The UK General Anti-Avoidance Rule: Transplants and Lessons

The UK General Anti-Avoidance Rule has been criticized both for being too narrow and too wide. This article examines the origins of the UK GAAR, its wording and evolution, and the use of concepts and phrases transplanted from the United Kingdom and used in the European Union’s ATAD and BEPS Action 6.

1. Introduction

General anti-avoidance rules (GAARs) are a hot topic in taxation. Although many jurisdictions have had GAARs for years, growing concerns about tax avoidance have resulted in the spread of this anti-avoidance tool. We now see the conceptual underpinning of the GAAR (that of a general anti-abuse principle overriding the particular rule, going beyond normal statutory interpretation) spreading into double taxation treaties by way of the principle purpose test (PPT), introduced through Action 6 of the OECD’s Base Erosion and Profit Shifting (BEPS) Project⁴ and the accompanying Multilateral Convention (MLI).⁵ We also see this influence in the European Union’s Anti-Tax Avoidance Directive (ATAD).⁶ This article will discuss the UK GAAR and, in particular, the language and concepts used in that legislation, which much of the literature assumes has influenced the development of the PPT and ATAD.

2. The UK GAAR: Transplanting Legal Concepts

The United Kingdom was a latecomer to the ever-growing list of jurisdictions with a legislative GAAR. Despite having bestowed the sometimes-disputed benefits of GAARs on many former colonies, the United Kingdom had strongly resisted introducing such a provision into its own law for many years. Even now, the United Kingdom has called its GAAR a general anti-abuse rule rather than a general anti-avoidance rule.

The use of the word “abuse” rather than the word “avoidance” was considered important at the time the rule was introduced, to underline the moderate nature of the rule proposed and convince doubters.⁴ The word “avoidance” has become so overused and devalued in the current debates that this switch of wording to abuse may be helpful, although the difference appears to be of little practical significance when comparing the UK GAAR with that of other jurisdictions. Therefore, the UK provision will here be called a GAAR, as will similar provisions in other jurisdictions.

Now that the United Kingdom does have a statutory GAAR, introduced in the Finance Act 2013, this very specific domestic legislation is being attributed with surprisingly extensive influence. This is possibly because the United Kingdom’s GAAR was developed at a time when both the European Union and the OECD were especially active in the fight against tax avoidance and, inevitably, ideas and language that were common in the discourse of the United Kingdom at the time were introduced into discussions in which UK experts played a role. In this way transplants of anti-avoidance legislative language took place. The UK GAAR was itself heavily influenced by other common law GAARs and the judicial attempts to rein in abuse in the United Kingdom in the Ramsay series of cases, so the transplants are more complex than might at first appear.⁷ It is important to note, however, that a transplant of language may result in very different consequences, taking one jurisdiction with another.⁸ Even Alan Watson, a strong proponent of legal transplants, who has argued that rules move easily from one system to another, recognizes that a successful legal transplant may grow differently in the host system from the way it develops in the parent.⁹ Watson also acknowledges that foreign law may be influential but misunderstood.

It is suggested in this article that some aspects of the UK GAAR have been transplanted and could work, but that there are also some misunderstandings about aspects of the wording, which has been criticized both for being too wide by some and too narrow by others. In addition, it is recognized that legislation takes on a life of its own once in force and that, in the United Kingdom as well as in other jurisdictions, there may be developments of the GAAR based on either misunderstanding or deliberate diversions. Thus, one can support the concept of a GAAR like

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1. OECD, Action 6: Preventing the Granting of Treaty Benefits in Inappropriate Circumstances.
the UK GAAR and even its initial drafting, while having concerns about the way it is evolving.

3. Key Characteristics of the UK GAAR

3.1. Background: UK case law and the Aaronson Study Group

The UK GAAR was initially proposed and drafted by Graham Aaronson QC, a very experienced tax barrister who had appeared for both revenue authorities and taxpayers in contentious tax matters for many years. At the request of the UK government, Aaronson formed a Study Group, of which this author was a member. This group assisted in formulating Aaronson's advice to be considered by the revenue authorities and the government. This was a novel way of proceeding in terms of writing UK tax policy. Aaronson and his group were heavily influenced by the particular problems arising from UK case law and by their experience in other common law jurisdictions.

For some time, it had been considered that the UK case law had created a judicial rule, colloquially known as "the Ramsay principle". This rule could be stated as follows: where there was a pre-ordained series of transactions with inserted steps with no commercial purpose other than the avoidance of tax and no practical likelihood that the events would not take place in the order ordained, the courts could view the scheme as a whole and tax on the basis of the overall result.

However, there were problems both with the legitimacy of the concept of a judicial rule and with its rigidity - as soon as a rule is created it can give opportunities for new types of avoidance. Taxpayers won some important cases on the basis that a scheme was not, for example, fully pre-ordained. The courts began to review their approach and assert that there was not, and never had been, a judicial rule. The result is that the so-called "Ramsay principle" is now said by the courts to be merely a form of statutory interpretation. This is an approach to construction where:

8. Aaronson, supra n. 4.
9. The full list of members was John Bartlett (Group Head of Tax, BP plc), Sir Launcelot Henderson (Judge of the Chancery Division of the High Court of Justice), The Rt. Hon. Lord Hoffmann (formerly Lord of Appeal, Non-Permanent Judge of the Court of Final Appeal of Hong Kong), Howard Nolan (formerly Tax Partner at Slaughter & May, part-time Judge of the First-Tier Tribunal (Tax Chamber)), John Tiley QC (Hon) Emeritus Professor of the Law of Taxation, Cambridge University), and Professor Judith Freedman, Oxford University, the author of this article. The resulting Aaronson Report was that of Mr Aaronson alone. The analysis was supported by the group, except that the judges were required to maintain strict neutrality as to whether a GAAR should be introduced or not.
11. This judicial 'rule' was fully set out in Furniss v. Dawson [1984] A.C. 474.

By formulating the rule in this way, the courts not only gave themselves more flexibility but also confronted head on the challenge to their powers. No one can object to judges applying statutory interpretation, but, in some hands, this approach goes well beyond normal purposive interpretation and reaches results that may involve some stretching of the wording. It might also fail to catch some abuses that are so clearly within the legislative wording that no method of interpretation can catch them. In view of this, the Aaronson Study Group considered the judicial rule of interpretation to be too uncertain and not wholly reliable. What is more, a judicial rule of interpretation cannot reconstruct transactions. The result of applying it is unclear. Further, it was considered desirable for taxpayers to have certain safeguards for cases where the wording of legislation was not to be applied in accordance with normal, purposive rules of interpretation.

3.2. A legislative GAAR with safeguards

A statutory GAAR was proposed by Aaronson in 2011, consulted upon by the government and then introduced into UK legislation in the Finance Act 2013. The prevailing attitude had turned against tax avoidance very firmly and Aaronson managed to win over the tax professional bodies, so that the opposition to introducing what had been presented as a moderate GAAR was fairly muted.

To support the statutory GAAR, the Aaronson Study Group proposed several safeguards. Some of these safeguards involved moderating the United Kingdom's usual very strict rules of evidence so that more note could and would be taken by the courts of the prevailing view and the stated views of HMRC at the time the transactions in question were entered into. This was important purely within a UK context.

Of more general significance was the introduction of the GAAR Advisory Panel (the Panel) and the provision of GAAR guidance notes. These two tools, originally intended to be helpful safeguards for taxpayers, have now been developed in ways that were not anticipated in the original Study Group report. However, Aaronson himself did play a significant role in developing these ideas. This shows how ideas can develop differently from the way initially envisaged even within one jurisdiction. It would be no great surprise, then, that wording and ideas taken from one jurisdiction and applied elsewhere could lead to different results.

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The ultimate question is whether the relevant statutory provisions, construed purposively, were intended to apply to the transaction, viewed realistically. (The Arrowtown test.)
3.2.1. GAAR Advisory Panel

The initial Aaronson study proposed that the Panel should be an independent advisory panel that would be a quick and cost-effective way of helping taxpayers and HMRC identify the scope of the GAAR without running the risk of giving greater discretionary powers to HMRC. It was to have a majority of non-HMRC members, to advise whether HMRC would be justified in seeking counteraction under the GAAR and the Panel was to publish (appropriately anonymized) digests of its advice. It would also help to approve the HMRC GAAR Guidance and keep it up to date. This Proposed Panel, which was based on the Australian GAAR Panel, was intended as a place for discussions between the revenue authority and the taxpayer and advisory community. It was not intended to be a judicial or quasi-judicial body and, significantly, it was clearly intended to include HMRC representatives. However, the Panel’s pronouncements were always to be significant. The GAAR legislation provides that a court must take GAAR Guidance approved by the Panel and the opinions of the Panel about the arrangements into account. This gives unusual strength to what is non-statutory guidance and therefore soft law. It is not binding on the courts and could be overruled, but it must be “taken into account”. This is another novel feature in the UK system, which rarely allows non-statutory material to be considered by a court.

Unfortunately, the Panel was not fully consulted upon when the legislation was in draft, for various reasons, but behind the scenes discussions resulted in a change of plan. Some commentators considered that a body could not be independent if it contained HMRC representatives. Strictly, of course, this was true, but it misunderstood the purpose of the exercise, which was to have a forum for discussion and not a decision-making body. The HMRC representative was removed but it still remains the case that the Panel Chair and members are appointed by the Commissioner of HMRC, which creates an awkward halfway house. Given the powers now exercised by the GAAR Panel, it would be more acceptable were they to be appointed like judges by the Judicial Appointments Committee.

HMRC can bring an action against a taxpayer to counteract a tax advantage under the GAAR by giving notice in the form specified in Schedule 43 of the Finance Act 2013. If the taxpayer does not then take the corrective action specified in that Schedule (which involves amending the tax return or claim or settling an appeal and notifying HMRC that this has been done and how much additional tax has or will become due or payable as a result of this corrective action), the matter will go to the Panel. On the basis of written representations only the Panel will then come to an opinion on whether the entering into and carrying out of the tax arrangements is a reasonable course of action in relation to the relevant tax provisions having regard to all the circumstances including the matters referred to in the GAAR legislation.

This opinion is then communicated to the taxpayer and may be published in an anonymized form. It must be taken into account by a court that hears the full case but of course that court may have information that the Panel did not have. An appeal is not in any way precluded, but the opinion of the Panel can form the basis for a penalty, without any further hearing.

Furthermore, there can now be generic referrals to tax arrangements and opinions of the Panel are important as the basis for applying other provisions requiring accelerated payment of tax even when litigation is under way and also for application of legislation directed at tax intermediaries (the enablers’ legislation).

Although the Panel is described by HMRC as a safeguard to taxpayers against whom all this new anti-tax avoidance legislation is applied, it is more accurate to say that the existence of the GAAR Panel has increased the capacity of the tax authority to pass measures directed at tax avoiders because they now have a mechanism for defining avoiders. This mechanism places great weight on the opinions of a Panel said not to be judicial.

HMRC is very clear that it does not believe the Panel to be judicial, stating in the GAAR Guidance:

> The Advisory Panel does not perform a judicial function and the Advisory Panel process does not involve formal hearings where cases will be presented and heard. The Advisory Panel delivers an opinion, not a judicial decision. The opinions are not binding on HMRC or the taxpayer.

Regardless of this comment, the significance of the opinions given for those involved is such that the powers of the Panel appear more than purely advisory. It is hard to believe that a court would not entertain an action for judicial review over the Panel’s decisions in an appropriate case, although no case of this kind has come to court at the time of writing.

The Panel has now published 12 anonymized opinions, coupled in each case with published guidance. Although most of these opinions relate to cases which might have been defeated on technical grounds anyway, so that the need for a GAAR can be disputed, there is no doubt that this is a way to make a point to taxpayers and their advisers. In each case the Panel decided that the entering into

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17. Id., at paras. 6.8-6.9.
19. The procedural rules summarized here are set out in Schedule 43 to the Finance Act 2013.
and carrying out of the tax arrangements was not a reasonable course of action in relation to the relevant tax provisions.

It is not surprising that HMRC would want to start out by taking only safe cases to the Panel that it knew it would win. On the other hand, these “opinions” look close to press releases or spotlight notifications by HMRC. It is not known whether there have been other cases where the Panel has held the course of action to be reasonable but has decided not to publish an opinion. The HMRC Guidance simply states that “it is expected that in most cases, shortly after each opinion is given, an anonymised version of the opinion will be published by HMRC.”

Perhaps there have been cases where the Panel has decided the course of action was reasonable, but, if so, there has been no publicity about them. This set of opinions does underline the rather curious hybrid nature of the Panel, somewhere between an Advisory Committee issuing deterrent notices and a quasi-judicial body making significant and consequential decisions about the position of individual taxpayers.

### 3.2.2. GAAR guidance

As already stated, HMRC’s GAAR Guidance is approved by the Panel and the approved Guidance as it was at the time the tax arrangements were entered into must be taken into account by the court in any GAAR case. The Guidance is now very extensive. Parts A, B and C (41 pages) set out the purpose and status of the Guidance and summarize what the GAAR is designed to achieve and how it operates. Part D contains 133 pages of examples. Part E deals with procedural issues (36 pages). Parts A to D have the approval of the Panel. Part E has a lower status as it does not have that approval, presumably because it governs the Panel itself.

The Guidance has become a form of soft law that is often cited as authority for a proposition. In theory this Guidance could be challenged in court but in practice it would be difficult to show that a proposition in Guidance could be challenged in court but in practice it is easier, though not easy, to decide whether the Panel are considered to be the arbiters.

### 3.3. Structure of the legislation

The drafting of the UK GAAR can be seen as creating a flow chart (see Diagram 1). Diagram 1, based on sections 206-209 of Finance Act 2016, is simplified but gives the general idea.

As can be seen from Diagram 1, the UK GAAR legislation has a carefully devised and logical scheme. It uses tests such as “abusive”, “reasonableness”, “main purpose or one of the main purposes” and “contrived steps”. These phrases are used within an intricate structure and are familiar words within the UK tax and general legal system. Taking these words out of this context may result in very different consequences.

### 4. Further Investigation of the Wording of the UK GAAR

#### 4.1. Main purpose or one of the main purposes

The notion that there can be more than one main purpose is a difficult one, but the phrase was first used in UK legislation in 1960 and so UK practitioners have considerable experience and much case law to rely upon. Even then the meaning is not straightforward. It can be stated that:

- simply making a tax saving does not necessarily constitute a main purpose being a tax advantage;
- the test is a subjective one and a matter of the intention of the parties to be decided as a question of fact;
- and a purpose can be more than “trivial” without being a “main” purpose. “Main” has a connotation of importance. A tax advantage that is ancillary or purely incidental is not a main object.

As can be seen, this wording is deliberately wide and subjective and is used in many targeted anti-avoidance rules (TAARs) in the United Kingdom for precisely this reason, giving HMRC considerable discretion. To require that the purpose should be solely or even mainly one of obtaining a tax advantage would give revenue authorities a very uphill struggle, since a taxpayer can always show some other motivation for an action: this is very easy to construct, and it is exceptionally difficult for courts to weigh different motivations against each other. The main purpose or one of the main purposes wording saves the courts from this task and it is easier, though not easy, to decide whether a tax motivation is purely ancillary or incidental.

It is for these reasons that, when the GAAR was introduced, the words were used, but only as part of a more elaborate structure that placed safeguards around this discretion. In practice, the GAAR may be more restrictive than many TAARs. As the GAAR Guidance explains:

> The broad definitions of “arrangements” and “tax arrangements” set a low threshold for initially considering the possible application of the GAAR. A much higher threshold is then set by confining the application of the GAAR to tax arrangements which are “abusive”.

Therefore, it is incorrect to state that the UK GAAR is based on a subjective test. The subjective test forms only a first step to a much more stringent set of conditions.

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26. HMRC, supra n. 24, E4.2.8, p. 27.
4.2. Reasonableness tests

There are several references to reasonableness in the UK GAAR legislation. Section 207 of the Finance Act 2013 sets out that:

(1) Arrangements are “tax arrangements” if, having regard to all the circumstances, it would be reasonable to conclude that the obtaining of a tax advantage was the main purpose, or one of the main purposes, of the arrangement.

(2) Tax arrangements are “abusive” if they are arrangements the entering into or carrying out of which cannot reasonably be regarded as a reasonable course of action in relation to the relevant tax provisions, having regard to all the circumstances, including:
   (a) whether the substantive results of the arrangements are consistent with any principles on which those provisions are based (whether express or implied) and the policy objectives of those provisions;
   (b) whether the means of achieving those results involves one or more contrived or abnormal steps; and
   (c) whether the arrangements are intended to exploit any shortcomings in those provisions.

This looks fairly cumbersome as a method of drafting but, in a UK context, achieves its aim. The main purpose test is converted to an objective test by prefacing it with a requirement that it should be reasonable to conclude that the obtaining of a tax advantage was the motivation. It is not, therefore, dependent on the views of the particular taxpayer. This is drafting born of experience of the difficulties caused by applying a purely subjective test in tax matters.

Further objectivity is built in by the so-called “double reasonableness test” in section 207(2), which also then gives illustrative but not exhaustive examples of the kind of behaviour that may not be considered reasonable. 32

In early discussions of the drafting in the Aaronson Study Group, the phrase “intention of Parliament” was

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Diagram 1 – Drafting of the UK GAAR

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1 To determine reasonableness, all circumstances must be considered, including principles and policy of legislation; contrived or abnormal steps; exploitation of shortcomings in the legislation.

2 Further indications of abusiveness include not corresponding with economic profit, gain, loss, etc., but only if it is reasonable to assume that such a result was not anticipated by the legislation when enacted. Not abusive if arrangement accords with established practice, and at time entered into HMRC had indicated acceptance of practice.
used, but given the jurisprudential and practical difficulties encountered with that phrase, the final wording was preferred, although there is reference to the policy objectives of the underlying legislation. The examples in the legislation anchor the courts in the substantive legislation under consideration and subsequent provisions make it clear that established practice, and HMRC’s stated views and practice at the time the transactions were entered into, might indicate that transactions were not abusive. This should give considerable comfort to taxpayers who are following normal practice and thus removes some of the uncertainty inherent in a test based on motivation.

5. Influence of the UK GAAR

The influence of the UK GAAR and case law on the European Union’s ATAD and the OECD’s MLI is very clear to see, and the outcome has been criticized in recent literature as giving both bodies a problem with a test that is too wide and too vague. It is true that the wording of the UK GAAR may have seeped through to that of other provisions without the full safeguards surrounding the UK GAAR being adopted. This is a warning against overenthusiastic transplantation of ideas. However, the evolution of these phrases may well differ from that in the United Kingdom. This is in the nature of legal transplants, as commented in the introduction. Although we may think that the ATAD and the MLI are moving us towards greater harmonization, we are unlikely to iron out local variations where the provision is so fact based and so much connected to the underlying local law.

5.1. ATAD

Article 6 of the ATAD requires that:

1. For the purposes of calculating the corporate tax liability, a Member State shall ignore an arrangement or a series of arrangements which, having been put into place for the main purpose or one of the main purposes of obtaining a tax advantage that defeats the object or purpose of the applicable tax law, are not genuine having regard to all relevant facts and circumstances. An arrangement may comprise more than one step or part.

2. For the purposes of paragraph 1, an arrangement or a series thereof shall be regarded as non-genuine to the extent that they are not put into place for valid commercial reasons which reflect economic reality. (Emphasis added)

Some of this wording has entered into EU law not via the GAAR but through the Halifax VAT case, but the words that have caused most concern are the reference to “main purpose or one of the main purposes” which differs from the test in the EU abuse of law cases (“sole” or “essential” purpose) and is thought by many commentators to be too wide. In Article 6 there is no reasonableness qualification of the main purpose test as is found in the UK GAAR, so whilst this test may have been borrowed from the United Kingdom it appears in a context where it is not constrained by safeguards.

However, it might be thought that article 6(2) goes some way towards adding in the objectivity to which the European Union is accustomed in its abuse of law cases. It is arguable that although the tests look very different on the face of it, they will not be applied in such a very different fashion.

Within the European Union, of course, the ultimate decisions will be made by the CJEU, which might eventually impose some kind of harmonized view of the meaning of the test that would, in turn, influence the domestic systems. Unfortunately it may be that the United Kingdom will not be part of that exercise if, as planned at the time of writing, it leaves the European Union and the jurisdiction of the CJEU completely.

5.2. The Principle Purpose Test in the MLI

Article 7 of the MLI, entitled “Prevention of Treaty Abuse”, states that:

Notwithstanding any provisions of a Covered Tax Agreement, a benefit under the Covered Tax Agreement shall not be granted in respect of an item of income or capital if it is reasonable to conclude, having regard to all relevant facts and circumstances, that obtaining that benefit was one of the principal purposes of any arrangement or transaction that resulted directly or indirectly in that benefit, unless it is established that granting that benefit in these circumstances would be in accordance with the object and purpose of the relevant provisions of the Covered Tax Agreement. (Emphasis added)

Once again, we can see the influence of the UK GAAR in this wording, but here we not only find that the obtaining of the benefit must be “one of” the principal purposes but also that the words “if it is reasonable to conclude” precede that principal purpose test. The move from “main” to “principal” seems to have been of some assistance in comprehension or perhaps it just makes for a better abbreviation! The Explanatory Statement makes it clear that clauses using the phrase “main purposes” are also acceptable and there is no significance in the difference of terminology.

Concerns about the introduction of a subjective test into the MLI are misplaced because of this qualification. The reasonableness requirement is not only about shifting the burden of proof, as Lang and others have argued, but about making this an objective test as Weber correctly discerns. It has been argued, for example by Kemmeren, that the reasonableness test creates uncertainty but, as

33. J. Freedman, supra n. 10.
38. OECD, Explanatory Statement to the Multilateral Convention to Implement Tax Treaty Related Measures to Prevent Base Erosion and Profit Shifting, Treaties & Models IBFD.
already shown, the reasonableness test should add to certainty rather than detract from it, especially if coupled with examples of what amounts to reasonableness, as in the UK GAAR. This could be built in by judicial decision and commentary in the MLI context.

Some of the misunderstandings in the literature arise from understandable lack of familiarity with the reasonableness test as used in the common law. This is a warning sign with regard to transplants, but it need not necessarily mean that the concept will not be transplanted successfully.

6. Conclusion

The UK GAAR is not perfect. It would have been better had the underlying tax system been simpler and clearer so that no GAAR was necessary. There have been some developments around the UK GAAR, making it the hook upon which to hang penalties and the further new anti-avoidance provisions (see section 3.2.1.), that may mean that the procedure around the GAAR, and the Panel in particular, will require reassessment and revision before too long. Some of these developments appear to this author to have gone too far. Furthermore, it has been regrettable that the UK legislation has continued to accrue new TAARs and other anti-avoidance provisions despite the existence of the GAAR, contrary to the expressed hopes in the Aaronson Study.

Finally, the case law continues to develop and apply the Ramsay principle, albeit as an enhanced principle of statutory interpretation. 42 This is something that cannot be removed - once the genie is out of the bottle it will not return. It remains to be seen whether the case law around this will continue to apply the rule expansively or will be reined in once the GAAR begins to take hold in a way that is observable to the courts.

However, the United Kingdom is not alone. No jurisdiction has yet managed to create a system that does not require anti-abuse rules, either legislative or judicial. At a domestic and international level, GAARs have become a necessary weapon in the armoury against tax avoidance. The transplant of language and concepts from the UK GAAR to EU and OECD-level legislation may or may not be helpful, but the development of those rules needs to be informed by the original meaning of those concepts in the country of origin. Thereafter the transplant will undoubtedly take on a life of its own, as the UK GAAR has done in its country of origin.

42 For example, in UBS AG (Respondent) v. HMRC [2016] UKSC 13.