Written evidence submitted by the Chartered Institute of Taxation for Finance (No.2) Bill 2024 (F2B03)

Clause 22

Transfer of Assets Abroad

Executive Summary

Clause 22 amends the Transfer of Assets Abroad (TOAA) anti-avoidance regime by extending the existing rules to scenarios where a limited company, rather than an individual, transfers assets abroad.

While agreeing with the government on the need to close down opportunities for tax avoidance we have a number of concerns about this proposal, including:

- **It adds complexity – including by using income tax legislation to tackle perceived corporate tax avoidance**
- **It is too wide - potentially catching things that are normal business practice and not tax avoidance**
- **It is misguided – trying to close a perceived 'loophole' but failing to recognise there may be commercial drivers**
- **It is uncertain – prompting many unanswered questions and unclear scenarios, potentially damaging the UK's competitiveness as a corporate headquarters**
- **It lacks fairness – in terms of how taxpayers are treated, including in its retroactive effect**
- **It is a missed opportunity – the TOAA regime needs a complete rethink not a sticking plaster in response to a court defeat**

Overview

1.1. The Transfer of Assets Abroad (TOAA) tax regime is an anti-avoidance regime dating back to the time when Neville Chamberlain was chancellor in 1936. It operates by imposing an income tax charge on a UK-resident individual who has the 'power to enjoy' the income belonging to a 'person' abroad (including non-natural persons like limited companies) as the result of a transfer of assets the individual has made to that person. Similarly, if the UK individual receives a capital sum (rather than income) from the person abroad (and even if he/she has no power to enjoy that income), the individual is still charged income tax on the income of the person abroad. These provisions are now contained in sections 720 and 727 of the Income Tax Act 2007 respectively.

1.2. A 'motive' defence is available under TOAA for genuine commercial transactions and for transactions where there was no income tax avoidance purpose.

1.3. Clause 22 is a response to the decision of the Supreme Court in the case of HMRC v. Fisher. That case involved a UK company transferring its tele-betting business to a Gibraltar-based company (the person abroad) in response to the effects of UK gaming duties, which would have had a severe impact on the business. HMRC sought to impose an income tax charge on the shareholders of the UK company on the basis that they were the transferors caught by

the TOAA legislation, so they should be assessed on the income of the Gibraltar company. However, the Supreme Court held that as the UK company had transferred the business abroad, rather than the individual shareholders, the latter could not be assessed as transferors. HMRC's assessments were therefore quashed.

1.4. In Fisher, HMRC had sought, essentially, to say that the individual and company were one and the same, but the courts disagreed. Clause 22 brings the two together if the individual is 'involved' in the company and was or ought to have been aware of both the company's transfer and the consequential avoidance of tax and did not object to it. An individual is automatically deemed to be 'involved' by virtue of being a 'participator' (i.e. shareholder – though that definition also includes loan creditors) in a 'closely-held' company, unless it can be demonstrated that the individual ordinarily had no direct or indirect involvement in the company's decision-making.

CIOT comments

2. Scope and approach of this measure

2.1. TOAA legislation exists within the Income Tax Act 2007. With clause 22 the government are extending it to cover avoidance of any tax through a transfer made by a closely-held company. While the closure of opportunities for tax avoidance is generally to be welcomed, doing so in this way is bad law and adds unnecessary complication to the tax system. If you are trying to counter corporate tax avoidance that should be done so far as possible through the corporate tax regime.

2.2. There are question marks over how necessary this measure is. In the explanatory notes to clause 22, HMRC say: *"This clause aims to tackle avoidance arrangements and does so by closing a loophole in TOAA provisions. This loophole allowed for the use of a company to transfer assets offshore in order to avoid UK tax"* (paragraph 28). We would argue that there is no such loophole, or at least that if there is it is far more limited than the government suggest. The Supreme Court in paragraph 87 of its Fisher judgment made it clear that a UK company incorporated to circumvent the TOAA code, i.e. used to transfer assets offshore, would not prevent the code from applying: *"The interposition of the UK company would be regarded as a device, and the substance of the transaction would still be a transfer of those assets by the individual to the foreign entity."* This did not apply in the Fisher case, the Supreme Court noted, because the company in question, SJA, was *"a bona fide company which had been trading for many years."* So in practice we are talking about well-established companies transferring assets abroad rather than companies being set up as vehicles for avoidance of personal taxes.

2.3. We are concerned about how widely these changes might apply. For example, consider a scenario whereby a UK holding company provides funds (e.g. a loan) to an offshore subsidiary, which in turn generates profits – this would appear to be caught by these changes. Also, would the initial establishment of the subsidiary be the relevant transfer, or would the loan? This is an entirely innocuous and commercial set of transactions, but the involvement and objection defences are ambiguous and uncertain and may prove onerous for taxpayers to substantiate.

2.4. The test as set out in the legislation leaves too much discretion to HMRC, compounding uncertainty, and can be expected to lead to increased numbers of enquiries and potentially appeals to the tax tribunals. The taxpayer should not have to satisfy HMRC on every transaction, however commercial. Given the proposed extension of the code even to transfers by a UK company setting up a foreign subsidiary this could seriously curtail the UK's attractiveness as an international headquarters. Families with large international

groups and a UK holding company will now be forced to consider the code every time a subsidiary is set up if there are any UK resident shareholders. Under the government's non-dom proposals, foreigners who are resident here for longer than four years will find that in relation to every transfer by their holding companies they will need to prove there was no indirect consequence of avoidance. There is no clearance procedure so the issue may end up being disputed years after the event.

2.5. With respect to the participators themselves:

2.5.1. Affected participators may not even be UK resident at the time of the company's transfer – yet they could be subject to an income tax charge if they subsequently become UK resident and will face having to prove why the company made the transfer and what they knew.

2.5.2. There are no bright line rules determining how the charge should be allocated in the case of multiple shareholders. The allocation is in the discretion of HMRC but there is no mechanism for HMRC to agree it before the individuals concerned are required to self-assess.

2.5.3. The default position that any participator is deemed to be involved in the company seems unfair. A company may have several minority shareholders who have no participation in the company's running. A 25% participation level should be a minimum for any question of involvement (in line with existing capital gains tax legislation). In the Fisher case itself, even the various meanings and extent of 'involved' was debated. Certain shareholders may not be in any position to object to a decision to transfer assets abroad, even if they were aware of it. It is directors who are involved in a company's day-to-day activities and decision-making, so it would be much fairer for only those participators who are also directors/shadow directors to be assumed to be involved.

3. Commencement and retrospective

3.1. Another concern is that this change appears to be retroactive as there is no date specified whereafter transactions are affected, only that income arising after April 2024 is caught.

3.2. There are potentially countless commercial transactions carried out many years ago with overseas companies which might be caught by this. Identifying relevant transactions and the reasons for them and who know about them would be a near impossible task, besides being grossly unfair on the participators concerned.

4. Potential improvements to the legislation

4.1. While we question the need for this legislation at all – and would prefer to see wholesale reform of the TOAA regime (see below) – if clause 22 is felt to be needed we suggest it could be improved with the following changes:

- Clause 22 should not be retroactive. People will find it difficult if not impossible to judge the effect of a corporate transfer many years ago.
- It should contain specific rules as to how income resulting from the corporate transfer is allocated and to whom. It is suggested this should be based on the individual's shareholding interest as a participator.
- Individual participations through a trust should be ignored. Thus a life tenant should not be regarded as a participator.
- Close company status resulting from partnership control should be disregarded.

- Individuals whose participation (when aggregated with connected parties) is below 25% should be excluded. This is in line with section 3 of the Taxation of Chargeable Gains Act (TCGA) 1992 and proves a clear bright line.
- Only the relevant participator with the tax avoidance purpose should be caught.
- “Taxation” in section 721A(5)(e) of the Income Tax Act 2007 should be limited to income tax and/or corporation tax in the same way that section 3 of TCGA 1992 is limited to capital gains tax and corporation tax.
- Transfers between members of a trading group should be carved out of the proposed legislation. These changes would bring the TOAA regime more into line with section 3 of TCGA 1992.
- All transfers within a non-resident group should be carved out of the legislation. The original transfer of assets to the group is the relevant transfer.
- Involvement in the decision making process should require the individual to be a director or shadow director of the transferor company. Mere awareness as a participator is not enough whether or not objection is made.

5. Reforming the TOAA regime

5.1. Notwithstanding our criticisms of the specifics of this measure, we are not arguing that the existing TOAA legislation should be left unchanged. To the contrary, it is notoriously badly drafted with piecemeal changes having been made over the years. Clause 22 seems to be simply a ‘kneejerk’ reaction to an individual case and will be merely another piecemeal change making already bad legislation even worse.

5.2. It would have made better sense to review the TOAA regime alongside the non-dom regime and inheritance tax domicile rules, as part of a wider review of tax rules for UK residents with overseas assets. Until now the non-dom and remittance rules have papered over some of the faults in the TOAA regime. But with the new residence based rules (the broad principle of which we support) this safety valve will no longer exist.

5.3. The TOAA code needs to be replaced with rules applicable to the fact patterns that occur today. The current regime dates back to the 1930s when air travel and modern communications were in their infancy. The number of cases HMRC have lost in recent years is indicative of how uncertain in meaning the code is, to which further applications of sticking plaster are no solution.

5.4. This is therefore a missed opportunity. Alongside the new non-dom rules, we need a proper overhaul of the TOAA provisions.

5.5. There are plenty of more modern models of drafting. Capital Gains Tax for instance has a ready-made set of rules for attributing capital gains which could fairly readily be adapted. And where the “person abroad” is a settlor interested trust, there is existing legislation which duplicates TOAA provisions.

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