

Do the haves come out ahead in tax litigation? An empirical study of the dynamics of tax appeals in the UK.

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Do the haves come out ahead in tax litigation? An empirical study of the dynamics of tax appeals in the UK.

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Abstract

This paper considers which parties appeal in tax cases and which parties win such appeals. It adapts party capability theory to derive hypotheses concerning the relative advantages of (certain types of) taxpayers and HMRC, and how this may be affected by institutional factors, such as requirements for permission to appeal, and factors associated with the resources of the parties, such as legal representation. These hypotheses are then tested, using statistical methods, on a dataset assembled by the author of all appeals (including further appeals) from Special Commissioners' decisions since 1981. In doing such this paper both questions what the functions of an appeal system are, and whether the appeal system satisfies these, as well as addressing the question of whether certain large corporates enjoy favoured treatment by HMRC, which has been a recent issue of public concern in the UK.

1 Introduction

This paper examines appeals from the decisions handed down between 1981 and 2009 of the Special Commissioners, the tax tribunal that generally heard the most complex tax cases. The outcome of such cases is clearly important to the parties but it has a much broader public importance, due to their value as precedents. This is due to the rule of *stare decisis*, discussed further in section 2 below, whereby such decisions generally bind the court that handed down the decision and inferior courts in subsequent cases. Additionally, such cases have a general significance, since by shaping the law they influence other taxpayers' liabilities in non-litigated matters – both in disputes that are settled outside litigation as well as in circumstances that do not give rise to disputes.

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Further, it is important to understand which cases are appealed, since it is only in those cases that parties choose to appeal that the courts have the ability to mould the law – and there is no reason to suppose that the cases that are appealed to any court are a representative sample of the cases heard in the court below. Also, as discussed further in section 7 below, if a type of party has a greater propensity to appeal losses than its adversary then it has the potential to shift the law in its favour, even if the superior court is no more generally disposed in favour of that party than the court/tribunal whose decisions are appealed. Clearly, knowing the way cases that are appealed are actually decided also assists our understanding of whether the appeals process shifts the law in a particular direction.

Despite the importance of understanding how the dynamics of the appeals process shapes the law, such empirical legal research has generally been restricted to studying appeals in the United States and even “where the courts of other countries are studied, they are mainly studied by American academics using the same theories and methods used to study American appellate courts.”¹ Yet there are important differences, even between the US and the UK. For example, in the US the general rule is that each party bears their own legal costs, regardless of whether they win or lose, although in tax cases even in the US adverse costs are generally available.² By contrast, as discussed further in section 2 below, the indemnity rule in the UK generally requires the unsuccessful party to pay the winning party’s legal costs. The UK rule on adverse costs might therefore be expected to deter economically weaker parties from appealing, since they might be expected to be more risk adverse. In turn, as discussed in section 7 below, this may result in the law shifting in favour of the economically stronger party. This paper therefore contributes to the existing literature by considering how the particular institutional framework in the UK affects the dynamics of tax appeals and the case law that is thereby developed.

Whether certain categories of taxpayer enjoy an advantaged position in their dealings with HMRC (the UK tax authority) has become a major issue of public concern in recent years. This has prompted enquires by both the Public Accounts Committee³ (PAC) and the National Audit Office⁴ (NAO) into certain settlements made by HMRC, most prominently with Goldman Sachs and Vodafone. This paper contributes to this public policy debate by considering how features of the appeal process (such as the rules on cost or permission) and factors associated with the economic resources of the parties (such as legal representation) might lead to certain parties winning more cases and thereby shaping the law in their favour.

This paper is in 8 sections, the first of which is this introduction. The second section sets out the institutional structure to appeals from Special Commission-

¹D Robertson, ‘Appellate Courts’ in P Cane and HM Kritzer (eds), *The Oxford Handbook of Empirical Legal Research* (OUP 2010) 573.

²26 USC § 7430.

³House of Commons Committee of Public Accounts, *HM Revenue & Customs 2010-11 Accounts: Tax Disputes: Sixty-first report of Session 2010-12* (HC 1531, 2011).

⁴National Audit Office, *HMRC: Settling Large Tax Disputes* (HC:188 2012-3).

ers' decisions and how this changed over the relevant period. The third section discusses the theoretical background, using party capability theory as originally developed in a seminal article by Marc Galanter.⁵ This takes as a starting point Galanter's categorisation of litigation between the IRS and the taxpayer as being an example of litigation between a "one shotter" and "repeat player", which would normally advantage the IRS as a repeat player. It also discusses how being an RP might cause the tax authority to play for precedent, rather than just the tax in issue in that particular dispute. Galanter's model is then problematised by considering how this position of advantage might be evened out or even reversed, in the case of some taxpayers, through factors including a better bargaining position (due to being credibly able to threaten migration from the UK) or even through access to expensive legal representation. Section 4 builds on this using a rational choice approach to develop falsifiable hypotheses in relation to who appeals, who wins on appeal and how these may be affected by requirements for permission to appeal and by different legal representation. Section 5 introduces the dataset of onwards appeals from Special Commissioners' decisions since 1981, on which the hypotheses generated in Section 4 are tested in section 6. Section 7 considers whether the appeal system itself favours particular parties – either due to one type of party having a greater propensity to appeal or due to judges at one level being more/less disposed to the taxpayer than their brethren at other levels. The paper concludes by considering the merits of the present four-tier appeal structure, standardised across each of the constituent nations of the UK following the introduction of tax appeals into the new tribunal structure in 2009. It considers the functions of an appeal system and argues that such an extensive appeals structure serves no useful purpose, especially since so many cases are appealed to the higher levels.

2 Legal Background

The Special Commissioners were the tribunal which generally heard the most complex first-instance direct tax appeals, until 2009 when their jurisdiction was transferred to the unified tribunal structure created in the Tribunals Courts and Enforcement Act 2007. Despite the changes in the appeals system, the significant continuity of personnel and procedure means that this study remains relevant.⁶

In consequence of tax pervading most forms of human endeavour, the topics litigated before the Special Commissioners were extremely varied.⁷ Appeals from decisions of the Special Commissioners could only be made on issues of law, not of fact.⁸ English Appeals from decisions of the Special Commissioners

⁵M Galanter, 'Why the haves come out ahead: Speculations on the limits of legal change' (1974) 9 *Law & Soc'y Rev.* 95.

⁶M Blackwell, 'Variation in the Outcomes of Tax Appeals Between Special Commissioners: An Empirical Study' [2013] *BTR* 154, 168.

⁷M Blackwell, 'Variation in the Outcomes of Tax Appeals Between Special Commissioners: An Empirical Study' [2013] *BTR* 154, 154.

⁸TMA 1970, s.56A(1). Prior to the substitution of a new s.56A in September 1994 this

lay to the Chancery Division of the High Court (ChD).⁹ Although since 1985¹⁰ it was possible to have a “leap-frog” appeal, direct to the Court of Appeal of England & Wales (CA) from the Special Commissioners, this only occurred in respect of 4 (2% of all onwards appeals from the ChD) of the decisions of the Special Commissioners in the dataset. Scottish and Irish appeals from the decisions of the Special Commissioners were heard by, respectively, the Court of Session sitting as the Court of Exchequer¹¹ (CS) and the Court of Appeal in Northern Ireland¹² (CANI). Appeals from the CA, SC and CANI lay to the House of Lords or UK Supreme Court following the transfer of jurisdiction in 2009 (HL). It was also possible to have a direct “leap-frog” appeal from the ChD to HL,¹³ however this only occurred in respect of 4 of the decisions of the Special Commissioners in the dataset. A diagram of the various appeal paths, together with the numbers of appeals at each stage is shown in Figure 1.

The first appeal to the courts from decisions of the Special Commissioners was of right, requiring no permission. Since the implementation of the recommendations of the Bowman Report¹⁴ in the Access to Justice Act 1999,¹⁵ any second appeal from the ChD to the CA required the permission of the CA.¹⁶ Prior to this reform such a second appeal was available as of right.¹⁷ Appeal from the CA or CANI to the HL required either the permission of the court whose decision was being appealed against, or of the HL. Appeals from the CS to the HL did not require permission,¹⁸ the only requirement being that the appeal petition must be signed by two counsel who must also certify that the appeal is reasonable.¹⁹ The test for permission differed significantly between appeals to the CA and HL, the threshold for permission being far more difficult to satisfy for the HL.²⁰

With regard to *stare decisis*, decisions of the Special Commissioners did not create a binding precedent – so subsequent panels of Special Commissioners

was in s.56(1) TMA 1970.

⁹TMA 1970, s.56A(1).

¹⁰TMA 1970, s.56A inserted by FA 1994.

¹¹TMA 1970, s.56A(10).

¹²TMA 1970, s.58.

¹³AJA 1969, s.12.

¹⁴J Bowman et al, *Review of Court of Appeal (Civil Division): Report to the Lord Chancellor* (Lord Chancellor’s Department, September 1997).

¹⁵Access to Justice Act 1999, s.55. See also *Clark (Inspector of Taxes) v Perks and other applications* [2000] STC 1080.

¹⁶CPR r.52.13.

¹⁷RSC, Order 59.

¹⁸Court of Session Act 1988, s.40(1).

¹⁹House of Lords Standing Order IV; Practice Direction 1.9.

²⁰In the HL leave was granted to “petitions that raise an arguable point of law of general public importance which ought to be considered by the House at this time, bearing in mind that the matter will already have been the subject of judicial decision and reviewed on appeal”: Practice Directions Applying to Civil Appeals (House of Lords), Direction 4.8. In contrast, since the Access to Justice Act 1999, the CA “will not give permission unless it considers that – (a) the appeal would raise an important point of principle or practice; or (b) there is some other compelling reason for the Court of Appeal to hear it.” Access to Justice Act 1999 s.55(1); CPR, r.52.13(2).

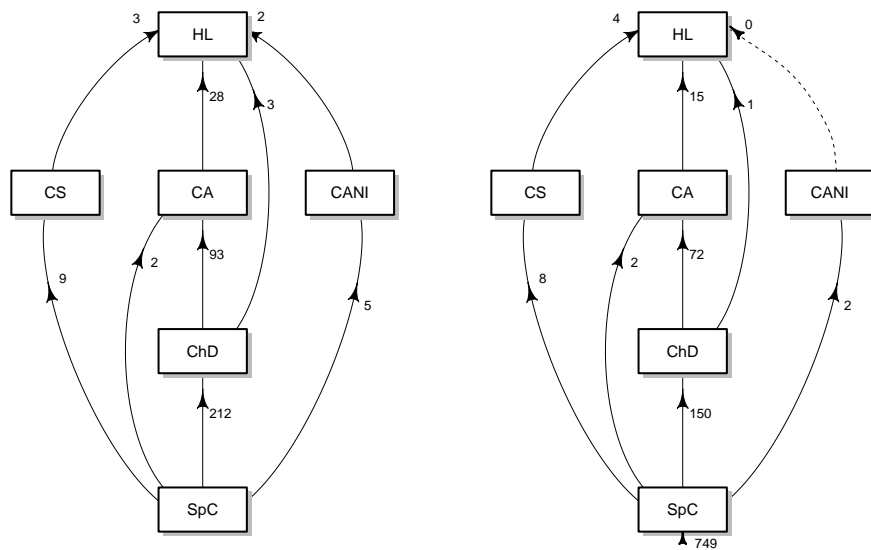


Figure 1: Diagrams of the appeal paths of appeals from decisions of the Special Commissioners. The diagram on the left shows all reported first and subsequent appeals reported since 1981 until 1995. The diagram on the right shows all appeals since 1995, when the decisions of the Special Commissioners themselves (rather than just the ones that were appealed) were reported. The reason for distinguishing between these two sets is discussed in the penultimate paragraph of section 5, below.

were free to depart from the reasoning of their brethren in earlier cases. Other courts were generally bound by their own precedents, as were the courts below them. The one exception to this was the HL. Although the HL had regarded itself as being free to depart from its own precedents since the 1966 Practice Statement,²¹ as a practical matter it rarely did so.

The general rule in English litigation is that the losing party not only has to pay their own legal fees (known as “costs”) but has also to pay the legal fees incurred by the successful party (known as “adverse costs”).²² However, although the costs of litigating a case before the Special Commissioners may be very high, the general rule was that adverse costs were not awarded. However adverse costs could be awarded where a party “acted wholly unreasonably in connection with the hearing in question”.²³ The frequency of such adverse costs awards was very low – in only 13 (1.7%) of the published decisions of the Special Commissioners is there a record of adverse costs being awarded.²⁴ In contrast, in appeals from the Special Commissioners the general rule was that adverse costs would be awarded.²⁵ It should be noted that a loss at the level of a second appeal and above would normally result in “costs below” being awarded – so if a party won in the House of Lords, having lost in the High Court and Court of Appeal, they would generally be entitled to be paid all their legal costs in the High Court, Court of Appeal and House of Lords (but still not before the Special Commissioners) and they would generally be entitled to a refund of any adverse costs they had paid. However, in some cases HMRC chose not to seek costs where they were successful in the High Court and above.²⁶

3 Theoretical background

3.1 Repeat players and the “haves”

As already noted in the introduction, in his seminal work²⁷ on the dynamics of litigation, Galanter characterised litigation between the IRS and the taxpayer as a typical example of litigation between a “repeat player” (RP) – the revenue authority – and a “one-shotter” (OS), the taxpayer.²⁸ Further, Galanter argued that when a RP litigated against an OS they had a structural advantage, which

²¹[1966] 3 All ER 77. See also discussion by J Tiley and S Oliver ‘Tax Law’ in L Blom-Cooper, B Dickson and G Drewry (Eds), *The Judicial House of Lords: 1876-2009* (OUP, 2009) 731.

²²CPR r.44.3(2).

²³Special Commissioners (Jurisdiction and Procedure) Regulations 1994 (SI 1994/1811), reg. 21(1).

²⁴M Blackwell, ‘Variation in the Outcomes of Tax Appeals Between Special Commissioners: An Empirical Study’ [2013] BTR 154, 157.

²⁵e.g. CPR r.44.3(2)(a) in respect of the ChD and CA.

²⁶Tax Law Review Committee, *The Tax Appeals System* (IFS, 1996) [2.32]

²⁷M Galanter, ‘Why the haves come out ahead: Speculations on the limits of legal change’ (1974) 9 Law & Soc’y Rev. 95.

²⁸M Galanter, ‘Why the haves come out ahead: Speculations on the limits of legal change’ (1974) 9 Law & Soc’y Rev. 95, 107.

often augmented other advantages that they enjoyed.²⁹ Although Galanter was considering federal tax litigation in the USA, this distinction between OS and RP clearly provides a useful analytical framework for considering revenue litigation more broadly. Indeed, it has been used as such by the Tax Law Review Committee.³⁰

Galanter's characterisation of HMRC as an RP would seem uncontroversial. Whilst Galanter characterises the taxpayer as an OS, the extent to which this is the case is likely to vary between disputes. An example of a RP v OS dispute might, for example, involve the chargeable gain from an individual selling a business on retirement or an inheritance tax dispute with an executor as a party. Even here the tax payer might still not be an OS, for example the executor might be a professional executor who therefore regularly administers estates and might have several on going disputes with HMRC.

At the other extreme are disputes between HMRC and large corporations such as FTSE100 companies, which can be characterised as an RP v RP dispute. For such companies there is likely to be an on-going relationship with HMRC, as complex tax issues, and so the potential for disputes, are likely to arise on an on-going basis. Whilst individual taxpayers and small businesses will have an on-going relationship with HMRC, the potential for complex tax affairs causing potential tax disputes is likely to be far higher for FTSE100 companies. This is shown in the NAO report where, based on the findings of Sir Andrew Park's review of five settlements, which commented:

The way that tax law applies to the complex facts in these cases is far from clear-cut. . . This contrasts with the simpler tax affairs of small businesses or individuals where the law, and how it applies to the case, are usually clearer.³¹

Galanter speculated that being a repeat player gave litigants an advantage for a number of reasons. These include specialised expertise, economies of scale, bargaining credibility and the ability to structure transactions.³² Indeed, this view was echoed by the Tax Law Review Committee, who also noted that being a repeat player gave the Revenue the ability to choose to litigate the case that they were most likely to win, when there were several potential disputes in relation to an issue.³³

Galanter theorised that one consequence of being an RP is that they might "play for the rules" in addition to (and sometimes in preference to) the outcome of particular disputes.³⁴ Such behaviour, which strategically seeks to set

²⁹M Galanter, 'Why the haves come out ahead: Speculations on the limits of legal change' (1974) 9 *Law & Soc'y Rev.* 95, 103.

³⁰Tax Law Review Committee, *The Tax Appeals System* (IFS, 1996) 11.

³¹National Audit Office, *HMRC: Settling Large Tax Disputes* (HC:188 2012-3) [1.18] see similar comment also at [2.7].

³²M Galanter, 'Why the haves come out ahead: Speculations on the limits of legal change' (1974) 9 *Law & Soc'y Rev.* 95, 125.

³³Tax Law Review Committee, *The Tax Appeals System* (IFS, 1996) [2.24-2.33].

³⁴M Galanter, 'Why the haves come out ahead: Speculations on the limits of legal change' (1974) 9 *Law & Soc'y Rev.* 95, 100.

precedents, is likely to be so for any revenue authority, who might have several disputes engaging the same set of rules, in addition to future revenues being contingent on the rules in dispute. In contrast playing for the rules is less likely to be important for the taxpayer, even those who are RPs. This is because their dispute with HMRC may concern a one-off transaction, or they may be able to structure future transactions to avoid the rule in question.

Galanter did not argue that RPs were synonymous with the “haves” but rather that there was:

a position of advantage in the configuration of contending parties and indicate how those with other advantages tend to occupy this position of advantage and to have their other advantages reinforced and augmented thereby. This position of advantage is one of the ways in which a legal system formally neutral as between haves and have-nots may perpetuate and augment the advantages of the former.³⁵

Clearly taxpayers (and especially taxpayers whose affairs are complex enough to create the possibility of a dispute with HMRC) are not “have-nots” in the sense of being economically disadvantaged in the same way as one might expect asylum seekers or benefits claimants to be. However, with regards to relative resources of time, experience and funds to conduct tax litigation they might be considered as “have-nots” in contrast to HMRC. But the repeat interactions between large businesses and HMRC, together with the size of their contribution to the UK exchequer and their perceived comparative ability to remove their taxable presence from the UK, might be thought to give them a stronger bargaining position against HMRC than small businesses and individuals. The potential impact of these businesses leaving the UK on the exchequer is illustrated by how:

In 2006-07, large businesses paid £23.8 billion in Corporation Tax, representing 54 per cent of the £44.3 billion Corporation Tax raised from all 1.8 million incorporated businesses in the United Kingdom.³⁶

Further, even within these 700 large business the incidence of corporation tax is heavily skewed, with 50 of them contributing 67 per cent of the total Corporation Tax raised from large businesses (and so 36 per cent of total Corporation Tax) in 2005-06.³⁷ Also, large businesses might be thought to be at an advantage (compared with small businesses and individuals) in that they have their in-house legal departments, which will mitigate the emotional and time costs of conducting litigation, which might be experienced by other taxpayers.

³⁵M Galanter, ‘Why the haves come out ahead: Speculations on the limits of legal change’ (1974) 9 Law & Soc’y Rev. 95, 103-3.

³⁶National Audit Office, *HMRC: Management of large business Corporation Tax* (HC:614 2006-7) [4].

³⁷National Audit Office, *HMRC: Management of large business Corporation Tax* (HC:614 2006-7) [1.12].

The common perception of a stronger bargaining position of large businesses was also demonstrated recently in the evidence before the PAC. Dave Hartnett (Permanent Secretary for Tax, HMRC) repeatedly stressed the desire to “make the relationship work”³⁸ between HMRC and Goldman Sachs. The MPs on the PAC contrasted this to the position of small businesses that would be “hounded and pursued for interest payments”,³⁹ whilst Goldman Sachs were not charged interest on unpaid tax when it could have legally been claimed. Similarly, the MPs contrasted Vodafone being given five years to pay tax due whilst small businesses were not given time to pay.⁴⁰

Whilst the foregoing somewhat anecdotal evidence does suggest that large corporates might enjoy favourable treatment, it should be noted that Sir Andrew Park’s report on five large tax settlements concluded that they were all reasonable and indeed one was “relatively advantageous” to HMRC.⁴¹ Perhaps, however, the robustness of Sir Andrew Park’s conclusion should be taken with some caution, since the disputes he considered often concerned highly factual issues and at one point the NAO report states that “Given the scope of his review, Sir Andrew Park could not consider all the extensive evidence prepared for the hearing.”⁴²

In summary, it would generally seem that HMRC’s position as an RP would generally give it an advantage in litigation against taxpayers and would also result in it often playing for the rules rather than just the tax in issue in that particular dispute. Further, it would seem that HMRC’s advantaged position might be reduced or reversed in its dealings with large companies, due to such companies themselves being RPs or due to the size of that company’s contribution to the UK tax base giving them a strong bargaining position.

3.2 Legal representation

With regard to legal representation, Galanter noted that the existence (and use of) a specialist bar might help the OS player overcome some of the gap in experience.⁴³ Galanter argued that lawyers tended to specialise in representing either OS or RP. Further, those that represented OS tended to “have some distinctive features”, including that:

they tend to make up the lower echelons of the legal profession. Compared to the lawyers who provide services to RPs, lawyers in these specialties tend to be drawn from lower socioeconomic origins, to have attended local, proprietary or part-time law schools, to

³⁸e.g. House of Commons Committee of Public Accounts, *HM Revenue & Customs 2010-11 Accounts: Tax Disputes: Sixty-first report of Session 2010-12* (HC 1531, 2011) Q38 Ev 4.

³⁹House of Commons Committee of Public Accounts, *HM Revenue & Customs 2010-11 Accounts: Tax Disputes: Sixty-first report of Session 2010-12* (HC 1531, 2011) Q46 Ev 5.

⁴⁰House of Commons Committee of Public Accounts, *HM Revenue & Customs 2010-11 Accounts: Tax Disputes: Sixty-first report of Session 2010-12* (HC 1531, 2011) Q724 Ev 62.

⁴¹National Audit Office, *HMRC: Settling Large Tax Disputes* (HC:188 2012-3) 18.

⁴²National Audit Office, *HMRC: Settling Large Tax Disputes* (HC:188 2012-3) 32.

⁴³M Galanter, ‘Why the haves come out ahead: Speculations on the limits of legal change’ (1974) 9 *Law & Soc’y Rev.* 95, 118.

practice alone rather than in large firms, and to possess low prestige within the profession.⁴⁴

and that:

the episodic and isolated nature of the relationship with particular OS clients tends to elicit a stereotyped and uncreative brand of legal services.⁴⁵

In UK tax cases it would be expected that this specialisation occurs to some degree, but it is highly questionable whether lawyers representing the taxpayer possess the distinctive features that Galanter outlines.

At the level of the Special Commissioners it was possible for litigation to be conducted (and indeed common for it to be) by professions other than solicitors, such as accountants. But for appeals from Special Commissioner's decisions it was not possible for such other professionals to do so.⁴⁶ However, it was possible to have litigants in person both at the Special Commissioners and for subsequent appeals.

With regard to the conduct of UK tax litigation by solicitors, where solicitors are involved HMRC are always represented by their in-house Solicitor's Office (part of Government Legal Services). Therefore these lawyers are themselves RPs since their practice exclusively consists of tax litigation, so they might also themselves have the advantage of specialist expertise which is a feature of parties that are repeat players. If the taxpayer retains solicitors they will always be from private practice. The extent to which these solicitors are RPs will depend on which firm is instructed. Some firms have specialist tax litigation teams, whilst in others tax litigation will be conducted by others who are either general litigators or who have a predominantly tax advisory role. Accordingly there is a perfect separation between solicitors who represent HMRC and those that represent the taxpayer.

With barristers there is more of an overlap. The position differs somewhat between barristers who are "juniors"⁴⁷ and for QCs. Generally, junior barristers representing HMRC are drawn exclusively from the members of the Attorney General's panels. Membership of the panels is by way of open completion for a fixed term of five years,⁴⁸ but only junior barristers are eligible for membership. Panel members may represent HMRC but, if available, they may also act for the taxpayer (clearly on different cases to those they act for HMRC). Non-panel juniors can generally only represent the taxpayer. So among junior barristers there is not the polarisation that is suggested in Galanter's model.

⁴⁴M Galanter, 'Why the haves come out ahead: Speculations on the limits of legal change' (1974) 9 Law & Soc'y Rev. 95, 116.

⁴⁵M Galanter, 'Why the haves come out ahead: Speculations on the limits of legal change' (1974) 9 Law & Soc'y Rev. 95, 117.

⁴⁶Legal Services Act 2007 s.12(1)(b), s13 and Sch.2(4).

⁴⁷a term used for barristers that are not (yet) awarded the rank of Queen's Counsel, the latter sometimes also being referred to as "Silks"

⁴⁸http://www.tsol.gov.uk/PanelCounsel/appointments_to_panel.htm (Accessed 24 August 2012).

There is no standing panel of Crown silks, with their services being retained on an *ad hoc* basis as required. Under the Code of Conduct of the English Bar barristers, including QCs, are bound by the “cab rank rule”⁴⁹ and so must, *inter alia*, accept any instructions in “any field in which he professes to practise in relation to work appropriate to his experience and seniority and irrespective of whether his client is paying privately or is publicly funded”.⁵⁰ However, there appears a reticence by some QCs to appear for the Crown. This was shown in Dave Hartnett’s evidence before the PAC where, as Permanent Secretary for Tax at HMRC, he was is questioned on whether he had lunch with David Goldberg (a QC specialising in tax law):

Q177 Mr Bacon: It says here, “Was David Goldberg, QC there?” That is my first question. Have you had lunch with Mr Goldberg?

Dave Hartnett: Yes. I had lunch with Mr Goldberg perhaps once, twice or three times in the last five years.

Q178 Mr Bacon: Three times in the last five years.

Dave Hartnett: He acts for us also.

Q179 Mr Bacon: Does he—because he is a leading tax silk?

Dave Hartnett: Yes. It took a long time, but we managed to persuade him to work for us. . . . Not all tax silks work for us.⁵¹

Given the cab rank rule, it is somewhat odd that silks should need to be persuaded to appear for the Crown. The answer to this conundrum would seem to be that they feel they can refuse instructions from the Crown under the exception to the cab rank rule that the remuneration offered by the Crown is not a “proper professional fee”.⁵² Indeed, the author is aware of one QC who refers to his appearances for HMRC as his *pro bono* work, as he regards such fees as small compared to what he can charge the taxpayer. Indeed, it would appear that the reticence to appear for the Crown is purely financial and not ideological. One tax silk told the author how members of his chambers enjoy receiving instructions tied in white tape.⁵³

This price differential also applies to junior barristers, who can charge a higher rate to taxpayers than the panel rate they are allowed to charge the Crown. Such price differential would seem a potential example of market failure. If a tax payer considers that the advantage given to them by the additional expenditure on legal fees would be off-set by an anticipated reduction in their tax burden, it is arguably surprising that HMRC do not consider that similar expenditure would be off-set by an increased tax yield – especially since these

⁴⁹ *Code of Conduct* (Bar Standards Board, 2012) para 601 et. seq.

⁵⁰ *Code of Conduct* (Bar Standards Board, 2012) para 602.

⁵¹ House of Commons Committee of Public Accounts, *HM Revenue & Customs 2010-11 Accounts: Tax Disputes: Sixty-first report of Session 2010-12* (HC 1531, 2011) Ev 15.

⁵² *Code of Conduct* (Bar Standards Board, 2012) para 604.

⁵³ Instructions from the Crown were historically tied up in white tape, compared to the “red tape” (which is more accurately described as pink ribbon) more generally used to tie up instructions to counsel.

costs would often be externalised (as adverse costs in onwards appeals from the Special Commissioners) to the taxpayer if they were successful. Indeed, such expenditure could be thought more justifiable for HMRC for two reasons. First, as an RP, a victory for HMRC would be likely to set a direct precedent in other identical cases so the total financial gain would be a multiple of the actual award in that case. Second, Alan Paterson’s research into the role of advocacy in the House of Lords suggests (at least there) that advocacy rarely affects the outcome of a case, but only the reasoning that the judges use to arrive at the outcome.⁵⁴ As discussed above, as an RP, HMRC should care not just for the outcome but the reasoning behind it (“play for the rules”) as these may set a precedent for cases which, while not identical, raise similar legal issues. Conversely, the taxpayer would be more interested in the outcome rather than the reasoning behind the outcome. If advocacy affects the reasoning rather than the outcome it would therefore seem to follow that it would be more valuable to HMRC than the taxpayer and that they should be willing to pay higher fees for better advocacy.

Perhaps the answer to this conundrum is that the higher fees tend to be charged by barristers who are specialists in tax law. Conversely, often the counsel instructed by HMRC have a more general practice. This adds value for taxpayers since they are themselves not experts in tax law (unlike HMRC). Such an argument is developed in Hypothesis 6, below. It has also been suggested to the author that (historically) the Revenue were reluctant to instruct barristers in sets specialising exclusively in tax law, due to a perceived fear of them being “leaky”, ie there was a perceived risk that information might be passed to taxpayers that HMRC wished to keep confidential. Historically, another reason for few junior specialist tax counsel being instructed by the Revenue might have been that to get on the Attorney General’s panel it was to have contentious experience in more than one area of law, but many tax counsel’s experience was limited to tax litigation (or sometimes even non-contentious tax advice).

By way of illustration of this client specialisation, in first appeals from pre-1995 Special Commissioners’ decisions, the taxpayers’ lead counsel was from a set exclusively specialising in tax law⁵⁵ on 58 per cent of such appeals, compared to 7 per cent of such appeals for the Revenue. The figures for post-1995 appeals are respectively 71 per cent and 11 per cent.

In summary, the profession is perfectly segregated with regards to the solicitors who conduct tax litigation between those who work for HMRC and those retained by taxpayers. Such segregation is less existent among barristers. Further, whilst Galanter speculated that the layers representing OS were inferior this does not seem to apply to tax litigation in the UK – indeed it appears that there are some barristers that are too expensive for HMRC. At one level this is perplexing, since it is anticipated that HMRC play for the rules and would be

⁵⁴Alan Paterson, *Lawyers and the Public Good: Democracy in Action? (The Hamlyn Lectures)* (CUP, 2012) 49. Citing Jonathan Sumption QC, as he then was.

⁵⁵These are the sets that are listed as “tax chambers” as opposed to “chambers with tax specialists” on the Revenue Bar Association web-site: <http://www.revenue-bar.org/chambers.asp> (Accessed 1 November 2012).

able to recover the costs of successful litigation. A possible explanation is that the expensive lawyers are tax specialists who add value for the taxpayer, but would not add value for HMRC, due to their internal tax expertise.

4 Hypotheses

This section develops some of the ideas discussed in the previous section into falsifiable hypotheses. These hypotheses are then tested in section 6 of the paper.

These hypotheses fall into three groups. Hypotheses 1 and 2 consider whether an appeal is made; hypotheses 3 and 4 concern the outcome when an appeal is made; and hypotheses 5 and 6 concern factors (requirements for permission and the nature of legal representation) that can moderate the effects of hypothesis 3 and 4. Examining these dynamics allows us to understand the process of the formation of precedent in tax cases and whether certain taxpayers are at an advantage, as discussed in the introduction.

Hypothesis 1: HMRC will be more willing to appeal losses against OSs (such as individuals and executors) than RP (PLCs and foreign companies). Some anecdotal evidence discussed in section 3 suggests that large corporate taxpayers enjoy favored treatment from HMRC, although as noted this conflicts with the perhaps more considered view of Sir Andrew Park. Assuming this to be the case, it might be expected that HMRC might be less willing to challenge losses against such taxpayers in order to keep their good will (and taxable presence in the UK). Admittedly, the nature of the cases between these different taxpayers is likely to be very different, with vastly more tax in issue in the case of large corporates. This may well counterbalance the hypothesised result.

Hypothesis 2: RP (such as PLCs and foreign companies) will be more willing to appeal losses against the revenue authority than should OS (such as individuals and executors). Large corporates will have more resources. They will also have the ability to more easily externalise all aspects of the litigation, so whether to pursue it becomes a purely financial question, rather than involving the undoubted aspects of stress that it might cause an individual taxpayer. Further, with such large corporates, the sums in dispute are likely to be large relative to the cost/adverse cost implications of continuing the litigation. However, the overall amount in dispute may be a smaller relative to their net wealth than for other taxpayers – so loss aversion is less likely to have the consequence of deterring them from litigation. Accordingly, once such a taxpayer has decided to commence litigation, they are less likely than other taxpayers to stop, until they have exhausted possible appeals.

Hypothesis 3: The majority of appeals by the Crown will be allowed. Since the Crown should generally play for the rules, it is not expected that they would choose to appeal cases that they would be likely to lose. This is especially so for first appeals from the decisions of the Special Commissioners, since (as discussed above) these decisions do not create a binding precedent – but an appeal from those decisions would. Creating a binding adverse precedent would clearly be

disadvantageous for HMRC, since it would influence the overall amount of tax collected, not just the tax in that particular case. This reasoning also applies to subsequent appeals, as HMRC should not want to appeal these cases if they thought they were likely to lose as it would create a precedent at a higher level that it would be difficult to overrule. Rather they would wish to consider appealing a similar case that they were likely to win – possibly due to different evidence – or to seek a legislative change. Accordingly, for any given case that HMRC chooses to appeal we would expect the anticipated prospects of success to be a value greater than 50 per cent, it would therefore follow that the majority of appeals by the Crown would be allowed (although this reasoning does not indicate how much more than 50 per cent of appeals would be allowed).

Hypothesis 4: The majority of appeals by the taxpayer will be dismissed, especially at the level of the Special Commissioners. When the taxpayer considers that their prospects of success exceeded 50 per cent it will normally be rational for the taxpayer to appeal. However, it may also be rational when prospects of success are less than 50 per cent, provided that the expected monetary gain is high.

For example, assume a taxpayers' prospects of success are 40 per cent and the tax in dispute is £500,000. If the costs of the appeal were £30,000 with the possibility, say, of £20,000 in adverse costs the expected financial gain from appealing is £170,000.⁵⁶ Clearly, this is very much a simplification – for example it ignores the possibility of a second appeal by the Crown, ignores the stress and lost opportunity costs due to the time consumed by the litigation and presumes risk neutrality. Whilst these additional elements are clearly significant, nonetheless, even allowing for such arithmetical complications in calculating overall utility, the logic suggests that for the taxpayer, who plays for the outcome and not the rules, it may be rational to litigate cases where the prospect of success is less than 50 per cent.

Applying this logic, appeals by taxpayers where there is a low prospect of success should be especially prevalent at the level of the Special Commissioners, since adverse costs are generally not awarded and so even a low prospect of success may result in there being an expected financial gain from appealing. Indeed, aside from the purely economic argument, especially in the case of individual tax payers, they might also be motivated to appeal by an emotional desire to vindicate a perceived right – even when their case is objectively weak. Such sentiments are shown in the reported exchanges between judge and taxpayer after the *ex tempore* judgment in *Briggenshaw v Crabb (H M Inspector of Taxes)*.⁵⁷

Singleton, J.: Your appeal must be dismissed. I will pass you back your documents. If I might add a word to you, it is that I hope you will not trouble your head further with tax matters, because you seem to have spent a lot of time in going through these various Acts, and if you go on spending your time on Finance Acts and the like,

⁵⁶ £170,000 = £500,000*0.4 - [20,000 + 30,000]*0.6.

⁵⁷(1948) 30 TC 331.

it will drive you silly.

Mrs. Briggenshaw: I will appeal to the higher Court.

Singleton, J.: I cannot stop you, if I would. The advice which I gave you was for your own good, I thought. That is all.

It would, generally, follow that most appeals by the taxpayer should be refused. This does not quite follow as a matter of logic, but requires certain other conditions⁵⁸ which, viewed realistically, are likely to be satisfied.

Corollary: the majority of appeals will be decided in favour of the Crown. This follows from Hypotheses 3 and 4.

Hypothesis 5: Where permission to appeal is required, and such permission is not a mere formality, the magnitude of the effects predicted by Hypotheses 3-4 will be reduced. A requirement for permission to appeal should be expected to disproportionately restrict appeals where the prospects of success are low.⁵⁹ Accordingly, such a requirement should reduce the numbers of unsuccessful appeals by the taxpayer. It should impact less upon appeals from the revenue authority, since (as predicted by Hypothesis 3) the Crown should be less likely to appeal where the prospects of success are low.

Hypothesis 6: The effect of legal representation on outcome will be more pronounced for the taxpayer than for the revenue authority. Whilst the revenue authority clearly have many internal experts on tax law, the taxpayer will generally be more reliant on external professional advisors for advice in relation to any tax litigation.

The taxpayer's prospects of success may be altered by the identity of their legal representative in a number of ways. Most obviously perhaps, by the representative's ability to convincingly present the taxpayer's case in written pleadings and oral argument. They will also rely on their representative's advice on prospects of success when deciding whether to settle or litigate – and this is likely to depend on the cautiousness or bullishness of the lawyer. As the revenue authority will be experts themselves, they will be less reliant on external counsel. This would explain why they do not generally consider the higher fees of certain counsel worth paying. It would follow that the identity of HMRC's lead counsel would be associated with less variation in the outcome of appeals than the identity of the taxpayer's counsel.

5 Dataset

The hypotheses in section 4 are tested against a dataset, assembled by the author, which contains all the appeals to the Special Commissioners since they were first reported in 1995, together with all statutory domestic appeals from

⁵⁸Other requirements would include that the judges in the court being appealed to are not more/less disposed, other things being equal, to one side than the court being appealed against.

⁵⁹J Bowman et al, *Review of Court of Appeal (Civil Division): Report to the Lord Chancellor* (Lord Chancellor's Department, September 1997) 32.

these decisions. The dataset also contains all statutory domestic appeals from the decisions of the Special Commissioners reported in *Simon's Tax Cases* where the first such appeal was reported in 1981 or later. 1981 is chosen as the starting point, as it is the year in which *W T Ramsay Ltd v IRC*,⁶⁰ which was then perceived to have introduced a judicial anti-avoidance rule, was heard by the House of Lords, so that might be thought of as the start of a new era in tax law. A start date of 1981 is also close to the time when the Special Commissioners were reformed by FA 1984⁶¹ requiring them to be legally qualified and appointed by the Lord Chancellor, rather than the Treasury as previously. Since this change was motivated by a desire to strengthen the independence of the Special Commissioners,⁶² this too might be regarded as the start of a distinct period. Also, including these initial 15 years also allows the dataset to be sufficiently large to make robust inferences concerning the identity of the legal representatives, to test Hypothesis 6.

Due to the Special Commissioners decisions being first reported in 1995, in the following analysis the data is divided between that concerning pre- and post-1995 Special Commissioners decisions. This avoids any inferential errors from comparing the pre-1995 decisions that are public (because they were appealed) to all post-1995 decisions – clearly decisions that are appealed are not likely to be representative of all decisions. However, such logic does not preclude a conflation of pre- and post- 1995 appeals from the Special Commissioners (not including the decisions appealed from), as is done when testing Hypothesis 6 below. Also, this division roughly coincides with the introduction of self-assessment in the 1996/7 tax year, which did away with appeals against estimated assessments,⁶³ which previously comprised a significant part of the commissioners' workload, although few were the subject of onward appeals.

The variables in the dataset include the court; the date of the decision; the sub-area of tax law (taken from the head-note at the start of the Special Commissioner's decision); who the appeal was by; whether the appeal was allowed or dismissed; the identity of the judges; and the identity of the advocates and their call dates. The dataset includes a reference for each case, which is identical for the same case at different levels of appeal, to allow the progression of cases through the appeal system to be tracked.

6 Results

Hypothesis 1: HMRC should be more willing to appeal losses against OSs (such as individuals and executors) than RP (such as PLCs and foreign companies). Table 1 shows the number and proportion of decisions lost by HMRC where that loss is appealed by HMRC, broken down by taxpayer entity types. It is

⁶⁰[1981] STC 174.

⁶¹FA 1984, Sch.22, replacing TMA 1970 s.4.

⁶²*The annual report of the Council on Tribunals for the period 1st August 1983 to 31st July 1984* (1984/85 HC 42) 20.

⁶³C Whitehouse, *Revenue Law: Principles and Practice* (18th edn Butterworths Tolly 2000) 27.

Taxpayer entity	HMRC loss not appealed	HMRC loss appealed	Total
Individual	104 (81%)	25 (19%)	129
Executor	23 (77%)	7 (23%)	30
Limited company	42 (68%)	20 (32%)	62
Other	32 (68%)	15 (32%)	47
Plc	30 (68%)	14 (32%)	44
Foreign company	8 (47%)	9 (53%)	17
Total	239 (73%)	90 (27%)	329

Table 1: Table showing the number and proportion of cases in the dataset lost by HMRC where HMRC appeals the decision, by type of taxpayer entity.

Taxpayer entity	Not appealed by taxpayer	Appealed by taxpayer	Total
Executor	42 (86%)	7 (14%)	49
Individual	272 (84%)	53 (16%)	325
Other	67 (80%)	17 (20%)	84
Limited company	100 (75%)	33 (25%)	133
Foreign company	8 (57%)	6 (43%)	14
Plc	29 (52%)	27 (48%)	56
Total	518 (78%)	143 (22%)	661

Table 2: Table showing the number and proportion of cases in the dataset lost by the taxpayer where they appeal the decision, by type of taxpayer entity.

apparent from that table that in fact losses against individuals and executors are appealed less than losses against other entities, the reverse of what the hypothesis would expect (so $P > 0.5$). The data shows that HMRC appeals losses to individuals and executors on 20% of occasions, compared to losses to PLCs and foreign companies on 38% of occasions. Thus the data provides no support for Hypothesis 1.

Hypothesis 2: RP (such as PLCs and foreign companies) should be more willing to appeal losses against the revenue authority than should OS (such as individuals and executors). Table 2 shows the number and proportion of decisions lost by the taxpayer where that loss is appealed by the taxpayer, broken down by taxpayer entity types. It is apparent that individuals and executors are less likely to appeal (combined they appeal 16% of their losses) than large corporate entities such as foreign companies and PLCs (which combined they appeal 47% of their losses). Such difference in proportions is statistically significant at all conventional levels of significance ($P < 0.0001$). Accordingly, there is statistical support for this hypothesis.

Hypothesis 3: The majority of appeals by the Crown should be allowed. In the entire dataset 52 per cent of appeals by the Crown are allowed, the statistics are (respectively) 48 per cent and 59 per cent for the pre- and post-1995 parts of the dataset. Whilst overall the majority of appeals by the Crown are allowed, it is only when looking at the period since 1995 in isolation when there is statistical

support for this hypothesis ($P < 0.05$). A detailed breakdown, by court, of the outcomes of appeals by the Crown is set out in tables 5 and 6 in the statistical appendix.

The lack of statistical support for the hypothesis might be thought to indicate that HMRC are less strategic than might be expected, and do not greatly prioritise establishing favorable precedents over the tax in issue in individual cases. Some further, tentative, support for this is shown by the breakdown by courts in tables 5 and 6. If HMRC were prioritizing playing for the rules, it might be expected that their win rate in cases they choose to fight (ie the ones they appeal) in the HL would be greater than in the ChD – as the consequence of an adverse precedent in the HL would be much worse for them. But in fact their win rate is actually higher in the ChD in such cases.

Hypothesis 4: The majority of appeals by the taxpayer should be dismissed, especially at the level of the Special Commissioners. In the entire dataset 32 per cent of appeals by the taxpayer are allowed, the statistics are (respectively) 28 per cent and 32 per cent for the pre- and post-1995 parts of the dataset. It should be noted that the heavy weighting of the total average towards the post-1995 figure is due to there being far more appeals by the taxpayer in the post-1995 appeals, due to the inclusion in there of almost all the appeals to the Special Commissions. The post-1995 proportion is not substantively different from the taxpayers' success rate (of 33 per cent) in the first-instance decisions of the Special Commissioners in the post-1995 period.⁶⁴

A detailed breakdown, by court, of the outcomes of appeals by the taxpayer is set out in tables 7 and 8 in the statistical appendix. In respect of both periods it is clear that the majority of appeals by the taxpayer are refused. For both periods this is statistically significant at all conventional levels of significance, ie it is possible to be confident at all conventional levels of statistical significance that it is not attributable to chance that less than 50% of all appeals by the taxpayer are successful.

Corollary: the majority of appeals should be decided in favour of the Crown. Overall 65 per cent of all decisions in the dataset are decided in favour of Crown. The statistics are (respectively) 60 per cent and 67 per cent for the pre- and post-1995 parts of the dataset. Thus in respect of both periods it is clear that the majority of appeals are determined in favour of the Crown. This is statistically significant at all conventional levels of significance.

Hypothesis 5: Where permission to appeal is required, and such permission is not a mere formality, the magnitude of the effects predicted by Hypothesis 4-3 should be reduced, but not eliminated. As noted previously, a requirement for permission from the CA for second appeals to the CA was introduced with effect from September 1999. Prior to this such appeals were available as of right. Figures for the success rates of applications for such permission are not available, however comparing the rates of appeal from the ChD to the CA in the period before and after the introduction of this requirement shows that the number of

⁶⁴M Blackwell, 'Variation in the Outcomes of Tax Appeals Between Special Commissioners: An Empirical Study' [2013] BTR 154, 160.

Application by:	Permission allowed	Permission refused	Total
HMRC	9 (47%)	10 (53%)	19
Taxpayer	7 (21%)	27 (79%)	34
	16 (30%)	37 (70%)	53

Table 3: Results of applications for permission to appeal to HL/UKSC

such appeals has increased. Of the appeals to the ChD reported in the period 1981 to 1999, 43 per cent were appealed to the CA. The comparable figure for 2000 to 2010 is 51 per cent. A detailed breakdown, by year, of appeals from the ChD to the CA is shown in table 9 in the statistical appendix. Accordingly, it does not appear that the requirement for permission has much effect in limiting appeals, although it is conceivable that the introduction of the permission requirement might account for the temporary drop in 2002 and 2003.

It contrast, it appears that requirement for permission to appeal to the HL has a very considerable effect at reducing appeals. The author has assembled a data on such applications from 1996 onwards. The data for this was assembled, in respect to petitions to appeal to the House of Lords, from the Appeal Committee Memoranda⁶⁵ available for inspection in the Parliamentary Archives. In respect of appeals to the Supreme Court of the United Kingdom the data was assembled from the on-line results of permission applications on the Supreme Court website.⁶⁶ This data is summarised in Table 3. It is apparent from the table that most of these applications for permission are refused. It is also apparent that appeals by the taxpayer are refused at a greater rate. This anticipated difference is statistically significant ($P < 0.05$).

Since the requirement for permission to appeal to the CA does not appear, in practice, to restrict appeals it is unsurprising that since the introduction of the requirement for permission there is still a high proportion of unsuccessful appeals by taxpayers to the CA, although this proportion has diminished somewhat. 39 per cent of appeals by the taxpayer to the CA in the dataset reported in 2000 and subsequently were successful, compared to 22 per cent of such appeals in the dataset reported between 1981 and 1999. This difference in proportions is not statistically significant at the 5 per cent level of significance ($P = 0.06$).⁶⁷ However, due to the small sample size and the fairly low P value this might be thought indicative of there being a difference in the proportions.

As noted the requirement for permission to appeal to the HL does appear to restrict appeals by taxpayer. As hypothesised, this appears to reduce the number of appeals by taxpayers before the HL that are lost. Thus 64 per cent of appeals by the taxpayer to the House of Lords, where permission was required (i.e. excluding Scottish appeals) were allowed, compared to only 39 per cent

⁶⁵Parliamentary Archives, HL/PO/JU/1.

⁶⁶<http://www.supremecourt.gov.uk/news/permission-to-appeal.html> (accessed 7 September 2012)

⁶⁷In the earlier period 16/72 appeals by the taxpayer were successful. In the later period 14/36 appeals by the taxpayer were successful.

of appeals to the CA. Whilst not statistically significant at the 5 per cent level ($P=0.07$), again due to the small sample size and the fairly low P value, this might be thought indicative of there being a difference in the proportions.

Hypothesis 6: The effect of outcome on legal representation should be more pronounced for the taxpayer than for the revenue authority. This hypothesis was tested by using a form of regression analysis similar to that used for the construction of value-added school league tables,⁶⁸ but adapted to account for the outcome variable being discrete (win/lose) rather than a continuous score (like exam marks). The effect on the outcome of the decision of the identity of the lead counsel for HMRC and the lead counsel for the taxpayer was modelled controlling for the (log adjusted) word count of the judgment, whether the appeal was brought by the taxpayer, the area of law and the identity of the judge – or where there were several judges, the identity of the judge who gave the lead decision. The model and the technical process of model selection is discussed in part C of the statistical appendix. It should be noted that the model does not account for the experience of counsel, just their identities.

The parameter estimates of the final model are set out in table 10 in the statistical appendix. It is clearly apparent from comparing the parameter estimates the estimated effect of taxpayer representation is much greater than that for HMRC representation – the estimated variance for the taxpayer representation parameter being 0.334 and that for HMRC’s representation being 0.038. However, as these are on a logit scale it is less easy to interpret these effects.

To help interpret the estimated effect of different legal representation, Figure 2 shows the estimated probability of a pro-taxpayer decision for each lead counsel in the dataset, for what may be thought of as an average case. Each dot represents the predicted value for a representative.

From the figure it is immediately apparent that there is hardly any expected variation in outcome contingent on the identity of HMRC’s lead representative, controlling for the other variables. The expected probabilities of a pro-taxpayer decision range from 28.1 to 29.4 per cent.

In contrast there is far more expected variation contingent on the identity of the taxpayer’s representative, controlling for the other variables. The left most point, marked with a large x , is for the predicted probability of a successful appeal by the taxpayer representing themselves in such a case. As might be expected, the expected probability of success for such taxpayers (13%) is much lower than that for a taxpayer represented by any of the lawyers in the dataset.

Even omitting the *sui generis* case of litigants in person, the estimated range in predicted probabilities of a pro-taxpayer decision in such a typical case contingent on the lead advocate for the taxpayer is very wide – ranging between 20.2 per cent and 41.2 per cent. Looking at this full range clearly focuses on extremes, ignoring the bulk of lawyers that fall within these two predicted values. Accordingly, a better estimate of the variation is the inter-quartile range (the middle half) that varies between 27.2 and 31.3. Even this variation is rather

⁶⁸eg H Goldstein and DJ Spiegelhalter ‘League Tables and Their Limitations: Statistical Issues in Comparisons of Institutional Performance’ (1996) 159(3) *Journal of the Royal Statistical Society: Series A (Statistics in Society)* 385-443.

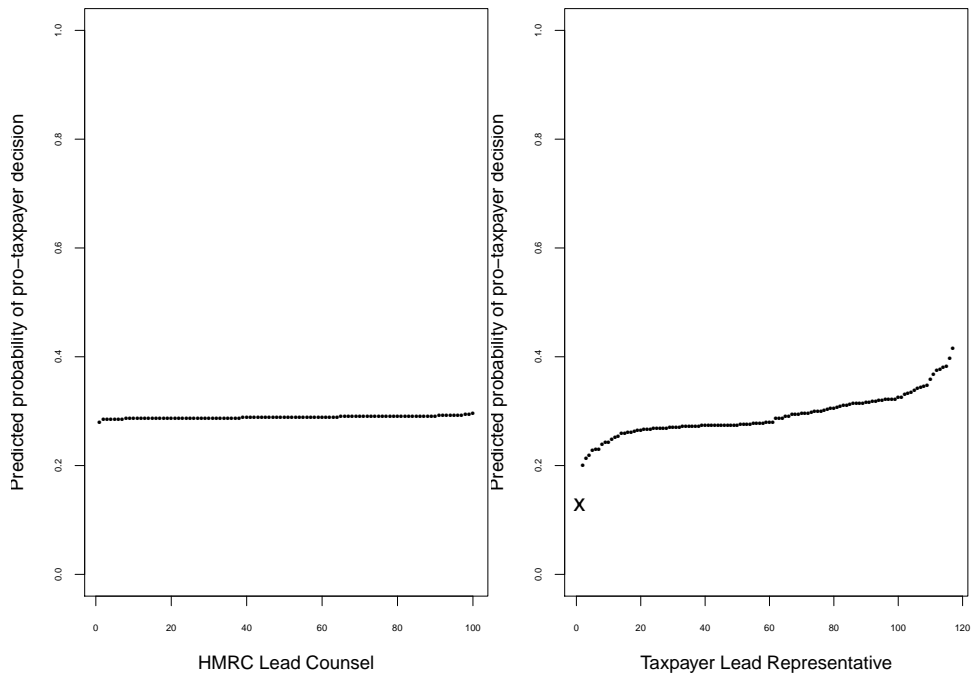


Figure 2: Estimated probabilities, for each lead counsel in the dataset, of a pro-taxpayer decision for an appeal by the taxpayer where all continuous variables are set to their mean values. The x represents the estimated probability for taxpayer litigants in person.

large, and clearly much larger than that associated with different representation of HMRC.

Another indication that effect of different legal representation on outcomes is more pronounced for the taxpayer than for the revenue authority is the DIC statistic that was partly used to select the variables to include in the model. The DIC statistic, discussed in more detail in part C of the statistical appendix, is a goodness of fit statistic – with lower values indicating a better fit. Table 11 contains the DIC statistics for models with each of the different possible combinations of judge, area of tax law, lead representation of HMRC and lead representation for the taxpayer, in each case controlling for the (log adjusted) word count of the judgment and whether the appeal was brought by the taxpayer. The table is ordered by size of DIC statistic. It is apparent that all the models that account for the lead representation of the taxpayer are better fits than any of the models that do not include this variable. In comparison, inclusion of the lead representative of HMRC generally only reduces the DIC statistic by a fairly trivial amount – and for some combinations of variables its inclusion slightly increases the DIC statistic. Accordingly, this is a further indication in support of Hypothesis 6.

It should be noted that due to the relatively small number of cases per advocate, there is a fair amount of uncertainty regarding the effect of any given advocate, but the far bigger variation in expected probabilities for the taxpayer still supports the foregoing analysis. The inclusion of years' call of the lead advocates in the model did not prove significant or improve the model fit. This would suggest that the variation in outcome attributable to the individual advocate is not associated with factors highly correlated to their experience. As previously noted, there are two possible explanations of effects of the identity of the advocate on the outcome – one being that the risk aversion/bullishness of the advocate influences the decision to litigate or settle, the other being that it is attributable to differences in the advocates' skills in presentation of the case. Whichever it is, the effect does not seem to apply to advocates appearing for the Crown – perhaps suggesting the effect is due to the first mechanism, since the effect of differences in advocacy might plausibly still be expected to be present even when advocates appear for HMRC, yet the specialist knowledge of HMRC would make them far less dependent on the views of counsel as to their prospects of success in deciding whether or not to appeal.

Synopsis: In summary, the majority of appeals are decided in favour of the Crown – however this is more attributable to the taxpayer appealing cases where they have low prospects of success (supporting Hypothesis 4) rather than the Crown being especially cautious as to which cases it appeals (Hypothesis 3 having limited support).

The increase in the success rate of appeals by the taxpayer to the CA since the introduction of the permission requirement is indicative that the permission requirement does tend to weed out some unmeritorious appeals, despite the proportion of HC cases having a second appeal (and hence third hearing) before the CA having increased over the period. However, as predicted, the effect of the permission requirement is far greater before the HL, where permission

(where required) is far more difficult to obtain than from the CA, resulting in a majority of appeals by the taxpayer to the HL being allowed.

It appears that the identity of the Crown’s counsel do not appear to effect the outcome of appeals, whilst the identity of the taxpayers’ does. It would seem that the most plausible explanation is that the associated difference in outcome is not attributable to the effect of advocacy, but rather it is due to differences in bullishness and risk aversion in counsels’ advice on the prospects of success – with the taxpayer being particularly vulnerable in this respect as, unlike the Revenue, they are unlikely to have the skills to make an accurate assessment for themselves.

Contrary to what would be expected if HMRC unduly favoured large taxpayers, HMRC are more likely to appeal losses against large corporates than against typically smaller taxpayers such as executors or individuals. In turn such large taxpayers are more likely to appeal losses against HMRC.

7 Are certain parties structurally disadvantaged by the appeals process?

This section considers two ways in which the appeals system might systematically favour parties. The first way is if one party had a greater propensity to appeal than their opponents. The other is if judges at one particular appeal level were more predisposed to the taxpayer than their brethren at other appeal levels.

Imagine we played a game where an unbiased coin was thrown and I kept it if it was heads and you did if it was tails. However, under the rules after the first throw either of us could demand it be re-thrown and we would be bound by the second throw. If I seldom asked for it to be re-thrown if I lost, but you often did if you lost, you would be likely to end up with more coins than me. This would be so even though the coin was unbiased. Similarly if the revenue or (certain types) of taxpayer had a greater propensity to appeal than their adversaries, then it would lead to more disputes being ultimately decided in favour of that taxpayer which would also result in a shift of the law in favour of that kind of party. The two situations have some important differences, but the basic principle is the same.

However, with regard to appeals from Special Commissioners’ decisions, these dynamics seem to off-set each other, so onward appeals neither particularly, in general, advantage HMRC or the taxpayer. Looking back to the last section a comparison of tables 1 and 2 suggests that the types of entities against which HMRC are most likely to appeal losses, are also the types of entities themselves which are likely to appeal their losses against HMRC.

The second possibility for structural bias would be if judges in general at a particular level of appeal more disposed (or otherwise) to the taxpayer. The author has often heard practitioners make such a claim,⁶⁹ although the claims of

⁶⁹For example, at the 2012 Oxford University Centre For Business Taxation Summer Con-

	Appeal levels after Special Commissioners			
	0	1	2	3
Executor	25 (51%)	21 (43%)	23 (47%)	23 (47%)
Individual	106 (33%)	97 (30%)	98 (30%)	97 (30%)
Other	31 (37%)	29 (35%)	30 (36%)	31 (37%)
Limited company	45 (34%)	41 (31%)	40 (30%)	41 (31%)
Foreign company	9 (64%)	7 (50%)	8 (57%)	7 (50%)
Plc	27 (48%)	24 (43%)	25 (45%)	27 (48%)
Total	243 (37%)	219 (33%)	224 (34%)	226 (34%)

Table 4: Number and proportion of ultimate pro-taxpayer decisions, from appeals of post-1995 Special Commissioner’s decision, adjusted for the expected number if the number of possible levels of appeal were reduced (see main text above for an explanation)

different practitioners vary remarkably as to at what level and in which direction such bias exists. Were this to be the case, it would be expected that a change in the number of levels of appeal might have an effect on the number of cases ultimately disposed in favour of the taxpayer. To test this, table 4 shows the proportion of ultimate pro-taxpayer decisions, by entity type, that would have been expected in the following alternatives: if no appeals were allowed and if the number of possible appeals was restricted to one, two or three levels. These figures are calculated as follows. The figure for no appeals assumes that the Special Commissioners decision in each case was the ultimate disposal. The figure for three levels looks at the actual disposal in the case. The figure for 1 level of appeal uses the Special Commissioners actual decision for cases that were not appealed, and the disposal on first appeal for all other cases – and so ignores any second or subsequent appeal. The figure for two appeals is similarly calculated. This is something of a simplification as it ignores the fact that some appeals (where there was a leapfrog or from Scottish or Northern Irish appeals) were limited to two appeals. Similarly, if levels of appeal were restricted some unappealed decisions might have been decided differently, due to different precedents existing. Yet this method provides a useful approximation.

It can be seen that the first level of appeal somewhat reduces the number of cases disposed of in favour of the taxpayer, but further levels of appeal do not substantively alter the proportion of cases disposed of in favour of the taxpayer.

Accordingly, it does not appear that judges at one level of the appeal system are any more disposed to the taxpayer than judges at any other level of the appeals system. Nor does it appear that any types of party is more likely to appeal than their opponent, which could also cause the appeal system to advantage a particular type of party.

ference (29 June 2012) one eminent practitioner expressed the view that the CA were especially hostile to the taxpayer in avoidance transactions.

8 Conclusion: too many appeals?

A somewhat remarkable feature of the appeal structure described above is that it consists of four tiers and that appeals to the third tier are made on a regular basis. The Tax Law Review Committee noted that New Zealand was the only other country that they studied that had such extensive possibilities for appeals.⁷⁰

The introduction of the requirement for leave⁷¹ to appeal to the CA for onward appeals from the Special Commissioners, where it would be a second appeal, was to implement the recommendation of the Bowman report that “one level of appeal should be the norm”.⁷² Yet in the case of onwards appeals from the Special Commissioners, this has not been the case. As noted above, of the appeals from the Special Commissioners to the ChD reported in the period 2000 to 2010, 51 per cent were appealed to the CA.

The huge proportion of appeals that reach the CA is demonstrated by a comparison of this figure of 51 per cent to some other areas of law, provided by the Bowman report. The highest rate of appeals they reported to the CA was from the Commercial Court where 43 per cent of judgments were appealed. The next highest was from the Chancery Division, 12 per cent of judgments being appealed to the Court of Appeal. However, both of these concern first appeals, the court whose judgment was appealed being a court of first instance, and so are to some degree unfair comparisons. The better comparison is with appeals from the Employment Appeals Tribunal and the Immigration Appeal Tribunal – since both involve second appeals – the statistics being respectively 1.92 and 0.91 per cent of their decisions being appealed to the CA. Admittedly, the difference with these tribunals might not be (solely) due to different rates of permission granted by the CA but might also be attributable to differences in the litigants’ abilities to fund second appeals.

Clearly there are advantages in an appeals system that readily allows at least one level of appeal. These are set out in the Bowman report as consisting of a public and a private purpose:

The private purpose is to correct an error, unfairness or wrong exercise of discretion which has led to an unjust result. The public purpose is to ensure public confidence in the administration of justice and, in appropriate cases, to: (i) clarify and develop the law, practice and procedure; and (ii) help maintain the standards of first instance courts and tribunals.⁷³

However, second and subsequent appeals may be thought less likely to positively contribute to these public and private purposes – indeed they may introduce

⁷⁰Tax Law Review Committee, *The Tax Appeals System* (IFS, 1996) 101. This is still the case in New Zealand, although their Supreme Court has replaced the Privy Council.

⁷¹AJA 1969, s.12.

⁷²J Bowman et al, *Review of Court of Appeal (Civil Division): Report to the Lord Chancellor* (Lord Chancellor’s Department, September 1997) 42.

⁷³J Bowman et al, *Review of Court of Appeal (Civil Division): Report to the Lord Chancellor* (Lord Chancellor’s Department, September 1997) 25.

rather than correct errors, although it is to be hoped the correct more than they introduce. Further such appeals may “create uncertainty and delay a litigant receiving the benefit of a judgment to which he is entitled”.⁷⁴ Blom-Cooper and Drewry have noted:

It can be argued that a continuous process of review results in a valuable process of refinement by increasingly eminent tribunals. There is an element of truth in this, but counter-argument may be founded on a law of diminishing returns. Each appeal has a price, both to the litigant and the State.⁷⁵

The possibility of a third appeal is not necessarily a bad thing, but only not so if permission is given sparingly – arguably at a rate not dissimilar to that for comparable appeals structures such as the Employment Appeals Tribunal and the Immigration Appeal Tribunal. An appeal structure where 51 per cent of first appeals are themselves appealed can properly be regarded as dysfunctional. Similarly, the desirability of a four-tier appeals structure may be questioned. The previous quote from Blom-Cooper and Drewry continues:

the marginal utility of providing a third appeal would be heavily outweighed by the disadvantages of expensive and protracted litigation.⁷⁶

Indeed, in a recent judgment of Baroness Hale she seems to suggest that it would have been desirable for the first instance jurisdiction of the Special Commissioners and VAT Tribunal to have been transferred to the Upper Tier Tribunal (UTT),⁷⁷ which would have created a three tier appeal structure.

In the case of appeals from tribunals the Bowman report also considered that:

It is important for a route of appeal to exist to a court able to take a generalist approach, regardless of the number of previous stages a case may have been through. A tribunal might take a technical approach to a particular issue which might be out of step with the law in general.⁷⁸

However, this does not provide a justification for appeals from the ChD, itself clearly a court able to take a generalist approach, to the CA. Nor does such reasoning provide a justification for second appeals from the UTT to the CA

⁷⁴J Bowman et al, *Review of Court of Appeal (Civil Division): Report to the Lord Chancellor* (Lord Chancellor’s Department, September 1997) 24.

⁷⁵L Blom-Cooper and G Drewry, *Final Appeal: A Study of the House of Lords in its Judicial Capacity* (Clarendon Press, Oxford 1972) 63.

⁷⁶L Blom-Cooper and G Drewry, *Final Appeal: A Study of the House of Lords in its Judicial Capacity* (Clarendon Press, Oxford 1972) 63.

⁷⁷*R (on the application of Cart) v The Upper Tribunal; R (on the application of MR (Pakistan)) v The Upper Tribunal (Immigration & Asylum Chamber) and Secretary of State for the Home Department* [2011] UKSC 28, [2011] STC 1659 [23]-[24].

⁷⁸J Bowman et al, *Review of Court of Appeal (Civil Division): Report to the Lord Chancellor* (Lord Chancellor’s Department, September 1997) 97.

under the new tribunal structure – since the new tribunal structure was introduced there have been five direct tax appeals heard as second appeals by the CA which have been reported in *Simon’s Tax Cases*, in each of these cases the UTT was chaired by a High Court judge. Indeed, in four of these five cases the High Court judge sat with a tribunal judge, which might be thought to strike an excellent balance between specialist expertise and a generalist approach.⁷⁹

Indeed, it can be legitimately questioned whether appeals to the courts from the Special Commissioners have added greatly to a generalist approach. Since most of the Special Commissioners were either former or current practitioners they will have been aware of the general law from their practice – since it is quite impossible to advise on tax law ignorant of the general legal framework. Were it the case that appeals to the courts resulted in a more generalist approach, it might be expected that the proportion of non-tax cases cited in the court’s judgments might be substantially greater than the proportion cited in the appealed decision of the Special Commissioners. Yet that does not appear to be the case. Looking at first appeals from post-1995 decisions of the Special Commissioners, the average (median) percentage of cases cited in judgment that were previously reported in either *Simon’s Tax Cases* or in the *HMRC’s Reports of Tax Cases* was 85 per cent. This is not substantively very different from the comparative figure of 88 per cent for post-1995 Special Commissioners’ decisions that were appealed.

Whilst the Bowman report highlighted the advantages of a route of appeal to the courts from tribunals, in tax disputes there are disadvantages too, as illustrated in the following quote of Lord Oliver:

The fact is that judges on the whole – there are a few honourable exceptions whom it would be invidious to name but amongst whom I certainly do not include myself – know very little about tax as a coherent subject. They are called on from time to time to examine under a microscope isolated points arising under particular sections of taxing statutes but few, if any of them have any comprehensive knowledge or understanding of revenue law. The case of the *Queen v. Attorney General ex parte ICI* (1987) 1 CMLR 72 over which I had the misfortune to preside in 1982 is a case in point. It concerned the petroleum revenue tax. I certainly – and I am tolerably certain, both of my colleagues – had never before heard of petroleum revenue tax. I am not sure that I understood it then, though they may have done; but in any event I have never had to refer to it since; and hope that I never shall.⁸⁰

Indeed, Lord Oliver’s description of the courts considering “under a microscope isolated points arising under particular sections of taxing statutes” hardly sug-

⁷⁹These figures are accurate as of 1 November 2012.

⁸⁰P R Oliver, ‘Judicial Approaches to Revenue Law’ in M Gammie (ed), *Striking the Balance: Tax Administration, Enforcement and Compliance in the 1990s* (IFS 1996) cited in Tax Law Review Committee, *The Tax Appeals System* (IFS 1996) 11.

gests the courts taxing a generalist approach, or even seeing the provisions within the general framework of tax law.

Given the foregoing argument that extensive appeals are a bad thing, depriving parties of certainty and not significantly improving the quality of outcomes, it might be questioned why the leapfrog arrangements outlined in section 1, above, were used so seldom. As noted only four appeals since 1985 (when it was introduced) took advantage of the possibility of leapfrog from the Special Commissioners direct to the CA. Similarly, there were only 4 instances of leapfrog from the ChD direct to the HL on appeals from the Special Commissioners decisions since 1981. Whilst the new tribunal structure does not have the possibility of such leapfrogs, it does have an alternative mechanism whereby the standard four-tier appeal structure can be reduced to three tiers – the first instance hearing can be transferred to the UTT in complex cases.⁸¹ So far this possibility has been utilised in one reported direct tax case heard by the CA, resulting in it being a first rather than second appeal.

When in practice, the author recalls sometimes suggesting a leapfrog appeal from the Special Commissioners to the CA. However, this was opposed by counsel who advised that it was desirable to have several bites at the cherry. Yet as argued in the discussion of table 4, above, neither the taxpayer nor Revenue appears (in general) structurally advantaged by having a more extensive appeals system. The only constituency that would appear to generally benefit from such extended litigation are the lawyers. One recalls how Galanter argued:

Lawyers should not be expected to be proponents of reforms which are optimum from the point of view of their clients taken alone. Rather, we would expect them to seek to optimize their clients' position without diminishing that of lawyers.⁸²

Perhaps this is the explanation for the extensive appeals structure (and the underutilisation of mechanisms that can shorten it).

⁸¹The Tribunal Procedure (First-tier Tribunal) (Tax Chamber) Rules 2009 (SI 2009 No. 273), rule 28.

⁸²M Galanter, 'Why the haves come out ahead: Speculations on the limits of legal change' (1974) 9 *Law & Soc'y Rev.* 95, 118-9.

Statistical Appendix

A Descriptive Statistics

Court	Dismissed	Allowed	Total
ChD	48 (48%)	53 (52%)	101
CANI	3 (75%)	1 (25%)	4
CS	4 (80%)	1 (20%)	5
CA	21 (58%)	15 (42%)	36
HL	12 (50%)	12 (50%)	24
Total	88 (52%)	82 (48%)	170

Table 5: Outcome of appeals by the Crown, by court, in relation to decisions of the Special Commissioners prior to 1995.

Court	Dismissed	Allowed	Total
ChD	22 (38%)	36 (62%)	58
CANI	0 (0%)	1 (100%)	1
SC	3 (60%)	2 (40%)	5
CA	11 (46%)	13 (54%)	24
HL	4 (40%)	6 (60%)	10
Total	40 (41%)	58 (59%)	98

Table 6: Outcome of appeals by the Crown, by court, in relation to decisions of the Special Commissioners since 1995.

Court	Dismissed	Allowed	Total
ChD	75 (71%)	30 (29%)	105
NICA	1 (100%)	0 (0%)	1
ScotCS	2 (50%)	2 (50%)	4
CA	46 (78%)	13 (22%)	59
HL	5 (50%)	5 (50%)	10
Total	129 (72%)	50 (28%)	179

Table 7: Outcome of appeals by the taxpayer in relation to decisions of the Special Commissioners prior to 1995.

Court	Dismissed	Allowed	Total
SpC	495 (67%)	243 (33%)	738
ChD	68 (76%)	22 (24%)	90
NICA	1 (100%)	0 (0%)	1
ScotCS	3 (100%)	0 (0%)	3
CA	32 (65%)	17 (35%)	49
HL	3 (30%)	7 (70%)	10
Total	602 (68%)	289 (32%)	891

Table 8: Outcome of appeals by the taxpayer in relation to decisions of the Special Commissioners since 1995.

Year	Decisions of ChD appealed to CA	Decisions of ChD not appealed to CA	Total
1981	10 (77%)	3 (23%)	13
1982	15 (65%)	8 (35%)	23
1983	13 (76%)	4 (24%)	17
1984	9 (75%)	3 (25%)	12
1985	9 (43%)	12 (57%)	21
1986	4 (31%)	9 (69%)	13
1987	7 (47%)	8 (53%)	15
1988	5 (42%)	7 (58%)	12
1989	4 (40%)	6 (60%)	10
1990	12 (67%)	6 (33%)	18
1991	6 (67%)	3 (33%)	9
1992	4 (36%)	7 (64%)	11
1993	7 (70%)	3 (30%)	10
1994	2 (33%)	4 (67%)	6
1995	4 (44%)	5 (56%)	9
1996	11 (55%)	9 (45%)	20
1997	9 (60%)	6 (40%)	15
1998	10 (71%)	4 (29%)	14
1999	4 (67%)	2 (33%)	6
2000	9 (90%)	1 (10%)	10
2001	8 (73%)	3 (27%)	11
2002	1 (9%)	10 (91%)	11
2003	1 (14%)	6 (86%)	7
2004	7 (88%)	1 (13%)	8
2005	5 (63%)	3 (38%)	8
2006	6 (50%)	6 (50%)	12
2007	5 (56%)	4 (44%)	9
2008	6 (38%)	10 (63%)	16
2009	5 (38%)	8 (62%)	13
2010	0 (0%)	3 (100%)	3

Table 9: Appeals from the ChD to the CA of decisions of the Special Commissioners.

B Statistical Model

Parameter	Estimate	SE	Estimated 95% central credibility interval
<i>Fixed part</i>			
Log-words	0.496	0.168	0.174, 0.829
Appeal by taxpayer	-0.647	0.201	-1.042, -0.250
Constant	-4.512	1.460	-7.407, -1.706
<i>Random Part</i>			
σ^2_{Area}	0.136	0.128	
σ^2_{Judge}	0.129	0.154	
$\sigma^2_{Taxpayer\ Lead\ Counsel}$	0.334	0.204	
$\sigma^2_{HMRC\ Lead\ Counsel}$	0.038	0.069	
DIC	741.26		

Table 10: Parameter estimates of a model predicting of whether there was a pro-taxpayer outcome of an appeal, controlling for controlling for log-words, whether the appeal was by the taxpayer, the judge hearing the case, the area of tax law, the lead counsel for the taxpayer and lead counsel for HMRC.

C Fitting the Model

A form of regression analysis was used to examine the partial effect of the independent variables on the expected probability of a pro-taxpayer decision.

The selection of independent variables was done by first fitting a non-hierarchical model including the log-adjusted word count and whether the appeal was by the taxpayer. Both variables were significant at all conventional levels of significance. The model was then re-estimated as a hierarchical model, alternatively using all possible combinations of the classifications in the table below. MCMC estimation in MLWin⁸³ using the runmlwin⁸⁴ interface was then used to perform a binary logistic regression, using a cross classified model.⁸⁵ Since the model which included all classifications had the lowest DIC⁸⁶ statistic, that model was selected. That model was then re-estimated including years call of HMRC and the taxpayer's counsel. The inclusion of neither variable (either alone or in combination) neither decreased the DIC statistic nor did the 95 per cent credibility interval of the coefficient include 0. Accordingly these variables were not

⁸³J Rasbash, C Charlton, W Browne, M Healy and B Cameron *MLwiN* (Version 2.1., Centre for Multilevel Modelling, University of Bristol, 2009)

⁸⁴G Leckie, and C Charlton, *runmlwin: Stata module for fitting multilevel models in the MLwiN software package* (Centre for Multilevel Modelling, University of Bristol 2011)

⁸⁵W Browne, *MCMC Estimation in MLwiN, v2.10* (Centre for Multilevel Modelling, University of Bristol 2009) Ch.15.

⁸⁶W Browne, *MCMC Estimation in MLwiN, v2.10* (Centre for Multilevel Modelling, University of Bristol 2009) 28.

included in the final model.

DIC statistic	Judge	Area	Taxpayer Lead Counsel	HMRC Lead Counsel
741.26	✓	✓	✓	✓
741.48	✓	✓	✓	
741.87		✓	✓	
742.81		✓	✓	✓
745.10	✓		✓	
745.68			✓	
745.93	✓		✓	✓
746.03			✓	✓
752.33	✓	✓		
753.06	✓	✓		✓
754.98		✓		
755.70		✓		✓
755.96	✓			
756.31	✓			✓
757.60				
758.31				✓

Table 11: DIC statistics, showing the goodness of fit of the model, for models predicting of whether there was a pro-taxpayer outcome of an appeal, controlling for log-words, whether the appeal was by the taxpayer and different combinations of the judge hearing the case; the area of tax law; the lead counsel for the taxpayer and lead counsel for HMRC. A ✓ denotes that the parameter was included in the model.

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