

# Tax avoidance

Law



## Taxation

Tax avoidance has been dealt with harshly by the courts. However, it is not something illegal and neither should it be. Therefore, the approach to tax avoidance should be reconsidered. To what extent can statutory interpretation be used in the battle against tax avoidance?

Tax avoidance is a legal practice of manipulating the stipulations of the tax law to minimize one's tax liability. It is different from tax evasion which is illegal manipulation of one's affairs to escape tax. Sometimes, it becomes very difficult to separate the two practices. The courts deal with tax avoidance very harshly because tax avoidance creates inequality between the groups which are capable of avoiding tax and the groups which are not. The " canon of equality" put forth by Adam Smith is not fulfilled.

Courts have, however, struggled in coping with tax avoidance in just and equitable manner. Different judges have passed different judgments for different types of transactions and schemes. They have developed an approach which has allowed them to disregard certain transactions which involve steps that have no commercial purpose. The problem is that certain statutes are not used for the purpose that these are enacted for. These are read in a different context and are interpreted differently. Courts have tried to be objective in such cases but they are of such a wide variety that it is almost impossible to provide justice.

The Duke of Westminster case was a frequently cited case in the judgment of tax avoidance cases. This case entitles the taxpayers to look to mitigate their tax liabilities according to their needs. The courts just used to look at the words and deeds of the individual transactions that formed a part of the scheme. This was changed by the development of Ramsay principle. This <https://assignbuster.com/tax-avoidance/>

principle enabled the courts to look at the substance of the scheme as a whole. The courts now looked at each and every step of a tax avoidance scheme. This shifted the balance in the favor of taxation authority as more and more schemes were nullified by the application of the Ramsay principle. However, it was soon discovered that the Ramsay principle was not applicable in each and every tax avoidance case. The funding in each case was provided differently and the sources of income were different in different cases. The Ramsay principle proved to be unable of having a general application due to its limited scope. In *Westmoreland v MacNiven*, it was proven that Ramsay principle was a method of interpreting only those statutes that referred to commercial terms but it had no application to legal or juristic terms. Over the years, different judges have passed different judgments and different remarks about tax avoidance. Each case is different from the next and complications increase.

Tax avoidance is a legal activity but there is a need to discourage this practice. Courts cannot discourage it because it is impossible to devise a rule or a principle that can be applied to each and every case. There are many ways of avoiding tax and each and every transaction that does that comes to the knowledge of taxation authorities after the financial period ends. At that time, they can only take measures to avoid such practice in the future but the tax that has been successfully avoided remains uncollected. When the next Finance Act comes into force, the taxpayers look to find other ways to mitigating their tax liabilities. The HMRC has made the “ promoters” of schemes to disclose specific information within five days of the scheme being implemented. This makes HMRC aware of what measures it should take to curtail tax avoidance. However, such measures also tend to make the

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taxation system complicated and the “ Canon of Certainty” is breached as a result.

It is very important to alleviate the factors that encourage tax avoidance. A taxpayer looks to avoid tax when he thinks that the tax liability is too high or unreasonable. The taxation authority applies high rates to generate more revenue but as a result, it ends up losing a lot of revenue due to tax avoidance. When a certain group of taxpayers has to pay a lower rate of tax and another has to pay a higher rate of tax, the latter would surely look to avoid tax or take such measures which make it fall into the category of lower rate paying group. Therefore, the basic problem is inequality of tax system. The Government always looks to alter the taxation system so that it fits to the fiscal needs of the country. Very often, it ends up creating an unequal tax system which causes resentment and encourages tax avoidance. The Government needs to employ such a tax system in which various income groups are treated equally and the tax rates are not unreasonably high. Otherwise, tax avoidance is likely to increase.

#### References

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