

Curtailing aggressive tax planning: the case for introducing mandatory disclosure rules in Australia (part 2) – cues from the United Kingdom and South Africa

Annet Wanyana Oguttu* and Ann Kayis-Kumar**

Abstract

Increased opportunities for aggressive tax planning (ATP) schemes by multinationals has heightened pressure on governments and policy-makers to curtail these activities. However, the design of most anti-avoidance rules is reactive rather than proactive. One exception is the use of mandatory disclosure rules (MDRs), which require the upfront disclosure of tax information.

Part 1 of this two-part study in the previous issue of this journal explored the case for introducing MDRs by presenting a case study of Australia's experience in considering whether to adopt such a regime. This article (part 2) explores the key design features of an effective MDR regime with reference to the OECD's recommendations and a comparative legal analysis of how these rules apply in the UK and South African contexts. This provides the framework for a review of the effectiveness of MDRs and presents useful 'lessons learnt' which are informative in framing a regime suitable for adoption in other Commonwealth law jurisdictions such as Australia.

Key words: mandatory disclosure rules, aggressive tax planning, multinationals, international tax law

* Professor in the Department of Taxation and the African Tax Institute, Faculty of Economic and Management Sciences, University of Pretoria. This article (written in collaboration with an academic at the School of Taxation and Business Law, UNSW) is in fulfilment of the duties required of the author as a recipient of the 2017 Abe Greenbaum Research Fellowship of the School of Taxation and Business Law, UNSW Sydney.

** Senior Lecturer in the School of Taxation and Business Law, UNSW Sydney.

1. INTRODUCTION

Aggressive tax planning (ATP) has been postulated as one of the main challenges that tax administrations would face in ensuring compliance with tax legislation in the coming years.¹ Part 1 of this study, in the previous issue of this journal, delineated the concept of ATP, namely tax planning that goes beyond what is legally acceptable in that it makes use of artificial transactions that have little or no economic impact and conflict with the intention of countries' tax legislation. Part 1 explained that, despite the fact that countries have various anti-avoidance rules – including penalty regimes, tax rulings and disclosure regimes² – tax administrations are still not able to respond quickly and adequately to prevent ATP schemes, due to the lack of timely, targeted and comprehensive information on ATP schemes.³ Tax administrations usually detect these schemes by auditing taxpayers' returns, which is followed by enactment of anti-avoidance rules. While audits remain a key source of relevant information, the inevitable delays in the rule-making process imply that years may pass by before the schemes are curtailed,⁴ rendering audits ineffective for early detection of ATP schemes.⁵

In response to these challenges, an increasing number of countries have enacted mandatory disclosure rules (MDRs).⁶ These rules require scheme promoters and/or their clients to report their planned ATP arrangements in advance, so that they can be curtailed before they are put into use. The timely and targeted detection of such schemes enables countries to quickly adopt risk management strategies as well as legislative and administrative measures to counteract tax risk.⁷ However, many Commonwealth jurisdictions such as Australia do not yet have these rules. The main argument is often put forward that these countries already have a number of anti-avoidance and disclosure rules which serve to deter ATP, thus leaving little need for these rules.

Nonetheless, the OECD's⁸ base erosion and profit shifting (BEPS) recommendations include highlighting the usefulness of MDRs as best practice⁹ in providing tax authorities with comprehensive and relevant information for the early detection of ATP strategies. Part 1 of this study presented a case study analysis of the Australian experience,¹⁰ supporting the introduction of MDRs in Australia.

¹ Organisation for Economic Co-operation and Development (OECD), *Seoul Declaration: Third Meeting of the OECD Forum on Tax Administration* (14-15 September 2006), <http://www.oecd.org/dataoecd/38/29/37415572.pdf> (accessed 9 July 2015).

² OECD, *Tackling Aggressive Tax Planning through Improved Transparency and Disclosure* (OECD Publishing, 2011) 11.

³ OECD, *Action Plan on Base Erosion and Profit Shifting* (OECD Publishing, 2013) 22.

⁴ Larin Gilles, Robert Duong and Lyne Latulippe, 'Effective Responses to Aggressive Tax Planning: What Canada Can Learn from Other Jurisdictions, Instalment 4: United Kingdom – Disclosure Rules' (Study by the Research Chair in Taxation and Public Finance, University of Sherbrooke, July 2009).

⁵ OECD, *Action Plan on Base Erosion and Profit Shifting*, above n 3, 22.

⁶ OECD, *Public Discussion Draft, BEPS Action 12: Mandatory Disclosure Rules* (11 May 2015) para 37.

⁷ OECD, 'OECD's Work on Aggressive Tax Planning', <http://www.oecd.org/tax/exchange-of-tax-information/atp.htm> (accessed 31 July 2017).

⁸ OECD, *Action Plan on Base Erosion and Profit Shifting*, above n 3, 22.

⁹ OECD, *Explanatory Statement – 2015 Final Reports*, OECD/G20 BEPS Project (2015) paras 11 and 18. Minimum standards were agreed in particular to tackle issues in cases where no action by some countries would have created negative spillovers into other countries. Best practices or common approaches are intended to facilitate the convergence of national practices by interested countries.

¹⁰ Australian Treasury, *OECD Proposals for Mandatory Disclosure of Tax Information: Discussion Paper* (2016).

Part 2 (this article) responds to the design aspect of MDRs as highlighted in the Australian Treasury's Discussion Paper,¹¹ in which the government anticipated further consultations on implementation design issues.¹² Accordingly, this article provides recommendations on the design features of MDRs in an Australian context which can be more widely applied by other Commonwealth law jurisdictions contemplating whether to introduce MDRs. This article sets out the OECD's recommended best practice design features of effective MDRs. Acknowledging the OECD recommendation that countries that wish to adopt MDR rules should draw on experiences of other countries that have such rules,¹³ this article provides a comparative study of how the rules apply in two Commonwealth countries – the UK and South Africa – whose experiences may be informative in framing a regime suitable for Australia.

The reasons for selecting these two jurisdictions is that, just like Australia, the UK and South Africa are part of the Commonwealth and they constitute two of Australia's large trading partners. The UK has an extensive economic and trade relationship with Australia. The UK is Australia's fifth largest two-way trading partner and export market for trade in goods and services, and its sixth largest source of imports. Both countries have a large commercial presence in the other's country.¹⁴ South Africa is Australia's 21st largest merchandise trading partner and it now represents Australia's 16th most significant merchandise export market. South Africa is Australia's most dynamic market in Africa and dominates stocks of African investment into Australia. Australian investment in South Africa has also increased over the years, mainly in mining, mining equipment, agriculture, agribusiness and infrastructure and services trade.¹⁵

Both the UK and South Africa have already introduced MDRs, as discussed below. Some of the concerns that Australia is contending with, regarding the introduction MDR (such as the proliferation of disclosure rules and balancing conflicting policy imperatives) were also faced by these two countries. Lessons could thus be gleaned from them with respect to how Australia can resolve its specific challenges.

In the section that follows, after considering the Australian Government's preliminary views, and taking into consideration the OECD recommendations as well as the pros and cons of the approaches in the UK and South Africa, recommendations are provided on design features for each of the relevant elements of a potential MDR regime.

2. KEY DESIGN FEATURES AND PRINCIPLES OF AN EFFECTIVE MANDATORY DISCLOSURE REGIME

In Action 12 of the OECD BEPS Reports, the OECD recommends that MDRs should cover:

- what has to be reported;

¹¹ *Ibid.*

¹² *Ibid.*

¹³ OECD, *Action Plan on Base Erosion and Profit Shifting*, above n 3, 22.

¹⁴ Australian Government, Department of Foreign Affairs and Trade 'United Kingdom Country Brief', <http://dfat.gov.au/geo/united-kingdom/Pages/united-kingdom-country-brief.aspx> (accessed 23 July 2018).

¹⁵ AiGroup, 'South Africa', <https://www.aigroup.com.au/business-services/trade/export/south-africa/> (accessed 23 July 2018); see also Mokhtar Metwally, Ann Hodgkinson and André Jordaan, 'An Assessment of the Trade Relationship between South Africa and Australia' (2006) 4(2) *International Journal of Applied Business and Economic Research* 79, 80.

- who has to report;
- information to be reported;
- when to report;
- identification of scheme promoters and/or users;
- consequences of non-compliance;
- how to use the information collected; and
- ensuring the rules cover international tax schemes.

As such, this section explores each of these design features, with a comparative analysis of how their application is carried out in the UK and South Africa. This is supplemented with an outline of overarching principles. This provides the conceptual framework for design recommendations for Australia.

2.1 What has to be reported?

2.1.1 *OECD recommendations on what has to be reported*

A country needs to decide what types of schemes or arrangements should be disclosed under its MDRs (ie, what transactions are reportable).¹⁶ The OECD recommends that this can be determined by use of tests such as threshold requirements, de-minimis filters or hallmarks. Each of these is briefly explained below.

Threshold requirements. Threshold requirements may be used to determine what is reportable. The threshold test may consider whether a transaction has the features of an avoidance scheme or whether the main benefit of the scheme is to obtain a tax advantage.¹⁷ This ensures that the transactions targeted are those that are likely to pose the greatest tax policy and revenue risks.¹⁸ This excludes irrelevant disclosures and reduces compliance and administrative burdens.¹⁹ The challenges of the ‘main benefit’ test as a threshold are that it sets a relatively high threshold for disclosure and it can be used inappropriately as a justification for not disclosing tax avoidance schemes that would be of interest to a tax administration. It may also make enforcement of the disclosure obligations more complex and create uncertain outcomes for taxpayers.²⁰ Where threshold requirements (like the main benefit test) are not used, there is the challenge of the rules generating a large number of disclosures, which would increase the costs to taxpayers and tax administrations and dilute the relevance of the information received. This disadvantage can be ameliorated by using defined de-minimis filters, hallmarks or listed transactions.²¹

De-minimis filter. The de-minimis filter could be considered as an alternative, or additional provision, to a threshold requirement. It may be based on certain monetary limits such that smaller transactions, below a certain amount, are excluded from the

¹⁶ OECD, *Mandatory Disclosure Rules: Action 12 – 2015 Final Report* (OECD Publishing, 2015) para 78.

¹⁷ *Ibid* para 79.

¹⁸ *Ibid* para 80.

¹⁹ *Ibid*.

²⁰ *Ibid* para 82.

²¹ *Ibid* paras 84-85.

disclosure requirements.²² A de-minimis filter could be applied to all transactions or to categories of transactions that might elicit large numbers of reportable transactions. The advantages of de-minimis filters are that they narrow the ambit of the rules, enhance the usefulness of the information collected, reduce excessive or defensive filings by focusing on transactions that pose significant tax risk, and reduce the costs to taxpayers and the administrative burden for tax administrations. The disadvantage of de-minimis filters is that they could suggest that tax avoidance, in small amounts, is acceptable.²³

Hallmarks. Hallmarks can also be used as tools to identify the features of schemes that tax administrations are interested in. Hallmarks help in setting the scope of the rules, so that they target only those transactions that raise tax avoidance concerns.²⁴ The proper design of hallmarks is critical to the effective functioning and compliance with the rules.²⁵ There are two categories of hallmarks: generic and specific.²⁶ Generic hallmarks target features that are common to promoted schemes; examples include use of mass marketed schemes, requirement of confidentiality by the promoter, charging premium fees for the value of tax benefits obtained under the scheme and mass marketed schemes (standardised tax products that are made available to more than one person).²⁷ Generic hallmarks can be used to capture ‘innovative’ tax planning arrangements that may be easily replicated and sold to a variety of taxpayers. This has the advantage of increasing the number of reportable transactions – enabling tax administrations to detect and react quickly to new innovative transactions and thus reduce their circulation in the market.²⁸ The disadvantage of generic hallmarks is that if they are ambiguously drafted, they have the potential to increase compliance costs for taxpayers and administrative costs for tax administrations.²⁹

In specific hallmarks, the disclosure obligation is triggered by describing certain potentially abusive transactions in regulations or by legislation. Specific hallmarks have the advantage of targeting the known vulnerabilities in a country’s tax system that are commonly used in tax avoidance arrangements.³⁰ The OECD recommends that specific hallmarks should be drafted broadly to avoid providing too much technical detail. Narrow or technical drafting can be given a restrictive interpretation by taxpayers or may provide opportunities for taxpayers and promoters to structure their disclosure obligations around them.³¹ Specific hallmarks have the advantage of keeping MDRs up to date and dealing with avoidance on non-mainstream taxes that reflect the key risk areas in a given jurisdiction. The main disadvantages of specific hallmarks are the costs and capacity issues for the tax administration and the reporting burden on taxpayers.³²

²² Ibid para 87.

²³ Ibid.

²⁴ Ibid paras 20, 23.

²⁵ Karen Payne, ‘Mandatory Disclosure Rules and reporting’ (Paper presented at the 2018 Financial Services Taxation Conference, Gold Coast, 7-9 February 2018) 11.

²⁶ OECD, *Mandatory Disclosure Rules: Action 12 – 2015 Final Report*, above n 16, para 91.

²⁷ Ibid para 92.

²⁸ Ibid para 91.

²⁹ Ibid para 132.

³⁰ Ibid para 91.

³¹ Ibid para 118.

³² Ibid paras 135-137.

2.1.2 UK rules on what has to be reported

An 'arrangement' for the purposes of the UK Disclosure of Tax Avoidance Schemes (DOTAS) regime means any scheme, transaction or series of transactions.³³ An arrangement has to be disclosed to HM Revenue and Customs if it satisfies three criteria. First, the arrangement enables, or might be expected to enable, a taxpayer to obtain a tax advantage in relation to the tax law in the UK. In this regard, a tax 'advantage' is defined in section 318(1) of the *Finance Act 2004* as the avoidance or reduction of tax, the obtaining or increase of an amount of tax relief or refund, the deferral of payment of tax or advancement of repayment of tax, or the avoidance of the obligation to deduct or account for tax. The second criterion is that the tax advantage constitutes, or might be expected to constitute, the main benefit or one of the main benefits of the arrangement. The third criterion is that the arrangement is likened to any of the arrangements whose hallmarks have an avoidance risk, as identified by HM Revenue and Customs under its regulatory power (prescribed arrangements, commonly referred to as 'hallmarked schemes').³⁴

From the above it is clear that the UK regime makes use of a threshold requirement (tax benefit) to determine what is reportable, as well as hallmarks prescribed in regulations to identify schemes of interest to HM Revenue and Customs. Generic hallmarks, such as mass marketed schemes, requirement of confidentiality and charging of premium fees are applied in the UK.³⁵

2.1.3 South African rules on what has to be reported

Under section 34 of the *Tax Administration Act 28 of 2011* (TAA), an 'arrangement' means 'any transaction, operation, scheme, agreement or understanding (whether enforceable or not)'. South Africa uses a threshold requirement (tax benefit) to determine what is reportable, as well as hallmarks prescribed in legislation and those listed in a public notice by the Commissioner of the South African Revenue Service (SARS).

Section 35 provides for two circumstances in which an arrangement would qualify as a reportable arrangement. The first circumstance is the specific reportable arrangements (specific hallmark) set out in section 35(1), under which an arrangement is reportable if a tax benefit is or will be derived or is assumed to be derived by any participant.³⁶

The second circumstance under which an arrangement is reportable is, under section 35(2) of the TAA, if the arrangement is listed by the Commissioner of SARS by public notice, being satisfied that the arrangement may lead to an undue tax benefit. However, this is subject to two categories of carve-outs. The first category is the 'specifically excluded arrangements' which are set out in section 36(1) (subject to certain exceptions), including loans and leases. The second category of excluded arrangements are those excluded by the Commissioner of SARS by public notice under section 36(4), being satisfied that the arrangement is not likely to lead to an undue 'tax benefit'. Essentially, the excluded transactions and arrangements that do not exceed ZAR 5

³³ *Finance Act 2004* (UK) s 318(1).

³⁴ *Finance Act 2004* s 306(1).

³⁵ OECD, *Mandatory Disclosure Rules: Action 12 2015 Final Report*, above n 16, para 92.

³⁶ TAA s 35(1); Ide Louw and Bronwyn Simpson, 'The Simple Life Before Reportable Arrangements', in DLA Cliffe Dekker Hofmeyr, *Tax Matters* (Winter 2010) 3, 4.

million, act as de-minimis filters³⁷ that reduce the risks of over-disclosure by focusing on transactions that pose significant tax risk, thereby reducing compliance costs for taxpayers and administrative burdens for the tax administration.

2.1.4 Australia's preliminary position on what has to be reported

The Australian Treasury's initial view is that the Australian Taxation Office (ATO) should have broad discretion (subject to the limits described below) in determining which ATP arrangements would trigger the MDRs.³⁸

If the government were to adopt a broad discretionary approach, the ATO would have to initiate action to set the rules in motion. The ATO would have to publish some regulations or guidelines which describe the disclosable arrangements envisaged; alternatively, these could be set out clearly in legislation (as is done in the UK and in South Africa).³⁹ The government's proposal to identify targeted aggressive tax arrangements in a manner similar to the Taxpayer Alerts has, however, been criticised by tax practitioners for lacking clarity – which is not suited for drafting the proposed MDRs.⁴⁰ For example, the Taxpayer Alerts refer to the offending arrangements as those which 'typically display' certain features and which display 'all or most of the features' – wording that tax practitioners have found confusing, and which raises concerns about penalties for failing to notify the ATO even where the ATO is not clear about what needs to be notified.⁴¹ The Australian Law Council suggests that, where broad discretion lacks clarity, this 'could be tempered by provisions for internal and external review and appeal'.⁴²

Australia could ensure clarity by emulating South Africa in this matter, where reportable arrangements are clearly set out in the legislation and the Commissioner of SARS has broad discretion to prescribe and update in a Gazetted Public Notice the arrangements that are of particular risk to revenue.⁴³ For Australia's circumstances, the hallmarks of an ATP arrangement should be derived from the 'prohibited conduct' provisions under the promoter penalty rules in section 290-B of Schedule 1 to the *Taxation Administration Act 1953* (discussed in Part 1 of this study).

The Australian Treasury's Discussion Paper⁴⁴ sought views on the use of generic hallmarks as triggers for MDRs, as well as their advantages and disadvantages.⁴⁵ Confidentiality may, for example, not be an appropriate hallmark for Australia

³⁷ OECD, *Mandatory Disclosure Rules: Action 12 2015 Final Report*, above n 16, para 87.

³⁸ Australian Treasury, *OECD Proposals for Mandatory Disclosure of Tax Information*, above (n 10, Table 2, Issue 2.

³⁹ Law Council of Australia, 'Mandatory Disclosure' (15 July 2016) para 14.3, <https://www.lawcouncil.asn.au/resources/submissions/mandatory-disclosure> (accessed 3 August 2017).

⁴⁰ Greenwoods & Herbert Smith Freehills, 'OECD Proposals for Mandatory Disclosure of Tax Information – Discussion Paper' (15 July 2016) para 4, <http://www.greenwoods.com.au/media/1798/oecd-proposals-for-mandatory-disclosure-of-tax-information-submission-to-treasury-july-2016.pdf> (accessed 3 August 2017).

⁴¹ *Ibid* para 4; Payne, above n 25, 6

⁴² Law Council of Australia, above n 39, para 14.3.

⁴³ See TAA s 35(2), which provides for the reporting of arrangements listed by the Commissioner of SARS by public notice.

⁴⁴ Australian Treasury, *OECD Proposals for Mandatory Disclosure of Tax Information*, above (n 10, Table 2, Issue 2.

⁴⁵ *Ibid* 20, para 11.4.

considering that the common law recognises legal professional privilege.⁴⁶ Rather, more appropriate hallmarks would be a lack of transparency (that is, the refusal of a person to disclose to a taxpayer or their advisers all the details of a particular arrangement, including any legal and other opinions that person relies on in support of the effectiveness of the arrangement)⁴⁷ or that the fee, or a proportion of the fee, is contingent on the scheme set up by the person charging for it being successful.⁴⁸ The OECD advises that this ‘premium fee’ hallmark is appropriate where the amount the client pays for the advice can be attributed to the value of the tax benefits obtained under the scheme (which is how it is applied in the UK).⁴⁹ It is important that generic hallmarks are designed clearly and targeted appropriately to minimise excessive and unnecessary disclosure of information by making it easy for advisers to understand and determine whether they need to disclose. Unnecessary disclosure would increase compliance and administrative costs, without improving the detection of ATP arrangements in the tax system.⁵⁰

Use of subjective or objective criteria in the rules is also an important matter to consider. A subjective approach to the rules can for instance be inferred from the ‘label’ given to the rules. The use of ‘scornful’ or pejorative labels, such as ‘aggressive tax arrangements’, may enhance deterrence in that they can create a negative perception among clients of scheme promoters, which may influence behaviour change from such promoters for fear of business reputation risks. Neutral labels, such as ‘reportable arrangements’ (as used in South Africa, may create a less ‘scornful’ perception but rather reflect the intelligence gathering objective of the rules. The effectiveness of neutral labels must however be accompanied by hallmarks that are based on objective criteria, as purposive elements would lead to uncertainty and be open to manipulation, which would undermine the rules.⁵¹

2.2 Who has to report?

2.2.1 OECD recommendations

MDRs need to identify the person who is obliged to disclose information under the regime. The OECD notes that there are two options that countries can apply. The first option is that both the promoter and the user have the obligation to disclose separately.⁵² The advantage of this option is that it has a stronger deterrent effect on both the promoter and the user, thereby reducing the risk of inadequate disclosure.⁵³ The disadvantage is that it places greater administrative costs on tax administrations due to the dual disclosure obligation imposed and it increases compliance costs for the taxpayers.⁵⁴

⁴⁶ *Baker v Campbell* [1983] HCA 39, 153 CLR 52; *Mann v Carnell* [1999] HCA 66, 201 CLR 1; *British American Tobacco Australia Ltd v Secretary, Department of Health and Ageing* [2011] FCAFC 107, 195 FCR 123.

⁴⁷ Law Council of Australia, above n 39, para 14.4.

⁴⁸ *Ibid.*

⁴⁹ OECD, *Mandatory Disclosure Rules: Action 12 2015 Final Report*, above n 16, para 92.

⁵⁰ Payne, above n 25, 11.

⁵¹ *Ibid.*

⁵² This is applied in Canada and the United States; see OECD, *Mandatory Disclosure Rules: Action 12 2015 Final Report*, above n 16, para 61.

⁵³ *Ibid.* paras 63-74.

⁵⁴ *Ibid.* paras 63-64.

The second option is that either the promoter or the taxpayer has the obligation to disclose, but the promoter has the primary obligation to disclose.⁵⁵ The advantage of placing the primary obligation to disclose on the promoter is that it ensures efficiency, particularly for mass marketed schemes, as the promoter has a better understanding of the scheme and the tax benefit arising under the scheme. The disadvantage arises where the promoter is offshore or asserts legal professional privilege as recognised by many common law jurisdictions; these may prevent the promoter from providing the required information.⁵⁶ In such cases, the OECD recommends that the obligation to disclose should shift to the user.⁵⁷

2.2.2 *Who has to report in the UK?*

In the UK, the duty to disclose a notifiable arrangement falls on three groups of persons. First, promoters have the primary duty to disclose to HM Revenue and Customs information on the arrangements a taxpayer has implemented further to their advice.⁵⁸ Subsections 307(1) and (2) of the *Finance Act 2004* state that a person is a promoter, in relation to a notifiable proposal, if in the course of a relevant business (any trade, profession or business involving the provision of taxation services to other persons, or business carried on by a bank or a securities house), that person is responsible for the design of the proposed arrangements, or if they make the notifiable proposal available for implementation by other persons. A person is also a promoter in relation to notifiable arrangements, if in the course of a relevant business, that person is responsible for the implementation of a notifiable proposal, or if that person is to any extent responsible for the design of the arrangements, or the organisation or management of the arrangements. It should be noted, though, that the UK MDRs provide for legal professional privilege. Section 314(1) of the *Finance Act 2004* provides that there is no requirement for any person to disclose any privileged information, which is defined in section 314(2) to mean information with respect to which a claim to legal professional privilege or to confidentiality of communications could be maintained in legal proceedings.

Where a promoter is outside the UK, section 309(1) of the *Finance Act 2004* places the second duty of disclosure on any person (the user) who enters into any transaction forming part of any notifiable arrangements. However, where a promoter complies with the duty to disclose a notifiable arrangement, as explained above, this discharges the duty of the client to disclose.⁵⁹ Thus, where the disclosure of the scheme by the promoter would infringe legal professional privilege (eg, if the promoter were a law firm whose clients enjoy legal professional privilege), then the duty of disclosure would fall on the user.⁶⁰

The third duty of disclosure is provided for under section 310 of the *Finance Act 2004*. It provides that any person who is a party to a notifiable arrangement that does not involve a promoter (section 308), or where the promoter is outside the UK (section 309), has a duty to disclose a notifiable arrangement at the prescribed time. In its consultation document, *Strengthening the Tax Avoidance Disclosure Regimes*, HM Revenue and

⁵⁵ *Ibid* para 61.

⁵⁶ *Ibid* para 70.

⁵⁷ *Ibid* para 68.

⁵⁸ Philip Baker, 'The BEPS Project: Disclosure of Aggressive Tax Planning Schemes' (2015) 43(1) *Intertax* 85, 87.

⁵⁹ *Finance Act 2004* s 309(2).

⁶⁰ Baker, above n 58, 87.

Customs noted that anyone working with a non-resident promoter (such as a business partner) should be required to disclose reportable arrangements that are promoted by the offshore promoter, to deter the use of offshore promoters to circumvent the UK disclosure requirements.⁶¹

2.2.3 *Who has to report in South Africa?*

The reporting obligation in South Africa is in the first instance on the promoter (defined under section 34 of the TAA as the person who is responsible for organising, designing, selling, financing or managing the reportable arrangement) as this is the person most likely to have insight into the whole transaction. If there is no promoter, or if the promoter is a non-resident, the participants to the transaction have the obligation to report. Section 34 of the TAA defines a participant to include not only a promoter but also a person who directly or indirectly will derive or assumes that will derive a 'tax benefit' or 'financial benefit' by virtue of an arrangement. The definition of participant also includes any other person who is party to an arrangement listed in a public notice by the Commissioner of SARS. This include companies and trusts.⁶²

2.2.4 *Australia's preliminary position on who has to report*

The Australian Treasury's initial view is that the MDRs should apply primarily to 'tax advisers who are involved in the design, distribution and management of aggressive tax arrangements'.⁶³ However, in limited circumstances, where the relevant tax adviser is offshore, the ATO may require disclosures to be made by the taxpayers.⁶⁴ This preliminary view is supported, as it is in line with the OECD recommendations and the approaches followed in the UK and in South Africa. The Australian Treasury's Discussion Paper suggested that the rules would provide a clear definition of targeted 'tax advisers' who are involved in the design, distribution and management of aggressive tax arrangements.⁶⁵

However, instead of using the term 'tax adviser', the term 'promoter' would be consistent with the use by both the OECD and also the UK and South Africa. This term more closely targets those who design, distribute and manage aggressive tax arrangements, rather than all tax advisers.⁶⁶ Thus, advisers who merely advise on the tax consequences of proposals put to them (eg, those who give second opinions) and tax return preparers who report the consequences of transactions on which others have opined, should not be within the scope of the rules.⁶⁷ It is however important to note that the tax advisory profession in Australia consists of various operators that may need specific consideration; these include: accountants, lawyers, tax lawyers, tax agents, financial planners, financial institutions, Australian Financial Services Licensees, as

⁶¹ HM Revenue and Customs, *Consultation Document: Strengthening the Tax Avoidance Disclosure Regimes* (31 July 2014), <https://www.gov.uk/government/consultations/strengthening-the-tax-avoidance-disclosure-regimes> (accessed 4 August 2017).

⁶² Louw and Simpson, above n 36, 3.

⁶³ Australian Treasury, *OECD Proposals for Mandatory Disclosure of Tax Information*, above n 10, Table 2, Issue 1.

⁶⁴ *Ibid.*

⁶⁵ *Ibid.*

⁶⁶ Joanna Mather, 'Lawyers, Accountants Balk at Disclosure Rules', *Australian Financial Review* (4 August 2016), <http://www.afr.com/news/policy/tax/lawyers-accountants-balk-at-disclosure-rules-20160802-gqj77u> (accessed 3 August 2017).

⁶⁷ Greenwoods & Herbert Smith Freehills, above n 40.

well as in-house and offshore advisers.⁶⁸ Some of these may be regulated by bodies such as the Tax Practitioners Board, others may not. Payne⁶⁹ takes the view that where an individual provides advice on behalf of a company or firm, then the obligation to disclose must be on that company or firm, as this would affect both regulated and unregulated advisers. It is important that the reporting rules do not fall on only regulated tax advisers, as this may encourage the unregulated ones to go offshore, which may present greater challenges in getting information from them, and thus turning to the Australian user for the disclosure who as the user may not know the details of how the scheme operates.

To ensure that the rules target specific taxpayer cohorts and preclude duplication with existing rules, we recommend that the rules expand on the definition of a 'promoter' in the promoter penalty rules in section 290-60 of Schedule 1 to the *Taxation Administration Act 1958* (Cth),⁷⁰ which as discussed in Part 1 mimic some mandatory provisions in MDRs. In terms of these rules, an entity is considered a promoter if it markets or encourages the growth of the scheme, the entity or its associate directly or indirectly receives consideration in respect of marketing or encouragement, it has a substantial role in the marketing or encouragement of the scheme or it causes another entity to be a promoter.⁷¹ For the purposes of the MDRs, the definition should cover all taxpayers – it should not be limited to entities only.

There may however be some difficulties where a taxpayer is a foreign resident who is an owner of an indirect Australian real property interest, and is advised by a foreign resident promoter. In such cases where substantial Australian assets are held indirectly, Australian MDRs should provide for specific rules to effectively address such issues.

2.3 Information to be reported

2.3.1 OECD recommendations

The OECD notes that it is imperative that once a transaction is reportable, the person who is obliged to disclose (promoter or user) must provide the tax authorities with particular information to enable them to understand how the scheme operates and how the expected tax advantage arises.⁷²

2.3.2 UK rules on information to be reported

In the UK, the disclosure obligations require identification of the details of the arrangements so that HM Revenue and Customs can understand how the scheme achieves a tax benefit for those who use it.⁷³ The information required must be provided in a form and manner specified by HM Revenue and Customs.⁷⁴ Where auditors have reasonable grounds for believing that promoters subject to the disclosure rules have not filed the prescribed form, they can ask them in writing to provide the reasons why they should not be subject to the disclosure rules. HM Revenue and Customs can obtain a court order enjoining a promoter to provide additional documents or information to

⁶⁸ Payne, above n 25, 20.

⁶⁹ *Ibid* 21.

⁷⁰ The rules require entities not to engage in 'prohibited conduct' or they will be penalised.

⁷¹ *Taxation Administration Act 1953* (Cth) s 290C.

⁷² OECD, *Mandatory Disclosure Rules: Action 12 2015 Final Report*, above n 16, paras 201-202.

⁷³ Baker, above n 58, 87.

⁷⁴ *Finance Act 2004* s 316.

explain the lack of prescribed forms or to clarify the information contained in a form it previously filed (supplementary filing order). HM Revenue and Customs could also obtain a court order regarding a promoter, which declares that an arrangement is a notifiable arrangement.⁷⁵ Where the court so orders, the promoter must then file the prescribed form as if the arrangement specified in the court order were a notifiable arrangement.

2.3.3 *South African rules on information to be reported*

Under section 38 of the TAA, a promoter or participant must submit (on the prescribed form) the following information in relation to a reportable arrangement, by the date specified:

- a detailed description of all its steps and key features, including, in the case of an arrangement that is a step or part of a larger 'arrangement', all the steps and key features of the larger arrangement;
- a detailed description of the assumed tax benefits for all participants, including, but not limited to, tax deductions and deferred income;
- the names, registration numbers, and registered addresses of all participants;
- a list of all agreements; and
- any financial model that embodies the projected tax treatment.

2.3.4 *Australia's preliminary views on information to be reported*

The Australian Treasury's initial view is that, to minimise unnecessary additional compliance costs, the legislation should clearly specify the information that is required to be disclosed under the MDRs.⁷⁶ The government is also of the view that a standard form should be provided by the ATO regarding the information that should be disclosed. The government sought views on how the legislative guidelines should be designed.⁷⁷ The government's view is in line with the approaches in the UK and in South Africa.

Legislative guidelines on information to be reported could be drawn from the OECD recommendations and the South African procedure (as set out above). To ensure that the rules do not overlap with existing rules, the information requirements could build on the provisions in the Reportable Tax Position Schedule⁷⁸ which (as discussed in Part 1) has mandatory provisions that mimic the MDRs.⁷⁹

⁷⁵ *Finance Act 2004* s 314A, as added by *Finance Act 2007* s 108.

⁷⁶ Australian Treasury, *OECD Proposals for Mandatory Disclosure of Tax Information*, above n 10, Table 2, Issue 3.

⁷⁷ *Ibid* 20, para 11.5.

⁷⁸ The Schedule requires some large corporations to make early disclosure of contestable and material tax positions which may not be sustained when analysed by the ATO. See ATO, 'Guide to Reportable Tax Positions' (2017), <https://www.ato.gov.au/Forms/Guide-to-Reportable-Tax-Positions-2017/> (accessed 3 August 2017).

⁷⁹ ATO, 'RTP Early Disclosure Form' (2011) Item 8, www.ato.gov.au/content/downloads/bus00279408nat73857.pdf (accessed 17 August 2017).

2.4 When to report

2.4.1 OECD recommendations

The OECD notes that, since the purpose of MDRs is to provide the tax administration with early information on ATP schemes and their users so as to deter the use of those schemes, the determination of the timeframe for when promoters and/or users are required to make a disclosure is key to achieving that goal.⁸⁰ The more quickly a tax administration can act against a scheme, the more this may enhance the deterrent effect by reducing the time available to take advantage of any tax benefit, and so altering the economics of the transaction.⁸¹ The timing of disclosure depends on two factors: the trigger event and the time period for reporting (this depends on the time allowed by the MDRs of a given country).⁸²

With respect to the first timing factor (trigger event), usually the event that triggers disclosure by a promoter could be linked to either the time the scheme is made available for users to implement or the time the scheme is implemented by users.⁸³ The OECD recommends that, where the promoter has the obligation to disclose, the time of disclosure should be linked to the availability of the scheme to the users rather than the time the scheme is implemented.⁸⁴ Where there is no promoter or where the promoter is offshore and the user is required to disclose, the OECD recommends that the reporting requirement should be linked to implementation rather than availability of a scheme, since it may be difficult to identify another point or event that provides an objective trigger for the reporting obligation.⁸⁵

As regards the time period for reporting,⁸⁶ in general the time in countries' MDRs can vary from within days, to months or longer. Similar times for disclosure normally apply for the promoter and for the user (depending on who has the obligation to disclosure). Either way, the OECD recommends that a shorter period of time enables the disclosure regime to meet its objectives of maximising the tax administration's ability to react to the scheme quickly and to influence taxpayers' behaviour.⁸⁷ The longer the gap between a scheme being marketed and the eventual disclosure, the more users there will be and greater loss of tax revenues.⁸⁸ The OECD, however, notes that there is less need to have a very short period if a government is unable to react quickly to change its legislation. This means that the administrative constraints on each tax administration need to be taken into account. The timeframe for disclosure should be as efficient as possible within the context of domestic law.⁸⁹

2.4.2 Time of disclosure in the UK

In the UK, the time of disclosure by a promoter is linked to the time the scheme is made available for users to implement. Section 308 of the *Finance Act 2004* requires that a

⁸⁰ OECD, *Mandatory Disclosure Rules: Action 12 2015 Final Report*, above n 16, para 139.

⁸¹ *Ibid.*

⁸² *Ibid.* 18.

⁸³ *Ibid.* para 156.

⁸⁴ *Ibid.*

⁸⁵ *Ibid.* para 152.

⁸⁶ *Ibid.* 18.

⁸⁷ *Ibid.* para 156.

⁸⁸ *Ibid.* para 155.

⁸⁹ *Ibid.*

promoter must provide HM Revenue and Customs information relating to any notifiable proposal on the earlier of: (a) the date on which the promoter makes a notifiable proposal available for implementation by any other person, or (b) the date on which the promoter first becomes aware of any transaction forming part of notifiable arrangements that implement the notifiable proposal. Thus, the date a promoter makes a notifiable proposal available to users for implementation is essentially the date when all the elements necessary for implementation of the scheme are in place and a communication is made to a client suggesting that the client might consider entering into transactions forming part of the scheme; it does not matter whether full details of the scheme are communicated at that time.⁹⁰

2.4.3 *Time of disclosure in South Africa*

Unlike the case in the UK, in South Africa the time of disclosure is the time the scheme is implemented by users. Section 37(1) of the TAA provides that a 'participant' in an 'arrangement' is required to disclose an arrangement on the date on which it qualifies as a 'reportable arrangement', and it should be reported within 45 business days after that date. Section 37(5) provides that SARS may grant an extension for disclosure for a further 45 business days, if reasonable grounds exist for the extension.

The disclosure obligation is therefore triggered within 45 days after there is receipt or payment of money for a transaction forming part of a reportable arrangement; this effectively shows that the arrangement has been implemented.⁹¹ The disadvantage with South Africa's trigger event is that it impacts on the tax administration's ability to react more quickly, potentially leading to greater revenue loss and a reduced deterrent effect.⁹²

2.4.4 *Australia's preliminary views on time of disclosure*

The Australian Treasury's initial position on the time of disclosure is that the ATO should have discretion to determine when tax advisers are required to disclose information.⁹³ Further, the timing should not be earlier than 90 days from the ATO publishing that a scheme is reportable.⁹⁴ The government indicated that there would be a mechanism for tax advisers to seek the ATO's approval for extending the timeframe for making a disclosure and sought community views on this matter.⁹⁵

In light of the OECD recommendations and the disadvantages of this approach (which is used in South Africa), we recommend that the UK approach be implemented in Australia whereby the time of disclosure by a promoter is linked to the time the scheme is made available for users to implement. With respect to the time of reporting, the important matter is to ensure that the time is not so long that it impacts on the ATO's ability to act quickly against ATP.⁹⁶

⁹⁰ *Ibid* para 141.

⁹¹ *Ibid* para 146.

⁹² *Ibid* para 147.

⁹³ Australian Treasury, *OECD Proposals for Mandatory Disclosure of Tax Information*, above n 10, Table 2, Issue 3.

⁹⁴ *Ibid*, Table 2, Issue 4.

⁹⁵ *Ibid*.

⁹⁶ OECD, *Mandatory Disclosure Rules: Action 12 – 2015 Final Report*, above n 16, para 157.

Advice or ideas developed in response to a request for advice should not be targeted, since the scheme would not be ready to be made available for users to implement. However, there may be challenges in establishing a clear distinction in certain circumstances. For example it may be difficult to distinguish between: a scenario suggestion and giving advice for implementation; ATP behaviour or general activities of tax professionals; the giving of second opinions by in-house advisers or advisers.⁹⁷ It is thus important that the key elements in determining the point at which an arrangement is substantially designed must be clearly set out in order to determine if it has been sufficiently developed, that it can be implemented by potential users.

2.5 Identification of scheme users

2.5.1 OECD recommendations

The ability of tax administrations to identify scheme users is an essential part of any mandatory disclosure regime. It allows a tax administration to improve risk assessment and it enables it to better quantify the extent of any tax loss.⁹⁸ Two methods can be used to identify users: use of scheme reference numbers and use of client lists.

Scheme reference numbers. Identification through use of scheme reference numbers enables the tax authorities to identify which taxpayer has used a specific scheme,⁹⁹ so that they can obtain information on the users of that specific scheme and build up a picture of the risk presented by individual taxpayers. The OECD recommends that, where the scheme reference number is allocated to the promoter, the promoter must provide the scheme reference number to the user within a given timeframe.

Client lists. Identification of scheme users could also be effected by imposing an obligation on the promoter to provide a list of clients who have made use of a disclosed scheme.¹⁰⁰ Requiring the promoter to provide a client list has the advantage of identifying other taxpayers that participated in a scheme but did not disclose this.¹⁰¹ The fact that the user knows they will be identified through a client list may deter some from using a scheme in the first place.¹⁰² Client lists can also enable tax authorities to carry out early interventions, such as contacting taxpayers who appear on the lists to advise them not to claim the effects of the avoidance scheme on their returns.¹⁰³

Some countries, including the UK, require identification through the use of both scheme reference numbers and client lists. Such dual identification is likely to help tax administrations to cross-check the information and to rapidly obtain an accurate picture of the extent of the tax risk posed by a scheme and to easily identify when a taxpayer has used a scheme.¹⁰⁴ The administrative burdens on tax administrations are, however, high.

⁹⁷ Payne, above 25, 22.

⁹⁸ OECD, *Mandatory Disclosure Rules: Action 12 2015 Final Report*, above n 16, para 168.

⁹⁹ *Ibid* para 158.

¹⁰⁰ *Ibid*.

¹⁰¹ *Ibid* para 168.

¹⁰² *Ibid* para 169.

¹⁰³ *Ibid* para 171.

¹⁰⁴ *Ibid* para 29.

2.5.2 UK rules on identification of schemes users

Under section 311(1) of the *Finance Act 2004*, where a person complies with the duty to disclose a notifiable arrangement or a notifiable proposal, HM Revenue and Customs may within 30 days allocate a reference number to the notifiable arrangement or to the notifiable proposal, and notify the relevant person of that number. Under section 312(1), any promoter who provides services to a client in connection with notifiable arrangements must, within 30 days, provide the reference number to the client. Under section 313(3), the regulations require that the reference number is included in any tax return or account. This allows HM Revenue and Customs to identify every taxpayer who has purchased and implemented a particular scheme. Inclusion of a DOTAS reference number on a tax return is almost certain to result in an audit of that particular taxpayer.¹⁰⁵

In addition to reference numbers, the UK also requires the promoter to provide quarterly client lists.¹⁰⁶ This additional mechanism is used for checking that schemes are disclosed by all users.¹⁰⁷

2.5.3 South African rules on identification of scheme users

Under section 39 of the TAA, after SARS has received the information relating to a reportable arrangement, it must issue a reportable arrangement reference number to each 'participant' for administrative purposes only.

2.5.4 Australia's preliminary position on identification of scheme users

The Australian Treasury's initial view on this matter is that all reported schemes will be assigned a reference number within 10 days of the date for required disclosure.¹⁰⁸ To avoid duplication, the taxpayer would not be required to provide the same information as reported by the tax adviser.¹⁰⁹

To ensure effectiveness of reference numbers, it is important that the government follows the UK's approach by developing a legislative provision that requires the reference number to be included in taxpayers' returns. This will enable the ATO to identify the taxpayer who has purchased and implemented a particular scheme, which could be followed by an audit of that taxpayer. Such use of reference numbers enhances the deterrence effect of the rules.

2.6 Consequences of non-compliance

2.6.1 OECD recommendations

Mandatory disclosure regimes cannot be effective unless promoters and taxpayers fully comply with the reporting requirements. Compliance with disclosure requirements can be enhanced through the imposition of penalties so as to increase the pressure to comply

¹⁰⁵ Baker, above n 58, 87.

¹⁰⁶ OECD, *Mandatory Disclosure Rules: Action 12 – 2015 Final Report*, above n 16, para 166.

¹⁰⁷ *Ibid* para 45.

¹⁰⁸ Australian Treasury, *OECD Proposals for Mandatory Disclosure of Tax Information*, above n 10, Table 2, Issue 5.

¹⁰⁹ *Ibid*.

with the law.¹¹⁰ Penalties could be monetary or non-monetary or include elements of both.

With respect to the structure and amounts of monetary penalties, the OECD notes that this is generally an issue for each country to consider.¹¹¹ The structure and amount of the penalty may depend on the type of taxpayer (ie, corporate or individual) and the type of transaction. Monetary penalties could be levied for non-disclosure of a scheme, failure to provide or maintain client lists, failure to provide a scheme reference number or failure to report a scheme reference number.¹¹² The OECD recommends that penalties should be set at a level that maximises their deterrent value without being overly burdensome or disproportionate. In setting penalty levels, jurisdictions may take into account factors such as whether there is negligence or deliberate non-compliance. Penalties may also be linked to the level of fees, the transaction size or the extent of the tax benefit.¹¹³ The OECD is of the view that penalty initiatives are likely to be more effective if they target promoters (rather than the end user, ie, the taxpayer) since promoters have greater knowledge of a scheme's tax effects and are better placed to know whether a scheme constitutes tax avoidance and are aware of any risks inherent in that scheme.¹¹⁴

Countries may also implement non-monetary penalties for non-disclosure. For example, a failure to disclose could suspend the efficacy of the scheme and taxpayers could be denied any tax benefit arising from the scheme.¹¹⁵

2.6.2 *UK rules on the consequences of non-compliance*

The UK rules emphasise penalising promoters so as to increase transparency and improve their behaviour. Section 313 of the *Finance Act 2004* provides that a promoter or reporting taxpayer who fails to comply with disclosure obligations is liable to a penalty not exceeding GBP 5,000, and if the failure continues after a penalty is imposed, further penalties apply not exceeding GBP 600 for each day on which the failure continues. Section 313(4) provides for situations where a person is not liable to a penalty with respect to some sections of certain Tax Acts.

2.6.3 *South African rules on the consequences of non-compliance*

Where a participant (as defined in section 2.5.3 above) fails to disclose the information in respect of a reportable arrangement, section 212 of the TAA sets out penalties. In the case of a promoter, a penalty of ZAR 100,000 applies per month of non-disclosure, up to 12 months. In the case of any other participant, a penalty of ZAR 50,000 per month is imposed, up to 12 months.

2.6.4 *Australia's preliminary position on consequences of non-compliance*

The Australian Treasury's initial view is that lateness or non-compliance with the disclosure obligation will be subject to monetary tax penalties on the tax adviser (or the

¹¹⁰ OECD, *Mandatory Disclosure Rules: Action 12 – 2015 Final Report*, above n 16, para 180.

¹¹¹ *Ibid* para 181.

¹¹² *Ibid* para 182.

¹¹³ *Ibid* para 183.

¹¹⁴ *Ibid*.

¹¹⁵ *Ibid* para 195.

taxpayer, depending on who the disclosure requirement is imposed on).¹¹⁶ This is in line with OECD recommendations and also with international practices. It is therefore recommended that, to ensure deterrence, Australia's MDRs should have specific monetary penalty provisions, which increase when non-compliance persists, as is the case with the UK and South African provisions. The non-monetary penalties should complement the monetary penalties by ensuring that the latter are designed in a robust way to ensure greater compliance. It is however important to take into consideration the fact that the majority of tax advisers in Australia are most likely within the regulatory environment, for instance the regulation by the Tax Practitioner's Board, which also sets out monetary and non-monetary penalties for non-compliance. It would thus be instructive for the rules to take into consideration the penalties for regulated tax advisers when designing the penalties for Australia's MDRs.¹¹⁷

2.7 How to use the information collected

2.7.1 *OECD recommendations*

The OECD recommends that, in order to enhance the deterrence effect of a disclosure regime, information collected be used quickly by the tax authorities to change behaviour and to counteract tax avoidance schemes.¹¹⁸ This can be done through administrative, regulatory and legislative changes to close down opportunities for tax avoidance.¹¹⁹ A risk assessment can also be carried out to determine whether further action can be taken; this can, for example, take the form of an audit or more inquiries or legislative change. The tax authorities could also come up with a communication strategy whereby they issue notifications to taxpayers that they have detected an arrangement in the marketplace and are currently considering its tax implications. In such publications, tax authorities could describe the arrangement and their concerns with the arrangement, so that taxpayers are aware of the risks in undertaking the scheme; this can play an important role in influencing taxpayers' and promoters' behaviour on tax compliance.¹²⁰

2.7.2 *How the information collected is used in the UK*

The UK regime has provided HM Revenue and Customs early information about tax avoidance schemes, allowing the UK Government, where appropriate, to introduce legislation closing them down before significant tax is lost and to deter such schemes.¹²¹

2.7.3 *How the information collected has been used in South Africa*

SARS data show that most of the disclosures relating to preference shares provided an insight into how preference share funding is utilised, which has informed the design of the new hybrid equity tax rules that were introduced.¹²² The information received has also been used by the Commissioner of SARS to quickly revise its Public Notices in the

¹¹⁶ Australian Treasury, *OECD Proposals for Mandatory Disclosure of Tax Information*, above n 10, Table 2, Issue 5.

¹¹⁷ Payne, above n 25, 24.

¹¹⁸ OECD, *Mandatory Disclosure Rules: Action 12 – 2015 Final Report*, above n 16, para 15.

¹¹⁹ *Ibid* para 213.

¹²⁰ *Ibid* para 217.

¹²¹ UK Government, 'HMRC Disclosure Statistics: Data for the period from 1 August 2014 to 30 September 2014', https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/379821/HMRC_-_Tax_avoidance_disclosure_statistics_1_Aug_2014_to_30_Sept_2014.pdf (accessed 7 July 2015).

¹²² OECD, *Mandatory Disclosure Rules: Action 12 – 2015 Final Report*, above n 16, para 42.

Government Gazette (under section 35 of the TAA) to target the disclosed schemes that cause tax risk (without having to wait for lengthy legislative procedures).

2.7.4 *Australia's preliminary position on the use of information collected*

The Australian Treasury's initial view is that, when a taxpayer has disclosed an arrangement, the ATO may take any of the following actions: use the information to improve risk assessment systems, review guidance and ruling products to determine suitability and contemporaneity, undertake additional educational programs and undertake case reviews and audits where appropriate or necessary.¹²³ The government's preliminary proposals are in line with OECD recommendations and international practices.

2.8 Ensuring the rules cover international tax schemes

2.8.1 *OECD recommendations*

Action 12 of the OECD BEPS Project requires that countries ensure that their MDRs are effective in detecting cross-border tax planning. When the OECD reviewed some countries' current MDRs, it noted that the rules largely cover domestic schemes and were not particularly effective in detecting cross-border ATP schemes. Thus, countries generally receive comparatively fewer disclosures of cross-border schemes and tax administrators find it difficult to obtain information on these schemes or to get a clear picture of the overall tax and economic consequences. This, the OECD explains, is because of the way cross-border schemes are structured and the approaches countries follow in formulating the requirements for disclosure of a reportable scheme.¹²⁴ In Action 12, the OECD presented the five recommendations set out below to ensure that MDRs can appropriately target cross-border transactions, while not placing undue compliance burdens on taxpayers.¹²⁵

(a) The hallmarks for an arrangement must cover cross-border tax planning. Cross-border schemes may be difficult to target by using generic hallmarks because these schemes often involve tailored commercial transactions (eg, acquisitions, refinancing or restructuring) which may not be widely promoted domestically.¹²⁶ Thus, the OECD recommends that cross-border schemes are best targeted by using specific hallmarks that focus on the tax policy or revenue concerns for a particular country.¹²⁷

(b) Ensure proper threshold conditions for disclosure of cross-border schemes. Unlike domestic schemes, cross-border schemes typically generate multiple tax benefits for different parties in different jurisdictions.¹²⁸ Thus, if disclosure focuses exclusively on domestic tax outcomes for domestic taxpayers, tax administrations will not be able to understand the global picture or capture information on cross-border tax planning. Thus,

¹²³ Australian Treasury, *OECD Proposals for Mandatory Disclosure of Tax Information*, above n 10, Table 2, Issue 5.

¹²⁴ OECD, *Mandatory Disclosure Rules: Action 12 – 2015 Final Report*, above n 16, para 227.

¹²⁵ *Ibid* para 228.

¹²⁶ *Ibid* para 230.

¹²⁷ *Ibid* para 240.

¹²⁸ *Ibid* para 228.

the OECD recommends that countries should streamline the disclosure requirements for cross-border schemes by removing the threshold condition for cross-border schemes.¹²⁹

(c) *The definition of an 'arrangement' should cater for cross-border tax planning.* The OECD recommends that countries should develop a broad definition of an arrangement to ensure that arrangements by domestic taxpayers include cross-border tax outcomes. Domestic taxpayers must disclose cross-border arrangements, even if they are not a direct party to the cross-border outcome. This would prevent the use of intermediaries and back-to-back structures to avoid disclosure.¹³⁰ However, a reporting jurisdiction should not require disclosure of cross-border arrangements that have no substantive connection with the reporting jurisdiction and that do not give rise to any tax revenue risks.¹³¹

(d) *Disclosure obligations must include cross-border transactions.* A country's disclosure rules should include cross-border schemes that have a substantive connection with that country and have domestic tax consequences for a domestic taxpayer.¹³² Even though taxpayers may not be aware of the offshore elements of the scheme or be in a position to properly understand its effects, the rules should not be framed in such a way as to encourage taxpayers to ignore the cross-border aspects of a scheme.¹³³ To prevent an undue burden on taxpayers, a country should only require disclosure from a taxpayer that was a party to the arrangement (eg, the information is within their knowledge, possession or control) or where the cross-border outcome arises within the same group of companies.¹³⁴

(e) *Information to be reported should cover cross-border schemes.* The OECD recommends that the information that should be disclosed in the cross-border context should generally be the same as the information required for domestic schemes. Such information should include information about the operation of the scheme, including key provisions of foreign law relevant to the elements of the disclosed transaction.¹³⁵ Where the information about the scheme is held offshore and may be subject to confidentiality or other restrictions on disclosure, the OECD recommends that domestic taxpayers, advisers and intermediaries should be required to disclose all material information about the scheme that is within their knowledge, possession or control. The information obtained could also be used as the trigger for spontaneous exchange with another jurisdiction under information exchange provisions.¹³⁶

2.8.2 UK regime and cross-border reporting

It should be noted that, although the UK DOTAS regime has a cross-border element, it is fundamentally a domestic scheme, and was never envisaged to specifically target international arrangements.¹³⁷ With respect to ensuring that the disclosure obligations cover cross-border disclosure, section 309(1) of the *Finance Act 2004* provides that

¹²⁹ Ibid para 244.

¹³⁰ Ibid para 241.

¹³¹ Ibid.

¹³² Ibid para 233.

¹³³ Ibid para 234.

¹³⁴ Ibid para 246.

¹³⁵ Ibid para 253.

¹³⁶ Ibid para 255.

¹³⁷ Baker, above n 58, 88.

where a promoter is resident outside the UK, any person (the client) who enters into any transaction forming part of any notifiable arrangement must report.

2.8.3 *South African regime and cross-border reporting*

With respect to the OECD recommendation to use specific hallmarks as the best method to target cross-border schemes, in South Africa reportable arrangements include those specifically listed by the Commissioner of SARS by public notice in the Government Gazette (section 35(2) of the TAA). Currently, this covers cross-border transactions such as those involving non-resident trusts, foreign insurers and services rendered to a permanent establishment of a non-resident person in South Africa.¹³⁸ To ensure that the disclosure obligations cover cross-border disclosure, section 34 of the TAA requires that if there is no promoter, or if the promoter is a non-resident, the participants to the transaction must report.¹³⁹

2.8.4 *Australia's views*

The Australian Treasury is yet to explore how to ensure the rules are effective in an international context. It is recommended that the design and drafting of MDRs for Australia should also take into consideration the OECD recommendations on cross-border matters as discussed above. The UK and South African approaches that have a cross-border element could be emulated.

2.9 **Principles to bear in mind when designing effective mandatory rules**

Overall, the OECD highlights that the design of MDRs should comply with the following principles:

- The rules should be clear and easy to understand so that taxpayers have certainty about what is required by the regime.¹⁴⁰
- The rules should balance additional compliance costs to taxpayers with the benefits obtained by the tax administration.¹⁴¹
- The rules should be effective in achieving the intended policy objectives and should accurately identify the schemes to be disclosed.¹⁴²
- The rules should be flexible and dynamic enough to allow the tax administration to adjust the system to respond to new risks (or carve-out obsolete risks).¹⁴³
- Information collected under mandatory disclosure should be used effectively to ensure change in behaviour and to counteract tax avoidance schemes.¹⁴⁴

¹³⁸ SARS Public Notice No. 140, para 2, in Government Gazette No. 39650 (3 February 2016).

¹³⁹ Louw and Simpson, above n 36, 3.

¹⁴⁰ OECD, *Mandatory Disclosure Rules: Action 12 – 2015 Final Report*, above n 16, 20.

¹⁴¹ *Ibid* 9.

¹⁴² *Ibid* 20, 23.

¹⁴³ *Ibid* 9.

¹⁴⁴ *Ibid*, Executive Summary.

The Australian Treasury's Discussion Paper alludes to the above principles – an indication of the government's intention to adhere to the same.¹⁴⁵ In particular the Discussion Paper makes it clear that the government's key priority will be ensuring that there is no unnecessary overlap with existing disclosure rules.¹⁴⁶

3. REVIEW OF THE EFFECTIVENESS OF MANDATORY DISCLOSURE REGIMES

This section assesses the effectiveness of MDRs in both the UK and South African contexts, thereby providing a platform for 'lessons learnt' that can be useful for policy-makers in other Commonwealth law jurisdictions, including Australia.

3.1 The UK's experience

HM Revenue and Customs asserts that the DOTAS regime has been a successful part of its multi-pronged strategy for dealing with tax avoidance. Most of the professional firms and the tax directors of large companies have agreed that DOTAS has been effective in reducing marketed tax avoidance schemes.¹⁴⁷

The DOTAS regime has been instrumental in providing HM Revenue and Customs with early information to ensure early detection of tax avoidance schemes. The early years following the introduction of the DOTAS regime saw a significant number of historical schemes disclosed. This gave rise to an initial spike of action to close down loopholes through legislative changes as more information became available about the schemes being promoted in the market.¹⁴⁸ Over the years, the number of disclosures, especially from most mainstream tax advisers, lessened, which implies a decrease in the number of reportable schemes that are being invented and offered to customers.¹⁴⁹ A 2011 OECD report indicated that the DOTAS rules have changed the economics of tax avoidance in the UK, and that the disclosures cut off over GBP 15 billion in avoidance opportunities.¹⁵⁰ DOTAS is believed to be one, but not the only, factor in this change in behaviour.¹⁵¹ As numbers of disclosures have got much lower in recent years, the UK tax administration assumes that this shows the market for ATP schemes is shrinking, but they have put measures in place to ensure this is not as a result of non-compliance with the DOTAS regime.¹⁵² The marketed avoidance schemes are now believed to be largely the province of a small minority of tax advisory firms, generally referred to as boutique firms in the UK.¹⁵³

The DOTAS regime has been an effective instrument in the identification of ATP schemes and their promoters and users. OECD statistics show that, from the introduction of DOTAS on 1 August 2004 up to 31 March 2013, around 2,366 schemes

¹⁴⁵ Australian Treasury, *OECD Proposals for Mandatory Disclosure of Tax Information*, above n 10, para 4.

¹⁴⁶ *Ibid.*

¹⁴⁷ Baker, above n 58, 87.

¹⁴⁸ UK Government, 'HMRC Disclosure Statistics', above n 121.

¹⁴⁹ UK House of Lords, Select Committee on Economic Affairs, *Tackling Corporate Tax Avoidance in a Global Economy: Is a New Approach Needed?*, 1st Report of Session 2013-14 (31 July 2013) para 41; Baker, above n 58, 88.

¹⁵⁰ OECD, *Tackling Aggressive Tax Planning*, above n 2.

¹⁵¹ OECD, *Public Discussion Draft*, above n 6, para 49.

¹⁵² *Ibid* para 50.

¹⁵³ Baker, above n 58, 87.

were disclosed and 925 of them were closed by legislative changes.¹⁵⁴ Over 200 stamp duty land tax schemes were closed by just three legislative changes.¹⁵⁵

Clearly, the rules have been effective in deterring the promotion and use of ATP schemes. The information provided to HM Revenue and Customs has been useful in allowing the UK Government, where appropriate, to introduce legislation to close down ATP schemes before significant tax revenue was lost. The time taken to shut down certain schemes has also been quick. In one occasion, a scheme was closed down within a week of the disclosure, protecting millions in tax revenue.¹⁵⁶ The use of client lists has enabled the government to put together an operational response unit that ensures the deployment of UK tax administration resources to be coordinated and planned more effectively to identify the number of possible cases at an early stage. Client lists have also provided an additional mechanism for checking that schemes are disclosed by all users.¹⁵⁷ The UK has also used the information provided to influence taxpayer behaviour. For instance, HM Revenue and Customs may use the disclosed information and the client lists to make early contact with promoters and potential users to encourage them to change their view of a scheme. Legislation was introduced in 2014 which may require disputed tax in disclosed schemes to be paid before the dispute is settled, thus ensuring that the Exchequer, not the taxpayer in question, holds the benefit of the money during the dispute.¹⁵⁸

It must be acknowledged, though, that the DOTAS regime can only do so much to reduce the UK tax gap. The 2014 HM Revenue and Customs statistics indicate that the UK tax gap was at 6.8 per cent of all tax liabilities (a total of GBP 34 billion), of which avoidance made up GBP 3.1 billion and ‘legal interpretation’ another GBP 4.5 billion.¹⁵⁹ Thus, the DOTAS regime has no impact on other elements of the tax gap, which include error, failure to take reasonable care, criminal attacks on the tax system, evasion, non-payment of tax and the hidden economy.¹⁶⁰

3.2 A review of South Africa’s provisions

South Africa’s reportable arrangement provisions¹⁶¹ work as an ‘early warning system’ for SARS, to identify aggressive transactions when they are entered into. This has allowed SARS to counter ‘innovative’ transactions as they are devised, instead of attempting to catch up a number of years later.¹⁶² When the rules were initially introduced in 2003,¹⁶³ they largely focused on structured financial arrangements facilitated by banks (eg, preference share arrangements, which are legitimate), so fewer than 150 transactions. Some taxpayers indicated that they had encountered fewer transactions that they believed would give rise to concern, while others raised technical

¹⁵⁴ OECD, *Public Discussion Draft*, above n 6, para 40.

¹⁵⁵ *Ibid.*

¹⁵⁶ *Ibid.*

¹⁵⁷ *Ibid* para 45.

¹⁵⁸ *Ibid* para 51.

¹⁵⁹ HM Revenue and Customs, *Measuring the Tax Gap: 2014 Edition* (2014), <http://webarchive.nationalarchives.gov.uk/20150612044958/https://www.gov.uk/government/statistics/measuring-tax-gaps>.

¹⁶⁰ Baker, above n 58, 88.

¹⁶¹ Part B of the TAA.

¹⁶² Louw and Simpson, above n 36, 3.

¹⁶³ Introduced by the *Revenue Law Amendment Act 45 of 2003*, and set in section 76A of the *Income Tax Act 58 of 1962* (now repealed).

points to avoid reporting or restructured their transactions to avoid the triggers for reporting.¹⁶⁴ With various revisions to rules over the years, their deterrent effect on aggressive tax avoidance became more apparent, particularly in light of the SARS Commissioner's Gazetted Public Notices of specific reportable arrangements, which have extended the scope of the rules with additional specific hallmarks targeting transactions that are of particular concern to the South African tax administration.¹⁶⁵ Data from SARS shows that 582 arrangements have been reported since 2009 and that the majority of disclosures under the 'specific reportable arrangements' were made during 2009 by several large companies.¹⁶⁶ SARS data shows that most of these disclosures comprised preference shares that are redeemable within 10 years of issue, which has provided an insight into how preference share funding is utilised. This understanding has informed the design of the new hybrid equity tax rules that have been introduced.¹⁶⁷

4. CONCLUSION AND RECOMMENDATIONS

This article is the follow up to Part 1 which presented a case study of Australia in considering whether to adopt MDRs and how such a regime should be framed in the Australian context. Part 1 argued that MDRs will enhance the information available to the ATO to crack down on ATP. It provided recommendations to ensure that the rules do not unnecessarily overlap with existing disclosure rules, avoid unnecessary compliance burdens on taxpayers and ensure an appropriate balance of competing policy priorities.

This article (Part 2) has explored the anticipated¹⁶⁸ implementation design issues of MDRs for the Australian context.¹⁶⁹ It draws on the OECD recommendations for the design features of effective MDRs and presents a comparative legal analysis of how MDRs apply in two Commonwealth countries – the UK and South Africa – whose experiences may be informative in framing a regime suitable for Australia's context and other Commonwealth countries contemplating the adoption of these rules. The article uses the OECD's recommended best practices to critique the approaches followed in the UK and in South Africa; from their success stories, if any, recommendations are provided on the matters the government sought community views on with respect to the design features for Australia's envisaged MDRs.

With respect to views sought by the government on the suitability of referring to some disclosure provisions in crafting some of the MDRs provisions,¹⁷⁰ this article asserts that this is a plausible approach that will ensure that the rules are crafted in light of Australia's circumstances. For example, some provisions in the existing promoter penalty regime (such as those relating to the definition of a promoter, meaning of prohibited conduct and the structure of penalties) could be expanded on and redrafted

¹⁶⁴ South African Institute of Chartered Accountants, 'New Reportable Arrangements Legislation' (2009) 150 *Tech Talk*

<https://www.saica.co.za/TechnicalInformation/Publications/TechTalk/tabid/711/itemid/1211/pageid/4/language/en-ZA/language/en-ZA/Default.aspx> (accessed 13 May 2012).

¹⁶⁵ OECD, *Public Discussion Draft*, above n 6, para 54.

¹⁶⁶ *Ibid* para 42.

¹⁶⁷ *Ibid*.

¹⁶⁸ Australian Treasury, *OECD Proposals for Mandatory Disclosure of Tax Information*, above n 10.

¹⁶⁹ *Ibid*.

¹⁷⁰ *Ibid*, Table 2, Issue 5.

to form certain sections of the envisaged MDRs. Similarly, some provisions in the Reportable Tax Position Schedule (as discussed in Part 1), such as those relating to reportable tax positions, could be redrafted to form certain sections of the envisaged MDRs that are suitable for Australia's circumstances.

Ultimately, it is hoped that this two-part study is useful for governments and policy-makers in Australia – and other Commonwealth countries more broadly – considering whether to implement an MDR regime.