested' idea.

On the other hand, if, for example, a bank, broker or other person approaches a client or potential client, either unsolicited or in response to a general request for ideas or proposals, and provides them with a presentation, term sheet or similar document, such that the client or potential client has a sufficient understanding of the proposal and its intended tax effects to be able to decide whether to implement the proposal (and would be in a position to obtain the relevant tax advantage), the bank, broker or other person will be making the proposal available for implementation by them.

It is not necessary in such circumstances for the proposal to have been tailored to the particular client – it might be sent to them in generic form.

Similarly, the proposal need not be made available to the client or potential client in written form but could be by way of oral presentation of the proposal.

Moreover, there may be cases where two or more proposals are made available for implementation by the relevant taxpayer, and the taxpayer does not decide which to use until the very last minute when the transaction is about to proceed. The fact that there are two or more alternative proposals will not of itself avoid the requirement to disclose each of them, at the stage when each alternative is "made available" for implementation.