

**The OECD's Project on High Net Worth Individuals
Discussion Paper for Public Comment
Response by The Chartered Institute of Taxation**

1. Introduction

- 1.1 The Chartered Institute of Taxation (CIOT) is pleased to comment on the discussion paper issued in October 2008 for public comment by the OECD in regard to its project on High Net Worth Individuals (HNWIs).
- 1.2 The discussion paper follows on from an OECD report entitled "Study into the Role of Tax Intermediaries", which was published in January 2008 and focused on the large corporate taxpayer segment, and concentrates on the potential of co-operative compliance approaches and how compliance relationships within existing legal frameworks can be improved.

2. General comments

- 2.1 HNWIs are not a homogenous group; they are a diverse population with widely different personal and business arrangements. Their approach to "risk" also varies quite widely. At best, the only link between HNWIs will be the scale and complexity of their arrangements.
- 2.2 The definition of a HNWI also varies between countries and in the UK there is no definitive definition. However, in defining the term "very wealthy" for a study on behalf of the UK's HM Revenue & Customs (HMRC), the National Centre for Social Research drew up a working definition of "very wealthy" with HMRC as "those who owned £5 million or more of disposable assets". However, this takes no account of the fact that many very wealthy people own no assets at all, since much of their wealth is held perfectly properly through trusts.
- 2.3 We would suggest that, initially at least, the focus should be on those HNWIs with access to at least £500 million of assets.
- 2.4 Those HNWIs are often very mobile and can relatively easily move their domestic and business relationships to lower tax jurisdictions. Therefore, to maintain their connection with the UK, it is important that they can be confident in both the stability and the certainty of the UK's tax system and that the UK's tax administrators will operate the regime fairly and consistently.
- 2.5 Tax advisers play an important role; they are there to give the best advice to their clients and help them pay the correct amount of tax on time. Tax

administrations should recognise the important and constructive role tax advisers play in assisting taxpayers to comply with their tax obligations. Tax advisers can also facilitate constructive dialogue with tax administrations, enabling potential areas of dispute to be quickly resolved.

- 2.6 The co-operative compliance approaches proposed (eg pre-filing meetings) could work well, but there does need to be some tangible benefit to a co-operative compliance approach (eg less risk of enquiry) to mitigate such concerns. This, in turn, involves development of expertise by HMRC in dealing with HNWIs and appreciating the full range of taxes with which they may be concerned.
- 2.7 Of further concern are the resources available to HMRC. A dedicated unit for HNWIs will require significant investment (resourcing should be proportionate to the contribution HNWIs make); there must be sufficient staff to properly service the unit, and they must be adequately trained and kept up to date with recent developments. In particular, there needs to be technical training and backup provided from the various specialist branches of HMRC, including across Charities Assets and Residence, including the IHT and Trusts offices as well as Residency, so that those staffing the unit have a reasonable level of technical expertise elsewhere within HMRC across all the taxes, understand how trusts operate properly, can appreciate offshore tax and succession issues and can refer problems and issues to further specialists elsewhere within HMRC. The level of training required (as the Irish experience shows) demonstrates that the commitment to train people versed in all the taxes as well as continuing training should not be underestimated.

3. Question 1: What are the important features of tax administration that may facilitate the co-operative compliance approach? Please build on positive and negative experiences in dealing with your tax administration.

- 3.1 It is important for taxpayers to have confidence in the tax system. A tax regime where there are regular significant changes to the legislation does not inspire confidence in the stability of that regime. Where new legislation is necessary, this should be subject to prior consultation, so that both the rationale for it and its impact can be understood prior to the new legislation being introduced, and, where necessary, there should be appropriate transitional measures.
- 3.2 In addition, legislation needs to be clear, so that its meaning can be easily understood, and proportional, so that no one taxpaying segment is overburdened. Legislation that is written so broadly that its potential impact has to be tempered by guidance that cannot be relied on in the Courts (for example, in the UK, the targeted anti-avoidance rule for capital losses) has no place in a tax system and will not inspire confidence in that regime.
- 3.3 There must be clear advantages to taxpayers to participating in co-operative compliance, if such an approach is to work. For example, tax administrations must be prepared to answer questions fully and decisively, so that issues of uncertainty are resolved as quickly as possible (even "agreeing" on which points there is disagreement can be a help), and taxpayers must be able to rely on the responses and decisions made. Advance clearances for particular transactions over a certain value would obviously be desirable.
- 3.4 Additionally, the level of staff required from tax administrations for co-operative compliance to work must be such that they can engage with taxpayers and

their advisers on both a personal and an intellectual level. Staff must be well trained and well advised, and must be able to deal with complex situations and both provide advice (with the aid of specialist back-up where necessary) and negotiate an agreed resolution. We suggest that regular yearly secondments both to and from HMRC to the private sector for those specialising in HNWIs should be considered, and would encourage a co-operative approach.

4. Question 2: Do you think that having a dedicated unit (or units) as part of your tax administration (either at national or at regional level) with particular responsibilities for HNWIs is a good idea? If you are generally supportive of such an idea, what roles and responsibilities do you think such a unit should assume?

- 4.1 "Local" teams dealing with a wide spread of technical tax issues can lead to inconsistencies (which may be to a taxpayer's advantage or detriment). However, the approach in Charities Assets and Residence, and HMRC generally, of focusing on specialist technical units dealing with particular areas of tax, also runs the risk of creating tax gaps. We suggest that, as with companies, there is room for continued separate technical units, but combined with one business unit with trained specialists on high net worth clients who have an adequate knowledge of all the taxes and in particular understand trusts and private company issues. The relationship manager is particularly important.
- 4.2 It would also be a good idea if the creation of a dedicated unit for HNWIs were used as a starting block to improve the overall quality of a tax administration's staff, their expertise and their ability to engage with taxpayers.

In particular do you have any views on the following points?

a. How should a tax administration best gain insights into the behavioral drivers and the general context within which HNWI and their advisors operate? For instance, by employing staff with relevant private sector experience perhaps on secondment, on short-term contracts, at the end of successful careers, or on permanent contracts. Should there be some form of "advisory board" involving advisors and other relevant market participants (e.g. private banks) or some other structured form of providing relevant background and context to the tax administration.

- 4.3 Employing or seconding staff with relevant experience is a good idea and has been adopted more widely in other countries, such as the USA.

b. What role and responsibility should the unit assume with respect to the affairs of the taxpayer (e.g. research and risk assessment or full responsibility for the file including potential audit)?

- 4.4 A single unit that can deal with all aspects (research and risk analysis, advice, auditing, etc) would offer the most co-ordinated approach. This would allow the unit over time to build up a greater background "knowledge bank" for the taxpayer, which should improve the unit's efficiency and effectiveness, especially when risk analysing.

c. What taxes relating to the HNWI and their affairs should such a unit deal with and why? For instance, should it be limited to income taxes or also cover inheritance and estate taxes, VAT/GST etc.?

- 4.5 We think that it would be better if the unit could deal with all taxes, although we can see that there is a case for separating out indirect taxes. If the unit deals with all taxes, it will allow all relevant points to be viewed in context and help to build a better insight into the affairs of HNWIs.

d. Should the unit be responsible also for the affairs of all/certain entities controlled by a HNWI (e.g. only the personal affairs of the taxpayer, all operating entities and non-trading entities or only non-trading entities)?

- 4.6 The unit should have general oversight and knowledge of the affairs of all entities controlled by a HNWI or in which he has any substantial involvement, including trusts, trading companies and partnerships. It may be that the tax returns and compliance of the particular entity such as the trust, etc are dealt with by a different office, but the office dealing with the HNWI needs to have complete knowledge of all his affairs and therefore be kept informed.

e. Should HNWIs and their advisors be assigned a designated contact point within the unit?

- 4.7 We think that it would be a good idea to have a relationship manager. The person must, however, be at a sufficiently high level and of high calibre, as well as possessing broad technical knowledge and experience, to be able to understand the wider issues (and have access to specialist resources).

f. Should the unit be tasked with preparing an annual or periodic report about the overall environment and key developments, including the most pressing issues identified by HNWI and their advisors for use by the heads of tax administrations and finance ministries?

- 4.8 We suggest there is a review at the end of two years. An annual report seems unnecessary.

g. Should additional safeguards and security procedures apply to the information held by the unit?

- 4.9 Tax administrations should safeguard the personal and confidential information they receive from all taxpayers. Improving the overall security of information should be a top priority of all tax administrations. All taxpayers are entitled to the same privacy guarantees.
- 4.10 HNWIs must be confident that information that could, for example, have a bearing on divorce proceedings will not become public knowledge. Similarly, an individual will want to be assured that details of a proposed business takeover, which the individual may provide in advance of a public announcement to obtain a ruling on the tax consequences, will not be leaked (if it were it could, for instance, affect the share price or give a competitor a commercial advantage).

5. Question 3: If you are from a country that currently has a dedicated unit dealing with HNWI what advantages or disadvantages have you seen in having such a unit and do you have any comments on the way it was set-up and is operated? What are the features that you find the most useful?

- 5.1 HMRC currently have "Complex Personal Return" teams which deal with returns from taxpayers with more complicated affairs, but this is not a dedicated unit for HNWI. However, it is apparent from the operation of these teams that taxpayers, and their tax advisers, who are able to have a meaningful dialogue with properly trained and experienced officers have a noticeably "better" experience of the tax system.

6. Question 4: If the tax administration offered this or a similar approach, what would encourage HNWI and their advisors to opt into it? In your answer please consider the points discussed below and indicate which points may be more important and which may be less important. Please also describe any other elements or concerns that you think would be relevant for HNWI and their advisors (e.g. privacy concerns), and how these may be addressed.

- 6.1 The discussion paper proposes that a country would offer a programme where any HNWI who volunteers for it agrees to have at least one pre-filing meeting at which the HNWI and his adviser would be expected to put any tax position they know involves a material degree of uncertainty or unpredictability on the table. In addition, the paper proposes that the pre-filing meeting may offer further certainty by way of pre-transaction rulings.
- 6.2 Key issues in determining whether clients will opt in are not only the character of the particular client but also the perceived technical adequacy and resources of the HMRC unit. If it is perceived that the unit understands the issues surrounding HNWI and is properly trained and staffed, then co-operation is more likely.
- 6.3 *No or reduced underpayment penalties or other civil administrative penalties*

We agree that, where a taxpayer has fully disclosed a relevant issue to the tax administration, either in a tax return or prior to filing the tax return (whether at a pre-filing meeting or otherwise), no civil penalties should be imposed if the position taken by the taxpayer is subsequently found to be incorrect. The UK tax system is recognised as being over-complex and it can be difficult for taxpayers to get it right all the time. The penalty prohibition must, however, apply to all taxpayers and there should be a reasonable, but finite, period for tax administrations to notify the taxpayer of the error.

7. Question 5: The Focus Group seeks input from HNWI and their advisors about the framework for voluntary disclosures and what particular elements would encourage taxpayers to come forward, e.g. solutions to issues such as lack of back-year records, inability to calculate final tax liability, concerns regarding privacy.

- 7.1 Taxpayers want to be confident that, when they do come forward with a voluntary disclosure, they will be able to reach a sensible agreement within a reasonable time. While tax administrations should not "do deals" with evaders, they should be able to take a "businesslike" approach to, for example,

quantifying back-years' liabilities. A pragmatic and reasonable attitude to voluntary disclosures by tax administrations would increase taxpayers' confidence in coming forward.

- 7.2 In the UK specifically, we think that it would be helpful, particularly in the light of recent UK case law (the *Wilkinson* case), if there were a legislative framework to allow HMRC greater discretion in dealing with voluntary disclosures; this could help taxpayers to be more confident that the tax administrators will not take a draconian line. The framework would need to distinguish between innocent errors (where, for instance, the disclosure could be agreed with minimal or no further compliance activity) and deliberate evasion. In the most serious cases, taxpayers may be deterred from making a disclosure because of the fear of criminal proceedings being instigated. Some form of disclosure regime that permits disclosure with a guarantee of no criminal proceedings, if the disclosure is full and complete, would therefore be desirable.
- 7.3 HNWIs will want to be confident that confidentiality is maintained and will also want to reach an early settlement.

8. Question 6: Please express your views on the merits of a product ruling regime in connection with HNWIs. In addressing this question please take a broad view of the term "product ruling" to include any form of advance certainty (whether formal ruling or not) and also consider which segment of HNWIs you think would be the users of the types of products for which product rulings could be made available (i.e., certain HNWIs might be more likely to enter into tailor made arrangements that do not lend themselves to product rulings).

- 8.1 Taxpayers want certainty, so advance rules, whether pre- or post-transaction rulings for specific arrangements or rulings on particular products, would generally be welcomed. The providers of publicly available products may also welcome such rulings, as it would enable them to market a product confident that the tax consequences have been agreed. Product rulings will also create "safe harbour" products, which may be more attractive than other products where no ruling has been sought.
- 8.2 Within the existing UK framework, it may be possible to integrate a system of product rulings with the existing tax avoidance disclosure regime.
- 8.3 However, it should be recognised that HNWIs are more likely to enter into tailored, one-off, transactions, rather than use "off the shelf" products. HNWIs would, therefore, probably require an advance ruling facility similar to that outlined at paragraph 30 in the discussion paper, ie as part of a framework for a co-operative compliance approach, and, since most HNWIs will want to maintain confidentiality, it is unlikely that tax administrations would be able to produce a public bank for these rulings. While this would take up resources, it could, over time, reduce the resources required to litigate after the event.

The Chartered Institute of Taxation
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10. The Chartered Institute of Taxation

10.1 The Chartered Institute of Taxation (CIOT) is a charity and the leading professional body in the United Kingdom concerned solely with taxation. The CIOT's primary purpose is to promote education and study of the administration and practice of taxation. One of the key aims is to achieve a better, more efficient, tax system for all affected by it – taxpayers, advisers and the authorities.

The CIOT's comments and recommendations on tax issues are made solely in order to achieve its primary purpose: it is politically neutral in its work. The CIOT will seek to draw on its members' experience in private practice, Government, commerce and industry and academia to argue and explain how public policy objectives (to the extent that these are clearly stated or can be discerned) can most effectively be achieved.

The CIOT's 14,000 members have the practising title of "Chartered Tax Adviser".