UK Government issues new rules on tax avoidance and Government contracts

The Chancellor’s Budget on 20 March 2013 confirmed that, from 1 April 2013, new rules will be in place, which will require potential suppliers under UK Government contracts to certify, as part of the procurement process, that they have not been involved in certain tax avoidance arrangements. The potential cost of not being able to certify is exclusion from the bidding process.

A number of relaxations from the original proposal were announced, including what is effectively a gradual phase-in of the scope of the proposals from 1 April 2013.

However, given that the proposals will start to take effect in just over a week’s time, companies will now need to consider how they are likely to be impacted by these proposals and what steps they need to take in the future to comply with the rules.

Budget announcements

The Budget announcements address the following key areas, although in a number of these areas, there may be further discussion and clarification.

Size of contracts covered by the new rules

It is now proposed that there will be a threshold of £5mn beneath which these “tax confirmation” rules will not apply. This is a higher threshold than previously proposed and it will be applied on a contract by contract basis.

Companies needing to provide the appropriate self-certification

There was significant concern with the original proposals that it might be necessary to consider every company in the group when making the certification. These concerns have been listened to and certification will
now only be required in respect of the “economic operator” who will fulfill the contract, as defined in the Public Contracts Regulations 2006. Certification in respect of other group companies will not generally be required, unless they are considered an economic operator by virtue of the activities they will provide in connection with the bid.

Where the economic operator is a joint venture or consortium, the self-certification must cover all members. The economic operator is not required to certify on behalf of any subcontractor or any other members of the supply chain, which will relieve some of the concerns with the original proposals. Where the economic operator is a partnership, limited partnership or limited-liability partnership (LLP), the self-certification must cover that entity but not the individual members.

**Self-certification information**

Procurement bidders will be asked to self-certify whether they have a history of using tax avoidance in the UK and have any “occasions of non-compliance” within a designated timeframe. An occasion of non-compliance occurs when an amendment is made to a tax return as a consequence of HM Revenue & Customs (HMRC) successfully challenging a taxpayer by reference to the general anti-abuse rule or the Halifax principle (developed in respect of VAT). In a significant change from the original proposals, an amendment due to a Targeted Anti-avoidance Rule (TAAR) (of which there are many) will no longer need to be included.

Non-compliance also occurs if a tax return is found to be incorrect because of the failure of a transaction which was, or should have been, notified under the Disclosure of Tax Avoidance Scheme (DOTAS) rules, or the supplier’s tax affairs have given rise to a conviction for tax related offenses or to a penalty for civil fraud or evasion. There may be certain transactions (such as leasing arrangements) that need to be disclosed under DOTAS primarily as part of HMRC’s information gathering process.

**Application of overseas taxes**

Foreign economic operators bidding will be required to self-certify their tax compliance against the equivalent tax rules in their territory. This raises concerns as to what is an “equivalent tax rule”. In particular, the proposed UK General Anti-avoidance Rule (GAAR) is intentionally narrower in scope than that found in many territories. In response to this, the Government points out that an occasion of non-compliance does not mean automatic exclusion from the bid process as bidders can put forward explanations, such as changes in approach, which will be taken into account as part of the bid process.

**Certification period**

In a further change from the 14 February proposal, only amendments made after 1 April 2013 in relation to returns submitted after 1 October 2012 will need to be considered by the certifying bidder. Going forward, bidders will need to look back six years for occasions of non-compliance (but never before the 1 April 2013/1 October 2012 commencement dates set out above). This refers to the time the adjustment was made to the tax return and so the period covered by the return may be more than six years ago.

**Effective date**

The rules do not require an Act of Parliament, and given the start date of 1 April 2013, no further significant changes are expected before they come into force. However, updated guidance is likely to be provided in due course. Furthermore, there will be a review of this policy within a year and the UK Government has noted that changes may, in particular, be made in the following areas depending upon taxpayer behavior:

- Inclusion of other incidents of non-compliance, for example, specific targeted anti-avoidance rules;
- Inclusion of other group entities in the certification, for example, if bidders use special purpose vehicles to make the bid, or take other measures, to exclude companies that have had an occasion of non-compliance from being included in the certification; and
- Amendments to how the rules apply with regard to overseas taxes.

**Actions required**

The changes to the proposals reduce the number of companies likely to be adversely affected by
the proposals and will make the rules more workable in practice. However, many companies will still need to consider the potential application of the rules given the range of sectors which contract with the UK Government.

As a first step in preparing for the new rules, affected groups need to understand when the group will first put in a bid to which the rules are expected to apply so that they know how long they have to prepare.

Bidders will then want to consider which entities in the group may fall with the definition of economic operator and put in place systems to monitor relevant adjustments agreed after 1 April 2013 in respect of those entities. More generally, bidders might wish to review and adapt as necessary their tax strategy going forward. An approach can then be agreed between the Board, the commercial teams and the tax department with regard to complying with the rules.
For additional information with respect to this Alert, please contact the following:

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