



HM TREASURY

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DAO(GEN)08/03

Dear Accounting Officer

22 May 2003

TAX PLANNING AND TAX AVOIDANCE

Purpose of this letter

The purpose of this letter is to advise departments:

- against using tax advisers to reduce departments' tax liabilities, other than in very restricted circumstances as described below;
- to base procurement decisions on the need to secure value for money, independent of any tax advantages that may arise from a particular bid; and
- to apply restrictions on the use of offshore jurisdictions by successful bidders to procurement contracts, where such restrictions are justified in terms of the objectives of the project and consistent with international obligations and stated objectives on tax transparency and openness.

It updates and extends the advice in DAO(GEN)6/00, issued on 22 May 2000.

Action and contacts

2. Departments are asked:

- to note the contents of this letter;



- to draw it to the attention of relevant staff in departments and agencies and to the attention of those NDPBs which they sponsor;
- to direct enquiries on specific cases to the Inland Revenue's Revenue Policy Strategy and Coordination Team, telephone 020 7438 6768 (for direct taxes) or HM Customs and Excise, Policy Group, Supply of Services and Public Bodies Team (for indirect taxes); and
- to direct enquiries on the policy matters covered by this letter to the Treasury's Private Finance Unit, telephone 020 7270 4488 (in relation to tax planning) and the Office of Government Commerce, telephone 020 7271 1334 (in relation to public procurement policy).

Tax Planning

3. In the course of their business, the activities of government departments and non-departmental public bodies frequently give rise to tax liabilities; either directly on their own account, or through contracts with other bodies where the tax system influences the terms of those contracts. In making their assessment of cost effectiveness in activities where tax considerations might be important, departments should bear in mind that savings arising from tax mitigation arise at the expense of other taxpayers, or other parts of the public sector. Departments therefore need to pay particular attention to avoid distorting their assessment of value for money for the taxpayer.

4. It is not good value for money for departments to seek to minimise their tax liability through transactions or activities for which there is no genuine justification in economic terms. Departments are therefore advised against using tax advisers to reduce their tax liabilities. In certain circumstances professional advisers may have a legitimate role to play in assisting a department with its tax affairs; for example, in managing statutory PAYE requirements, or in complex commercial contracts. Departments should also not be deterred from taking advantage of arrangements in the tax system aimed at supporting good employment practices. In particular, where departments find that the use of salary sacrifice arrangements genuinely help to support the Government's objectives, including by supporting parents to balance work and family life through childcare support, as opposed to acting as a tax saving device, then salary sacrifice arrangements are permissible. In these circumstances, or in other areas where departments are faced with complex tax issues, the first port of call should be the Inland Revenue or HM Customs and Excise.

Procurement and tax avoidance

5. Public procurement decisions can give rise to a number of issues relating to tax planning. Consistent with the need to ensure fair and transparent procurement processes in line with legal obligations, departments should base such decisions on the need to secure value for money – independent of the tax advantages for

individual departments that may arise from a successful bid from an offshore company, or from complex or artificial tax arrangements which have no underpinning economic basis.

6. There will be discretion on departments to consider restrictions on bidders where they are justified in terms of the objectives of the project and consistent with international obligations and stated objectives on tax transparency and openness. In considering applying restrictions of this nature, Accounting Officers should seek legal advice, and would need to consider whether they were consistent with the overriding obligation, as set out in Chapter 22 of Government Accounting, to obtain value for money in all procurement, taking account of propriety and regularity.

7. The general principles which apply to the acquisition of goods and services are set out in Chapter 22.1 of Government Accounting. The procurement process for Government purchases above specified value thresholds is generally governed by law in the Public Works Contracts Regulations 1991 (S.I 1991 No.2680), the Public Services Contracts Regulations 1993 (S.I 1993 No. 3228) and the Public Supply Contracts Regulations 1995 (S.I 1995 No.201), which implement the relevant EC public procurement Directives. The UK is also party to the WTO Agreement on Government Procurement (“the GPA”) of 1994. The grounds for exclusion of bidders are very limited. Under regulation 14(g) of the Public Supply Contracts Regulations (there is parallel provision in the other Regulations), bidders should be excluded if they have “not fulfilled obligations relating to the payment of taxes under the law of the United Kingdom or the State in which the supplier is established”.

8. It would however be possible for departments to make it a contract condition (notified in advance when advertising the contract) that the successful bidder will be prohibited from using particular tax arrangements, including offshore tax havens, provided such a restriction would not in fact be directly or indirectly discriminatory between EC/GPA bidders.

9. It is important that departments take advantage of the specialist practical and legal advice available to them internally, whilst the Office of Government Commerce provides support on procurement policy more generally. Accounting Officers should pay particular attention to transactions which might give rise to concerns about the propriety of tax arrangements, and should set internal management processes which ensure that such transactions are brought to their attention, and if necessary (and in line with the responsibilities set out in annex 4.1 of Government Accounting) to the attention of Ministers.

Harmful Tax Competition

10. Particular care should be taken with transactions involving bodies with tax residence in offshore financial centres, or which involve tax arrangements that the UK government regards as harmful tax competition. It is standard guidance that, when considering a range of bids for Government contracts, departments must be

confident that those bids are sustainable and robust over the long term. Where those bids are derived in part from the use of tax regimes that are the subject of UK or international pressure for reform, there may be higher levels of tax risk involved which departments should consider when satisfying themselves that such bids are sustainable in this way. In these circumstances, departments should discuss the issue with the Inland Revenue

PFI and Public Sector Comparators

11. In the case of bids under the Private Finance Initiative, it is particularly important to ensure that comparisons of competing bids with a Public Sector Comparator take account of any tax planning by bidders. The 2003 “Green Book” made provisions for a tax adjusted Public Sector Comparator to reflect the fact that there is likely to be a material tax difference between PFI and the wholly public sector alternative. It would be inappropriate to apply a tax adjusted PSC test to bids where tax planning has cancelled out this effect.

Transfer of Real Estate and Other Capital Assets

12. Public procurement projects involving the transfer of real estate or assets that are likely to appreciate in value can often give rise to specific tax issues, in particular the liability to capital gains tax. Where departments are involved in negotiations with bodies who wish to structure procurement proposals in this way, they should engage the Treasury and the Inland Revenue at an early stage to identify the likely tax implications and the resulting impact on value for money for Government as a whole.

Conclusion

13. Guidance on individual cases which departments consider might be covered by this letter should be sought from Inland Revenue or Customs and Excise. The Revenue Departments will not of course be able to provide information about individual bidders which would contravene normal taxpayer confidentiality, though they will be able to comment on the tax implications which the bidder has proposed to departments as part of the procurement process.

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