

**PUBLIC LAW AND PUBLIC MANAGEMENT:  
‘THEORY’ AND ‘VALUES’ IN  
CORPORATION TAX REFORM**

by

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## ABSTRACT

Reforming the UK's corporation tax code is becoming more of a widespread political concern than the preoccupation of specialists. This functionalist study offers an interpretation, and assesses the arguments. It views the corporation tax code as public law, energised by political values whose meaning and prioritisation are shaped by the prudential logic of effectiveness. The institutions that generate the code, and the challenges of globalisation to the nation state, have highlighted historic tensions between Crown and Parliament, and the latter's scrutiny of the managerialist governance style that the code's reform involves. This style is apparent in the ideology of the public interest that reform is designed to promote, a process that involves the skilful balancing of efficiency and fairness. Surprisingly, perhaps, there is little in the conduct of reform that violates the traditions of the UK's representative democracy. The result is a code that, given its public law status, is a pre-eminent example of political jurisprudence. Its values, their prioritisation, and their change and complexity, are inevitably contentious, because they are the products of representative institutions. Criticism of the code generally understates these points. What are presented as impartial legal arguments are often simply rival views of the public interest.

To the memory of my father, Eddie Snape, and of my mother, Betty Snape.

*Requiescant in pace.*

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My father, Edward Snape, and my mother, Elizabeth Brigid Snape, died within three weeks of each other, almost to the hour, as the study was in its last stages, and it is therefore respectfully dedicated to their memory, with love and with gratitude for their encouragement and example. Andrew Snape and Dr Michael Snape have been to me all that brothers could be over these difficult months.

E.J.S.,

29 February 2008.

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## TABLE OF ABBREVIATIONS

AC	Law Reports, <i>Appeal Cases</i>
ACE	allowance for corporate equity
A.-G.	Attorney-General
ACT	advance corporation tax
All ER	<i>All England Law Reports</i>
ASB	Accounting Standards Board
BBA	British Bankers' Association
BJPIR	<i>British Journal of Politics and International Relations</i>
BTR	<i>British Tax Review</i>
CA 1985	Companies Act 1985
CA 2006	Companies Act 2006
CAA 2001	Capital Allowances Act 2001
C.B.	Chief Baron (of the Exchequer)
CBI	Confederation of British Industry
CCCTB	common consolidated corporate tax base
CFC	controlled foreign company
Ch	Law Reports, <i>Chancery Division</i>
CIOT	Chartered Institute of Taxation
C.I.R.	Commissioners of Inland Revenue
CJQ	<i>Civil Justice Quarterly</i>

CLJ	<i>Cambridge Law Journal</i>
CLR	<i>Commonwealth Law Reports</i> (Australia)
CLSA	<i>Current Law Statutes Annotated</i>
Cm	Command Papers (Sixth Series, 1986 onwards)
CMLR	<i>Common Market Law Reports</i>
CMLRev	<i>Common Market Law Review</i>
Cmnd	Command Papers (Fifth Series, 1956-1986)
Conv.	<i>Conveyancer and Property Lawyer</i>
CRCA 2005	Commissioners for Revenue and Customs Act 2005
CSIH	Inner House of the Court of Session
CTSA	corporation tax self-assessment
DLR	<i>Dominion Law Reports</i> (Canada)
EBT	employee benefit trust
ECHR	Convention for the Protection of Human Rights and Fundamental Freedoms ('the European Convention on Human Rights')
ECtHR	European Court of Human Rights
ECHRDR	<i>European Commission of Human Rights Decisions and Reports</i>
ECJ	European Court of Justice
ECR	<i>European Court Reports</i>
EHRR – Comm Supp	<i>European Human Rights Reports – Commission Supplement</i>
ER	<i>English Reports</i>

ESC	Extra-Statutory Concession
EWCA	Court of Appeal of England and Wales
EWHC	High Court of Justice of England and Wales
FA	Finance Act
FB	Finance Bill
FDI	foreign direct investment
Fla. Tax Rev.	<i>Florida Tax Review</i>
FMI	Financial Management Initiative
FOREX	foreign exchange
FS	<i>Fiscal Studies</i>
GAAP	generally accepted accounting practice
GAAR	general anti-avoidance rule
GANTIP	general anti-avoidance principle
GATT	General Agreement on Tariffs and Trade
Harv. L. Rev.	<i>Harvard Law Review</i>
H.M.	her Majesty's
HMG	H.M. Government
HMRC	H.M. Revenue and Customs
HMSO	Her Majesty's Stationery Office
HRA 1998	Human Rights Act 1998
IAS	International Accounting Standard
IASB	International Accounting Standards Board
IASCF	International Accounting Standards Committee Foundation

ICAEW	Institute of Chartered Accountants in England and Wales
ICTA 1988	Income and Corporation Taxes Act 1988
<i>IDS Bulletin</i>	<i>Institute of Development Studies Bulletin</i>
IFS	Institute for Fiscal Studies
IMF	International Monetary Fund
IRC	Commissioners of Inland Revenue
ITA 2007	Income Tax Act 2007
ITEPA 2003	Income Tax (Earnings and Pensions) Act 2003
ITTOIA 2005	Income Tax (Trading and Other Income) Act 2005
JBL	<i>Journal of Business Law</i>
J. Env. L.	<i>Journal of Environmental Law</i>
Jnl Publ. Pol.	<i>Journal of Public Policy</i>
Jo. of Law & Soc.	<i>Journal of Law and Society</i>
LQR	<i>Law Quarterly Review</i>
LS	<i>Legal Studies</i>
LT	<i>Law Times</i>
MLR	<i>Modern Law Review</i>
MNC	multinational corporation
MP	Member of Parliament
MR	Master of the Rolls
NAO	National Audit Office
Nat. Tax Jo.	<i>National Tax Journal</i>
NLJ	<i>New Law Journal</i>

NPM	New Public Management
OECD	Organisation for Economic Co-operation and Development
OJ	<i>Official Journal of the European Communities</i>
OJLS	<i>Oxford Journal of Legal Studies</i>
PFI	Private Finance Initiative
PL	<i>Public Law</i>
PN	Press Notice
PPP	Public-Private Partnership
QB	Law Reports, <i>Queen's Bench Division</i>
QC	Queen's Counsel
RIA	regulatory impact assessment
Sched.	Schedule (to a statute)
S.I.	statutory instrument
S.O.	Standing Order of the House of Commons
SP	Statement of Practice
SpC	Special Commissioners' case
Stat LR	<i>Statute Law Review</i>
STC	<i>Simon's Tax Cases</i>
STC (SCD)	<i>Simon's Tax Cases (Special Commissioners' Decisions)</i>
St. Tr.	<i>State Trials</i>
SWTI	<i>Simon's Weekly Tax Intelligence</i>
TAAR	targeted anti-avoidance rule

TC	<i>Tax Cases</i>
TCGA 1992	Taxation of Chargeable Gains Act 1992
TJN	Tax Justice Network
TSO	The Stationery Office
UKHL	United Kingdom House of Lords
UKHRR	<i>United Kingdom Human Rights Reports</i>
VAT	value added tax
VATDT	VAT and Duties Tribunal
V.-C.	Vice-Chancellor
WLR	<i>Weekly Law Reports</i>
WN	<i>Weekly Notes</i>
WTO	World Trade Organization
YLJ	<i>Yale Law Journal</i>

## NOTE ON BIOGRAPHICAL DETAILS

In cases where it has been considered appropriate to include biographical details of individuals referred to in the text, the sources of the relevant information have been abbreviated as follows: *ODNB* (*Oxford Dictionary of National Biography: from the earliest times to the year 2000*, ed. by H.C.G. Matthew and Brian Harrison (Oxford: Oxford University Press, 2004)); *Dod* (*Dod's Parliamentary Companion 2005* (London: DOD, 2005)); and *WW* (*Who's Who*, 159<sup>th</sup> edn (London: A&C Black, 2007)). Where biographical sources other than these have been used, their details have been set out in full.

## NOTE ON DATES

Since firm names change frequently, as do the holders of ministerial office, names and titles are given as at the date of the event or quotation under discussion. The text seeks to reflect developments as at 29 February 2008.



## Chapter 1

### INTRODUCTION

#### CORPORATION TAX REFORM

United Kingdom law, in common with that of many other countries,<sup>1</sup> requires a company resident within its territory to pay corporate income tax – ‘corporation tax’ – ‘on all its profits’.<sup>2</sup> It does not matter, for the purposes of this ‘worldwide profits rule’, whether the profits are made at home or abroad.<sup>3</sup> Such is one of the axioms of corporation tax. To it may be added another fundamental proposition, i.e. that a company not resident in the UK is liable to pay corporation tax on its profits ‘if, and only if, it carries on a trade in the United Kingdom through a permanent establishment<sup>4</sup> in the United Kingdom’.<sup>5</sup> Where the latter rule applies, the company’s profits liable to tax are those which are ‘attributable to’ the permanent establishment in question.<sup>6</sup> The two rules together, it is contended, contain the foundational ideas of corporation tax. Whilst they are not the only way of taxing companies, they nonetheless encapsulate the approach that the UK has so far taken.

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<sup>1</sup> See the lists in Roy Rohatgi, *Basic International Taxation*, 2<sup>nd</sup> edn, vol. 1 (Richmond: Richmond Law and Tax, 2005), pp. 197-199.

<sup>2</sup> See ICTA 1988, s. 8(1). On residence, see FA 1988, s. 66 and Sched. 7 and SP 1/90 (9 January 1990). ‘Profits’ include, not only income profits, but also chargeable gains (see ICTA 1988, s. 6(4)(a)).

<sup>3</sup> See ICTA 1988, s. 8(1).

<sup>4</sup> See FA 2003, s. 148.

<sup>5</sup> See ICTA 1988, s. 11(1) (as substituted by FA 2003, s. 149(1), for accounting periods beginning after 31 December 2002). See ICTA 1988, s. 834(1) for the definition of an ‘accounting period’.

<sup>6</sup> See ICTA 1988, s. 11(2).

The two statutory formulations just recited, the former embodying the so-called ‘residence jurisdiction’, the latter the ‘source jurisdiction’,<sup>7</sup> have practical, or technical, as well as theoretical dimensions. Thus, as the last rays of winter sunlight glance off the buildings on the City skyline, the weary corporate tax lawyer might wonder about the practical effect of the residence jurisdiction or the source jurisdiction on the contents of the file open on the desk before her. So, too, at his desk in the gracious surroundings of Whitehall, might the senior civil servant agonise over the theoretical compatibility of certain aspects of the worldwide profits rule with the principles of the European Treaty.<sup>8</sup> Indeed, even when there is no European or international aspect to a company’s activities, the question of how its profits should be measured has important theoretical, no less than practical, aspects. Profits are no more, and, significantly, no less than, the ‘base’ of corporation tax, the ‘thing ... which is liable to the tax’.<sup>9</sup> No profits, no tax. And telescopically brief though the statement may be, the process of working through some of its more detailed implications, under conditions of unprecedented and rapid change in global financial markets,<sup>10</sup> has been one of the major UK tax law reform projects of the last 15 years or so. But this is not all. The ongoing, and incremental, process of reform has itself coincided with a radical shift in governmental approaches to the development of public policy, not least tax policy, in part attributable to ‘New Right’ theories about the respective roles of Government and special

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<sup>7</sup> For a brief overview of the ‘jurisdiction to tax’, see Brian J. Arnold and Michael J. McIntyre, *International Tax Primer*, 2<sup>nd</sup> edn (The Hague: Kluwer, 2002), ch. 2; for the origins and history of the residence jurisdiction and source jurisdiction, see Sol Picciotto, *International Business Taxation* (London: Weidenfeld and Nicolson, 1992), ch. 1.

<sup>8</sup> See Houlder, *Financial Times*, 6 December 2004, 3; Sanger, *Financial Times*, 21 September 2006, 14; H.M. Treasury and HMRC, *Taxation of the foreign profits of companies: a discussion document* (London: H.M. Treasury, 2007); Houlder, *Financial Times*, 22 June 2007, 2; Houlder, *Financial Times*, 20 July 2007, 3.

<sup>9</sup> See *Davies: Principles of Tax Law*, ed. by Geoffrey Morse and David Williams, 5<sup>th</sup> edn (London: Sweet and Maxwell, 2004), para. 1-09.

<sup>10</sup> See, e.g., Mike Buckle and John Thompson, *The UK Financial System: Theory and Practice*, 4th edn (Manchester: Manchester University Press, 2004), pp. 51-54.

interest groups in the policy-making process,<sup>11</sup> and in part attributable to some high-profile failures<sup>12</sup> of the Departments responsible for Government policy on taxation.

The remodelling of various aspects of the corporation tax base can perhaps be characterised in terms of four main themes. The first of these has been an increasingly close alignment of profits measurement for corporation tax purposes and their measurement for the purposes of generally accepted accounting practice (GAAP).<sup>13</sup> We shall be calling this first theme ‘the accounting theme’. The Finance Act (FA) of 1993 introduced a new corporation tax code for the tax treatment of profits and losses arising on a company’s foreign exchange (FOREX) transactions.<sup>14</sup> This was followed, in 1994, with new rules for the taxation of financial instruments<sup>15</sup> and, in FA 1996, with new rules on the tax treatment of a company’s ‘loan relationships’.<sup>16</sup> Rather more was happening, with all three developments, than may have been apparent to the casual observer. Although the tenor of these ‘distinct but overlapping, independent but interdependent’, separate but integrated,<sup>17</sup> codes was largely to assimilate corporation tax and GAAP, they also removed, in the areas to which they applied, the time-honoured corporation tax distinction between income and capital. Not even the use of GAAP in computing trading profits under Schedule D, Case I,<sup>18</sup> an area in which recent

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<sup>11</sup> For an overview, see David Richards and Martin J. Smith, *Governance and Public Policy in the UK* (Oxford: Oxford University Press, 2002).

<sup>12</sup> Including the handling of some high-profile prosecutions and the involvement of two of the Departments in a PFI-related offshore tax avoidance scheme (see n. 78 below).

<sup>13</sup> A surprisingly loose term: see Allister Wilson, Mike Davies, Matthew Curtis and Gregory Wilkinson-Riddle, *UK and International GAAP: Generally Accepted Accounting Practice in the United Kingdom and under International Accounting Standards*, 7<sup>th</sup> edn (London: Butterworths Tolley, 2001), pp. 66-70; *GAAP 2004: UK Financial Reporting and Accounting*, ed. by Chris Harrison and others (Kingston upon Thames: Croner CCH, 2004), pp. 2-3.

<sup>14</sup> See FA 1993, ss. 60, 92-96, 125-170, Schedules 15-18; S.I. 1994 Nos 3226-3232.

<sup>15</sup> See FA 1994, ss. 147-177 and Sched. 18; S.I. 1994 No. 3233.

<sup>16</sup> See FA 1996, ss. 80-105; Schedules 8-15.

<sup>17</sup> David Southern, *Taxation of Corporate Debt, Foreign Exchange and Derivative Contracts*, 7<sup>th</sup> edn (London: Lexis Nexis, 2004), p. 2.

<sup>18</sup> See ICTA 1988, s. 18(3).

years have seen some notable case and statute law,<sup>19</sup> has had so radical an effect. The full significance of this point will be explored in a later chapter.<sup>20</sup> For the present, however, it is sufficient to note - as does David Southern - that the three 'special codes' on corporate finance have fundamentally altered the nature of the corporation tax base, or at least of a substantial part of it.<sup>21</sup> Deemed a success, if a qualified one, by members of the practising legal and accounting professions,<sup>22</sup> in 2002, the special codes were nonetheless significantly remodelled, becoming, in the process, two, rather than three.<sup>23</sup> As Ruth Kelly, MP,<sup>24</sup> the Economic Secretary to the Treasury, explained, at the Committee Stage of the 2002 Finance Bill, '[a]lthough all three regimes were thought radical in their time, they have suffered from two main problems: complexity and lack of fairness'.<sup>25</sup> Remodelled though the special codes were, the basic idea of the alignment of tax law with GAAP remained; consistent with this, FA 2002 also saw the broad assimilation of the corporation tax treatment of intellectual property and other intangibles with their accounting treatment.<sup>26</sup>

If lack of simplicity had implications for efficiency, then the other reason advanced for refashioning the special codes in 2002, 'lack of fairness', provided the impetus for combating tax avoidance. 'The Government', explained the Economic Secretary in the

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<sup>19</sup> See, e.g., *Herbert Smith (A Firm) v. Honour (Inspector of Taxes)* (1999) 72 TC 130 (Lloyd J.), [11]-[32], where the case law is reviewed; also *Revenue and Customs Commissioners v. William Grant and Sons Distillers Ltd*; *Small (Inspector of Taxes) v. Mars UK Ltd* [2007] UKHL 15; [2007] STC 680; also the articles in *British Tax Review – Special Issue – Accounting Standards and Taxable Profits* [1995] BTR 433-510. See also FA 1998, s. 42, requiring the use of GAAP to calculate trading profits, 'subject to any adjustment required or authorised by law'.

<sup>20</sup> See Chapter 4 below.

<sup>21</sup> See Southern, n. 17 above, p. 2.

<sup>22</sup> See the (qualified) admiration accorded by Julian Ghosh and Ian Johnson, in their loose-leaf, *Taxation of Loan Relationships and Derivatives* (London: Butterworths LexisNexis, 1999), p. vii, a comment which first appeared in Issue 8, in December 2002.

<sup>23</sup> See FA 2002, ss. 69-79 and Sched. 23; FA 2002, s. 80 and Sched. 24; FA 2002, s. 81; FA 2002, s. 82 and Sched. 25; FA 2002, s. 83 and Schedules 26-28; FA 2002, s. 104.

<sup>24</sup> Ruth Kelly was Economic Secretary to the Treasury from 2001 to 2002 and Financial Secretary from 2002 to 2004 (see [www.dodonline.co.uk](http://www.dodonline.co.uk) (accessed 12 September 2005)). She had been an economics writer for *The Guardian* newspaper from 1990 to 1994.

<sup>25</sup> See Hansard HC Standing Committee F, 11 June 2002, col. 318.

speech already referred to, ‘are [*sic*] determined to remove avoidance opportunities as far as possible, so that all companies pay their fair share of tax and compete on a level playing field’.<sup>27</sup> This leads on to the second theme in the ongoing process of reforming the corporation tax base: the progressive introduction of statutory anti-avoidance provisions. We shall be calling this ‘the anti-avoidance theme’. If the provisions discussed as part of the accounting theme are designed to ‘fine tune’ the way in which the corporation tax base is defined, then these anti-avoidance provisions are designed to prevent the tax base so defined from being manipulated in ways considered to be unacceptable. There are two important examples of such measures within the special codes themselves, i.e. a somewhat narrowly-focussed transitional attack on attempts to gain a tax benefit by altering a company’s accounting date,<sup>28</sup> plus a much broader ‘general anti-avoidance rule’,<sup>29</sup> the well known ‘paragraph 13’, which disallows deductions attributable to so-called ‘unallowable purposes’.<sup>30</sup> However, of arguably much more general significance have been anti-avoidance provisions, in generally quite separate areas, introduced in 2003, 2004 and 2005. In 2003, measures were introduced which were designed to limit corporation tax deductions for contributions to employee trusts,<sup>31</sup> and FA 2004 extended pre-existing legislation on transfer

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<sup>26</sup> See FA 2002, s. 84; Sched. 29.

<sup>27</sup> See Hansard HC Standing Committee F, 11 June 2002, col. 319.

<sup>28</sup> See FA 2002, Sched. 23, para. 25, which replaced FA 1993, s. 166 (repealed by FA 2002, s. 79(1)(b)).

<sup>29</sup> i.e. in the sense of a provision designed to prevent abuse of a particular statutory regime (see Morse and Williams, n. 9 above, para. 2-15). The much wider notion of a ‘GAAR’ along the lines of Commonwealth examples, and floated in 1998, was originally dropped in favour of the disclosure rules introduced by FA 2004, ss. 306-319 and S.I. 2004 No. 1865. However, in evidence to the House of Lords Select Committee on Economic Affairs, in June 2006, Dave Hartnett, Director General, Compliance Strategy and Business, HMRC, indicated that the earlier decision could be revisited (see House of Lords Select Committee on Economic Affairs, *6<sup>th</sup> Report. The Finance Bill 2006, Volume II: Evidence* (House of Lords Papers, Session 2005-2006, 204) (London: TSO, 2006), pp. 105-106).

<sup>30</sup> See FA 1996, Sched. 9, para. 13 (as amended by FA 2002, ss. 79 (Sched. 23), 82 (Sched. 25), 141 (Sched. 40)).

<sup>31</sup> See FA 2003, s. 143 and Sched. 24, enacted in response to the taxpayer’s success before the Special Commissioners in *Macdonald (H.M. Inspector of Taxes) v. Dextra Accessories Ltd and*

pricing to transactions entered into between UK resident companies.<sup>32</sup> The essence of the transfer pricing provisions, which take in provisions on thin capitalisation,<sup>33</sup> is to require UK-resident companies to enter into transactions with connected UK companies on an ‘arm’s length’ basis.<sup>34</sup> Sections 306 to 319, FA 2004, also famously imposed mandatory notification requirements on the promoters of ‘tax avoidance schemes’,<sup>35</sup> the results of which led directly to the introduction in FA 2006 of four targeted anti-avoidance rules (TAARs) designed to prevent corporation tax avoidance through the unacceptable ‘creation and use of corporate capital losses’, measures that were further strengthened in FA 2007.<sup>36</sup>

In a project the evident purpose of which is to strengthen the corporation tax base, the third theme has an almost inevitable quality. There would be no point in defining the tax base and preventing its unacceptable manipulation without ensuring that tax due and payable is collected and enforced. The third theme, much more lightly sketched in what follows, is therefore compliance and enforcement. The main innovation here has been the introduction, ‘in relation to accounting periods ending on or after [1 July 1999]’,<sup>37</sup> of corporation tax self-assessment (CTSA). We shall be calling this third theme ‘the compliance and enforcement theme’. It is necessary to take account of it, but CTSA is not a major theme of the study, not least because it has proved relatively uncontroversial.

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*Others* [2002] STC (SCD) 413 (ultimately reversed by the House of Lords on 7 July 2005, see [2005] UKHL 47; [2005] STC 1111; also Levy, *Tax Journal*, 25 July 2005, 9-11).

<sup>32</sup> See FA 2004, ss. 30-37 and Sched. 5, amending ICTA 1988, Sched. 28AA.

<sup>33</sup> See FA 2004, s. 34.

<sup>34</sup> Subject to exceptions for small- and medium-sized enterprises (see FA 2004, s. 31).

<sup>35</sup> See n. 29 above.

<sup>36</sup> See FA 2006, ss. 69-72 (as amended by FA 2007, ss. 27 and 32), adding TCGA 1992, ss. 16A and 184A-184I; also H.M. Revenue and Customs, *HMRC Guidance: Avoidance through the creation and use of capital losses by companies*, 27 July 2006 (available from [www.hmrc.gov.uk](http://www.hmrc.gov.uk) (accessed 28 July 2006)); also H.M. Revenue and Customs, *HMRC Guidance: Capital Gains Tax - Avoidance through the creation and use of capital losses*, 19 July 2007 (available from [www.hmrc.gov.uk](http://www.hmrc.gov.uk) (accessed 17 February 2008)); also David F. Williams, ‘Avoidance through the creation and use of capital losses by companies’ [2006] BTR 23-33, on the original FA 2006 provisions.

When picking out the three themes just identified, it is tempting to assume that, given the general taxation context, H.M. Government (HMG) has had a free hand in policy development. However, the UK's status as a Member State of the EU, as well as its membership - along with the EU itself - of the World Trade Organization (WTO), means that this is not so. Both of these, but especially the latter, have, until recently, been somewhat understated influences on UK tax policy. And whilst the effect of the latter has perhaps yet to be felt, the impact of the fundamental freedoms conferred by the European Treaty on corporation tax law has been growing ever more acute. A fourth theme, therefore, is the possible impact of the EU (particularly through the European Commission and the European Court of Justice (ECJ)) and the WTO on the UK's freedom of action in delineating the corporation tax base. We shall be calling this fourth theme 'the European and international theme'. The attention that had once focussed on the apparent inability of the Commission to move beyond a handful of legislative measures on corporate tax<sup>38</sup> has shifted to the role of the ECJ in holding certain long-standing elements of corporation tax law to fall foul of various Treaty provisions, most often those on freedom of establishment.<sup>39</sup> There is a winding path of ECJ jurisprudence, four milestones on which include: in 1998, a ruling as contrary to Arts 43 and 48, European Treaty (ex 52 and 58) domestic legislation restricting entitlement to consortium relief to holding companies whose business consisted wholly or

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<sup>37</sup> See FA 1998, s. 117(4), (5) and Sched. 18; S.I. 1998 No 3175.

<sup>38</sup> See the Assessment Assistance Directive (Council Directive 77/799/EEC [1977] OJ L336 15); the Merger Directive (Council Directive 90/434/EEC [1990] OJ L225 1); the Parent-Subsidiary Directive (Council Directive 90/435/EEC [1990] OJ L225 6); the Arbitration Convention (Convention 90/463/EEC [1990] OJ L225 10); the Savings Interest Directive (Council Directive 03/48/EC [2003] OJ L157 38); and the Interest and Royalty Directive (Council Directive 03/49/EC [2003] OJ L157 49). See Ben J.M. Terra and Peter J. Wattel, *European Tax Law*, 4<sup>th</sup> edn (The Hague: Kluwer Law, 2005), chs 16, 10, 9, 11, 14 and 13.

<sup>39</sup> See, e.g., Troup, *Financial Times*, 5 February 2003, 17. This does not, of course, only affect the UK (see Case C-168/01, *Bosal Holding BV v. Staatssecretaris van Financiën* [2003] 3 CMLR 22 - Dutch law provision preventing relief for interest on loans to purchase shares in companies

mainly in the holding of shares in 90 per cent. UK-resident subsidiaries;<sup>40</sup> in 2001, the striking-down, for the same reason, of the disqualification of a UK-resident subsidiary of a non-resident holding company from making a group income election;<sup>41</sup> in 2005, a decision that Arts 43 and 48 rule out the restriction of group relief to UK-resident groups;<sup>42</sup> and, in 2006, a decision that Arts 43 and 48 also preclude the maintenance in its then form of the UK's controlled foreign company (CFC) regime.<sup>43</sup> When not overtaken by separate developments, each of these rulings has required HMG to make appropriate changes to UK law.<sup>44</sup> Moreover, although the European and international theme assumes the restrictive influence of supranational – or international – organisations (in this case the EU and the WTO), it should also be recognised that at least one other international organisation, the Organisation for Economic Co-operation and Development (the OECD) can be regarded as having a 'positive' influence, i.e. in diffusing tax policy ideas, not only at the national level,

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resident in other Member States held to be against the Parent-Subsidiary Directive (Council Directive 90/435/EEC [1990] OJ L225 6)).

<sup>40</sup> See Case C-264/96, *Imperial Chemical Industries plc. v. Kenneth Hall Colmer (H.M. Inspector of Taxes)* [1998] 3 CMLR 293; (see now ICTA 1988, s. 403D, 403E, inserted by FA 2000, s. 97, Sched. 27).

<sup>41</sup> See Case C-397/98, *Metallgesellschaft Ltd and Others v. C.I.R. and A.-G.* [2001] ECR I-1727 ('the *Hoechst* case'). Group income elections were abolished when advance corporation tax (ACT) was abolished by FA 1998 (see below); also *Pirelli Cable Holdings N.V. and Others v. Customs and Revenue Commissioners* [2006] UKHL 4; [2006] STC 548; also Foster, *Tax Journal*, 27 February 2006, 9-12 and Tait, *Financial Times*, 9 February 2006, 4.

<sup>42</sup> See Case C-446/03, *Marks and Spencer plc. v. Halsey (H.M. Inspector of Taxes)* [2006] 1 CMLR 18; [2006] EWHC 811; [2006] STC 1235 (Park J.); affirmed [2007] EWCA Civ 117; [2007] 2 CMLR 21.

<sup>43</sup> See Case C-196/04, *Cadbury Schweppes plc. and another v. Inland Revenue Commissioners* [2007] 1 CMLR 2. Consequential amendments appear in FA 2007, s. 48 and Sched. 15.

<sup>44</sup> See Case C-324/00, *Lankhorst-Hohorst GmbH v. Finanzamt Steinfurt* [2003] STC 607. Note also the comments of Advocate General Geelhoed in Case C-524/04, *Test Claimants in the Thin Cap Group Litigation v. Commissioners of Inland Revenue* [2007] 2 CMLR 31, para. AG84, on whether it had actually been necessary for H.M. Government to amend the pre-FA 2004 UK thin capitalisation legislation (see nn. 32 and 33 above and Lagerberg [2004] 1 CLSA 12-55-12-56).



but also at the European and international level, through ‘voluntary co-operation’.<sup>45</sup> This ‘policy transfer’ is a topic that we shall touch on again in Chapter 3.

If corporation tax reforms can be seen in terms of the four themes just discussed, then changes in the approach of the relevant Government Departments to the development of corporation tax policy can possibly be viewed in terms of three further themes. One of these, which we shall be designating ‘the consultation theme’, has been the increased and ever more detailed - although not necessarily more timely - use of consultation. True, there had been consultation processes<sup>46</sup> - even before the FA 1993 introduction of the FOREX legislation – but, as Malcolm Gammie, a prominent tax lawyer and author on tax law,<sup>47</sup> pointed out in an influential 1988 lecture, ‘draft legislation ... [had] not [been] produced, often because the timetable for change ... [was] too short’.<sup>48</sup> The FOREX legislation marked something of a departure in this respect; consultation on the way in which FOREX gains and losses should be treated for tax purposes, the result of which was the FA 1993 rules, had begun four years before, in 1989,<sup>49</sup> within a year of Gammie’s lecture calling for a new approach to the enactment of tax legislation. The evolution of the first three themes in the remodelling of the corporation tax base, as elaborated above, can be traced by reading a succession of ‘consultative documents’ and ‘technical notes’. Take as one example the three

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<sup>45</sup> See *Bowett’s Law of International Institutions*, ed. by Philippe Sands and Pierre Klein, 5<sup>th</sup> edn (London: Sweet and Maxwell, 2001), para. 6-029.

<sup>46</sup> See the exhaustive analysis in Malcolm Gammie, *The Enactment of Tax Legislation: An Analysis of the Consultative Process and the Finance Acts 1979 to 1987* (London: Law Society of England and Wales, 1988).

<sup>47</sup> Gammie, now a barrister, became a Queen’s Counsel in 2002. In 1988, he was a partner in what was then Linklaters and Paines, a leading City law firm; he had previously been Deputy Head of the Confederation of British Industry’s (the CBI’s) tax department from 1978 to 1979 and, from 1979 to 1984, director of the national tax office of what was then Thomson, McLintock and Co., the City accountancy firm (see *WW*).

<sup>48</sup> See Malcolm Gammie, ‘The Process of Fiscal Reform in the United Kingdom’ [1989] BTR 252-264, 256. See the Opposition complaints at lack of consultation prior to the introduction of corporation tax in 1965 (see Hansard HC, 8 December 1964, cols 1322-1324).

(subsequently two) special codes on the tax treatment of loan relationships, FOREX and financial instruments. Consultation on the tax treatment of ‘swap’ fees began in 1989;<sup>50</sup> 1991 saw the publication of a consultative document on financial instruments,<sup>51</sup> the result of which were the provisions included in FA 1994; and, on a brisk morning in November 1995,<sup>52</sup> practitioners (or, more accurately, one suspects, their trainees and ‘outdoor clerks’) had waited outside Somerset House for the distribution of copies of *The Taxation of Gilts and Bonds: A Consultative Document*,<sup>53</sup> the deliberations on which led in turn to the ‘loan relationships’ provisions of FA 1996. Even the 2002 remodelling of the special codes discussed above was preceded by at least four separate discussion documents.<sup>54</sup> A second example of this more extensive approach might be the series of consultative documents which eventually led to the 2004 extension of the transfer pricing and thin capitalisation rules. The process began in August 2002, with a consultation document<sup>55</sup> canvassing views on the corporation tax treatment of capital assets, both as to the possibility of assimilating capital and income gains (along the lines of the special codes) and abolishing the concept of capital allowances; the removal of the distinction between trading and investment

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<sup>49</sup> See Inland Revenue, *Tax Treatment of Foreign Exchange Gains and Losses: A Consultative Document* (London: Inland Revenue, 1989).

<sup>50</sup> See Inland Revenue, *Tax Treatment of Swap Fees: A Consultative Document* (London: Board of Inland Revenue, 1989).

<sup>51</sup> See Inland Revenue, *Financial Instruments: The Tax Treatment of Financial Instruments for Managing Interest Rate Risk: a Consultative Document* (London: Board of Inland Revenue, 1991).

<sup>52</sup> See Ballard and Staveley, *Tax Journal*, 7 December 1995, 4-9.

<sup>53</sup> London: Board of Inland Revenue, 1995.

<sup>54</sup> See Inland Revenue, *Corporate Debt, Financial Instruments and Foreign Exchange Gains and Losses* (London: Board of Inland Revenue, 2000); Inland Revenue, *Corporate Debt, Financial Instruments and Foreign Exchange Gains and Losses: a Consultative Document* (London: Board of Inland Revenue, 2001); Inland Revenue, *Loan Relationships, Derivative Contracts and Foreign Exchange Gains and Losses: a Technical Note* (London: Board of Inland Revenue, July 2001); and Inland Revenue, *Loan Relationships, Derivative Contracts and Foreign Exchange Gains and Losses: a Technical Note* (London: Board of Inland Revenue, December 2001).

<sup>55</sup> H.M. Treasury and Inland Revenue, *Reform of Corporation Tax: A Consultation Document* (London: Inland Revenue, 2002).

companies;<sup>56</sup> and (even) the ‘rationalisation’ of the ‘Schedular’ system itself.<sup>57</sup> Transfer pricing and thin capitalisation were not mentioned anywhere. The 2002 document, which, so HMG reported, had attracted in excess of 150 written replies,<sup>58</sup> was followed by a further document almost exactly a year later.<sup>59</sup> This requested further comments on a narrower range of issues than those in the paper of 2002, albeit in the same three areas.<sup>60</sup> However, HMG also announced its intentions with regard to transfer pricing and thin capitalisation and requested views on those areas too.<sup>61</sup> To this document, HMG received 147 ‘substantive written responses’,<sup>62</sup> and, in a technical note of December 2003, published draft legislation on the two areas which it was at that time inclined to carry forward: transfer pricing and thin capitalisation, and changes to the rules for the deduction of management expenses. Drafted in ‘the modern style developed by the Tax Law Rewrite project’, these clauses became, without significant amendment, the FA 2004 provisions mentioned above.<sup>63</sup> In relation to the other matters raised for consultation in the 2002 document, a December 2004 technical note brought forward draft clauses to replace the corporation tax Schedules with a single set of

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<sup>56</sup> See, e.g., *Revenue Law - Principles and Practice*, ed. by Natalie Lee, 24th edn (Haywards Heath: Tottel, 2006), paras [41.22], [41.47]-[41.49], ch. 48 and para. [41.71].

<sup>57</sup> For the Schedular system, see, e.g., John Tiley, *Revenue Law*, 5<sup>th</sup> edn (Oxford: Hart Publishing, 2005), pp. 135-137. See also Stephen Dowell, *A History of Taxation and Taxes in England from the Earliest Times to the Present Day*, 3<sup>rd</sup> edn, rev. by A. R. Ilersic, 6 vols (London: Frank Cass, 1965), II, pp. 225-226, 230-231 (discussed in *London County Council v. Attorney-General* [1901] AC 26, at 37-40 (Lord Macnaghten)); and Martin Daunton, *Trusting Leviathan: The Politics of Taxation in Britain, 1799-1914* (Cambridge: Cambridge University Press, 2001), pp. 45, 183-193. The abolition of the Schedular system for corporation tax, already effected by the Income Tax (Trading and Other Income) Act 2005 (ITTOIA 2005) for income tax purposes, has been the subject of consultation, although this seems to have been abandoned as too costly.

<sup>58</sup> See H.M. Treasury and Inland Revenue, *Corporation Tax Reform: A Consultation Document* (London: Inland Revenue, 2003), p. 1.

<sup>59</sup> *Ibid.*

<sup>60</sup> *Ibid.*, pp. 13-14.

<sup>61</sup> *Ibid.*, ch. 3.

<sup>62</sup> Inland Revenue, *Corporation Tax Reform: The Next Steps – Inland Revenue Technical Note December 2003* (London: Inland Revenue, 2003), para. 1.2.

<sup>63</sup> See nn. 32 and 33 above. For the Tax Law Rewrite, see n. 88 below.

rules for a company's 'operating business'.<sup>64</sup> The third proposal made in 2002, i.e. reforming the corporation tax treatment of capital assets, was put on hold and, as matters turned out, the 'operating business' concept did not make it to either of the FAs of 2005. Ironically, although capital allowances reform was taken up again in 2007, a significant part of this (the abolition of industrial buildings allowances) was effected without warning, consultation being confined to a set of proposals designed to reduce 'the distortive impact' of such allowances.<sup>65</sup>

What we shall be calling 'the technical theme' in corporation tax reform has been an increase in the nature and scope of the technical material promulgated by the Government Departments responsible for corporation tax policy. Some of this is recognisably 'law' in a rather narrow formal sense, i.e. secondary legislation in the form of statutory instruments (S.I.s) (the sheer quantity of these being a striking feature of the 1993 FOREX regime). Other types of technical material, such as Statements of Practice (SPs) and Extra-Statutory Concessions (ESCs), not to mention Press Notices (PNs), are each well-established features of the system, even though they might not recognisably be 'law' in the sense that statutory instruments are. However, the corporation tax reforms of the 1990s have seen a range of other types of material, too. One is the phenomenon of the 'explanatory notes' that have accompanied new legislation since 1999.<sup>66</sup> To take just one example at random, we might observe that the Exchange Gains and Losses (Bringing into Account Gains or Losses) Regulations 2002,<sup>67</sup> which contained the detailed mechanics of turning the three special

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<sup>64</sup> See Inland Revenue, *Corporation Tax Reform: Technical Note December 2004* (London: Inland Revenue, 2004), para. 1.2.

<sup>65</sup> See FA 2007, ss. 36-37; H.M. Treasury and HMRC, *Business tax reform: capital allowances changes July 2007* (London: H.M. Treasury, 2007).

<sup>66</sup> See Michael Zander, *The Law-Making Process*, 6<sup>th</sup> edn (Cambridge: Cambridge University Press, 2004), pp. 179-182, citing Christopher Jenkins, 'Helping the reader of Bills and Acts', 149 NLJ 798.

<sup>67</sup> S.I. 2002 No. 1970.

codes into two, were accompanied by an ‘Explanatory Note’ summarising the instrument and explaining its effect.<sup>68</sup> Although, as we shall see, the production of such explanatory notes is not without interest in the specific context of corporation tax, it is not unique, having become endemic in policy areas other than taxation.<sup>69</sup> What is unique to the tax context, however, is the publication on the web, subject to certain reservations,<sup>70</sup> of Inland Revenue, and latterly, H.M. Revenue and Customs (HMRC), staff instruction manuals. The company taxation section of the Government website includes manuals on CTSA (CT10000), loan relationships (CT12000), plus FOREX and financial instruments (CT13200).<sup>71</sup>

Reference to HMRC instruction manuals has brought us to the seventh and final theme in our discussion of corporation tax reform, although it would also be relevant to any discussion of tax law reform in the UK in the last 15 years or so. This is the ongoing process of reorganisation in the Government Departments responsible for tax policy, especially the former Board of Inland Revenue, the Department that, with H.M. Treasury, has historically been responsible for all of the reforms and approaches discussed above. We shall be calling this ‘the Departmental theme’. The expression ‘ongoing’ process is accurate to the extent that it refers to a group of developments that is, in the nature of things, ever incomplete. The reference to the historical position is to the 2005 amalgamation of the Inland Revenue with H.M. Customs and Excise, to form HMRC. However, we should note that, especially as regards developments in the last three years or so, the ongoing reorganisation process has

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<sup>68</sup> The order was consequent on the remodelling of the special codes as two, rather than three, in 2002 (see n. 23 above).

<sup>69</sup> See *Callery v. Gray (No. 2)* [2001] EWCA Civ 1246; 4 All ER 1, paras 48-54 (‘collective conditional fees’ and the Explanatory Notes to the Access to Justice Bill 1999, Lord Phillips of Worth Matravers MR); *Regina (Westminster City Council) v. National Asylum Support Service* [2002] UKHL 38; 1 WLR 2956, paras 1-6 (Lord Steyn).

<sup>70</sup> See, e.g., the first page of the FOREX and financial instruments manual (CT13200), ‘... [t]he text at this point has been withheld under the Code of Practice on Access to Government Information’ (see [www.hmrc.gov.uk/manuals/ct56manual/ct13000/ct13200.htm](http://www.hmrc.gov.uk/manuals/ct56manual/ct13000/ct13200.htm), accessed 14 September 2005).

<sup>71</sup> See [www.hmrc.gov.uk/manuals/ct123manual/index.htm](http://www.hmrc.gov.uk/manuals/ct123manual/index.htm) (accessed 14 September 2005).

been something of a reactive one. Responsibility for direct taxes, including corporation tax, was historically that of the Inland Revenue, while its ‘sister’ Department, H.M. Customs and Excise, was responsible for indirect tax policy. Although this is something of an oversimplification, both Departments, each of which was subordinate to the Treasury, had, since the early 1980s, been reformed along lines suggested by the New Right ideologies that were gaining ground in the closing decades of the twentieth century, latterly by what is still, albeit somewhat quaintly, referred to as ‘the New Public Management’ (NPM).<sup>72</sup> The key objective of these reforms might be described as the attainment of what Frampton characterises as the ‘administrative virtue’ of increased efficiency; to this end, public servants staffing the Inland Revenue, along with those in other Government Departments, were encouraged to have a ‘better business focus’.<sup>73</sup> The process has been through a number of stages, including ‘Raynerism’,<sup>74</sup> the Financial Management Initiative (FMI), ‘Next Steps’,<sup>75</sup> and ‘Gershonisation’,<sup>76</sup> the cumulative results of which will be assessed in subsequent chapters. Most importantly, for present purposes, by the early 1990s, the (then) 63,000 staff of the Inland Revenue were being reorganised ‘on Next Steps lines’.<sup>77</sup> It will be noted that this is almost exactly the period over which the reforms discussed above were taking shape. Whether, and to what extent, this market-oriented approach ultimately led to subsequent failures of management in the Inland Revenue,<sup>78</sup> especially under its last

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<sup>72</sup> See, e.g., Owen E. Hughes, *Public Management and Administration: An Introduction*, 2<sup>nd</sup> edn (London: Macmillan, 1998), *passim*.

<sup>73</sup> See Dennis Frampton, *Practical Tax Administration* (Bath: Fiscal Publications, 1993), p. 58.

<sup>74</sup> Named after Sir Derek (later Lord) Rayner.

<sup>75</sup> See Richards and Smith, n. 11 above, pp. 104-111; also Frampton, n. 73 above, ch. 4.

<sup>76</sup> After Sir Peter Gershon (see Robert Peston, *Brown’s Britain* (London: Short Books, 2005), p. 150).

<sup>77</sup> See Gavin Drewry, ‘The New Public Management’, in *The Changing Constitution*, ed. by Jeffrey Jowell and Dawn Oliver, 4<sup>th</sup> edn (Oxford: Oxford University Press, 2000), pp. 167-189 (p. 177).

<sup>78</sup> See n. 12 above and House of Commons Treasury Committee, *10<sup>th</sup> Report. Inland Revenue Matters* (House of Commons Papers, Session 2002-2003, 834) (London: TSO, 2003).

permanent Chairman, Sir Nicholas Montagu,<sup>79</sup> does not need to be examined here. What does need to be stressed, however, is that the Government's reaction to these failures was the institution of a large-scale review of the 'Revenue Departments',<sup>80</sup> chaired by Gus O'Donnell,<sup>81</sup> and that its report, which appeared in March 2004,<sup>82</sup> has resulted in the amalgamation of the two old Departments, in the new, hapless and (some would say) under-funded HMRC.<sup>83</sup>

Such then are what, for the purposes of the present study, are taken to be the seven main themes in the reform of corporation tax, and in the changes in the policy approach to the tax. It would be possible to highlight other, subsidiary elements, relative to each main theme. One might, for instance, in relation to both the accounting and the European and international themes, emphasise the effect on corporation tax legislation of the compulsory adoption of International Accounting Standards (IASs) for quoted companies after 31 December 2004.<sup>84</sup> Or one might emphasise the abolition, without consultation, after Labour's landslide General Election victory in May 1997, of advance corporation tax (ACT).<sup>85</sup> Or again, one might stress the lowering of the full rate of corporation tax after

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<sup>79</sup> Montagu retired in 2004. He had been a philosophy lecturer before becoming a Whitehall civil servant (see *WW*).

<sup>80</sup> See H.M. Treasury Press Release 78/03, *Chancellor announces major review of Inland Revenue and Customs and Excise*, 3 July 2003 (reprinted at [2003] SWTI 1202-1204).

<sup>81</sup> Currently (as Sir Gus O'Donnell), Secretary of the Cabinet and Head of the Home Civil Service. He was briefly an economics lecturer before becoming a Treasury civil servant in 1979. At the time of the O'Donnell report, he was Permanent Secretary to the Treasury (see *WW*).

<sup>82</sup> *Financing Britain's Future: Review of the Revenue Departments* (Chair, Gus O'Donnell) (Cm 6163) (London: TSO, 2004).

<sup>83</sup> See Houlder, *Financial Times*, 20 November 2007, 2; Houlder, *Financial Times*, 21 November 2007, 2; Burns and Eaglesham, *Financial Times*, 14 December 2007, 2; also, generally, the Commissioners for Revenue and Customs Act 2005.

<sup>84</sup> See CA 1985, s. 227(2) and European Parliament and Council Regulation EC/1606/02 [2002] OJ L243 1, Art. 4; see H.M. Revenue and Customs, *International Accounting Standards – The UK tax implications*, 29 September 2005 (see [www.hmrc.gov.uk/practitioners/int\\_accounting.htm](http://www.hmrc.gov.uk/practitioners/int_accounting.htm), accessed 6 February 2006); also [2005] SWTI 1623.

<sup>85</sup> See FA 1998, s. 31 and Sched. 3. For the background, see William Keegan, *The Prudence of Mr Gordon Brown* (Chichester: John Wiley, 2003), pp. 140, 194-195 and 260; also Peston, n. 76 above, pp. 101-104.

1997.<sup>86</sup> Yet again, one might choose to emphasise the drive for greater intelligibility in the drafting of tax legislation, in the shape of the Tax Law Rewrite project,<sup>87</sup> even if its impact on corporation tax is only beginning to be felt.<sup>88</sup> For the purpose of the study, however, we shall not be taking these ‘subsidiary’ changes, though important, as being characteristic of corporation tax reform in the way that the seven themes drawn out above are considered to be. Moreover, the references to ‘corporation tax reform’ should not be taken to imply a tightly unified reform process. Although the first four themes represent, as we shall see, the realisation of a ‘vision’ for the tax, they have been ‘incremental’, and often reactive, in nature.

#### THEORISING CORPORATION TAX REFORM

The first four themes just introduced have been distilled from a highly technical legal literature on corporation tax.<sup>89</sup> The various works to which reference has been made have

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<sup>86</sup> Since April 2007, corporation tax rates have comprised a ‘small companies’ rate’ of 20 per cent., on profits under £300,000 (see ICTA 1988, s. 13; FA 2007, s. 3), and a full rate of 30 per cent. on profits over £1.5m (see FA 2006, s. 24). There is a progressive increase in the rate of tax on profits between £300,000 and £1.5m, using a ‘marginal relief’ fraction of 1/40 (see FA 2007, s. 3(2)(a)).

<sup>87</sup> See Lee, n. 56 above, para. [1.22] (see [www.hmrc.gov.uk/rewrite/index.htm](http://www.hmrc.gov.uk/rewrite/index.htm) (accessed 19 September 2005)).

<sup>88</sup> To date, there have been four ‘rewrite’ Acts and one ‘rewrite’ S.I., i.e.: Capital Allowances Act 2001 (CAA 2001); Income Tax (Earnings and Pensions) Act 2003 (ITEPA 2003); Income Tax (Pay As You Earn) Regulations 2003 (S.I. 2003 No. 2682); ITTOIA 2005 (see n. 57 above); and Income Tax Act 2007. Of these, only CAA 2001 relates to both corporation tax and income tax. The first corporation tax ‘rewrite’ Bill was published amid controversy in February 2008 (see Houlder, *Financial Times*, 25 February 2008, 4); the earliest rewritten clauses had appeared for consultation in May and June 2006 (see Papers CC/SC (06) 04-07, available from [www.hmrc.gov.uk/rewrite/exposure/menu.htm](http://www.hmrc.gov.uk/rewrite/exposure/menu.htm) (accessed 28 September 2006)); also Hansard HL, 23 March 2005, col. 331 (Lord Howe of Aberavon)).

<sup>89</sup> See, e.g., *Taxation of Companies and Company Reconstructions*, ed. by Richard Bramwell, Alun James, Mike Hardwick and John Lindsay, 8<sup>th</sup> edn (London: Sweet and Maxwell, 2002); also Ghosh and Johnson, n. 22 above; also Judith Freedman, ‘Taxation Research as Legal Research’, in *Taxation: An Interdisciplinary Approach to Research*, ed. by Margaret Lamb *et al.* (Oxford: Oxford University Press, 2005), pp. 13-34, esp. 19-20.



largely, though not exclusively, been written by the practising lawyers and accountants whose business it is to advise clients on the practical implications of the legal developments to which the various themes refer. As Christopher Wales has written: ‘For lawyers and accountants, there are very few rewards to be earned from considering how ... [things] should be or how to influence change’.<sup>90</sup> For this reason, the technical literature does not always make very accessible reading, even to the well informed. Since much of it is of the highest quality, however, considerable reference will be made to it in what follows.

Although the technical writing has a certain theoretical dimension (insofar, for instance, as it consists of detailed discussions of the relevance of accounting theory to tax law),<sup>91</sup> what is conspicuous by its absence is a more generally theorised discussion of the implications of the interaction of the last three themes among those of the first four. The inspiration for this study, at the highest level of abstraction, was a perception that the critique of corporation tax reform has tended to concentrate on its practical, or technical, dimension, and has somehow failed to capture some important theoretical issues which might reasonably be expected to arise, not only from the reforms themselves, but also from the institutions involved in effecting them, and the processes by which the various reforms have been approached. This

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<sup>90</sup> See Christopher Wales, ‘The Implications of the O’Donnell Review for the making of Tax Policy in the UK’ [2004] BTR 543-565, 559. Historically, technical writing has been the predominant approach to writing about tax law: see, e.g., *Dowell’s Income Tax Laws*, ed. by P.M. Smyth, 9<sup>th</sup> edn (London: Butterworth, 1926), an elaborately detailed and extremely long annotation of the relevant legislation; Edwin Max Konstam, *The Law of Income Tax: A Treatise Designed for the Use of the Taxpayer and his Advisers*, 12<sup>th</sup> edn (London: Stevens and Sons, 1952), an austere exposition of, in this case, the Income Tax Act, 1952; and G.S.A. Wheatcroft, *The Law of Income Tax, Surtax and Profits Tax* (London: Sweet and Maxwell, 1962), which was ‘based on’ Konstam’s work, whilst much more readable, and which was itself the forerunner of Bramwell, n. 89 above.

<sup>91</sup> See n. 19 above. See also Graeme Macdonald and David Martin, *Tax and Accounting: A Response to the 2003 Consultation Document on Corporation Tax Reform* (London: Institute for Fiscal Studies, 2004).

situation, a characteristic of tax law writing, no less in the United States than in the UK,<sup>92</sup> is hardly surprising, given the need for the practising professions to digest, and to work with, a considerable, ever-expanding body of material. A notable exception is the corporation tax section of Tiley's well-known textbook,<sup>93</sup> which refers extensively to what might be thought of as the 'non-technical', i.e. theoretical, literature on corporation tax reform. The compendious nature of his work, however, means that it can only suggest, rather than develop, the wider possibilities that the material might offer.

If we cast the net wider, we find that the theoretical writing on corporation tax reform, as distinct from the technical literature, tends to present it an enterprise of classical political economy.<sup>94</sup> We therefore find that discussions of corporation tax are indebted, to a greater or lesser extent, to the four 'maxims' of taxation – those of 'equality', 'certainty', convenience and cost-effectiveness - propounded in Book V, Chapter II,<sup>95</sup> of Adam Smith's *The Wealth of Nations*.<sup>96</sup> The extent of this theoretical literature is such that, as Mintz reports, corporation tax is possibly the subject of more anxious scrutiny than any other tax.<sup>97</sup> 'Countless numbers of professionals', he tells us, 'study the impact of corporate tax law on

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<sup>92</sup> See Beverley I. Moran, 'Taxation', in *The Oxford Handbook of Legal Studies*, ed. by Peter Cane and Mark Tushnet (Oxford: Oxford University Press, 2003), pp. 377-396; also Daniel M. Schneider, 'Interpreting the Interpreters: Assessing Forty-Five Years of Tax Literature' (1999) 4 Fla. Tax Rev. 483-529.

<sup>93</sup> See Tiley, n. 57 above, chs 44-52. See the comments in Freedman, n. 89 above, pp. 18-19.

<sup>94</sup> See Simon James, 'Taxation Research as Economic Research', in Lamb *et al.*, n. 89 above, pp. 35-53, esp. 44. The term 'political economy' has been traced to a work by Antoyne de Montchrétien (c. 1576-1621), *Traicté de l'oeconomie politique* (see *The economic limits to modern politics*, ed. by John Dunn (Cambridge: Cambridge University Press, 1990), p. vii). See Montchrétien's *Traicté de l'æconomie politique* (Geneva: Slatkine Reprints, 1970), pp. xxiii-xxiv.

<sup>95</sup> Book V is entitled, *Of the Revenue of the Sovereign or Commonwealth*, and Chapter II bears the heading 'Of the Sources of the general or publick Revenue of the Society'.

<sup>96</sup> See Adam Smith (1723-1790), *An Inquiry into the Nature and Causes of the Wealth of Nations*, ed. by R.H. Campbell and A.S. Skinner (textual editor W.B. Todd), 2 vols (Oxford: Clarendon Press, 1976), II, pp. 825-828.

<sup>97</sup> See Jack Mintz, 'The Corporation Tax', in *The Economics of Tax Policy*, ed. by Michael P. Devereux (Oxford: Oxford University Press, 1996), pp. 137-187.

the affairs of the corporation'.<sup>98</sup> In the years since the introduction of corporation tax in 1965,<sup>99</sup> there have been possibly four critiques which still form important points of departure in discussions of the tax, and which, though diverse in origin and date, will be taken to typify the theoretical literature. The four consist of the theoretically pleasing, if somewhat unrealistic, discussion of corporation tax in the Meade Committee Report, of 1978;<sup>100</sup> the much lauded, though inconclusive, 1982 Green Paper on corporation tax reform;<sup>101</sup> the discussion of corporation tax in the latest (1990) edition of Kay and King's widely-cited economics textbook on the tax system in Britain;<sup>102</sup> and Mintz's paper on corporation tax,<sup>103</sup> to which reference has just been made. In addition, there has been an important recent study, by Devereux, Griffith and Klemm,<sup>104</sup> which seeks to account for the revenue-generating success of the tax, while casting doubt on its continuing ability to produce such comparatively high levels of revenue. This particular choice of four or five examples would not necessarily, of course, correspond to the choice that another might make. Its importance, however, is that it is able to illustrate certain key features of the way in which corporation tax reform has historically been presented.

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<sup>98</sup> *Ibid.*, p. 137

<sup>99</sup> See FA 1965, ss. 46-89 (Part IV of the Act). For the background, see David Kynaston, *The City of London, vol. IV: A Club No More, 1945-2000* (London: Chatto and Windus, 2001), pp. 300-301, 304, 307, 311-312.

<sup>100</sup> See *The Structure and Reform of Direct Taxation: Report of a Committee chaired by Professor J.E. Meade* (London: George Allen and Unwin, 1978).

<sup>101</sup> See *Corporation Tax: Presented to Parliament by the Chancellor of the Exchequer by Command of Her Majesty January 1982* (Cmnd 8456) (London: HMSO, 1982).

<sup>102</sup> See J.A. Kay and M.A. King, *The British Tax System*, 5<sup>th</sup> edn (Oxford: Oxford University Press, 1990), chs 10 and 11.

<sup>103</sup> See Mintz, n. 97 above.

<sup>104</sup> See Michael P. Devereux, Rachel Griffith and Alexander Klemm, 'Why Has the UK Corporation Tax Raised So Much Revenue?' (2004) 25 FS 367-388.

Given the wealth of technical and theoretical material, it is surprising that, despite occasional promptings,<sup>105</sup> legal scholars have not embarked on a systematic analysis of the possible significance of the themes in corporation tax reform. What makes this even more intriguing is the widespread renewal of interest in constitutional and administrative law, i.e. in public law,<sup>106</sup> during the 1990s. Tax is, after all, even in common law jurisdictions, ‘indisputably part of public law’.<sup>107</sup> Perhaps, to adopt an insight of Fisher’s, albeit from a different area of policy making, one reason for the neglect of the public law implications of corporation tax reform is that ‘[t]he law in ... [the area of corporation tax] has always seemed too ad hoc, too shambolic and too much the product of pragmatic compromise to be easily theorised about – let alone linked to the broader field of public law’.<sup>108</sup> Another reason might be that, with public law scholarship for long focussed on judicial review, corporation tax law and policy – with its historically rather limited scope for that procedure – has seemed rather unpromising territory.<sup>109</sup> Whatever the reasons may be, at the next level of generality, the study has been inspired by the need to develop a public law conception of corporation tax. Insofar as this would enable an interpretation of the seven themes with which the study began, it might offer powerful insights into the political acceptability – the legitimacy – of an area of law and policy often assumed to be of only ‘technical’ or ‘economic’ significance.<sup>110</sup>

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<sup>105</sup> See Tiley (2003) 26 *The Reporter* 19-24, 21-22. See also the Introduction to *Studies in the History of Tax Law*, ed. by John Tiley (Oxford: Hart Publishing, 2004), p. vii.

<sup>106</sup> See Eric Barendt, ‘Constitutional Fundamentals’, in *English Public Law*, ed. by David Feldman (Oxford: Oxford University Press, 2004), para. 1.08; also *Council of Civil Service Unions and Others v. Minister for Civil Service* [1985] AC 374, 407-410 (Lord Diplock) and 414-415 (Lord Roskill); also John F. McEldowney, *Public Law*, 3<sup>rd</sup> edn (London: Sweet and Maxwell, 2002), para. 1-001.

<sup>107</sup> See Victor Thuronyi, *Comparative Tax Law* (The Hague: Kluwer Law, 2003), p. 60; see *Ferrazzini v. Italy* [2001] STC 1314, 1319c, 1320g-j.

<sup>108</sup> See Fisher (2001) 13 J. Env. L. 115-117, 115 (book review).

<sup>109</sup> See, e.g., H.W.R. Wade, ‘Procedure and Prerogative in Public Law’ (1985) 101 LQR 180-199.

<sup>110</sup> See Assaf Likhovski, ‘A Map of Society: Defining Income in British, British Colonial and American Tax Legislation’ [2005] BTR 158-179, 177-179, on the absence of an obvious link between payments and policies (unlike with personal taxes).

This in turn might, for instance, illuminate the anti-avoidance theme and assist in mapping out the boundaries of the acceptable in tax avoidance. At the very least, the development of such a public law framework for corporation tax reform would provide a useful basis for further ‘empirical’ investigation.<sup>111</sup>

In order to lay the foundations for the investigation in subsequent chapters, the discussion in the rest of the present chapter unfolds in three main stages. First, we need to clarify why it is that corporation tax reform should be regarded, not simply as a technical exercise, but as a ‘political practice’ too. This is of some importance because, to the extent that the investigation uncovers the basis on which the state and corporations engage in the reform process, it also reveals the role to be assigned to public law in regulating the relationship between them.<sup>112</sup> Further, however, it gives rise to questions surrounding the nature and scope of public law itself. To the limited extent that the public law nature of taxation has been scrutinised in the literature, such scrutiny has neglected to take account of developments in public law scholarship over the past couple of decades.<sup>113</sup> The second part of the discussion therefore seeks to clarify both the nature and the scope of public law, as it is apprehended in these pages, and, in so doing, to stress that the approach to be taken to the material is an ‘interpretative’ and a ‘functionalist’ one.<sup>114</sup> Relatively recent developments in public law scholarship figure prominently in the analysis as a whole. A powerful stimulus to

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<sup>111</sup> See, e.g., Tony Prosser, ‘Towards a Critical Public Law’ (1982) *Jo. of Law & Soc.* 1-19, 1.

<sup>112</sup> See Martin Loughlin, ‘Constitutional Law: the Third Order of the Political’, in *Public Law in a Multi-Layered Constitution*, ed. by Nicholas Bamforth and Peter Leyland (Oxford: Hart Publishing, 2003), pp. 27-51, 42.

<sup>113</sup> See, e.g., Malcolm Gammie, ‘Tax Avoidance and the Rule of Law: a Perspective from the United Kingdom’, in *Tax Avoidance and the Rule of Law*, ed. by Graeme S. Cooper (Amsterdam: IBFD Publications, 1997), pp. 181-218; also Philip Baker, ‘United Kingdom’, in *The Principle of Equality in European Taxation*, ed. by Gerard T.K. Meussen (The Hague: Kluwer Law International, 1999), pp. 165-167. See Chapter 4 below.

<sup>114</sup> See Martin Loughlin, *Public Law and Political Theory* (Oxford: Clarendon Press, 1992), esp. ch. 10.

the study was the insights that the work of the ‘Sheffield school’<sup>115</sup> seemed to provide to those engaged in the theoretical analysis of public law. However, it is first necessary to place this and other approaches to public law in context, so the discussion of the nature and scope of public law begins with a survey of the main trends in public law writing. The key insight that the Sheffield school has suggested is that the UK’s unwritten constitution, in tax matters no less than in any other, could be regarded as a ‘structure of values’.<sup>116</sup> What proved unsatisfactory to the present author was both the Sheffield school’s claim to elevate constitutional values to the status of ‘rule of law values’<sup>117</sup> and its inability satisfactorily to explain either the provenance of those values or the relationship between them. Much more satisfactory seems to be Martin Loughlin’s conception of public law as ‘the third order of the political’.<sup>118</sup> Without denying the significance of ‘values’, his theory of public law seems both to explain their provenance (as growing out of the ‘political realm’) and to suggest ways of analysing the relationship between them. It follows that, in conceiving of corporation tax as public law, the study seeks to investigate what light Loughlin’s conception of the subject can throw on the interpretation of corporation tax reform. Greatly as it is indebted to it, the study does not, however, attempt an unqualified application of Loughlin’s theory. For example, as we shall see, the traditional view of corporation tax as an enterprise of classical political economy requires us to place a greater emphasis on ‘values’ – or ‘maxims’ – than perhaps Loughlin would regard as ideal. Again, the study rejects another possible consequence of Loughlin’s theory, that corporation tax reform might be interpreted in terms

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<sup>115</sup> So called in reference to the group of public lawyers working at the University of Sheffield since the 1980s, especially, perhaps, Ian Harden and Norman Lewis, both of whose work is discussed below.

<sup>116</sup> See n. 227 below.

<sup>117</sup> *Ibid.*

<sup>118</sup> See Loughlin, n. 112 above, pp. 40-42.

of systems theory.<sup>119</sup> These two main differences are discussed further below.<sup>120</sup> However, they do not detract from the overall usefulness of a version of Loughlin's conception of public law to the interpretation of the themes under consideration.

All of this brings us, in the final part of the chapter, to a drawing together of the seven themes outlined at the beginning, of the political element in corporation tax reform, and of the nature and scope of public law. In this final part, we seek to show the ways in which a public law approach can illuminate aspects of corporation tax reform. This last part begins by emphasising the centrality of tax law to public law, even where, as in the UK, constitutional arrangements do not take the form of 'some slim constitutive document'.<sup>121</sup> It does so by taking as its model the application of public law scholarship to regulation, something pioneered by Sheffield school writers, and, in so doing, seeks to explain the relationship between taxation – in this case corporate taxation – and other forms of regulation. This final part of the chapter also maps out the structure of the study in the light of this 'regulatory' model.

The development of a public law conception of corporation tax reform should thus provide a context in which the technical and theoretical traditions of corporation tax scholarship can illuminate each other. It should also enable the utilisation of new types of source material, as well as the interpretation of established types of source material in new ways. To these ends, the study draws upon a range of material, including scholarship on the role of special interest groups in policy making,<sup>122</sup> as well as on quantities of technical literature generally thought, perhaps, to be of merely transient significance. Although it has benefited from some discussion with public servants and with members of the practising

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<sup>119</sup> See n. 410 below.

<sup>120</sup> See nn. 410 and 415 below.

<sup>121</sup> See Loughlin, n. 114 above, p. 241.

<sup>122</sup> In this case, accountants and lawyers.

professions, the study's empirical dimension, gathered around the seven themes outlined above, is drawn from vast amounts of under-theorised official and secondary published material.

## THE POLITICS OF CORPORATION TAX REFORM

Crucially important to the study is the contention that the significance of corporation tax reform is not encapsulated in the devising of elegant solutions to intricate technical problems. This is, to be sure, one of its most important jobs. At a much deeper level, however, it is also an arena in which, to paraphrase Carl Schmitt, there is an ever-present potential for conflict.<sup>123</sup> Moreover, when ministers, civil servants, lawyers, accountants, corporations, and economists, engage in the process of consultation and negotiation on corporation tax reform, they are engaged in the 'practices of politics'.<sup>124</sup> The reader with a background in political theory or political science will find both of these statements unexceptionable. It is suggested, however, that, judging by the writings referred to above, for the economist, for the accountant, and – possibly – even for the lawyer, these statements will be controversial. Even outside the two categories of writing referred to in the previous part, the process of corporation tax reform is often presented as a preoccupation of the specialist,

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<sup>123</sup> See Carl Schmitt (1888-1985), *The Concept of the Political*, trans. by George Schwab (Chicago: University of Chicago Press, 1996), p. 29. Although the references are to this 1996 translation, *The Concept of the Political* was first published in 1932 (see *Der Begriff des Politischen. Text von 1932 mit einem Vorwort und drei Corollarien* (Berlin: Duncker and Humblot, 1963)). See also Renato Cristi, 'Carl Schmitt', in *Continental Political Thought*, ed. by Terrell Carver and James Martin (Basingstoke: Palgrave Macmillan, 2006), pp. 120-135. The writer has thought extremely carefully about making reference to Schmitt's work but, ultimately, has been satisfied with the rationalisation offered by, e.g., Paul Piccone and G.L. Ulmen, in their 'Introduction to Carl Schmitt' (1987) 72 *Telos* 3-14.

<sup>124</sup> This distinction between 'the concept of the political' and the 'practices of politics' follows Loughlin's conception of the 'first and second orders of the political' (see Loughlin, n. 112 above, pp. 30-40).



rather than the subject of a wider political discourse. Thus Peters, in his study of taxes and politics in OECD countries in the early nineties,<sup>125</sup> devotes only a small part of his analysis to specific issues raised by corporate income taxation.<sup>126</sup> The specialist nature of the subject matter means that, so far as the lawyer and the accountant are concerned, the arguments to which it gives rise are such as to seem to remove them from the arena of ‘the political’. There has been, as we shall see, some discussion of ‘the politics of corporate taxation’, notably by Radaelli;<sup>127</sup> but even this, it is contended, radically underestimates what it is that is political about it. In arguing for a political status for corporation tax reform, the present study is not merely saying that it is a practice of ‘political economy’, since this is of course the case. Rather, its claim is that, despite the polished manners and well-tailored suits of its chief protagonists, corporation tax reform is characterised by the need to find ‘workable’ solutions to profound, but skilfully obfuscated, antagonisms.<sup>128</sup> In order to sustain this argument, it is necessary to identify what is ‘political’ about corporation tax reform and to interrogate something of the nature of the politics involved.

### **The technical and the political**

The first four of the seven themes delineated at the beginning of the study bear the traces both of the potential for conflict, but also of its careful management. Thus, the accounting theme can be seen in terms of a manifestation of the jostling interests, not simply of rival

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<sup>125</sup> See B. Guy Peters, *The Politics of Taxation: A Comparative Perspective* (Oxford: Blackwell, 1991).

<sup>126</sup> *Ibid.*, pp. 31-32.

<sup>127</sup> See, e.g., Claudio M. Radaelli, *The Politics of Corporate Taxation in the European Union: Knowledge and International Policy Agendas* (London: Routledge, 1997). See below in this chapter.

<sup>128</sup> See Schmitt, n. 123 above, *loc. cit.*

groups of professionals – in this case, of lawyers and accountants<sup>129</sup> – but also of the corporate sector and the state. And yet, as befits an ongoing process of carefully handled conflict, it is not always possible to develop a clear sense of who the ‘winners’ and ‘losers’ are. What appears to be an ongoing assimilation of tax law to GAAP can, to the extent that only accountants are fully equipped to interpret its scope, be viewed as a something of a victory for the accountancy, as against the legal profession. But it is nonetheless difficult to assess the significance of that victory, if such it be, because, as Southern has pointed out, one little-remarked effect of removing the distinction between income and capital within the loan relationships code was to broaden the corporation tax base.<sup>130</sup> Even this does not enable us to declare a clear ‘winner’, however, because another consequence of introducing the loan relationships code was to enable companies to claim, for the first time, a tax deduction for the accruing discount on a zero-coupon bond.<sup>131</sup> Similar signs of conflict averted, albeit temporarily, are to be detected in relation both to the anti-avoidance theme and the compliance and enforcement theme. Even more clearly than with the accounting theme, we can detect in these two areas a background of fundamentally opposed positions on what, so far as the state and the corporate sector are concerned, is the question of the ‘fair share’ of tax for the latter to bear.<sup>132</sup> The clarity of these fundamentally opposed positions is starkly illustrated every time the UK courts have to rule on the latest anti-avoidance device, as well as each subsequent occasion on which, when successful, the device in question is met with

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<sup>129</sup> Or, as Sir Leonard Hoffmann (as he then was) once described them, ‘rival tribes’ (see *Law and Accountancy – Conflict and Co-operation in the 1990s*, ed. by Judith Freedman and Michael Power (London: Paul Chapman Publishing, 1992), p. v).

<sup>130</sup> See Southern, *Tax Journal*, 23 November 1995, 6-9. See also n. 17 above.

<sup>131</sup> See Southern, n. 17 above, pp. 44-45.

<sup>132</sup> Although we should note, as Kay has pointed out, that corporation tax should perhaps be viewed as a tax on all those associated with companies, rather than the companies themselves (see Kay, *Financial Times*, 25 October 2005, 19; also John Kay and Jadu Sen, ‘The Comparative Burden of Business Taxation’ (1983) 4:3 FS 23-28, 23); also Malcolm Gammie, ‘Reforming Corporate

(sometimes retrospective) anti-avoidance legislation.<sup>133</sup> As for the compliance and enforcement theme, the management of the corporate sector's disquiet over proposals to synchronise the deadlines for submitting corporation tax returns to HMRC and corporate accounts to Companies House,<sup>134</sup> also demonstrates how potential conflict has not become a reality.<sup>135</sup> All of the foregoing may yet, however, pale into relative insignificance next to the potential for conflict arising out of the European and international theme. The issues at stake here illustrate the problems of thinking of the tax unit, in the corporation tax context, as being that of the individual – or 'solus' – company. What the unfolding of the European and international theme has illustrated more than anything else is the difficulty of managing the differing objectives and values, not merely of the state and the corporation, but of the state, the EU, and the multinational corporation (the MNC).<sup>136</sup>

The initial contention that corporation tax reform is a political arena, its significance far from exhausted by its technical complexity, relies on the constant potential for conflict, express or implied, suggested by each of the above examples. This potential is not, as we shall see, diminished by the fairly refined and courteous way in which it is handled. And it presents us with the task of providing some interpretation of what has been happening in the reform process, especially over the period of the last 15 years or so. For this, we have to turn to politics or, to be more precise, to what political theory has to tell us about the 'concept of

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Taxation: An Evaluation of the United States Treasury Integration Proposals and other Corporate Tax Systems in an International Context: Part 1' [1992] BTR 148-173, 149.

<sup>133</sup> See, e.g., *Macdonald (H.M. Inspector of Taxes) v. Dextra Accessories Ltd and Others* and FA 2003, s. 143 and Sched. 24, n. 31 above. For the distinction between 'retrospective' and 'retroactive' see Bobbett [2006] BTR 15-18.

<sup>134</sup> See Companies House and HMRC, *Aligning Filing Dates for Companies: A Consultation Document*, November 2005, available from [www.hmrc.gov.uk](http://www.hmrc.gov.uk) (accessed 19 July 2006).

<sup>135</sup> See Scott, *Tax Journal*, 27 February 2006, 13-14; Houlder, *Financial Times*, 3 March 2006, 3; Houlder, *Financial Times*, 12 July 2006, 2.

<sup>136</sup> See Case C-446/03, *Marks and Spencer plc. v. Halsey (H.M. Inspector of Taxes)*, n. 42 above, and the subsequent changes to UK legislation announced on 20 February 2006 (see HMRC 12/06,

the political'.<sup>137</sup> This 'first order of the political' is not, as Loughlin points out, the same as 'the practices of politics',<sup>138</sup> to which, in the corporation tax context, we shall return in a moment. This is the 'essential character' of the political, what Schmitt bleakly calls the 'ever present possibility of conflict',<sup>139</sup> capable of existing to varying degrees, and in differing contexts, until the point at which it results in the identification of 'the friend' and the (political) 'enemy',<sup>140</sup> the foe that must be defeated.<sup>141</sup> In relations between states, 'the political' holds out the uttermost possibility of 'armed combat'.<sup>142</sup> Within its own territory, however, it is the power of the stable state that manages 'domestic antagonisms', so that they remain 'below the level of intensity of friend versus enemy'.<sup>143</sup> It is important to stress that what is being described here is the 'possibility of conflict', not necessarily the actual practices of, in this case, the corporate sector or of the state. As for 'lower level' antagonisms, these are the potential clash of the ruling ideology with the values of the corporate sector, but they are not necessarily translated into practice. One financial journalist has characterised the potential for conflict with a telling example: '[A] quoted company audit committee that puts its tax advice out to tender [he says,] is likely to be asked by competing

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reproduced at [2006] SWTI 453). On the special tax problems presented by MNCs, see Peter Muchlinski, *Multinational Enterprises and the Law* (Oxford: Blackwell, 1999), ch. 8.

<sup>137</sup> See Loughlin, n. 112 above, p. 30.

<sup>138</sup> *Ibid.*, p. 31.

<sup>139</sup> See Schmitt, n. 123 above, p. 32; also Andrew Gamble, *Politics and Fate* (Cambridge: Polity, 2000), pp. 8-9.

<sup>140</sup> See Schmitt, n. 123 above, p. 29. 'The enemy is *hostis*, not *inimicus* in the broader sense ...' (*ibid.*, p. 28). See Duncan Kelly, *The State of the Political: Conceptions of Politics and the State in the Thought of Max Weber, Carl Schmitt and Franz Neumann* (Oxford: Oxford University Press, 2003), pp. 217-223.

<sup>141</sup> See Loughlin, n. 112 above, p. 32.

<sup>142</sup> See Schmitt, n. 123 above, p. 32. This is why Schmitt's opening gambit is that '[t]he concept of the state presupposes the concept of the political' (see Schmitt, n. 123 above, p. 19). The ability of the stable state to withstand other states depends on the 'externalisation' of the 'friend-enemy grouping' (*ibid.*, p. 29, and Loughlin, n. 112 above, p. 34).

<sup>143</sup> See Loughlin, n. 112 above, p. 34; also Chantal Mouffe, *On the Political* (London: Routledge, 2005), p. 16.

firms where, on the spectrum of tax management from “caution” to “extreme aggression”, it wishes to be’.<sup>144</sup>

So we might, it is suggested, quite fairly speak of the ‘antagonism’ of the collective wisdom of the corporate sector, to the ideology of the governing party.<sup>145</sup> And, if ‘antagonism’ seems too emotive a word, consider, for example, the threat implied by the reported comments of the chief executives of two UK listed groups in December 2003. According to one, his group’s ‘investment priorities were in other markets [i.e. outside the UK]’, because of the additions to his company’s ‘UK cost base’ of “interventionist” government policies’.<sup>146</sup> To another was attributed the elliptical claim that ‘it now “notionally” paid 53 per cent of its profits in taxation’, with, again, the threat implied in the comment that he ‘would not want to see that going up any further’.<sup>147</sup> Examples of such language abound, and, like the one just quoted, they usually involve the more or less veiled threat of ‘capital flight’.<sup>148</sup> ‘If you do not play ball with us’, these voices suggest, ‘we shall take the ball away’. And each example tends to support Schmitt’s claim that ‘[t]he political can derive its energy from the economic ... [It] does not describe its own substance, but only the intensity of an association or dissociation of human beings whose motives can be ...

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<sup>144</sup> See Plender, *Financial Times*, 18 March 2004, 18; Parker, *Financial Times*, 4 May 2004, 4 (‘Ernst & Young are probably the most aggressive, creative, abusive provider of schemes and arrangements among the major accountancy firms.’ (Anonymous ‘Whitehall official’).)

<sup>145</sup> As to which, see Tiley, n. 57 above, pp. 8-9; also Parker, n. 144 above, reporting views of ‘left-of-centre ministers’; also the comments of Ruth Kelly MP, n. 27 above.

<sup>146</sup> See Boxell and Jones, *Financial Times*, 5 December 2003, 1 (Philip Bowman, Allied Domecq).

<sup>147</sup> *Ibid.* (Anonymous, Tesco).

<sup>148</sup> See Parker, *Financial Times*, 24 February 2004, 1 (Jonathan Symonds, AstraZeneca); Houlder, *Financial Times*, 22 November 2004, 9 (Aidan O’Carroll, Ernst and Young); Houlder, *Financial Times*, 3 October 2005, 17; Editorial, *Financial Times*, 9 November 2005, 18; Eaglesham, *Financial Times*, 6 December 2005, 4 (Sir Digby Jones, CBI); Adams, *Financial Times*, 6 December 2005, 5 (Malcolm Webb, UK Offshore Operators Association); Houlder, *Financial Times*, 23 December 2005, 4 (*inter alia*, Chris Spooner, HSBC Holdings); Seib, *Times*, 17 January 2006, see <http://business.timesonline.co.uk> (accessed 22 February 2008) (Guy Brannan, Linklaters, and Patrick Mears, Allen and Overy); Houlder, *Financial Times*, 20 June 2006, 3; Houlder, *Financial Times*, 23 July 2007, 7.

economic ... and can effect at different times different coalitions and separations'.<sup>149</sup> The idea that tax policy can energise the political can be illustrated, not only by reference to the clash between corporate values and the governing ideology, but by reference to the increased prominence which issues of fairness in corporation tax have gained in the public consciousness. In a striking comparison, the director of the OECD's centre for tax policy and administration has been quoted as saying that '[t]ax is where the environment was 10 years ago', thereby underlining the parallels between corporate social responsibility in taxation matters and in environmental matters.<sup>150</sup> The idea of tax policy energising the political is also demonstrated by the establishment of new activist groups, recent years having seen the appearance of articulate and technically very well-informed bodies such as the Tax Justice Network (TJN),<sup>151</sup> and, in the United States, Citizens for Tax Justice.<sup>152</sup> Although Loughlin does not, in the present writer's view, sufficiently underscore the problems with Schmitt's work, he is surely correct to treat it as a modern version of ideas traceable back through Hobbes,<sup>153</sup> and, ultimately, to Plato.<sup>154</sup> It provides us with a useful basis for investigating the political practices of corporation tax reform.<sup>155</sup>

If, as is contended, the first four themes announced at the beginning bear all the signs of 'lower level' antagonisms managed by the government of a stable state, the next question is

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<sup>149</sup> See Schmitt, n. 123 above, p. 38.

<sup>150</sup> See Houlder, *Financial Times*, 22 November 2004, 9. On this basis, Mr Owens has also opined that it would not be good for MNCs to move holding companies abroad in the absence of a 'business reason', i.e. solely or mainly for corporation tax reasons (see Houlder, *Financial Times*, 23 December 2005, 4).

<sup>151</sup> See [www.taxjustice.net/cms/front\\_content.php?idcat=2](http://www.taxjustice.net/cms/front_content.php?idcat=2) (accessed 9 March 2006).

<sup>152</sup> See [www.ctj.org/](http://www.ctj.org/) (accessed 9 March 2006).

<sup>153</sup> See Thomas Hobbes (1588-1679), *Leviathan, or The Matter, Forme, & Power of a Commonwealth Ecclesiasticall and Civill*, ed. by C.B. Macpherson (London: Penguin, 1985), pp. 185-186; also Thomas Hobbes, *On the Citizen*, ed. and trans. by Richard Tuck and Michael Silverthorne (Cambridge: Cambridge University Press, 1998), pp. 144-145.

<sup>154</sup> See Plato (427-347 BC), *The Laws*, ed. by Trevor Saunders (London: Penguin, 2004), pp. 5-6. In Loughlin's approving phrase, Schmitt follows 'an understanding of the political to its very foundations' (see Loughlin, n. 112 above, p. 32).

as to Loughlin's 'second order of the political', the 'practices of politics'.<sup>156</sup> How might we interpret the process by which the types of antagonisms referred to above are managed? A useful answer depends on the view that is taken of what the practice of politics is all about. In his admirable overview, Heywood offers four possible views of politics, i.e. as 'the art of government'; as 'public affairs'; as 'compromise and consensus' and, finally, as 'power and the distribution of resources'.<sup>157</sup> In what follows, the view is taken that, in the context of corporation tax reform, politics is best seen as the art of government, or rather, of 'governance'.<sup>158</sup> It is in the context of this examination that we consider how and why, in the writer's view, Radaelli's conception of 'the politics of corporate taxation'<sup>159</sup> radically underestimates its 'political' dimension.

### **Politics and 'the art of government'**

The practice of politics, the 'second order of the political', has classically been defined as 'the art of government'.<sup>160</sup> Within the state, the 'human community' that, in Weber's definition, '(successfully) claims the *monopoly of the legitimate use of physical force* within a given territory',<sup>161</sup> Loughlin tells us, the 'activity of governing' entails drawing a distinction between 'a governing authority and its subjects'.<sup>162</sup> Although we explore the significance of this often understated distinction in Chapter 2, what we can say for present purposes is that it is the office of the government to promote the responsibilities of the

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<sup>155</sup> This corresponds to Loughlin's 'second order of the political' (see n. 124 above).

<sup>156</sup> See Loughlin, n. 112 above, p. 31.

<sup>157</sup> See Andrew Heywood, *Politics*, 2<sup>nd</sup> edn (Basingstoke: Palgrave Macmillan, 2002), pp. 5-7.

<sup>158</sup> See Richards and Smith, n. 11 above, pp. 3-6. See also Chapter 2 below.

<sup>159</sup> See n. 127 above.

<sup>160</sup> See Heywood, n. 157 above, p. 5.

<sup>161</sup> See Max Weber (1864-1920), 'Politics as a Vocation', in *From Max Weber: Essays in Sociology*, trans. by H.H. Gerth and C. Wright Mills (London: Routledge, 1991), pp. 77-128, 78 (Weber's italics); also the references given in Herman Finer, *The Theory and Practice of Modern Government*, 4<sup>th</sup> edn (London: Methuen, 1961), p. 10.

state,<sup>163</sup> encapsulated by Cicero in the idea, ‘*salus populi suprema lex esto*’, ‘let the welfare of the people be the supreme law’.<sup>164</sup> The various meanings attributed to this elusive ‘law’ have been analysed by Oakeshott, in the posthumously published *The Politics of Faith and the Politics of Scepticism*.<sup>165</sup> Whilst describing it as ‘the emblem of all the ambiguity of our political vocabulary’,<sup>166</sup> Oakeshott is nonetheless able to find five historical meanings of the word ‘*salus*’,<sup>167</sup> of which the most appropriate in the present context is indeed probably ‘welfare’.<sup>168</sup> Loughlin draws attention to the point that, from the mid-twentieth century onwards, the promotion of the people’s welfare has been taken to comprise, not only Hobbes’s classical four jobs (defence, ‘acquisition of wealth, so far as this is consistent with public security’, law and order, and the ‘full enjoyment of innocent liberty’),<sup>169</sup> but a widening range of social tasks including social provision and environmental regulation.<sup>170</sup>

Promoting the welfare of the state and its people, that is, governing, is the preoccupation of a considerable literature, not only in political science, but also in the business, schools. In the UK, the scholarship has tended to concentrate on the changes of emphasis suggested by a transition, over the latter decades of the twentieth century, from ‘government’ to ‘governance’.<sup>171</sup> The latter term, once taken to be merely synonymous with the former,<sup>172</sup>

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<sup>162</sup> See Martin Loughlin, *The Idea of Public Law* (Oxford: Oxford University Press, 2003), p. 5.

<sup>163</sup> *Ibid.*, p. 7.

<sup>164</sup> See Marcus Tullius Cicero (106-43 BC), *de Re Publica; de Legibus*, ed. and trans. by Clinton Walker Keyes (London: William Heinemann, 1928), p. 466 (also, *ibid.*, p. 404, on ‘*salus*’ as a Roman deity); also Hobbes, *On the Citizen*, n. 153 above, p. 143, where ‘*salus*’ is translated as ‘safety’.

<sup>165</sup> Edited by Timothy Fuller (London: Yale University Press, 1996), p. 39. Michael Oakeshott (1901-1990) was a conservative political theorist (see *ODNB*).

<sup>166</sup> *Ibid.*, p. 39.

<sup>167</sup> *Ibid.*

<sup>168</sup> Oakeshott refers to Fleming C.B.’s rendering of ‘*salus populi*’ in *Bates’s* case (1606) 2 St. Tr. 371, 389, as ‘the general benefit of the people’ (see Oakeshott, n. 165 above, p. 40n).

<sup>169</sup> See Hobbes, *On the Citizen*, n. 153 above, p. 144.

<sup>170</sup> See Loughlin, n. 162 above, pp. 8-12. Also Martin van Creveld, *The Rise and Decline of the State* (Cambridge: Cambridge University Press, 1999), chs 3 and 4.

<sup>171</sup> See the literature reviewed in Chapter 2 below.



has come to signify a shift from what is generally referred to as the ‘Westminster model’, a ‘top-down’ idea of policy-making, dominated by the Cabinet and senior civil servants,<sup>173</sup> to what Rhodes has characterised as a ‘differentiated polity’ model, with government operating closely with civil society, in a context where policy-making is conditioned by the UK’s place, not only in Europe, but also in the wider world.<sup>174</sup> The shift is as significant in corporation tax policy as in any other area of public policy-making. We have already referred to one element of this transition, the Departmental theme in corporation tax reform, introduced at the beginning. This is the move within the Inland Revenue to NPM from its older, less theorised, counterpart, the idea of ‘public administration’.<sup>175</sup> However, both the consultation theme and the European and international theme are also symptomatic of the transition. The shift from government to governance is thus essentially concerned with who is involved in making public policy<sup>176</sup> and the ways, and to what ends, such policy is made. Public policy making, be it noted, is by definition, a goal-oriented activity.<sup>177</sup> Tax policy, as an aspect of public policy-making, raises particularly sensitive issues. We return to these issues in detail in Chapters 2 and 3; for the moment it is sufficient simply to allude to them.

It is, so we are told, ‘the activity of governing’ that has given rise to the practice of politics,<sup>178</sup> and every conception of politics as the art of governing must ultimately take its

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<sup>172</sup> See, e.g., Harold Wilson, *The Governance of Britain* (London: Sphere, 1977); Ministry of Justice, *The Governance of Britain* (Cm 7170) (London: TSO, 2007).

<sup>173</sup> See, e.g., R.A.W. Rhodes, *Understanding Governance: Policy Networks, Governance, Reflexivity and Accountability* (Maidenhead: Open University Press, 1997), pp. 5-7.

<sup>174</sup> *Ibid.*, pp. 7-22.

<sup>175</sup> See Patrick Dunleavy, ‘Is there a radical approach to public administration?’ (1982) 60 *Public Administration* 215-224.

<sup>176</sup> For tax policy as public policy, see Arye L. Hillman, *Public Finance and Public Policy: Responsibilities and Limitations of Government* (Cambridge: Cambridge University Press, 2003), ch. 7.

<sup>177</sup> Not least because the antonym of ‘policy’ is, of course, ‘aimlessness’ (see Wayne Parsons, *Public Policy: An Introduction to the Theory and Practice of Policy Analysis* (Cheltenham: Edward Elgar, 1995), p. 13).

<sup>178</sup> See Loughlin, n. 162 above, p. 32.

inspiration from Machiavelli.<sup>179</sup> Faintly distasteful as it may seem, the ‘odd politician’<sup>180</sup> provides both the key to understanding the practice of politics, and a useful guide to its practitioners themselves.<sup>181</sup> For Machiavelli, as Fleisher puts it, ‘there is no power of [practical] reason superior to *prudenza*’,<sup>182</sup> to ‘prudence’. Thus Loughlin quotes Fleisher’s summary of Machiavelli’s notion of prudence:

‘Machiavelli’s *prudenza* is rooted in his conception of the human world. Prudence is not to be measured principally by the existing standards of right and wrong but by the requirements of the situation, by necessity, and by the assessment of the best means to achieve one’s ends. Prudence is not synonymous with caution, nor is it the dominance of reason over the appetites and passions. It is, instead, the cool calculation of what must be done in a given situation to accomplish one’s purposes without judgment of the situation being unduly affected by passions or the contemporary conventions and ideals of right and wrong.’<sup>183</sup>

It is interesting that, despite the Machiavellian emphasis on assessing ends and means, as well as on judging situations in a cool and calculating way, Machiavelli’s prudence has not become more closely associated with the former Chancellor of the Exchequer’s, the Rt Hon. Gordon Brown, MP’s, well-known ‘prudence ... for a purpose’.<sup>184</sup> In other words, with that studious care with which, on the election of Labour to office in 1997, the Labour Chancellor,

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<sup>179</sup> See, especially, Niccolò Machiavelli, *The Prince*, trans. by Peter Bondanella (Oxford: Oxford University Press, 2005), esp. chs XXV and XXVI.

<sup>180</sup> See *The Tragedy of Hoffman by Henry Chettle* (1631), Act II, line 511 (Oxford: Malone Society, 1950).

<sup>181</sup> See Les Metcalfe and Sue Richards, *Improving Public Management*, 2<sup>nd</sup> edn (London: Sage, 1990), p. 211. See Parsons, n. 177 above, pp. 42-43, for a persuasive gathering of material attesting to Machiavelli’s continuing relevance.

<sup>182</sup> See Martin Fleisher, ‘A Passion for Politics: The Vital Core of the World of Machiavelli’, in *Machiavelli and the Nature of Political Thought*, ed. by Martin Fleisher (London: Croom Helm, 1973), pp. 114-145, 139.

<sup>183</sup> *Ibid.*, pp. 139-140. (In fact, Loughlin’s transcription (see Loughlin, n. 112 above) is a slight mistranscription of Fleisher’s wording, but this is not material.)

<sup>184</sup> See Hansard HC, 21 March 2000, col. 860 (‘Budget Statement’); also *Prudent for a Purpose: Working for a Stronger and Fairer Britain: Economic and Fiscal Strategy Report and Financial Statement and Budget Report March 2000* (House of Commons Papers, Session 1999-2000, 346) (London: TSO, 2000); also Keegan, n. 85 above, p. 333; also Keegan’s comments on the lessons

now Prime Minister, had aimed ‘at a reputation for fiscal responsibility in the early years ... in order to ... earn the credentials with “Middle England” and the financial markets, for higher spending in years three to five and the second term “without being blown off course”’.<sup>185</sup> Or again, with the Chancellor’s early commitment to continuing the Conservatives’ Private Finance Initiative (PFI) and Public-Private Partnerships (PPPs), as ‘a way of demonstrating that [Labour] ... could do business with the City’.<sup>186</sup> The common thread is the management of the existential conflict between the City and a Labour Government. This management, as we shall see in Chapter 2, has for over a decade been ‘steered’ by Gordon Brown’s Treasury and by members of City institutions. The former Chancellor’s choice of the Rt Hon. Alistair Darling, MP, as his successor, suggested a continuance of the same approach. It is what Gordon Brown has himself referred to as ‘credible socialism’, ‘to be socialist and at the same time credible’.<sup>187</sup> Thus, in November 1999, we find Gordon Brown announcing that:

‘The reforms made and the reforms to be made today reflect our resolve that Britain must leave behind the sterile, century-long conflict between enterprise and fairness – between the left, which promoted the good society at the expense of the good economy, and the right, which promoted the good economy at the expense of the good society, and too often achieved neither. Only by pursuing enterprise and fairness together – enterprise and fairness for all – can we equip all of Britain for our future and secure rising living standards for all.’<sup>188</sup>

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the former Chancellor learnt from his political ‘hero’, James Maxton, *loc. cit.*, showing that this is far from idle speculation.

<sup>185</sup> See Keegan, n. 85 above, p. 242.

<sup>186</sup> *Ibid.*, p. 269 (quoting an unnamed ‘Treasury official closely involved’).

<sup>187</sup> See Peston, n. 76 above, p. 21, quoting a 1997 speech in commemoration of Anthony Crosland (1918-1977).

<sup>188</sup> See Hansard HC, 9 November 1999, col. 883 (‘Pre-Budget Statement’).

Redolent though it is of the ‘Third Way’,<sup>189</sup> this is a clear affirmation of politics as being about the management of potential conflict and thus as the art of government. What is important about ‘prudence’, says Loughlin, is that ‘[i]t is to be distinguished from rule-governed action or from following the precepts of conventional morality primarily because new situations require innovative responses’.<sup>190</sup> In the case of Gordon Brown, it has meant an effort to meet the challenges and opportunities presented by global business with prudence. Nowhere, perhaps, has this been demonstrated more decisively than in May 1997, in the ‘hollowing out’ of the Treasury’s responsibilities, by the transfer of responsibility for the control of interest rates from the Treasury to the Bank of England.<sup>191</sup> In the specific context of corporation tax reform, it has meant harnessing the NPM reforms of the 1980s to the development of co-operation between HMRC and the corporate sector.<sup>192</sup> This is something which the latter has seemed extremely keen to encourage,<sup>193</sup> despite occasional threats to ‘withdraw support from the government if taxes on business income rise any further’.<sup>194</sup>

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<sup>189</sup> See Anthony Giddens, *The Third Way; the Renewal of Social Democracy* (Oxford: Polity Press, 1998), ch. 3, and Anthony Giddens, *The Third Way and its Critics* (Cambridge: Polity Press, 2000), ch. 3.

<sup>190</sup> See Loughlin, n. 112 above, p. 38. Moreover, ‘... the limits of laws should be ... acknowledged and rulers might find it necessary, for the promotion of the common good, to break promises, to proceed deceptively or act belligerently’ (*ibid.*, referring to Machiavelli’s account of Florence’s ruler between 1502 and 1512, Piero Soderini, and his fatal patience and unfailing good nature (see Niccolò Machiavelli, *The Discourses*, ed. and trans. by Bernard Crick, Leslie J. Walker and Brian Richardson (London: Penguin, 2003), p. 431).

<sup>191</sup> See Peston, n. 76 above, p. 112.

<sup>192</sup> e.g. as in the establishment of the Government’s Business Tax Forum (see Parker, *Financial Times*, 24 February 2004, 1); also the *2006 Review of Links with Large Business: November 2006* (Chair, Sir David Varney) (London: HMRC, 2007); also HMRC, *Giving Certainty to Business through Clearances and Advance Agreements: Consultation Document 20 June 2007* (London: HMRC, 2007); also Wharrad, *Tax Journal*, 2 July 2007, 17; Houlder, *Financial Times*, 25 July 2007, 4. See Chapter 2 below.

<sup>193</sup> See, e.g., *Financial Times*, 2 November 2004, 18 (letter from Loughlin Hickey, KPMG); also Houlder, *Financial Times*, 17 November 2006, 3; also Houlder, *Financial Times*, 21 June 2007, 3.

<sup>194</sup> See Houlder, *Financial Times*, 7 November 2005, 3. Peston, n. 76 above, reports that Gordon Brown ‘is neurotically fearful of the damage that can be done to the poorest through a policy of redistribution that would drive wealth creators to countries with lower taxes’ (*ibid.*, p. 21).

The politics of corporation tax have never, no doubt for the reasons discussed in the second part of the chapter, received systematic academic consideration in the UK context. The topic has, however, been discussed by Radaelli, in the context of a UK/Italian comparative study, from the late 1990s.<sup>195</sup> Though valuable – reference will be made to it later in the study – it does not attempt to reach into the essence of what is ‘political’ in UK corporation tax reform, and it is heavily reliant on Gammie’s<sup>196</sup> views of the reform process. Possibly because he is concerned with developments related to the European and international level theme, Radaelli seems to follow a combination of Heywood’s second and third concepts of politics<sup>197</sup> and, although he concedes that ‘[p]olitics generates conflict’,<sup>198</sup> sees the salvation of any project to harmonise corporate taxation within the EU as being the slow but steady ‘politicization’ of a project originally conceived in purely ‘technocratic’ terms.<sup>199</sup> In short, like the theoretical literature referred to above, in the second part of the chapter, it understates the ‘political’ in ‘political economy’, in the particular context of corporation tax reform.

The study’s conception of corporation tax reform as a public law enterprise next requires us to consider some of the contours of public law discourse, and to seek some explanation of the significance of ‘theory’ and ‘values’ within it.

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<sup>195</sup> See Radaelli, n. 127 above, pp. 125-131.

<sup>196</sup> See n. 47 above.

<sup>197</sup> See n. 157 above.

<sup>198</sup> See Claudio M. Radaelli, *Technocracy in the European Union* (London: Longman, 1999), p. 154. (In the light of the previous discussion, this seems a curious inversion of the elements at play here.)

<sup>199</sup> *Ibid.*, ch. 7. See also Claudio M. Radaelli, ‘The Political Economy of EU Direct Tax Policy’, in *Contemporary Issues in Taxation Research*, ed. by Andy Lymer and David Salter (Aldershot: Ashgate Publishing, 2003), pp. 145-165.

One of the most intriguing features of the notion of public law in the UK is the elusiveness of some reassuringly straightforward definition of the term itself.<sup>200</sup> This, no doubt, is due to the relatively late appearance - during only the early 1980s - of the expression 'public law' in the mouths of British judges.<sup>201</sup> McEldowney notes the traditional absence of the public/private distinction<sup>202</sup> in quoting van Caenegem's observation that:

'Until the nineteenth century, and even beyond, English doctrine proudly maintained that, unlike the continent, England knew no separate public law or public-law courts: the traditional common law assumed that the law was indivisible in the sense that the same body of rules applied to the government and its agents as well as to private citizens.'<sup>203</sup>

Allowing for this historical phenomenon, McEldowney does, however, make the allusion to the 'traditional' English viewpoint having already characterised public law as '... broadly referring to the relationship between the citizen and the state'.<sup>204</sup> The cautious generality of his definition, especially given the mainly student readership of McEldowney's wide ranging account, should not however be taken to restrict its scope to the relationship between the state and human agents. Nor should it, with its implicit emphasis on civil liberties, be taken to restrict the concept of public law to matters of law and order. Whilst it is undoubtedly

<sup>200</sup> Unlike, e.g., in Roman law (see *The Digest of Justinian*, ed. and trans. by Theodor Mommsen, Paul Krueger and Alan Watson (Philadelphia: Pennsylvania, 1985), p. 1 (Book One, I.1.2. ('*de iustitia et iure*')), which reads, in part: '*publicum ius est quod ad statum rei Romanae spectat*' ('public law is that which relates to the Roman state'))).

<sup>201</sup> See Barendt, n. 106 above, para. 1.08. See *Davy v. Spelthorne Borough Council* [1984] AC 262, 276 (Lord Wilberforce); but also *O'Reilly and Others v. Mackman and Others* [1983] AC 237, 273-285 (Lord Diplock).

<sup>202</sup> See McEldowney, also n. 106 above, para. 8-001.

<sup>203</sup> See R.C. van Caenegem, *An Historical Introduction to Western Constitutional Law* (Cambridge: Cambridge University Press, 1995), p. 3; also H. Patrick Glenn, *Legal Traditions of the World*, 2<sup>nd</sup> edn (Oxford: Oxford University Press, 2004), p. 234n; also N.E. Simmonds, *The decline of*

correct to emphasise the ultimately human ownership of the joint-stock corporation or corporate group,<sup>205</sup> it is unnecessary so to do in order to bring the relationship between the state and legal persons within the ambit of public law as conceived of in the UK. As long ago as 1973, the Royal Commission on the Constitution<sup>206</sup> highlighted the importance of the relationship between the state and the corporation, in promoting national prosperity and managing the economy.<sup>207</sup> No doubt taking account of factors such as these, although not with an eye specifically on tax as public law, Birkinshaw offers the following definition of the term:

‘Public law denotes that system of law that deals with our public affairs. It denotes the public sphere, defines its extent, the relationship between different tiers in the public sphere and between those tiers and individuals, corporate or personal, citizen or alien. Public law is primarily concerned with the exercise or non-exercise of public power, sometimes by private actors, and its fairness, rationality, legality and proportionality.’<sup>208</sup>

The usefulness of this definition to the study should perhaps be underlined. First, and most importantly, it was made in the context of an analysis of the ways in which UK public law has been influenced by both the public law of the EU and that of its individual Member States.<sup>209</sup> Understood not as ‘... a distinct body of law applied in a distinct body of courts or

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*juridical reason: Doctrine and theory in the legal order* (Manchester: Manchester University Press, 1984), pp. 130-131.

<sup>204</sup> See McEldowney, n. 106 above, para. 1-003.

<sup>205</sup> See Kay, n. 132 above.

<sup>206</sup> See *Royal Commission on the Constitution 1969-1973, vol. I, Report: Presented to Parliament by Command of Her Majesty October 1973* (Cmnd 5460) (London: HMSO, 1973), p. 76.

<sup>207</sup> As witness the prominence which Loughlin gives both to this point and to the Royal Commission report (see Loughlin, n. 162 above, p. 12).

<sup>208</sup> See Patrick Birkinshaw, *European Public Law* (London: Butterworths LexisNexis, 2003), p. 562.

<sup>209</sup> As to which note, e.g., the French law concept of *droit public interne*, consisting of *le droit constitutionnel et politique* and *le droit administratif* (see *A Source-Book on French Law – Public Law: Constitutional and Administrative Law; Private Law: Structure, Contract – Kahn-Freund, Lévy, Rudden*, ed. by Bernard Rudden, 3<sup>rd</sup> edn (Oxford: Clarendon Press, 1991), p. 19 (extracting J.-M. Auby et R. Ducos-Ader, *Droit Public* (1966), vol. 1, pp. 1-7)); also, generally, L. Neville Brown and John S. Bell, *French Administrative Law*, 4<sup>th</sup> edn (Oxford: Clarendon Press, 1993), ch.

jurisdiction ... [but as] a body of evolving principles, shaped by a variety of jurisdictions and their mutual intercourse',<sup>210</sup> it is something to which we shall briefly return later in the study. Here, it is sufficient to note that any discussion of UK public law must take account of the public law of the EU, not least when it comes to assessing the influence of the EU on UK tax policy.<sup>211</sup> Secondly, in describing public law as a 'system of law', Birkinshaw elsewhere makes explicit the fact that it comprehends what he refers to as 'regulatory law', and he instances as falling within this category '[c]ompetition, data protection, environmental protection and access to environmental information, procedures for public procurement *and so on ...*'.<sup>212</sup> This acceptance of public law as including forms of regulation is emphasised, too, by Loughlin, who describes the practitioner's 'loose-leaf encyclopaedias' on subjects such as these, rather than 'some slim constitutive document' as symbolic of '[t]he empirical world of public law'.<sup>213</sup> The claim of tax law and policy to be included in such a list, something already referred to,<sup>214</sup> is developed in the next part of the present chapter. That public law also relates to the behaviour of the institutional actors involved in regulatory law and policy, not all of which may be 'public' actors, is the third feature of Birkinshaw's definition that we should note. Public law is applicable, not only to the exercise of governmental power but also, as its practitioners would doubtless expect, to the non-exercise of that power.<sup>215</sup> Finally, as Birkinshaw tells us, certain values, such as fairness, are to be regarded as part of public law. A principal concern of the study will be to demonstrate that the list of values is not a closed one, and that its content, no less than the emphasis to be

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1); also John Bell, *French Legal Cultures* (London: Butterworths, 2001), pp. 30-31 and chs 5 and 6.

<sup>210</sup> See Birkinshaw, n. 208 above, pp. 578-579.

<sup>211</sup> See the European and international theme in corporation tax reform identified above.

<sup>212</sup> See Birkinshaw, n. 208 above, p. 563 [*emphasis added*].

<sup>213</sup> See Loughlin, n. 114 above, p. 241.

<sup>214</sup> See Thuronyi, n. 107 above, *ibid*.



placed on particular values over others, will vary according to the policy area under consideration. Recent years have seen a sometimes acrimonious debate about the sources and scope of public law values, the contours of which we shall need to explore as a preliminary to interrogating the place of corporation tax within public law.

### **‘Values’ in public law**

In line with the preceding discussion, the present study envisages the British constitution as what might be described as a teleologically defined and ordered configuration of values.<sup>216</sup> In doing so, it emphasises that these ‘values’ – or ‘principles’ – are what W.B. Gallie characterised as ‘essentially contested concepts’.<sup>217</sup> In other words, the content of these values, as well as their relationship with each other, is conditioned by what we think public law is all about. In the context of the study, it has been decided not to follow the example of Sheffield school writers and refer to these as ‘rule of law values’, since the use of that term is controversial, both as to the nature and scope of the values themselves and their relationship to what Dicey<sup>218</sup> referred to as ‘the rule of law’.<sup>219</sup>

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<sup>215</sup> See Ian Harden and Norman Lewis, *The Noble Lie: The British constitution and the rule of law* (London: Hutchinson, 1986), ch. 8.

<sup>216</sup> See Terence Daintith and Alan Page, *The Executive in the Constitution: Structure, Autonomy and Internal Control* (Oxford: Oxford University Press, 1999), p. 18.

<sup>217</sup> See W.B. Gallie, ‘Essentially Contested Concepts’ (1955-1956) 56 *Aristotelian Society (Proceedings)* 167-198; also William E. Connolly, *The Terms of Political Discourse*, 3<sup>rd</sup> edn (Oxford: Blackwell, 1993), pp. 10-12, 225-231.

<sup>218</sup> Albert Venn Dicey (1835-1922), barrister, fellow of Trinity College, Oxford. A ‘double first’, he was distinguished as a technical lawyer (*Dicey and Morris on the Conflict of Laws* is still in print), as a theorist (see the text above) and as a pamphleteer (vociferously opposed, as he was, to Irish Home Rule). He also had a successful career at the Bar and became a Queen’s Counsel in 1890 (see *ODNB*).

<sup>219</sup> See A.V. Dicey, *Introduction to the Study of the Law of the Constitution*, ed. by E.C.S. Wade, 10<sup>th</sup> edn (London: Macmillan, 1965), Part II. Earlier, in a carefully wrought account, Hearn had described a similar idea of ‘the supremacy of the law’ (see William Edward Hearn, *The Government of England: its Structure and its Development*, 2<sup>nd</sup> edn (London: Longmans, Green, 1887), esp. pp. 89-91).

Ever since the publication in 1986 of Harden and Lewis's *The Noble Lie*,<sup>220</sup> its highly critical reception - significantly by Loughlin<sup>221</sup> - and the latter's own contributions, *Public Law and Political Theory*, in 1992,<sup>222</sup> and *The Idea of Public Law*, in 2003,<sup>223</sup> much attention has been focussed on the respective roles of 'values' and 'theory' in public law. Even more recent contributions, by Cane<sup>224</sup> and by Craig,<sup>225</sup> no less than by Loughlin himself,<sup>226</sup> have, as is said, 'breathed new life' into the debate. Difficult as it is to do justice to the complexities of the controversy, yet, in the context of the present study, its main insights are important and rewarding. It is to these that we turn next, in analysing the significance of 'rule of law values' to the present endeavour, and the reasons why we have opted to refer simply to 'values'.

The catalyst of the debate, as indicated above, is Harden and Lewis's *The Noble Lie*, a work which focussed attention on the possibility of conceiving of public law in terms of certain 'values', arrived at by a process of what its authors described as '[a]n immanent critique'.<sup>227</sup> Pre-eminent among those values were the 'open and accountable conduct of government and public affairs',<sup>228</sup> and their existence enabled a remodelling of Dicey's

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<sup>220</sup> See n. 215 above.

<sup>221</sup> See Martin Loughlin (1988) 51 MLR 531-548 ('Review Article'); also 'The Pathways of Public Law Scholarship', in *Frontiers of Legal Scholarship: Twenty five years of Warwick Law School*, ed. by Geoffrey P. Wilson (Chichester: John Wiley, 1995), pp. 163-188, esp. 176-179; also the much less critical reception to *The Noble Lie* accorded by Trevor Smith [1987] PL 642-643 (book review).

<sup>222</sup> See n. 114 above.

<sup>223</sup> See n. 162 above. There is also a third book, to which occasional reference will be made, but this offers a conspectus of existing learning, rather than formulating a new theory (see Martin Loughlin, *Sword and Scales: An Examination of the Relationship between Law and Politics* (Oxford: Hart Publishing, 2000).

<sup>224</sup> See Peter Cane, 'Theory and Values in Public Law', in *Law and Administration in Europe: Essays in Honour of Carol Harlow*, ed. by Paul Craig and Richard Rawlings (Oxford: Oxford University Press, 2003), pp. 3-21.

<sup>225</sup> See Paul Craig, 'Theory and Values in Public Law: A Response', in *ibid.*, pp. 23-46.

<sup>226</sup> See Martin Loughlin, 'Theory and Values in Public Law: An Interpretation' [2005] PL 48-66.

<sup>227</sup> See Harden and Lewis, n. 215 above, p. 10.

<sup>228</sup> *Ibid.*, p. 288.

somewhat restrictive notion of ‘the supremacy or the rule of law’.<sup>229</sup> It was not to be seen simply in terms of Dicey’s three ‘distinct though kindred conceptions’<sup>230</sup> of the ‘absence of arbitrary power’;<sup>231</sup> the universal application of ‘the ordinary law administered by ordinary tribunals’;<sup>232</sup> and the contribution of ‘judicial decisions determining the rights of private persons in particular cases brought before the courts ...’.<sup>233</sup> Instead, the rule of law was to be viewed as a transcendent concept<sup>234</sup> and ‘master ideal’,<sup>235</sup> which consisted of values (‘rule of law values’)<sup>236</sup> facilitating ‘... the exclusion of arbitrariness: the minimization of the contribution of naked social, economic and physical power to public life’.<sup>237</sup> If it was possible so to conceive of public law, then it was also possible to analyse existing institutions, processes and policy solutions in such terms. Ultimately, such an approach would, so Harden and Lewis claimed, yield ‘... a new descriptive and analytical model of constitutionally legitimate action in Britain’.<sup>238</sup> Even today, 20 years on, the authors’ excitement at their creation is palpable on every well-thumbed page of the remaining library copies of *The Noble Lie*. It was an ambitious claim and, had it been somewhat less aggressively or uncompromisingly argued, it might not have collided so violently with other strands of scholarly opinion.<sup>239</sup>

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<sup>229</sup> See Dicey, n. 219 above, Part II.

<sup>230</sup> *Ibid.*, p. 187.

<sup>231</sup> *Ibid.*, p. 188 (marginal note).

<sup>232</sup> *Ibid.*, p. 193 (marginal note).

<sup>233</sup> *Ibid.*, p. 195.

<sup>234</sup> See Harden and Lewis, n. 215 above, p. 17.

<sup>235</sup> *Ibid.*, p. 13 (quoting Philip Selznick, *Law, Society and Industrial Justice* (New York: Russell Sage Foundation, 1969), p. 28).

<sup>236</sup> See Harden and Lewis, n. 215 above, p. 302.

<sup>237</sup> *Ibid.*

<sup>238</sup> *Ibid.*, p. 7.

<sup>239</sup> See, e.g., Loughlin (1988), n. 221 above, *passim*.

What is important about Harden and Lewis's approach is that, to the extent that it deliberately addressed itself to areas of the constitution other than human rights,<sup>240</sup> its argument occupies a different intellectual space from the arguments over rights that have become a feature of public law discourse. Moreover, although, as Daintith has pointed out,<sup>241</sup> the authors' selection of values, like that of others in search of a 'structure of values',<sup>242</sup> 'is inherently open to question', and, despite the fact that the '... chosen values ... may not be precise enough to guide decision-making in practice or to test its legitimacy',<sup>243</sup> conceiving of the constitution as a configuration of values has one pre-eminent virtue. It is, as Daintith and Page elegantly conclude, the only vision of the constitution '... which might be capable both of accommodating norms of executive self-management as part of the constitution ...'.<sup>244</sup> In the context of our analysis of corporation tax policy, policy conducted, as we shall see, often without the accountability mechanisms applicable to other areas of governmental activity, this is a particularly important point. Nonetheless, the difficulties inherent in Harden and Lewis's method need to be addressed, and Loughlin, who can only be described as 'antagonistic' to their approach, suggests a number of theoretical elements, which, for present purposes, may usefully be made to illuminate it. It should be stressed, however, that

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<sup>240</sup> See Harden and Lewis, n. 215 above, p. 310.

<sup>241</sup> See the discussion in Terence Daintith, 'Comment on Lewis: Markets, Regulation and Citizenship', in *Law and The Public Interest: Proceedings of the 1992 ALSP Conference*, ed. by Roger Brownsword (Stuttgart: Franz Steiner, 1993), pp. 140-146.

<sup>242</sup> See, e.g., Patrick McAuslan, 'Administrative Law, Collective Consumption and Judicial Policy' (1983) 46 MLR 1-20; T.R.S. Allan, *Law, Liberty, and Justice: The Legal Foundations of British Constitutionalism* (Oxford: Clarendon Press, 1993); also T.R.S. Allan, *Constitutional Justice: A Liberal Theory of the Rule of Law* (Oxford: Oxford University Press, 2001); also Sir John Laws, 'Is the High Court the Guardian of Fundamental Constitutional Rights?' [1993] PL 59-79 and Sir John Laws, 'Law and Democracy' [1995] PL 72-93.

<sup>243</sup> See Daintith and Page, n. 216 above, p. 18.

<sup>244</sup> *Ibid.*

Loughlin does not himself present them as elucidations of Harden and Lewis's thesis;<sup>245</sup> they are instead elements of his own, entirely distinctive, public law method.

Since we shall not be adopting the term 'rule of law values', it is necessary to explain the rationale for the decision. In favour of its use is the fact that, as Cane makes clear,<sup>246</sup> it is now widely accepted that English public law has certain 'immanent' values. He himself lists a number of illustrative values, four of which are as follows: 'representation', the idea that, being democratically sanctioned, legislation takes priority over judge-made law; 'accountability' which, among other things '... underpins ... the principle that governmental power must be exercised according to law'; 'participation', that is, in the sense that individuals should have the opportunity to participate in governmental processes,<sup>247</sup> and 'transparency', a value now illustrated by the 'right to know' provided by the Freedom of Information Act 2000.<sup>248</sup> Cane's list – any such list, indeed – is not a closed one, and, in specifically including accountability and transparency (what used to be called 'openness'), is obviously similar to that of Harden and Lewis. Although Loughlin does not find satisfactory Harden and Lewis's identification of these values with 'the rule of law',<sup>249</sup> and, although he does so specifically in reference to Cane's arguments, the existence of these 'immanent values' is something that even he accepts.<sup>250</sup> Where Loughlin differs from Cane, and presumably from Harden and Lewis also, is in reference to the significance that these values have. They may - or may not - be 'legal' in origin, but they are less significant, in Loughlin's

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<sup>245</sup> In fact, 'Loughlin does no more than mention the work of Harden and Lewis in passing' (see Prosser [1993] PL 346-357, 353 (Review Article)). But see Loughlin (1995), n. 221 above, pp. 176-179.

<sup>246</sup> See Cane, n. 224 above, pp. 14-17.

<sup>247</sup> *Ibid.*, pp. 15-16.

<sup>248</sup> As to the general provisions of which, see *O. Hood Phillips & Jackson: Constitutional and Administrative Law*, ed. by Paul Jackson and Patricia Leopold, 8<sup>th</sup> edn (London: Sweet and Maxwell, 2001), paras 26-029-26-031.

<sup>249</sup> See Loughlin (1988), n. 221 above, p. 540.

<sup>250</sup> See Loughlin, n. 226 above, p. 59.

view, than the theory which makes sense of them. This reflects the functionalist, rather than normativist, nature of Loughlin's approach. It is something to which we shall return in a moment; for the present, it is important simply to note a general willingness to assent to values such as accountability, openness, representation and participation. That said, although the general assent to these values might speak in favour of the use of 'rule of law values', the difficulty with using the 'rule of law' in the expression may require some further elaboration. In its 'Diceyan' sense, after all, the rule of law seems to have three fairly specific components. Accountability, which informs the principle that the power of government must be exercised according to law, is certainly within the spirit, if not the letter, of the second of Dicey's three 'kindred conceptions'. The 'classical' conception of the rule of law, broader than Dicey's uniquely British one, and going back at least as far as Aristotle<sup>251</sup> and forward as far as Rawls,<sup>252</sup> does indeed speak to values or principles.<sup>253</sup> Finally, even if, as discussed below, we characterise the immanent values of public law as in origin political, rather than legal, it could be argued that the political dimension to the classical rule of law means that there is no inherent contradiction in speaking of 'rule of law values'. As Allan says of its British conception: 'Allegiance to the rule of law is not ... a technical (or even "lawyerly") commitment: it is necessarily allegiance to a political philosophy – albeit a practical philosophy grounded in existing constitutional tradition'.<sup>254</sup> The problem with using the expression 'rule of law values', however, is that it fits uneasily with the approach to be taken in the study. This is essentially a functionalist inquiry, and the expression 'rule of law

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<sup>251</sup> See Aristotle, *The Nicomachean Ethics*, ed. and trans. by J.A.K. Thomson, Hugh Tredennick and Jonathan Barnes (London: Penguin, 2004), pp. 129, 156; also van Caenegem, n. 203 above, pp. 17-21; also Loughlin, n. 223 above, pp. 69-70.

<sup>252</sup> See John Rawls (1921-2002), *A Theory of Justice*, rev. edn (Oxford: Oxford University Press, 1999), pp. 206-213.

<sup>253</sup> See Allan, n. 242 above, ch. 2. But see Judith Shklar, 'Political Theory and the Rule of Law', in *The Rule of Law: Ideal or Ideology?*, ed. by A.C. Hutchinson and P. Monahan (Toronto: Carswell, 1987), pp. 1-16.

values’ seems too closely associated with a liberal normativist approach, with a view of the ‘rule of law’ as somehow existing outside politics.

### **‘Theory’ in public law**

Acerbic as it often is, Loughlin’s writing brings an acute awareness of the historical development of British political theory to the debate on public law. Our main business in this chapter is with *Public Law and Political Theory*,<sup>255</sup> although it will be necessary to refer to various aspects of Loughlin’s development of its thesis as the study progresses. Unavoidable though Dicey is, for Loughlin, he is not where the debate on public law begins. Loughlin’s earlier work starts by identifying the particular nature of Dicey’s project: ‘Dicey’s objective ... [was] to sever links and to establish [constitutional law as] an autonomous subject’. By contrast, the eighteenth century thinkers of the Scottish Enlightenment,<sup>256</sup> pre-eminently Smith himself, whose work on taxation has already been mentioned, had been concerned to build up a complete ‘science of legislation’.<sup>257</sup> Far from trying to unravel the task of law in constitutional theory, Smith, and later Millar,<sup>258</sup> took a range of political, social and legal thought, with the object of drawing general conclusions by making connections between the disciplines. Even the *Wealth of Nations* of 1776<sup>259</sup> was only a segment of what, in Smith’s case, was an unfinished ‘scheme for constructing a complete social philosophy’.<sup>260</sup>

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<sup>254</sup> See Allan, n. 242 above, pp. 21-22.

<sup>255</sup> See n. 114 above.

<sup>256</sup> See Roy Porter, *Enlightenment: Britain and the Creation of the Modern World* (London: Penguin, 2000), pp. 242-257.

<sup>257</sup> See Loughlin, n. 114 above, pp. 4-13.

<sup>258</sup> John Millar (1735-1801) was Regius Professor of Law at the University of Glasgow (1761-1801) and author of *An Historical View of the English Government* (1787) (see Knud Haakonssen, ‘John Millar and the Science of a Legislator’ (1985) *Juridical Review* 41-68) (see also *ODNB*).

<sup>259</sup> See Smith, n. 96 above.

<sup>260</sup> See Loughlin, n. 114 above, p. 5.

For Loughlin, ‘theory’, not ‘values’, is at the heart of public law. Values – or principles – have a role to play, but even they are shaped by theory. He accordingly identifies what he terms ‘normative’ and ‘functionalist’ theoretical approaches to the subject.<sup>261</sup> Normative theory, which ‘reflects an ideal of the autonomy of law’,<sup>262</sup> is associated, in its liberal form, with Hayek,<sup>263</sup> especially in *Law, Legislation and Liberty*,<sup>264</sup> and Nozick,<sup>265</sup> in *Anarchy, State, and Utopia*.<sup>266</sup> Its conservative variant, which is ‘the dominant tradition of public law thought’,<sup>267</sup> finds its most eloquent expression in Oakeshott,<sup>268</sup> especially in his final work, dealing with law and government, *On Human Conduct*.<sup>269</sup> Normative theory, which begins with Dicey, is, says Loughlin, ‘rooted in a belief in the ideal of the separation of powers and in the need to subordinate government to law’.<sup>270</sup> The failure of normativism to reflect, not only history, but also rapid change, has made it largely irrelevant, however.<sup>271</sup> Although Oakeshott’s work remains valuable, conservative normativism has been overtaken by the pace of change,<sup>272</sup> while normativism’s liberal variant ‘fails on grounds of historical fact’.<sup>273</sup>

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<sup>261</sup> *Ibid.*, pp. 59-61. Craig did not agree with the ‘normative’/‘functionalist’ labels (see Craig [1993] LS 275-283, 276).

<sup>262</sup> See Loughlin, n. 114 above, p. 60.

<sup>263</sup> *Ibid.*, p. 84 (Friedrich August von Hayek (1899-1992)). Philosopher and Nobel Prize-winning economist (1974); though born in Austria, Hayek’s works were produced mainly in the UK (he was Tooke Professor of Economic Science in London University between 1931 and 1950) and the United States, where he was held a chair of social and moral science at the University of Chicago, from 1950 to 1962 (see *ODNB*). His work had a profound influence on Lady Thatcher (see Margaret Thatcher, *The Path to Power* (London: HarperCollins, 1995), pp. 50-51).

<sup>264</sup> F.A. Hayek, *Law, Legislation and Liberty: A new statement of the liberal principles of justice and political economy* (London: Routledge and Kegan Paul, 1982).

<sup>265</sup> See Loughlin, n. 114 above, p. 94 (Robert Nozick (1939-2002)) (see *ODNB*).

<sup>266</sup> Robert Nozick, *Anarchy, State, and Utopia* (Oxford: Blackwell, 1980).

<sup>267</sup> See Loughlin, n. 114 above, p. 139.

<sup>268</sup> *Ibid.*, p. 64. See n. 165 above.

<sup>269</sup> (Oxford: Clarendon Press, 1975). This work might be seen as complimentary to H.L.A. Hart’s, *The Concept of Law* (Oxford: Clarendon Press, 1961).

<sup>270</sup> See Loughlin, n. 114 above, pp. 60, 144; also Rodney Barker, *Political Ideas in Modern Britain* (London: Methuen, 1978), pp. 193-194.

<sup>271</sup> Loughlin’s view of ‘liberal normativism’ reflects something of Huxley’s definition of tragedy (quoted in Guy Chapman, *A Passionate Prodigality: Fragments of Autobiography* (London: MacGibbon and Kee, 1965), p. 68).

<sup>272</sup> See Loughlin, n. 114 above, p. 237.



By contrast, ‘the functionalist style has a certain affinity with a political theory of socialism’, or, more accurately, can be identified with ‘those who adopt a collectivist social ontology’.<sup>274</sup> Functionalism:

‘... views law as part of the apparatus of government. Its focus is upon law’s regulatory and facilitative functions and therefore is oriented to aims and objectives and adopts an instrumentalist social policy approach. Functionalism reflects an ideal of progressive evolutionary change.’<sup>275</sup>

Chief among functionalists, historically, has been Duguit<sup>276</sup> who, in his *Law in the Modern State*,<sup>277</sup> sought to create an ‘empirical’ concept of public law, under the intellectual influence of the sociological positivism of Comte<sup>278</sup> and Durkheim.<sup>279</sup> Whilst it has been equipped to confront the growth of the regulatory state, functionalism ‘seems to have lost much of its power’,<sup>280</sup> given the ever more moribund ‘empiricist’ and ‘positivist’ forms that it has taken. Among modern ‘normativist’ writing, Loughlin instances<sup>281</sup> work by Wade (a conservative normativist and Dicey’s modern champion),<sup>282</sup> by Dworkin<sup>283</sup> (a liberal normativist, whose work is elaborated in the public law context by Allan,<sup>284</sup> Lester<sup>285</sup> and

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<sup>273</sup> *Ibid.*, p. 240.

<sup>274</sup> *Ibid.*, p. 105.

<sup>275</sup> *Ibid.*, p. 60.

<sup>276</sup> Duguit (1859-1928) was Professor of Law at the University of Bordeaux, from 1886 to 1928.

<sup>277</sup> Léon Duguit, *Law in the Modern State*, trans. by Frida and Harold Laski (New York: Howard Fertig, 1970). See Martin Loughlin, ‘The Functionalist Style in Public Law’ (2005) 55 *University of Toronto Law Journal* 361-403, 368-374.

<sup>278</sup> Isidore Auguste Marie François Xavier Comte (1798-1857). See Frank E. Manuel, *The Prophets of Paris: Turgot, Condorcet, Saint-Simon, Fourier, and Comte* (New York: Harper and Row, 1965), ch. 6.

<sup>279</sup> Emile Durkheim (1858-1917). See Gianfranco Poggi, *Durkheim* (Oxford: Oxford University Press, 2000), ch. 6, esp. pp. 100-101.

<sup>280</sup> See Loughlin, n. 114 above, p. 235.

<sup>281</sup> *Ibid.*, pp. 207-208.

<sup>282</sup> See H.W.R. Wade, ‘Law, Opinion and Administration’ (1962) 78 LQR 188-204, esp. 189-190.

<sup>283</sup> See Ronald Dworkin, *Taking Rights Seriously* (London: Duckworth, 1977); Ronald Dworkin, *A Matter of Principle* (Cambridge, Mass.: Harvard University Press, 1985); and Ronald Dworkin, *Law’s Empire* (Cambridge, Mass.: Belknap Press, 1986).

<sup>284</sup> See now Allan (1993) and (2001), n. 242 above, *passim*.

Jowell<sup>286</sup>) and, finally, by Rawls.<sup>287</sup> Leading ‘functionalists’, by contrast, include McAuslan<sup>288</sup> and Griffith<sup>289</sup> but, although their functionalist approach is good, it needs to be revived.<sup>290</sup> Possibly, had he included it in this survey, Loughlin would regard the Sheffield school style as a fatally flawed, though nevertheless functionalist, style. What he does say is that systems theory, the relevance and claims of which we consider presently, might help to revivify the functionalist approach.<sup>291</sup>

### **An ‘interpretative’ and ‘functionalist’ approach**

The idea that ‘rule of law values’, in the sense considered above, cannot be satisfactorily reconciled with Loughlin’s theoretical approach does not, however, preclude the possibility of interrogating, in their proper context, immanent public law values. Thus, in order to be able to interpret the thematic development of some area of public law, it is necessary, not only to be able to identify its immanent values, but also to have some idea of the contexts in which one, or more, of them may have to give way to another, or to others. The role, for instance, which has been accorded to fairness in corporation tax reform might be one such question, and the contexts in which it has been made to give way to the value of efficiency

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<sup>285</sup> See Jeffrey Jowell and Anthony Lester, ‘Beyond *Wednesbury*: substantive principles of administrative law’ [1987] PL 368-382.

<sup>286</sup> See Jeffrey Jowell, ‘The Rule of Law Today’, in *The Changing Constitution*, ed. by Jeffrey Jowell and Dawn Oliver, 5<sup>th</sup> edn (Oxford: Oxford University Press, 2004), pp. 5-25.

<sup>287</sup> See Rawls, n. 252 above; *A Theory of Justice*, rev. ed. (Oxford: Oxford University Press, 1999); John Rawls, *Political Liberalism* (New York: Columbia University Press, 1993); also Samuel Freeman, *Rawls* (London: Routledge, 2007).

<sup>288</sup> See McAuslan, n. 242 above; also ‘Legitimacy and the Constitution: the dissonance between theory and practice’, in *Law, Legitimacy and the Constitution*, ed. by Patrick McAuslan and John F. McEldowney (London: Sweet and Maxwell, 1985).

<sup>289</sup> See, e.g., J.A.G. Griffith, ‘Comment’ (1963) PL 401-402; J.A.G. Griffith, ‘The Political Constitution’ (1979) 42 MLR 1-21.

<sup>290</sup> A view shared by Daintith and Page (see n. 216 above). Also Loughlin, n. 277 above, 402-403.

<sup>291</sup> See Loughlin, n. 114 above, p. 250.

would be another. The status of equity and efficiency as ‘values’ will be assessed in Chapter 4.

The important point at this juncture is that neither Cane, in speaking of ‘immanent’ values, nor Harden and Lewis, in talking about ‘rule of law values’, can explain how the values relate to each other. That they need to do so is explicitly recognised by Cane, who acknowledges, but does not resolve, the problems both that ‘[b]ecause the immanent values of (public) law are abstract, people may disagree about what concrete rules they require or justify ...’<sup>292</sup> and that ‘... public law values may be in competition with one another ...’.<sup>293</sup> The need for a theory which helps to identify and prioritise values is something which Loughlin does however specifically address:

‘We need to lay bare the conceptual structures through which we come to describe and explain the subject, and to understand the relations and features entailed in these structures and the assumptions on which they are founded. And we must subject the structures and assumptions which pervade public law thought to critical scrutiny.’<sup>294</sup>

What Loughlin proposes, as mentioned above, is a ‘revitalized functionalist style’<sup>295</sup> and he wonders whether, in the quest for such an approach, Luhmann’s<sup>296</sup> ‘sociological theory of

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<sup>292</sup> See Cane, n. 224 above, p. 17.

<sup>293</sup> *Ibid.*, p. 16.

<sup>294</sup> See Loughlin, n. 114 above, p. 36; also Loughlin, n. 226 above, p. 59.

<sup>295</sup> See Loughlin, n. 114 above, p. 250.

<sup>296</sup> (1927-1998). English-speaking commentators tend to be sceptical: see, e.g., J.W. Harries, *Legal Philosophies*, 2<sup>nd</sup> edn (London: LexisNexis, 1997), p. 251.

law’,<sup>297</sup> the biologically inspired theory of legal systems as ‘self-referential systems’<sup>298</sup> – as ‘autopoiesis’<sup>299</sup> – might prove illuminating. An autopoietic system, Luhmann tells us:

‘ ... constitutes the elements of which it consists through the elements of which it consists. ... [S]ocial systems [for instance, the legal system] can themselves be regarded as special kinds of autopoietic systems. [Such systems are ‘operationally closed’, in that] ... all operations always reproduce the system.’<sup>300</sup>

However, since a legal system consists of ‘normative expectations’<sup>301</sup> – not ‘cognitive’ ones<sup>302</sup> – it may be said to be ‘normatively closed’.<sup>303</sup> Normative closure means that ‘only the legal system can bestow legally normative quality on its elements and thereby constitute them as elements. Normativity has no purpose beyond this ...’.<sup>304</sup> Normatively closed as it is, however, a legal system is able to communicate with, and respond to, its environment, because it is ‘cognitively open’.<sup>305</sup> Such communication takes place through the concept of ‘structural couplings’, orderly systemic responses to outside influences.<sup>306</sup> It is thus that Luhmann is able to intone the mantra of law being ‘a normatively closed but cognitively

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<sup>297</sup> See Niklas Luhmann, *A Sociological Theory of Law*, trans. by Elizabeth King and Martin Albrow (London: Routledge and Kegan Paul, 1985), esp. ch. 2; Niklas Luhmann, ‘The Unity of the Legal System’, in *Autopoietic Law: A New Approach to Law and Society* (Berlin: Walter de Gruyter, 1988), pp. 12-35; Niklas Luhmann, *Law as a Social System*, ed. by Fatima Kastner, Richard Nobles, David Schiff, and Rosamund Ziegert (Oxford: Oxford University Press, 2004).

<sup>298</sup> See Loughlin, n. 114 above, p. 255.

<sup>299</sup> See Humberto R. Maturana and Francisco J. Varela, *Autopoiesis and Cognition: The Realization of the Living* (Dordrecht: Reidel Publishing, 1980), esp. pp. 63-72 (by Stafford Beer), 73-76; Michael King and Chris Thornhill, *Niklas Luhmann’s Theory of Politics and Law* (Basingstoke: Palgrave Macmillan, 2003), pp. 204-206.

<sup>300</sup> See Luhmann (1988), n. 297 above, pp. 14-15 (emphasis added).

<sup>301</sup> i.e. ones that do *not* need to be modified if disappointed.

<sup>302</sup> i.e. ones that *do* need to be modified in such circumstances (see Luhmann (1988), n. 297 above, p. 19).

<sup>303</sup> *Ibid.*, p. 20; Luhmann (2004), n. 297 above, pp. 107-109.

<sup>304</sup> *Ibid.*, p. 20. This normative ‘function’, as Freeman reminds us, differs from Hart’s ‘rule of recognition’ (see Hart, n. 269 above, p. 92ff) in that it ‘ ... is a part of the legal system and is distinctly separate from the society’ (see *Lloyd’s Introduction to Jurisprudence*, ed. by M.D.A. Freeman, 7<sup>th</sup> edn (London: Sweet and Maxwell, 2001), p. 701).

<sup>305</sup> See Luhmann (1988), n. 297 above, p. 20; Luhmann (2004), n. 297 above, pp. 109-113.

<sup>306</sup> See Luhmann (2004), n. 297 above, ch. 10.

open system'.<sup>307</sup> Whether Luhmann's systems theory, to the extent that it seeks to illuminate the processes by which a range of possible policy alternatives are narrowed down to the probable, is useful in helping us to interpret the reform of corporation tax, is something to which we shall return in Chapter 3.

The emphasis placed at the end of the previous paragraph on 'interpretation' is of considerable importance to the study as a whole. It seeks to take an interpretative approach to three distinct, yet interrelated, aspects of corporation tax reform: the institutions involved in it; the processes by which policy solutions have been reached; and the adopted solutions themselves.<sup>308</sup> In each of these areas, the seven themes identified at the beginning of the study have varying degrees of importance. The study recognises that, whilst it is possible, though difficult, to 'articulate the standards of objectivity relevant to different domains of inquiry',<sup>309</sup> positivism does not provide a satisfactory alternative because, as Loughlin says, 'in the field of law fact and value cannot be kept categorically distinct'.<sup>310</sup> So we must look for 'human purposes' and attempt to distil meaning from the processes by which policy solutions have been reached. Secondly, just as an interpretative approach is taken, so also it is intended that the discussion will be attentive to the history of the 15 or so years over which the seven themes have unfolded, particularly with regard to the implications for public law values and theory of the speed and scope of changes in global financial markets, and in approaches to public policy, especially NPM.<sup>311</sup> Indeed, the lack of a satisfactory historical dimension in the 'immanent critique' employed in Harden and Lewis's *The Noble Lie*<sup>312</sup>

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<sup>307</sup> See Loughlin, n. 114 above, pp. 255; Luhmann (2004), n. 297 above, p. 106.

<sup>308</sup> The reasons for approaching the material in this way are discussed in the next part of the chapter.

<sup>309</sup> See Richard J. Bernstein, *The Restructuring of Social and Political Theory* (Oxford: Basil Blackwell, 1976), p. 111.

<sup>310</sup> See Loughlin, n. 114 above, p. 36.

<sup>311</sup> See n. 72 above.

<sup>312</sup> See n. 215 above.

was the subject of one of Loughlin's most telling criticisms of that work.<sup>313</sup> Important though the historical dimension is, Loughlin also – thirdly - calls on students of public law to be critical, 'both in subjecting various interpretations to rational scrutiny and to inquiry in respect of empirical understandings of the functions of government and law'.<sup>314</sup> This means testing the relationships between the immanent values of public law by 'the basic canons of rationality (consistency, coherence and non-contradiction)'.<sup>315</sup> This will also be an important element in the discussion in subsequent chapters. Finally, in accordance with Loughlin's remaining injunction, the discussion will be 'empirical' in the sense that our interpretation will be 'rooted in an appreciation of government and the functions law is expected to perform in respect of those functions'.<sup>316</sup> However, it should be stressed that the purpose of the discussion is not to make proposals for further reform; the study has the much less ambitious objective of interpreting what is happening and suggesting aspects on which greater emphasis might be placed in the future.

Building on the approach discussed above, and in the light of the definitions offered at the beginning of this part of the chapter, it should now be possible to deepen our understanding of public law and possibly even to assent to Loughlin's functionalist and interpretative definition of the subject:

'Public law is a set of practices concerned with the establishment, maintenance and regulation of the activity of governing the state ... [T]he nature of these practices can be grasped only once that activity is conceptualised as constituting an autonomous sphere: the political realm.'<sup>317</sup>

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<sup>313</sup> See Loughlin (1988), n. 221 above, pp. 535, 546.

<sup>314</sup> See Loughlin, n. 114 above, p. 36.

<sup>315</sup> See Loughlin, n. 226 above, p. 59.

<sup>316</sup> See Loughlin, n. 114 above, p. 231.

<sup>317</sup> See Loughlin, n. 226 above, p. 58.

When speaking of corporation tax reform as an enterprise of public law, we do so in accordance with the ideas encapsulated in this formulation, although subject to the two main qualifications which have already been mentioned.<sup>318</sup> The scope of public law is indeed broad enough, as Loughlin, McEldowney and Birkinshaw each imply,<sup>319</sup> to refer to the relationship between the state and the corporation, whether in its national or in its multinational forms.

Defined as a ‘set of practices’, public law is not limited to formal types of law, such as legislation and case law, because it is an aspect of ‘the activity of governing the state’, which is the business of politics. Viewed in this light, aspects of the technical theme, such as ESCs and SPs, seem less aberrant than ‘analytical’ or ‘empiricist’ accounts of tax law,<sup>320</sup> as well as the occasional judicial pronouncement,<sup>321</sup> might otherwise lead us to believe. This, Loughlin’s view of the subject, is neither Cane’s legal positivism, nor the ‘law behind law’ of Allan and Laws.<sup>322</sup> It is that public law may be regarded, to use Loughlin’s own term, as ‘the third order of the political’.<sup>323</sup> Public law, and therefore corporation tax law, is fundamentally about governing – or governance – and the maintenance and regulation of this activity requires constant responsiveness to changing circumstances. To the extent that public law ‘operates in accordance with its own conceptual logic and remains free from gross manipulation by power-wielders’,<sup>324</sup> its ‘even-handedness’ helps to ‘create intimacy, shape identity, generate trust, and strengthen allegiance’.<sup>325</sup> Such a formulation might possibly be

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<sup>318</sup> See n. 120 above.

<sup>319</sup> See nn. 202 and 208 above.

<sup>320</sup> See, e.g., Lee, n. 56 above, paras [1.25]-[1.40].

<sup>321</sup> See, e.g., *Vestey (No. 2) v. IRC* [1979] 2 All ER 225, 233 (Walton J.); but also *R v. IRC, ex parte Fulford-Dobson* [1987] STC 344, 351 (McNeill J.)

<sup>322</sup> See Loughlin, n. 226 above, pp. 53-55. (See also n. 242 above.)

<sup>323</sup> See Loughlin, n. 112 above, pp. 40-42.

<sup>324</sup> *Ibid.*, p. 41.

<sup>325</sup> *Ibid.*, pp. 40-41.

regarded as a modern version of the rule of law but, unlike Harden and Lewis<sup>326</sup> and the Sheffield school, the study does not thereby attempt to rely on ‘rule of law values’. Since it operates in the realm of the political, the values of public law are political ones, and what we should at least ask of public law solutions is that they are coherent, consistent and non-contradictory. The more successful public law is in promoting these values within a rational theoretical framework, the greater the legitimacy – the political acceptability - of the solutions offered.

In seeking to interpret the various themes in corporation tax reform, therefore, it is essential to recognise that they have nothing to do with personal morality. It is no use, therefore, to appeal to generalised notions of morality,<sup>327</sup> to notions of honesty and dishonesty,<sup>328</sup> when attempting to distinguish, for instance, between acceptable and non-acceptable ways of attempting to avoid corporation tax. However, corporation tax reform has a great deal to do with Machiavellian prudence, with both political values and the theory that makes sense of them. As Loughlin points out:

‘In the interpretative mode, theory is to values what grammar is to vocabulary. The meaning of words such as ... accountability can be determined only by observing their grammar, the way in which they are set to work within a defined field.’<sup>329</sup>

Thus, corporation tax reforms are more likely to be successful the more HMG observes the ‘prudential necessity’ of ensuring that they reflect, not only political values, but a clear view of the theory that demonstrates, in the particular context, the importance of those values relative to each other. Equally, an interpretation of corporation tax reform is more likely to

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<sup>326</sup> See n. 215 above.

<sup>327</sup> As, e.g., Dave Hartnett, then Inland Revenue Director-General, Policy and Technical, appeared to do in a speech in 2003 (see Parker, *Financial Times*, 4 May 2004, 4).

<sup>328</sup> But see *Furniss (Inspector of Taxes) v. Dawson and related appeals* [1984] AC 474, 518 (‘a simple and honest scheme’ (Lord Brightman)).



be successful the more it reflects an appreciation of the ‘field’ in which political values have been deployed, as well as the way in which the deployment has taken place.

In the final part of the chapter, therefore we relate each of the above points to the specific policy area of corporation tax reform and, in so doing, draw out the theoretical framework on which the rest of the study is based.

## CORPORATION TAX AS PUBLIC LAW

Although, following devolution, the UK might almost be regarded as a federal state, its historically unitary nature,<sup>330</sup> together with the absence of a ‘slim constitutive document’,<sup>331</sup> has tended to militate against any necessity to define the concept of a tax for constitutional law purposes.<sup>332</sup> Whether the reference to ‘local taxes to fund local authority expenditure’ in the Scottish devolution scheme,<sup>333</sup> or those to ‘taxation’ in the European Treaty,<sup>334</sup> will eventually require the courts to pin the idea down, as the federal constitutions of a number of

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<sup>329</sup> See Loughlin, n. 226 above, p. 65.

<sup>330</sup> See Jackson and Leopold, n. 248 above, paras 2-001-2-005.

<sup>331</sup> See Loughlin, n. 213 above. Baker’s claim, that ‘the United Kingdom ... has never had a written constitution’ is too literal (see Baker, n. 113 above, p. 165). The 1653 Instrument of Government, which was in force between 1653 and 1660, under the Protectorate, covered Scotland and Ireland, as well as England and Wales (reproduced in Samuel R. Gardiner, *Constitutional Documents of the Puritan Revolution 1625-1660*, 3<sup>rd</sup> edn (Oxford: Clarendon Press, 1906), pp. 405-417).

<sup>332</sup> But see, e.g., *Aston Cantlow and Wilmcote with Billesley Parochial Church Council v. Wallbank and Another* [2001] EWCA Civ 713; [2002] Ch 51, para. 40 (Sir Andrew Morritt V.-C., holding chancel repair liability to be a tax), overruled by HL at [2003] UKHL 37; [2004] 1 AC 546 (esp. para. 133) (Lord Scott of Foscote, disagreeing with Morritt V.-C.’s analysis); also Paul K. Marchetti, ‘Distinguishing Taxes from Charges in the Case of Privileges’ (1980) 33 Nat. Tax Jo. 233-236.

<sup>333</sup> Scotland Act 1998, Sched. 5, Part II, Head A1.

<sup>334</sup> See Art. 90, European Treaty (ex 95) and, e.g., Case C-10/65, *Deutschmann v. Germany* [1968] CMLR 259; Case C-74/76, *Iannelli and Volpi v. Meroni* [1977] 2 CMLR 688. Article 90 is the European Treaty’s ‘national treatment obligation’ and, as such, is the equivalent, in relation to trade within the EU, of Art III(2), GATT 1994.

Commonwealth countries have done,<sup>335</sup> remains to be seen. For the present, the significance of a tax in UK law has largely centred on the prohibition in the 1689 Bill of Rights on ‘the levying of money for or to the use of<sup>336</sup> the Crown by pretence of prerogative without grant of Parliament’.<sup>337</sup> Since the prohibition refers to the ‘levying of money’, it has not resulted in the making of fine distinctions between taxes and distinct types of levy, but on the presence or absence of statutory authority for the levy in question.<sup>338</sup> Although Dicey devotes a separate chapter to ‘the revenue’,<sup>339</sup> this is mainly concerned with the rules under which revenue raised is expended, and, although he refers to the principle of the Bill of Rights, he does not analyse it in detail.<sup>340</sup> Unless some other approach can be found, therefore, those

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<sup>335</sup> See, especially, *Re Eurig Estate* (1999) 165 DLR (4<sup>th</sup>) 1; also the survey of the Commonwealth case law in Tiley, n. 57 above, pp. 3-5; also, for a comparative conspectus, see Thuronyi, n. 107 above, pp. 45-54.

<sup>336</sup> The wording ‘for or to the use of’ seems to encompass both the possibility of an outright grant of money to the Crown and also a grant on trust.

<sup>337</sup> Bill of Rights 1689, fourth indent (reproduced in Geoffrey Wilson, *Cases and Materials on Constitutional and Administrative Law*, 2<sup>nd</sup> edn (Cambridge: Cambridge University Press, 1976), pp. 2-6).). Previously, certain types of tax had been upheld under the royal prerogative in foreign policy (see *Bates’s case*, n. 168 above, and *R. v. Hampden* (1637) 3 St. Tr. 825). But see the 1653 Instrument of Government, n. 331 above, Recital 6, and Art. 30, and Adam Tomkins, *Our Republican Constitution* (Oxford: Hart Publishing, 2005), pp. 74-76, 83-87; also Toby Barnard, *The English Republic 1649-1660* (Harlow: Longman, 1982), pp. 38, 46-48.

<sup>338</sup> See, e.g., *Brewster v. Kidgill* (1697) 88 ER 1239; *Baker v. Greenhill* (1842) 114 ER 463, 470 (Lord Denman C.J.); *Coltness Iron Company v. Black (Surveyor of Taxes)* (1881) 1 TC 287, 316-317 (Lord Blackburn); *Bowles v. Bank of England* [1913] 1 Ch 57 (Parker J.); *Attorney-General v. Wilts United Dairies Ltd* (1921) 124 LT 319, 322-323 (Bailhache J., overruled by CA and HL at [1922] WN 217, 218); *Ormond Investment Company, Limited v. Betts (H.M. Inspector of Taxes)* (1928) 13 TC 400, 422 (Lawrence L.J.), 434 (Lord Atkinson); *Scott v. Russell (H.M. Inspector of Taxes)* (1948) 30 TC 394, 419 (Porter L.J.); *Congreve v. Home Office* [1976] QB 629 (EWCA); *Daymond v. South West Water Authority* [1976] AC 609; *IRC v. Océ van der Grinten* [2000] STC 951; *Steele Ford and Newton and Others v. Crown Prosecution Service (No. 2)* [1994] 1 AC 22, 33E-F (Lord Bridge of Harwich); and *Aston Cantlow v. Wallbank* (EWCA), n. 332 above.

<sup>339</sup> See Dicey, n. 219 above, ch. 10.

<sup>340</sup> *Ibid.*, p. 315. This is surprising, since Dicey seems to have had an extensive tax practice: see, e.g., *Bowers (Surveyor of Taxes) v. Harding* (1897-1898) 3 TC 22, 24, 28-30; *Bartholomay Brewing Company v. Wyatt (Surveyor of Taxes)* (1897-1898) 3 TC 213, 218; *Nobel Dynamite Trust Company v. Wyatt (Surveyor of Taxes)* (1897-1898) 3 TC 224, 229; and *Leeds Permanent Benefit Building Society v. Mallandaine (Surveyor of Taxes)* (1897-1898) 3 TC 577, 589-590. (Although each of these reports appear in the same TC volume, they were decided over the period 1891-1897.)

looking for a sense of the deep structure of corporation tax are confronted with the largely ‘uncoupled’ technical and theoretical strands of scholarship discussed earlier in the chapter.

It is suggested that, by using a functionalist and interpretative public law approach to corporation tax, a new and, it is suggested, more rewarding way, into the material can be found. This is by regarding the tax as being, in essence, no different from any other form of regulation. Most scholars, notably Picciotto, have long regarded the taxation of corporations, especially MNCs, as constituting a self-evidently ‘regulatory system’.<sup>341</sup> What might at first sound like a dissentient voice is that of Majone,<sup>342</sup> who, taking tax policy to be in essence ‘redistributive’, might be understood to view regulation as involving somewhat distinct considerations. However, on a close reading, it is clear that this comment is made with regard solely to the majoritarian nature of the processes by which tax policy decisions should be reached.<sup>343</sup> Even this point does not, however, relieve us of the obligation of deciding on what are taken to be the defining characteristics of regulation. Consistent with the idea that politics is concerned with the art of government, or of governance, the contention in the study will be that ‘regulation’ is a large enough term to cover all ways of bringing about a particular policy objective. Again, cast in wide terms though it is, Parker and Braithwaite’s definition of regulation as ‘influencing the flow of events’,<sup>344</sup> as well as Baldwin, Scott and Hood’s definition of regulation as ‘an authoritative set of rules, accompanied by some mechanism, typically a public agency, for monitoring and promoting compliance with these

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<sup>341</sup> See Picciotto, n. 7 above, p. 83. So-called ‘corrective taxes’ have long been regarded as regulatory in nature (see, e.g., Anthony Ogus, ‘Corrective Taxation as a Regulatory Instrument’, in *Regulation and Deregulation: Policy and Practice in the Utilities and Financial Services Industries*, ed. by Christopher McCrudden (Oxford: Clarendon Press, 1999), pp. 15-36).

<sup>342</sup> See Giandomenico Majone, *Regulating Europe* (London: Routledge, 1996), p. 294.

<sup>343</sup> *Ibid.*, p. 285. See also Radaelli, n. 198 above, pp. 34-35.

<sup>344</sup> See Christine Parker and John Braithwaite, ‘Regulation’, in Cane and Tushnet, n. 92 above, pp. 119-145, 119.

rules<sup>345</sup> each seem no less apposite to the case of taxation than to any other policy arena.<sup>346</sup> As a form of regulation, corporation tax counts, of course, as economic, rather than social, regulation.<sup>347</sup> Its immediate policy objective might, at a fairly superficial level, be stated as the fair and efficient raising of revenue. Digging deeper, however, we might look to statements of Government economic policy to relate that objective to the broader one of fostering economic growth. This is something to which we shall return before the end of the chapter, since it is essential to the respective roles of ‘theory’ and ‘values’ in the study as a whole. For the present, it is enough to underline the dimension of corporation tax as economic regulation. Even if Majone is right, and this does not capture some ‘redistributive’ element in the notion of taxation,<sup>348</sup> it is at least enough to cover the mechanisms by which that revenue is gathered in the first place. Moreover, it is clear from both HMG’s use of ‘regulatory impact assessments’ (RIAs) in reforming corporation tax,<sup>349</sup> as well as from the European Commission’s view of regulation as including corporate tax matters,<sup>350</sup> that corporation tax policy is regarded as a regulatory activity, both at the domestic and at the European levels. Each of these empirical examples reflects the wider academic consensus

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<sup>345</sup> See *A Reader on Regulation*, ed. by Robert Baldwin, Colin Scott and Christopher Hood (Oxford: Oxford University Press, 1998), p. 3.

<sup>346</sup> This is not to deny that the term ‘regulation’, when restricted to ‘command and control’ regulation, has often been contrasted with taxation (see *R. and the Minister of State for the Commonwealth v. Barger* (1908) 6 CLR 41, 120 (Higgins J.)) and that, thus contrasted, it is itself capable of imposing costs similar to taxation on those regulated (see Mark Kelman, *Strategy or Principle? The Choice between Regulation and Taxation* (Ann Arbor: University of Michigan Press, 1999)).

<sup>347</sup> See Tony Prosser, *Law and the Regulators* (Oxford: Clarendon Press, 1997), pp. 4-6; also Picciotto, n. 7 above, p. 83.

<sup>348</sup> Including, e.g., progressive rates of taxation and the application of the revenue raised.

<sup>349</sup> See, e.g., *Regulatory Impact Assessment for Reform of the Corporate Debt, Financial Instruments and Foreign Exchange Gains and Losses Regimes*, 15 April 2002 (London: Inland Revenue, 2002). See Chapter 3 below.

<sup>350</sup> See, e.g., Document No. IP/05/1382, *Transparency and Better Regulation: Commission puts online a public register of expert groups*, 8 November 2005 (Brussels: European Commission, 2005). The expert groups referred to in this press release include the Common Consolidated Corporate Tax Base (CCCTB) Working Group, as well as various other tax and tax-related groups.

referred to above, that taxation is one form, perhaps one of the earliest forms,<sup>351</sup> of economic regulation.<sup>352</sup>

If, as is contended, corporation tax can be viewed as being essentially similar to any other form of regulation, it becomes possible, in interpreting it, to draw selectively on a vast theoretical literature. Regulation has been analysed both from a law and economics perspective,<sup>353</sup> and also from a public law perspective, where the emphasis has been on regulatory legitimacy.<sup>354</sup> The latter has been a major preoccupation of regulation scholarship ever since it began to acquire a public law dimension in the mid-1980s. Motivated as it was by the concern that NPM reforms were being rolled out under the Thatcher Government with no obvious regard for their constitutional implications, regulation scholarship began to look for accountability mechanisms which might nonetheless provide some safeguard for both the subject and the consumer, and possibly even guide future reform. This is why Baldwin, Scott and Hood, in the definition of regulation set out above, refer to public agencies, rather than Government Departments.<sup>355</sup> It was against this background that the Sheffield school began to look for ‘rule of law values’ in the UK’s constitutional arrangements.<sup>356</sup> Other areas of regulation, pre-eminently areas of social regulation, could usefully be viewed in this

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<sup>351</sup> See Parker and Braithwaite, n. 344 above, p. 120.

<sup>352</sup> See Baldwin, Scott and Hood, n. 345 above, *ibid.* To similar effect, although in the context of seventeenth-century ‘mercantilism’, see Jürgen Habermas, *The Structural Transformation of the Public Sphere*, trans. by Thomas Burger, with Frederick Lawrence (Cambridge: Polity Press, 1992), p. 24.

<sup>353</sup> Notably by Anthony Ogus (see Anthony Ogus, *Regulation: Legal Form and Economic Theory* (Oxford: Oxford University Press, 1994)); also Black (1996) 16 OJLS 699-711 (Review Article).

<sup>354</sup> See, e.g., in relation to ‘a classic example of social regulation’, Chris Hilson, *Regulating Pollution: A UK and EC Perspective* (Oxford: Hart Publishing, 2000).

<sup>355</sup> See nn. 75 and 77 above.

<sup>356</sup> See, esp., Harden and Lewis, n. 215 above.

prism.<sup>357</sup> Corporation tax reform has been unusual, however, since it is one area to which this approach has not yet been systematically applied.<sup>358</sup>

Granted that what has just been said is well-founded, the next question is that of what additional elements taxation might have, above and beyond other forms of economic regulation. More recently, although in a different jurisdiction, and with separate though related concerns in mind, legal and political philosophers have begun to look anew at the legitimacy of taxation. The pre-eminent contribution to this debate has been Murphy and Nagel's *The Myth of Ownership*,<sup>359</sup> a provocatively entitled interrogation of two pervasive ideas: those of 'pre-tax ownership' and of tax justice. Although the two are closely intertwined, we need here to place the accent on the former,<sup>360</sup> since it offers a theoretical perspective on the nature of taxation itself. The taxation of corporations is scoped out of Murphy and Nagel's inquiry,<sup>361</sup> but both main elements of their theory have interpretative resonances even in this area. Most importantly, they ask us to accept the 'conventionality of property', as contrasted with a concept of it as being in some sense 'morally fundamental'.<sup>362</sup> 'We have to think of property', claim Murphy and Nagel, 'as what is created by the tax system, rather than what is disturbed or encroached on by the tax system. Property rights are the rights people have in the resources they are entitled to control after taxes, not before.'<sup>363</sup> Their argument, heavily consequentialist as it is, can be assimilated to a functionalist

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<sup>357</sup> See Hilson, n. 354 above.

<sup>358</sup> That constitutions might entrench certain expectations about the tax system, of which tax reformers should be aware, is explored at some level of abstraction, in John G. Head, 'Tax Reform: A Quasi-Constitutional Perspective', in Cooper, n. 113 above, pp. 155-180. Freedman also uses a Dworkinian methodology in the specific context of a 'GANTIP' (see Judith Freedman, 'Defining Taxpayer Responsibility: In Support of a General Anti-Avoidance Principle' [2004] BTR 332-357).

<sup>359</sup> (Oxford: Oxford University Press, 2000).

<sup>360</sup> See Chapter 4 below.

<sup>361</sup> See Murphy and Nagel, n. 359 above, p. 10.

<sup>362</sup> *Ibid.*, p. 175.

<sup>363</sup> *Ibid.*

perspective on tax law as public law, despite having much in common with what we are content to accept is the ‘liberal normativist’ tradition of Rawls<sup>364</sup> and Dworkin.<sup>365</sup> Contentious as it is,<sup>366</sup> this ‘conventional’, rather than ‘moral’, view of property rights is accepted in what follows.<sup>367</sup> It is a key contention of the study that it is not even possible to begin to articulate a convincing interpretation of, say, tax avoidance measures, without rejecting the notion that taxes involve the ‘exactions’<sup>368</sup> of property which can be said to be the absolute moral entitlement of its owner.<sup>369</sup> Its significance in what follows is elaborated in a later chapter,<sup>370</sup> in connection with the choice of one policy solution over others. What is plainly inadequate, however, is the generality of Dicey’s statement about the liability of the subject to pay taxes<sup>371</sup> or Lord Clyde’s homely metaphor, often cited, of the ‘shovel’ and the ‘stores’ in connection with tax avoidance.<sup>372</sup> As Simester and Chan forcibly point out, few, if any, lawyers really believe this type of statement any more.<sup>373</sup> To the extent that Murphy and Nagel are almost exclusively concerned with substantive issues, rather than institutional or

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<sup>364</sup> See Rawls (1999), n. 252 above, esp. pp. 245-247 and 249-251.

<sup>365</sup> See n. 283 above.

<sup>366</sup> It is clearly incompatible, e.g., with Nozick’s famous characterisation of ‘[t]axation of earnings from labor ... [as being] on par with forced labor’ (see Nozick, n. 266 above, p. 169). For a cogently argued dissent from Murphy and Nagel’s thesis, see Felix Maultzsch (2004) 67 MLR 508-523 (Review Article). The idea of taxation as ‘slavery’ is an ancient one; it appears, for instance, in Herodotus (see James Macdonald, *A Free Nation Deep in Debt: The Financial Roots of Democracy* (Princeton: Princeton University Press, 2006), pp. 20-21). See also Jean-Jacques Rousseau, *Discourse on Political Economy and The Social Contract*, trans. and ed. by Christopher Betts (Oxford: Oxford University Press, 1994), p. 126 (in ‘The Social Contract’).

<sup>367</sup> See also A.P. Simester and Winnie Chan (2003) 23 OJLS 711-726 (Review Article).

<sup>368</sup> See *Commissioner of Internal Revenue v. Newman* 159 F 2d 848, 851 (1947) (Learned Hand J., dissenting).

<sup>369</sup> As witnessed by the exception for taxation in the right to property enshrined in the ECHR (see ECHR, First Protocol, Art. 1).

<sup>370</sup> Particularly as regards ‘societal fairness’, rather than ‘tax fairness’. See Chapter 4 below.

<sup>371</sup> See Dicey, n. 219 above, p. 315.

<sup>372</sup> See *Ayrshire Pullman Motor Services and D.M. Richie v. IRC* (1929) 14 TC 754, 763. It is slightly odd that Lord Clyde should have looked for homely metaphor. Although Montchrétien compares the management of the commonwealth with that of the household (see n. 94 above, p. 31), both Aristotle and Rousseau makes it plain that it is a ‘mistake’ so to do (see Aristotle, *The Politics*, ed. by Stephen Everson (Cambridge University Press: Cambridge, 1988), p. 1; Rousseau, n. 366 above, pp. 3-6).

procedural ones, their thesis complements the regulatory material outlined above. Their preoccupation is not, indeed, surprising. A concern for, for instance, accountability, a key legitimising value, has only relatively recently surfaced in the language of tax reform in the UK,<sup>374</sup> in the context of the discussion in the O'Donnell Report.<sup>375</sup> It is thus that it seems appropriate, in what follows, to combine elements of a view of corporation tax as regulation, with Murphy and Nagel's conception of taxation as involving only 'conventional' property rights.

In the rest of the study, a functionalist and interpretative approach is followed in three interrelated, but distinct, stages. Consistent with the idea of corporation tax as public law, with attributes peculiar to the taxation of corporations, as well as ones common to economic regulation generally, we contemplate the phenomenon of corporation tax reform from three different angles: institutions, processes and policy solutions.<sup>376</sup> Taken as a whole, this structure is the clearest sign of the influence on the study of Sheffield school writers such as Hilson, who organises his examination of one area of social regulation, at least in part, on these lines,<sup>377</sup> and Lewis, who takes a similar approach in discussing law and governance.<sup>378</sup> Where the study differs from that body of work, however, is in its rejection, on historical and interpretative grounds, of a Sheffield school methodology. This allows us to say rather more

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<sup>373</sup> See Simester and Chan, n. 367 above, p. 711.

<sup>374</sup> Although Robinson and Sandford's 1983 study was concerned with the types of accountability mechanisms discussed in Chapters 2 and 3 below, e.g., the system of Parliamentary committees, the expression 'accountability' is not used (see Ann Robinson and Cedric Sandford, *Tax Policy-Making in the United Kingdom: A Study of Rationality, Ideology and Politics* (London: Heinemann, 1983).

<sup>375</sup> See, e.g., Cm 6163, n. 82 above, pp. 11-12.

<sup>376</sup> See, e.g., Majone, n. 342 above, p. 291. As Majone points out (*ibid.*), discussions of the institutions of the EU have made similar divisions in the material (referring to Joseph H.H. Weiler, 'After Maastricht: Community Legitimacy in Post-1992 Europe', in *Singular Europe: Economy and Polity of the European Community after 1992*, ed. by William James Adams (Ann Arbor: University of Michigan Press, 1992), pp. 11-41).

<sup>377</sup> See n. 354 above.



about the content and relative importance of the values at work in corporation tax reform than might otherwise have been possible.

A functionalist style, one that ‘reflects an ideal of progressive evolutionary change’, requires us to be ever alert to public law’s ‘aims and objectives’.<sup>379</sup> Given a certain sensitivity of approach, the wealth of material making up the technical theme in corporation tax reform enables us, with perhaps unusual clarity, to uncover and interpret those aims and objectives. The Budget ‘red books’ published over the period of Gordon Brown’s Chancellorship comprise a particularly rich source of information. Although we shall have occasion to return to these in greater detail at various points in the study, it is worth referring here to the kinds of aims and objectives that they contain.

One of the earliest such documents that we shall be considering is the incoming Labour Government’s first full Budget report, published in March 1998.<sup>380</sup> Here it was stated that the four objectives of the Government’s economic strategy were ‘to ensure economic stability, reward work, encourage enterprise and promote fairness’.<sup>381</sup> To these ends, there would be ‘enterprise reforms, including major corporation tax changes’, and ‘fairness measures’, including anti-avoidance provisions, which would be designed to ‘ensure that people and companies pay a fair share of tax’.<sup>382</sup> It was predicted that corporation tax would, in 1998-1999, raise 23.79 per cent. of ‘total Inland Revenue’.<sup>383</sup> Two years later, in Budget

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<sup>378</sup> N. Douglas Lewis, *Law and Governance: The Old Meets the New* (London: Cavendish Publishing, 2001).

<sup>379</sup> See extract relating to n. 275 above.

<sup>380</sup> See *New Ambitions for Britain: Financial Statement and Budget Report March 1998* (House of Commons Papers, Session 1997-1998, 620) (London: TSO, 1998). July 1997, a matter of months after the General Election, had seen the publication of a mini Budget (see *Equipping Britain for our long-term future: Financial Statement and Budget Report July 1997* (House of Commons Papers, Session 1997-1998, 85) (London: The Stationery Office, 1997)).

<sup>381</sup> *Ibid.*, para. 1.01.

<sup>382</sup> *Ibid.*

<sup>383</sup> i.e. £30 billion of a predicted total tax yield from ‘Inland Revenue’ taxes of £126.1 billion (*ibid.*, p. 117). (Figures calculated on a ‘cash basis’ and including what was then ACT: see n. 40 above.)

2000, the Government ambitiously stated that it was pursuing a ‘comprehensive and coordinated strategy to fulfil Britain’s national economic potential and deliver the objective of high and stable levels of growth and employment – with rising living standards for all’.<sup>384</sup> This required ‘a fair and efficient tax system’, a blot on which was the failure of ‘individuals and businesses [to] pay their fair share of taxes’.<sup>385</sup> To this end, Budget 2000 promised ‘a package of measures’ to ‘tighten up the controlled foreign company rules’.<sup>386</sup> Corporation tax was predicted, in 2000-2001, to raise 23.50 per cent. of ‘total Inland Revenue’.<sup>387</sup> The equivalent opening statement on the Government’s objective in Budget 2003 closely followed that of 2000: ‘[t]he Government’s objective [it ran] is to deliver high and stable levels of growth and employment, with opportunity and rising living standards for all – a Britain of economic strength and social justice’.<sup>388</sup> Again, emphasis was placed on tax avoidance as an obstacle to tax fairness, further measures being announced on controlled foreign companies (CFCs),<sup>389</sup> as well as on life insurance companies.<sup>390</sup> There was also a ‘compliance and enforcement package’:

‘We want to make sure that the burden of tax does not fall unfairly on taxpayers who play by the rules and pay their fair share. This package is the first step in a new strategic approach to compliance work, designed to modernise the way risks to revenue are assessed and managed by the Inland Revenue. It identifies areas of the tax system where the potential loss of revenue is high and targets resources and compliance activity

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<sup>384</sup> See *Prudent for a Purpose: Working for a Stronger and Fairer Britain*, n. 184 above, para. 1.1.

<sup>385</sup> *Ibid.*, para. 1.25.

<sup>386</sup> *Ibid.*, para. 5.116.

<sup>387</sup> i.e. £33.8 billion of a predicted total tax yield from ‘Inland Revenue’ taxes of £143.8 billion (*ibid.*, p. 203).

<sup>388</sup> See *Building a Britain of economic strength and social justice: Economic and Fiscal Strategy Report and Financial Statement and Budget Report April 2003* (House of Commons Papers, Session 2002-2003, 500) (London: The Stationery Office, 2003), para. 1.1.

<sup>389</sup> *Ibid.* p. 193.

<sup>390</sup> *Ibid.*; see H.M. Treasury PN07, *Fairness in Taxation – Protecting Tax Revenues*, 9 April 2003, available from [www.hm-treasury.gov.uk](http://www.hm-treasury.gov.uk) (accessed 19 July 2006).

accordingly; and creates a more stable framework upon which to plan public investment.<sup>391</sup>

This time, it was predicted that, for 2003-2004, corporation tax would generate 19.09 per cent. of 'total Inland Revenue'.<sup>392</sup> Three years later, Budget 2006 proclaimed that '[t]he Government's economic objective is to build a strong economy and a fair society, where there is opportunity and security for all'.<sup>393</sup> Again, a strong anti-avoidance line was to the fore; although there was a recognition that, at the same time as blocking avoidance opportunities, 'the competitiveness of the UK ... [had to be] maintained'.<sup>394</sup> Measures were therefore announced to 'close down a number of avoidance schemes which use financial products' and to 'close a loophole in the controlled foreign companies legislation'.<sup>395</sup> For 2006-2007, the predicted 'take' from corporation tax was very roughly 16.7 per cent. of taxes formerly collected by the Inland Revenue.<sup>396</sup> Such statements together enable us to infer that one aim of corporation tax reform is the moulding of a tax that raises something around very approximately 20 per cent. of the total tax 'take',<sup>397</sup> consistent with promoting economic growth and achieving fairness. The public interest requires, not only the promotion of the former, which is a question of efficiency, but also the drawing of a clear distinction between acceptable and unacceptable forms of tax avoidance, which is a question of fairness. It follows that, to identify those areas in which this double objective may be frustrated, it is

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<sup>391</sup> *Ibid.*, Rt Hon. Dawn Primarolo MP, Paymaster General.

<sup>392</sup> i.e. £30.8 billion of a predicted total tax yield from 'Inland Revenue' taxes (excluding social security contributions) of £161.3 billion (see *Building a Britain of economic strength and social justice*, n. 388 above, p. 257).

<sup>393</sup> See *A strong and strengthening economy: Investing in Britain's future: Economic and Fiscal Strategy Report and Financial Statement and Budget Report March 2006* (House of Commons Papers, Session 2005-2006, 968) (London: The Stationery Office, 2006), para. 1.1.

<sup>394</sup> *Ibid.*, p. 119.

<sup>395</sup> *Ibid.*, p. 120.

<sup>396</sup> i.e. £49 billion out of a total yield from former 'Inland Revenue' taxes of £292.9 billion (see *A strong and strengthening economy*, n. 393 above, p. 262).

<sup>397</sup> Lee's figures are consistent with this: see Lee, n. 56 above, para. [1.5].

necessary to scrutinise each element of corporation tax reform, whether it be the institutions, the processes, or the policy solutions actually adopted. To the extent that the values at work in each aspect of corporation tax reform, as well as the significance accorded to each one relative to the others, seem to make a rational whole, we can say that they are satisfactory, and therefore legitimate. In relation to the former point, values such as certainty and accountability, may help to further the efficiency and fairness objectives. However, to the extent that, in particular contexts, values conflict with each other, they may need to be reconciled to the objective of corporation tax reform set out above, in accordance with prudential techniques. The reconciliation of conflicting values through prudence is a much more difficult task even than the identification of the values themselves.

The argument against approaching the material in the manner just described is that documents such as the Budget *Financial Statement* may conceal the reality or, at the very least, the objectives that they contain may be highly contestable ones. The former might seem to be a point well made. Recall, however, the interpretative dimension of the study discussed above. This requires us, being historically sensitive all the while, to look for any inconsistencies, contradictions or incoherence in the Government's stated aims and objectives. In the absence of a journalist's dream, such as a compromising Departmental memorandum accidentally left on the Tube, or a wayward email, such canons of rationality are the sharpest tools we have. Rationally, we can only assume, absent such incriminating evidence to the contrary, that the Government is acting to promote 'the welfare of the people',<sup>398</sup> to promote the public interest. The latter point, i.e. the contestability of the object itself, does, however, have greater merit. It is Oakeshott who, in *On Human Conduct*,<sup>399</sup>

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<sup>398</sup> We assume here that 'the welfare of the people' can be equated with 'the public interest' (see Robert Baldwin and Martin Cave, *Understanding Regulation: Theory, Strategy, and Practice* (Oxford: Oxford University Press, 1999), p. 9n). See n. 168 above, and Chapter 3 below.

<sup>399</sup> See Oakeshott, n. 269 above.

points to the ‘puzzle set by the character of a modern European state’, the ‘unresolved tension’ between the ‘irreconcilable’ conceptions of a state as ‘*societas*’ and as ‘*universitas*’.<sup>400</sup> What the latter implies, that the former does not, is ‘the pursuit of some acknowledged substantive end, ... the promotion of some specified enduring interest’.<sup>401</sup> Although, in interpreting corporate tax reform, we confront the problem that notions of the modern state combine elements of both, it is also the case that the regulatory state, the state as *universitas*, predominates.<sup>402</sup> Modern politics in Europe tends to be concerned, not with the existence, but with the nature and extent of the regulatory state. What renders acceptable a certain view of it, if only for a time, is the policy of a democratically elected Government. Corporation tax reform, in short, is about the legitimate facilitating of the aims and objectives of a democratically elected government in the particular policy area. But there is no doubt about the contestability, the political, nature of the solutions adopted. The only question is the prudence with which they are managed. It is not even a case of Lord Hailsham’s ‘elective dictatorship’,<sup>403</sup> because a democratically elected government may be both constrained and empowered by human rights law, although this is itself a – distinct - political arena.<sup>404</sup>

In each of the study’s three divisions, our initial concern will be the identification of aims and objectives, and relative thereto, the interpretation and prioritisation of the political values

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<sup>400</sup> *Ibid.*, pp. 200-201.

<sup>401</sup> *Ibid.*, p. 203. What characterises the state as ‘*societas*’ is ‘not that of an engagement in an enterprise to pursue a common substantive purpose or to promote a common interest, but that of loyalty to one another’ (*ibid.*, p. 201).

<sup>402</sup> As witness the massive administrative machinery of modern European states (see Loughlin, n. 162 above, p. 18).

<sup>403</sup> See Lord Hailsham, *The Dilemma of Democracy: Diagnosis and Prescription* (London: Collins, 1978), ch. 20, esp. 126-127.

<sup>404</sup> See Loughlin, n. 162 above, ch. 7. Technically, the Human Rights Act 1998 can, of course, be repealed, as the Conservatives advocated in their 2005 General Election campaign. (The Conservatives’ latest plan does not, apparently, involve the repeal of HRA 1998 (see Hall, *Financial Times*, 26 June 2006, 2)).

at work in each area. Chapter 2 pursues this inquiry in relation to the Departmental theme picked out at the beginning of the study. The discussion is not, however, confined to H.M. Treasury and to HMRC, but reaches out to the impact of non-governmental bodies such as the International Accounting Standards Board (the IASB).<sup>405</sup> This is both to reflect the overall objective of NPM reforms, that of greater efficiency, and to enable an assessment of the institutional significance of other reforms, such as those comprised in the accounting theme. Examining the political values at work at the Treasury, for example, depends on an analysis, not only of its aim, but of the qualities that its personnel bring to their task.<sup>406</sup> Thus, in the context of the Treasury's single aim, to '[r]aise the rate of sustainable growth and achieve rising prosperity and a better quality of life, with economic and employment opportunities for all',<sup>407</sup> we need to assess the qualities of both politicians and officials in promoting it. Efficiency, as we have said, is a deeply embedded value, because of its importance to effectiveness. However, as we have also said, other values, most importantly, after O'Donnell,<sup>408</sup> accountability, have assumed a greater importance. The functionalist approach requires us to be sensitive both to the way in which, in the particular context of corporation tax reform, the Treasury's overall aim shapes the content of the values that it embodies, as well as their importance relative to each other. New Public Management has tied both 'policy networks' and non-governmental institutions, such as the IASB, ever more closely into the making of corporation tax policy.

One of the more controversial consequences of the O'Donnell report has been the severe restriction of HMRC's policy making function, and the concentration of policy mainly (though not exclusively) in H.M. Treasury. This is reflected in the relatively low profile

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<sup>405</sup> See [www.iasb.org](http://www.iasb.org) (accessed 30 March 2006).

<sup>406</sup> See [www.hm-treasury.gov.uk/about/about\\_aimsobject.cfm](http://www.hm-treasury.gov.uk/about/about_aimsobject.cfm) (accessed 28 March 2006).

<sup>407</sup> *Ibid.*

<sup>408</sup> See n. 82 above.

accorded to HMRC in both Chapter 2 and Chapter 3, although it will be seen from Chapter 3 what is crucial about HMRC's 'presentation' and 'delivery' function. In Chapter 3, too, it is necessary to elaborate briefly on the reasons for excluding Luhmann's systems theory from the analysis.<sup>409</sup> Although Loughlin originally suggested that systems theory might assist in the interpretation of the emergence of the probable from a range of possibilities,<sup>410</sup> the study rejects this approach. The rationale for the rejection, together with an assessment of the interpretative significance of a number of rival theories,<sup>411</sup> forms an introduction to Chapter 3. Our interest in Chapter 3 is in constituent power, so, rather than clinging to Luhmann, or analysing Habermas's 'democratic principle',<sup>412</sup> or the 'deliberative democracy' of Sunstein,<sup>413</sup> we attempt to pinpoint the reality of tax policy-making in this particular representative democracy. In relation to the policy-making process, the dominant idea is prudence, in which reform may, or may not, be the result of consultation and participation. Experts are crucially important, but alone, as Loughlin points out, they cannot solve the problems of public law.<sup>414</sup> He might have added that this is as true of corporation tax as any other area of the subject.

The anti-avoidance theme figures prominently in the discussion of the evolving corporation tax code in Chapter 4. This, too, is where the accounting and European and international themes come to the fore. What values, we need to ask, are at work in aligning the measurement of tax profits and accounting profits? Why are certain tax avoidance

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<sup>409</sup> See n. 120 above.

<sup>410</sup> See n. 305 above.

<sup>411</sup> On the possibility that systems theory might help to interpret at least what we refer to as the accounting theme in corporation tax reform, see Judith Freedman, 'Aligning Taxable Profits and Accounting Profits: Accounting standards, legislators and judges' (2004) 2 *eJournal of Tax Research* 71-99, 98-99.

<sup>412</sup> Especially as developed in *Between Facts and Norms*, trans. by William Rehg (Cambridge: Polity Press, 1997), pp. 457-458.

<sup>413</sup> See, e.g., the contribution of Cass Sunstein and others to *Deliberative Democracy*, ed. by Jon Elster (Cambridge: Cambridge University Press, 1998).

techniques unacceptable? How are policy choices constrained or facilitated by the UK's European and international commitments? It is in offering answers to these questions that we make our second major departure from Loughlin.<sup>415</sup> This is in the relative weight to be accorded to theory and values in analysing the policy choices actually made. The best discussions of corporation tax reform would hark back to Smith and to Millar, and to the 'science of legislation'.<sup>416</sup> Values need to be given a higher prominence in the specific area of corporation tax than perhaps Loughlin would accord them. This is because corporation tax discourse has always been, as the above discussion has demonstrated, conducted in terms in which principles – or values – have been uppermost. A key challenge in analysing solutions to corporation tax problems is in mapping the classification and content of the four maxims of 'equality', 'certainty', convenience and cost-effectiveness in the corporation tax context. Equally important, however, is the need to consider how and why Smith's maxims are modified to take account of the policy objectives that, as reformed, corporation tax is intended to serve.

Since this is a functionalist, not a normative, inquiry, the aim of analysing the three areas in Chapters 2 to 4 is not to produce some 'blueprint' for reform. Its primary purpose is to offer an interpretation of the public law implications of the seven themes set out at the beginning. In reflecting *in extenso* on this interpretation, in Chapter 5 below, it is hoped to identify areas in which the prudential quality of corporation tax reform appears weak. Although this has implications for the direction that corporation tax reform might take in future, Loughlin is right to emphasise that the functionalist approach is a scholarly, rather

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<sup>414</sup> See Loughlin, n. 226 above, p. 66.

<sup>415</sup> See n. 120 above.

<sup>416</sup> See nn. 258 and 259 above.



than an active one. If the tax law scholar, a non-practitioner, has anything to contribute to the discourses on reform, it is a competing, but distinct, type of discourse.<sup>417</sup>

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<sup>417</sup> See Loughlin, n. 226 above, p. 66.

## Chapter 2

### THE REFORMERS

#### PROLOGUE

A visitor to London in the first decade of the twenty-first century can take a ride on the London Eye, one of the capital's remaining millennium attractions. From the gondolas of this gigantic fairground wheel, mounted above the brown-green waters of the River Thames, can be seen, does one choose to remark them, the tangible manifestations of the political institutions most closely associated with the themes announced at the beginning of Chapter 1.

The view to the south is dominated by the Victorian Gothic splendour of the Palace of Westminster and the Houses of Parliament.<sup>1</sup> There, although in committee rooms and in Westminster Hall,<sup>2</sup> rather than in the main chambers, have individual Finance Act provisions been debated by some numbers of the elected representatives of the people. There, too - perplexingly for anyone expecting more tangible signs of a 'separation of powers' - at the bar of the House of Lords, the Law Lords have handed down the most important judgments in corporation tax appeals. Just to the right, clearly discernible to the north west of Westminster, are the impressive and newly modernised New Government Offices on Horse

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<sup>1</sup> See Simon Bradley and Nikolaus Pevsner, *The Buildings of England – London 6: Westminster* (New Haven and London: Yale University Press, 2003), pp. 216-218.

<sup>2</sup> *Ibid.*, pp. 229-231.

Guards Road, the western part of which houses H.M. Treasury.<sup>3</sup> The Treasury building, in Whitehall, is nearer to the Houses of Parliament than any of the other Departmental buildings in the area; it is also, with the exception of the Foreign Office, the most imposing of them. This is where the economic policies that help to shape the reform of corporation tax have been evolved.

Further to the north east, by Waterloo Bridge, no more than a mile away, can be discerned the classical lines of Somerset House in the Strand, the western part of which, in Lancaster Place, has been the seat of successively, the Inland Revenue and H.M. Revenue and Customs (HMRC).<sup>4</sup> Just visible behind it are the Royal Courts of Justice, the principal seat both of the Court of Appeal and of the High Court. The Government buildings are not, however, all that the interested visitor might see. Signs of the presence of ‘policy community’ membership, close to the centres of tax policy, are visible too. Located somewhere between the Treasury and Somerset House, above Charing Cross railway station, and looking out over the Golden Jubilee Bridges, is the headquarters, in Embankment Place, of one of the ‘Big Four’ accountancy firms, PricewaterhouseCoopers.<sup>5</sup> Ernst and Young, another Big Four firm, has its headquarters on the other side of the river, in Lambeth Palace Road, near Tower Bridge.<sup>6</sup> If the location of the Treasury building is symbolic of the centrality of tax policy to the British state,<sup>7</sup> then the presence of the imposing premises of two Big Four accountancy practices, so close to the nerve centre of H.M. Government (HMG), is surely emblematic of

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<sup>3</sup> Which modernisation only the London Eye has made clearly visible from outside the building. The modernisation was designed by Foster and Partners, ‘from 2000, creating open-plan offices and making lesser courtyards and light wells into glass-roofed communal spaces’ (see Bradley and Pevsner, n. 1 above, p. 270).

<sup>4</sup> *Ibid.*, p. 324. Although it should be noted that the Business Tax Unit is based in Kingsway, which is near Somerset House.

<sup>5</sup> ‘Mysteriously lit, with a fountain issuing as if from a giant pipe, ... [the reception area of Embankment Place] suggests the sanctum of some strange earth-cult’ (*ibid.*, p. 300).

<sup>6</sup> See Chapter 1 above, nn. 144 and 148; also n. 124 below.

<sup>7</sup> See, in another context, Fisher (2001) 13 J. Env. L. 115-117, 115 (book review).

the importance of accountants in the formulation of tax policy. The presence of other professionals, though less visible from the Eye, is no less striking. From the Treasury in Whitehall, to St Paul's, in the heart of the City, is a little over a mile and a half - a cab-ride away for the busy civil servant, accountant or solicitor with the inevitable 'pilot case' of A4 policy documents and multi-volume taxation statutes.<sup>8</sup> Within the City's 'square mile' are the offices of no less than 40 major international and European and domestic banks, including Goldman Sachs,<sup>9</sup> Merrill Lynch,<sup>10</sup> Nomura and Deutsche Bank;<sup>11</sup> no less than two dozen fund managers, including Fidelity Investments, Henderson Global Investors, and Schroders;<sup>12</sup> at least a dozen international law firms, including Allen and Overy, Freshfields, and Slaughter and May; and the other two Big Four accountancy practices, Deloitte and KPMG.<sup>13</sup> Even Canary Wharf, the City's Docklands extension, with its 50-storey, 800-foot tower, and its two slightly smaller 42-storey companions, each dominating the eastern horizon seen from the Eye, is only two miles or so from St Paul's, and not much more than two and a half miles, as the crow flies, from Whitehall and the Houses of Parliament. Canary Wharf, once 'unfashionable', is now home to at least ten other major banks, including Credit Suisse and Morgan Stanley,<sup>14</sup> and the law firm Clifford Chance.<sup>15</sup>

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<sup>8</sup> Tax specialists in the practising professions universally use commercially-produced anthologies of tax legislation, annual publications which incorporate legislative amendments made from FA to FA.

<sup>9</sup> Whose offices, *Pevsner* tells us, are 'a sleek, complex pile, not the usual atrium block' (see Simon Bradley and Nikolaus Pevsner, *The Buildings of England – London 1: The City of London* (London: Penguin, 1997), p. 500).

<sup>10</sup> Merrill Lynch, Goldman Sachs and Morgan Stanley ('MGM') are the world's leading investment banks, known as 'the super bulge' (see Philip Augar, *The Greed Merchants: How the Investment Banks Played the Free Market Game* (London: Allen Lane, 2005), pp. 37-39).

<sup>11</sup> See the large-scale map in the *Financial Times Special Report: The New City*, 27 March 2006, 2 and 5.

<sup>12</sup> *Ibid.*

<sup>13</sup> Part of KPMG will relocate to a new building in Canary Wharf in 2009 (see Jopson and Pickard, *Financial Times*, 7 November 2006, 27).

<sup>14</sup> See Pickard, *Financial Times*, 3 April 2007, 19.

Faced with the economic might whose ‘lifeworld’ seems so vivid from the Eye,<sup>16</sup> it might seem perverse, almost, to begin this chapter by highlighting certain analytical problems in interpreting the significance of institutions to the process of corporation tax reform. It is, to be sure, a matter of understanding their make-up, objectives and values, but, equally importantly, we need to be able to interpret the significance of the relationships between the institutions of HMG and those of the corporate sector.<sup>17</sup> Describing the duties and powers of political institutions is something that comes rather easily to public lawyers – briefly turning up a standard constitutional law<sup>18</sup> or taxation law<sup>19</sup> text will illustrate the truth of this point. Since, however, we are engaged in a functionalist and interpretative inquiry, and since Loughlin’s references to political institutions occur in the context of ‘high-level’ discussions of representation, sovereignty and constituent power,<sup>20</sup> we need to look beyond the public law texts themselves, to find ways of understanding the wider significance of institutions, and the ways in which they interact, in the reform of corporation tax. The task is complicated by the fact that the discourse on institutions (the ‘new institutionalism’)<sup>21</sup> in the field of

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<sup>15</sup> The offices of which are so impressive that its ‘entrance halls ... (one visiting judge observed) could accommodate a small law practice’ (see Anthony Sampson, *Who Runs This Place? The Anatomy of Britain in the 21<sup>st</sup> Century* (London: John Murray, 2004), p. 181).

<sup>16</sup> London, in the words of Ed Balls MP, the Economic Secretary to the Treasury until 28 June 2007, vies with New York as ‘the world’s greatest global financial centre’ (quoted in Freeland, *Financial Times*, 4-5 November 2006, 11).

<sup>17</sup> See Charles J. Fox and Hugh T. Miller, *Postmodern Public Administration: Toward Discourse* (Thousand Oaks: Sage, 1995), pp. 91-92.

<sup>18</sup> See, e.g., Paul Jackson and Patricia Leopold, *O. Hood Phillips & Jackson: Constitutional and Administrative Law*, 8<sup>th</sup> edn (London: Sweet and Maxwell, 2001), Parts II and III; also R.A.W. Rhodes, *Understanding Governance: Policy Networks, Governance, Reflexivity and Accountability* (Maidenhead: Open University Press, 1997), pp. 76-77.

<sup>19</sup> See, e.g., John Tiley, *Revenue Law*, 5<sup>th</sup> edn (Oxford: Hart Publishing, 2005), pp. 62-65.

<sup>20</sup> See Martin Loughlin, *The Idea of Public Law* (Oxford: Oxford University Press, 2003), chs 5 and 6.

<sup>21</sup> ‘Old institutionalism’, though still useful, is not unlike the kind of descriptive public law to which reference has just been made. For an example, see the topics covered in Herman Finer, *The Theory and Practice of Modern Government*, 4<sup>th</sup> edn (London: Methuen, 1961).

politics has as many as six distinct strands.<sup>22</sup> These range from the ‘normative institutionalism’ of March and Olsen,<sup>23</sup> which emphasises ‘the “logic of appropriateness” as a means of shaping the behaviour of the members of institutions’,<sup>24</sup> via the ‘rational choice institutionalism’ of, for instance, Tsebelis and Money,<sup>25</sup> to the ‘empirical institutionalism’ of Weaver and Rockman.<sup>26</sup> All have insights to offer; all are, broadly speaking, ‘functionalist’ accounts. A further complication arises from the fact that there is little published material that applies the new institutionalism to the particular institutions centred on the imposing buildings visible from the London Eye. Fortunately, however, David Judge makes a valuable attempt to interpret these particular institutions in terms that combine various elements of the new institutionalism.<sup>27</sup> Using an ‘organizing perspective’, of a type suggested by Andrew Gamble,<sup>28</sup> rather than a general theory, he takes new institutionalism to conceive of political institutions as contingent ‘formal organizations and structures ... mediated by wider social, economic and political conditions and forces’. The activities of such structures and organisations are delimited and defined by their ‘interactions’ with other institutions, and, insofar as they correspond to ‘normatively appropriate behaviour’, reflect ‘internal organizational norms and values’ shaped by ‘wider societal understandings and expectations’.<sup>29</sup>

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<sup>22</sup> See the list in B. Guy Peters, *Institutional Theory in Political Science: The ‘New Institutionalism’*, 2<sup>nd</sup> edn (London: Continuum, 2005), pp. 19-21.

<sup>23</sup> James G. March and Johan P. Olsen, *Rediscovering Institutions: The Organizational Basis of Politics* (New York: Free Press, 1989), esp. ch. 9.

<sup>24</sup> See Peters, n. 22 above, p. 19.

<sup>25</sup> See George Tsebelis and Jeannette Money, *Bicameralism* (Cambridge: Cambridge University Press, 1997).

<sup>26</sup> See R. Kent Weaver and Bert A. Rockman, *Do Institutions Matter? Government Capabilities in the United States and Abroad* (Washington, DC: Brookings Institution, 1993).

<sup>27</sup> See David Judge, *Political Institutions in the United Kingdom* (Oxford: Oxford University Press, 2005).

<sup>28</sup> See Andrew Gamble, ‘Theories of British Politics’ (1990) 38 *Political Studies* 404-420, 404-406.

<sup>29</sup> See Judge, n. 27 above, p. 21.

The insights that Judge offers, as well as the approaches that he synthesises, though useful in interpreting how institutions function, do not, however, set out to identify the true ‘source of authority’ when it comes to public policy decisions.<sup>30</sup> The need to pinpoint this brings us back to texts that are foundational to public law as a ‘political practice’. In Hobbes’s analysis of ‘the Seat of Power’,<sup>31</sup> as Loughlin reminds us,<sup>32</sup> authority originates from the ‘COMMON-WEALTH, in latine CIVITAS’,<sup>33</sup> the entity that Hobbes himself refers to as the ‘STATE’.<sup>34</sup> Although the state is a ‘fictitious person’, it is not like others, since both it, and its representative, the Crown in Parliament,<sup>35</sup> ‘are instituted precisely for the purpose of creating law’.<sup>36</sup> This is a particularly important point, since much of the material in the politics field, especially as it relates to governance,<sup>37</sup> tends to underestimate the pre-eminent place of the state in the policy-making process.<sup>38</sup> Whatever the objectives and values of the non-state actors in corporation tax reform – whether accountants, bankers, lawyers, or policy networks drawing in each of these groups – it is important to recognise that they may not be the same as those of the state. Possible divergences, in the purposes and objectives of institutions, as well as in the values that they promulgate, form the first important strand in the following discussion. When the visitor to London catches sight of the Palace of Westminster, the New Government Offices, Somerset House or the Royal Courts of Justice, what he or she is seeing is the physical location of the institution which ‘represent[s]’ the

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<sup>30</sup> See Loughlin, n. 20 above, p. 54.

<sup>31</sup> See Thomas Hobbes (1588-1679), *Leviathan, or The Matter, Forme, & Power of a Commonwealth Ecclesiasticall and Civill*, ed. by C.B. Macpherson (London: Penguin, 1985), p. 75.

<sup>32</sup> See Loughlin, n. 20 above, p. 55.

<sup>33</sup> See Hobbes, n. 31 above, p. 227.

<sup>34</sup> *Ibid.*, p. 81.

<sup>35</sup> See Loughlin, n. 20 above, p. 84.

<sup>36</sup> *Ibid.*, p. 60.

<sup>37</sup> See Chapter 1 above, pp. 32-33.

<sup>38</sup> See Jon Pierre and B. Guy Peters, *Governance, Politics and the State* (Basingstoke: Macmillan, 2000), p. 82; also Martin Loughlin, ‘The State, the Crown and the Law’, in *The Nature of the*

‘LEVIATHAN’<sup>39</sup> - that is, the state - in this particular area of policy-making.<sup>40</sup> Only the state, the ‘United Kingdom of Great Britain and Northern Ireland’, the ‘fictitious’ personality<sup>41</sup> represented by the Crown in Parliament, and created by the ‘authorization ... [of the] multitude’,<sup>42</sup> is sovereign. The power to impose or repeal taxes is one of its most fundamental attributes.<sup>43</sup> A second important strand in the discussion is thus the sovereign status of the Crown in Parliament and the point, all too easily elided, that the ‘transfer of jurisdiction and competence’ in matters other than taxation,<sup>44</sup> to the institutions of the EU, has not necessarily affected the sovereign status of the UK in corporation tax matters.<sup>45</sup> Pressing though the problems of the European and international theme may be, they are problems of jurisdiction and competence rather than ones of sovereignty.

The extent to which public lawyers have underestimated the concept of sovereignty is a crucial element in Loughlin’s conception of public law. Sovereignty must be thought of separately from the person of the sovereign. It has both a legal and a political dimension, he argues, and public lawyers must be alive to the precise significance of each of them. The legal dimension of sovereignty is the relationship between state and ‘subject’;<sup>46</sup> its political facet is the relationship between state and people.<sup>47</sup> The former, a ‘distributive

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*Crown: A Legal and Political Analysis*, ed. by Maurice Sunkin and Sebastian Payne (Oxford: Oxford University Press, 1999), pp. 33-76, 34.

<sup>39</sup> See Hobbes, n. 31 above, pp. 81 and 227.

<sup>40</sup> See Loughlin, n. 20 above, p. 56.

<sup>41</sup> *Ibid.*, p. 59.

<sup>42</sup> *Ibid.*, p. 58. See Hobbes, n. 31 above, p. 227.

<sup>43</sup> See Jean Bodin (1530-1596), *On Sovereignty: Four chapters from The Six Books of the Commonwealth*, ed. and trans. by Julian H. Franklin (Cambridge: Cambridge University Press, 1992), p. 81; also Hobbes, n. 31 above, pp. 235, 236; also Deborah Bräutigam, ‘Building Leviathan: Revenue, State Capacity and Governance’ (2002) 33:3 *IDS Bulletin* 10-20.

<sup>44</sup> See Art. 95(2), European Treaty (ex 100a).

<sup>45</sup> See Loughlin, n. 20 above, p. 94.

<sup>46</sup> See Hobbes, n. 31 above, p. 228.

<sup>47</sup> See Loughlin, n. 20 above, p. 67.



conception',<sup>48</sup> which Loughlin calls 'competence',<sup>49</sup> is constructed on the latter, a 'generative conception',<sup>50</sup> which he designates 'capacity'.<sup>51</sup> The former is the absolute authority of the Crown in Parliament to enact law;<sup>52</sup> the latter, 'inextricably linked' to authority, is 'political sovereignty' or 'constituent power', the 'power to model a state',<sup>53</sup> which is confided 'in trust' to HMG.<sup>54</sup> Political sovereignty is therefore a 'relational concept', and, 'being relational, ... [it] does not reside in any particular locus'.<sup>55</sup> It is dependent on the relationship between state and people or, possibly, between state and society. It is 'power to',<sup>56</sup> and, as such, is different from 'power over',<sup>57</sup> which is mere domination. A third significant element of the discussion is therefore how HMG's sovereignty in corporation tax is not merely a matter of competence. Whatever competence HMG may have in such matters is in turn founded on capacity, and thus upon the quality of the relationship between state and non-state actors involved in corporation tax reform.

Developing a positive relationship between state and non-state institutions therefore depends on constantly augmenting the 'bonds of allegiance' between the government and the

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<sup>48</sup> *Ibid.*, p. 160.

<sup>49</sup> *Ibid.*, p. 84.

<sup>50</sup> *Ibid.*, p. 160.

<sup>51</sup> *Ibid.*, p. 85.

<sup>52</sup> *Ibid.*, p. 84. This is, of course, Dicey's 'sovereignty of Parliament' (see A.V. Dicey, *Introduction to the Study of the Law of the Constitution*, ed. by E.C.S. Wade, 10<sup>th</sup> edn (London: Macmillan, 1965), pp. 39-40). Also Jeffrey Goldsworthy, *The Sovereignty of Parliament: History and Philosophy* (Oxford: Clarendon Press, 1999).

<sup>53</sup> See Loughlin, n. 20 above, p. 85, quoting George Lawson (c1598-1678), *Politica Sacra et Civilis: or, A Modell of Civil and Ecclesiasticall Government*, ed. by Conal Condren (Cambridge: Cambridge University Press, 1992), p. 47.

<sup>54</sup> See Loughlin, n. 20 above, p. 85, quoting Emmanuel Joseph Sieyès (1748-1836), *What is the Third Estate?*, ed. by S.E. Finer and trans. by M. Blondel (London: Pall Mall Press, 1963), pp. 124-128.

<sup>55</sup> See Loughlin, n. 20 above, p. 112.

<sup>56</sup> See Hobbes, n. 31 above, p. 150.

<sup>57</sup> *Ibid.*; and Thomas Hobbes, *The Elements of Law Natural and Politic*, ed. by Ferdinand Tönnies, 2<sup>nd</sup> edn (London: Frank Cass, 1969), p. 34 (see Mark Anthony Wenman, 'Power', in *Political Concepts: A Reader and Guide*, ed. by Iain MacKenzie (Edinburgh: Edinburgh University Press, 2005), pp. 370-385, 371-372).

governed.<sup>58</sup> Such a process goes to the heart of promoting the public interest, that is, of governing. The nature of corporation tax reform, especially given the prominence of the anti-avoidance and compliance and enforcement themes, means that augmenting these bonds is no easy task. Nonetheless, '[t]he vital function [says Loughlin] of the established framework of constituted authority [,] is that of being able to generate trust between governors and governed'.<sup>59</sup> Generating trust depends on a range of factors, including effective action, the cultivation of democratic values,<sup>60</sup> the creation of suitable systems of accountability, and (even), in appropriate situations, on the transference of 'jurisdiction' or 'competence' to the EU. A fourth - perhaps the most important - strand in the discussion is therefore the extent to which the structure, objectives and values of the institutions involved in corporation tax reform help to build up trust and strengthen allegiance to the state in this particular policy area. Such a task is, of course, an exercise in 'constitutionalism',<sup>61</sup> an aspect of state building, albeit in a rather arcane area of public policy. It complements the discussion in Chapter 3, where some of the emphasis passes to the processes by which the goals of corporation tax policy are determined. Generating trust and confidence in the institutions, in a policy area with so great a corporate sector involvement, is difficult because of the accountability problems to which it gives rise.

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<sup>58</sup> See Loughlin, n. 20 above, p. 85.

<sup>59</sup> *Ibid.*, p. 104, quoting John Locke (1632-1704), *Two Treatises of Government*, ed. by Peter Laslett (Cambridge: Cambridge University Press, 1988), p. 407.

<sup>60</sup> See Loughlin, n. 20 above, p. 85.

<sup>61</sup> *Ibid.*, p. 69, referring to Stephen Holmes, *Passions and Constraint: On the Theory of Liberal Democracy* (Chicago: University of Chicago Press, 1995), p. xi.

## INSTITUTIONS AND OBJECTIVES

Within the framework just outlined, this chapter seeks to analyse the institutional dimension of corporation tax reform. Fundamental to HMG's power to initiate successful processes for realising policy objectives - the subject matter of Chapter 3 - is the effectiveness of the institutions engaged in those processes. An introduction to the 'governance perspective',<sup>62</sup> to be taken throughout the study, forms the first part of the discussion. This is an attempt to understand the opportunities, as well as the challenges, presented by possible divergences between the objectives and values of the state, on the one hand, and the corporate sector, on the other. Surprisingly perhaps, for a discussion that began with a mental image of central London, this first part of the discussion requires us to drop a strict 'Westminster model' of the institutions of HMG, in favour of one which is 'fragmented [, and predicates] ... a maze of institutions and organizations'.<sup>63</sup> To isolate how institutional structures, objectives, and values may strengthen or weaken sovereignty, from the processes by which policy goals are set, is no easy task. Yet each is no less important than the other in enhancing trust and confidence in corporation tax policies. Hilson, in his discussion of an entirely distinct policy area, one of 'social regulation',<sup>64</sup> does so with some success, but his analysis, which emphasises institutional accountability, without explaining its relationship to institutional effectiveness, makes use of the 'Sheffield school' approach, rejected on historical and methodological grounds in Chapter 1.

This brings us to an attempt to encapsulate, in the second part of the discussion, the objectives and values of the corporate sector, especially those of multinational corporations

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<sup>62</sup> See Gerry Stoker, 'Governance as theory: five propositions' (1998) 50 *International Social Science Journal* 17-28.

<sup>63</sup> *Ibid.*, p. 19.

(MNCs) and the City of London. This is, in a sense, about how far government may be dominated by economic power, but it is also about whether, prudently managed, the corporate sector may serve the public interest. What we find is rather surprising. Although contemporary political debate is dominated by the tensions between the nation state and the multinational corporate sector, we discover that, given the political choices discussed in Chapter 3, there is a fundamental unity of interest in this particular area between public and private sector institutions. There are tensions, to be sure, but there are also commonalities. To try to pinpoint what these may be, we need to distinguish between different constituencies of economic power, between inward investment by multinationals, and the allocation of funds by international fund managers. Although the differences between these two constituencies could be over-stated, what cannot be denied is the fundamental importance to current political choices of finding some such identity of interest.

The difficulties, given that a government is seeking to build up trust and confidence in its corporation tax policies, are highlighted in the third and fourth parts of the chapter, which examine the constitutional opposition between the structure, objectives and values of Parliament, on the one hand, and, on the other, the Treasury and HMRC (together the Crown). The study takes as axiomatic the view of the UK's constitutional arrangements so elegantly articulated by Adam Tomkins.<sup>65</sup> This is that Parliament holds power which has, over centuries, been 'forced' from the Crown,<sup>66</sup> and that '[t]o the extent that there is a separation of powers in English public law it is a separation between the Crown on the one hand, and Parliament on the other'.<sup>67</sup> What we need to identify in the third and fourth parts of the chapter, therefore, are the characteristics of Parliament and of HMG (here, the

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<sup>64</sup> See Chris Hilson, *Regulating Pollution: A UK and EC Perspective* (Oxford: Hart Publishing, 2000), ch. 4.

<sup>65</sup> See Adam Tomkins, *Public Law* (Oxford: Oxford University Press, 2003).

<sup>66</sup> *Ibid.*, p. 42.

Treasury and HMRC) that may contribute to, or detract from, generating trust and confidence in corporation tax reform. So far as Parliament is concerned, our main concern is the effectiveness with which it holds HMG to account. With the Treasury and HMRC, however, the concern is rather with the qualities that may contribute to their effectiveness in the art and science of governing.<sup>68</sup> Our discussion of the Treasury begins, therefore, with power, and how it is wielded effectively; our discussion of Parliament starts with how HMG is made to account for the wielding. The discussion of Parliament is therefore mainly about parliamentary select committees, while that of the Treasury and HMRC is about prerogative power and how it is constrained.

What we are envisaging, then, is an institutional framework in which there is a pervasive tension between Parliament and Crown. The Crown perceives that it needs to involve the corporate sector, given the similarities in their respective interests. Parliament, however, fears the lack of accountability that this may bring. Accordingly, in the fifth part of the chapter, we need to look a little more closely at the objectives and values of those who are often seen merely as ‘technicians’ in the reform process, and at their relationship with HMG. These are the specialists (lawyers, accountants, etc.), whose presence near the seat of power is so striking to the visitor looking across London from the Eye. The technical expertise of accountants and lawyers, as well as of ‘policy networks more generally’, means that they have a crucial role in bringing to prominence certain policy issues, and co-ordinating representations thereon. Their contributions will be referred to again in the discussion of policy-making in Chapter 3. For present purposes, however, it is policy networks, as institutions, that claim our attention. This is because, besides private sector bodies, some such networks incorporate public servants. Others, however, do not; recent years have seen

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<sup>67</sup> *Ibid.*, p. 44.

the emergence of extremely well informed ‘issue networks’, anxious to highlight what they perceive to be injustices caused by the manipulability of the corporation tax system.

By the end of the chapter, therefore, the key actors, and the dynamics between them, will have been established. The foregoing has posited the fundamental Crown/Parliament opposition: the opportunity of the former to involve the corporate sector, and the concerns of the latter at the accountability problems that this may raise. One other institutional actor needs to be reflected, however: the judiciary. In the sixth, and final, part of the chapter, we look at the role of the judges in corporation tax reform. Following Tomkins and Loughlin, we place them closer to the Crown than to Parliament (judiciary and Crown being related simply by trust),<sup>69</sup> and we consider how the judiciary’s presence may affect the range of reform alternatives. Judicial review is important here, to be sure, but equally so, it is contended, is the judiciary’s approach to interpreting corporation tax legislation.

Corporation tax law as ‘practice’, as the area of public law tasked with enhancing the capacity of the state to ensure that the corporate sector assumes its ‘fair share’ of the overall tax burden, operates in a complex institutional setting. We begin, therefore, with one way of interpreting the interaction between state and corporate sector: the ‘organizing perspective’ of governance. According to Gamble, such an ‘organizing perspective’ provides ‘a framework for analysis, a map of how things relate ...’.<sup>70</sup> In the words of Judge and others (in a different context), it provides ‘a language and frame of reference through which reality can be examined and [which] lead[s] [us] to ask questions that might not otherwise occur’.<sup>71</sup>

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<sup>68</sup> See Chapter 1, nn. 160-164.

<sup>69</sup> See *In re M.* [1994] 1 AC 377, 425D (Lord Woolf) (see Tomkins, n. 65 above, pp. 51-55; Loughlin, n. 20 above, p. 152).

<sup>70</sup> See Gamble, n. 28 above, p. 405.

<sup>71</sup> See David Judge, Gerry Stoker and Harold Wolman, ‘Urban Politics and Theory: An Introduction’, in *Theories of Urban Politics*, ed. by D. Judge, G. Stoker and H. Wolman (London: Sage, 1995), pp. 1-12, 3.

It will readily be appreciated that the ‘organizing perspective’ of governance both complements and illuminates the functionalist, interpretative, public law, inquiry on which we are engaged. What we want, in Isaiah Berlin’s words, is to bring to ‘consciousness ... the model or models that dominate and penetrate ... thought and action’,<sup>72</sup> in particular, in this case, the idea of governance. For this, we need to turn to politics and, in particular, to the ‘new institutionalism’, to test governance values for coherence, consistency and non-contradiction, while appreciating the role that public law plays in shaping and prioritising these values. The UK may well retain its sovereignty in tax matters, but this depends on HMG’s capacity to shape corporation tax policy and this, in turn, depends on how institutional structures, objectives and values help to build up trust, and to strengthen allegiance to the British state.

#### GOVERNANCE, PUBLIC MANAGEMENT AND CORPORATION TAX REFORM

John Tiley, when discussing the ‘constitutionality’ of Extra-Statutory Concessions (ESCs),<sup>73</sup> describes the running of ‘the UK tax system’ with characteristic pungency. The system is, he says, ‘a club’, one whose membership consists of ‘the professions and the department’,<sup>74</sup> i.e., accountants and lawyers, on the one hand, and the ‘Commissioners for Her Majesty’s Revenue and Customs’,<sup>75</sup> on the other. Tiley’s ambiguous imagery contains the kernel of a ‘governance perspective’ on the various institutions whose impressive ‘homes’ are visible from the London Eye. This kernel is an obvious alertness to the implications of involving

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<sup>72</sup> See Isaiah Berlin, ‘Does political theory still exist?’, in *The Proper Study of Mankind: An Anthology of Essays*, ed. by Henry Hardy and Roger Hausheer (London: Pimlico, 1998), pp. 59-90, 76.

<sup>73</sup> See *Vestey (No. 2) v. IRC* [1979] 2 All ER 225, 233 (Walton J.) (referring to *Godden v. Hales* (1686) 89 ER 1050).

<sup>74</sup> See Tiley, n. 19 above, p. 64.

both state and non-state actors in corporation tax reform. Gone, we reiterate, is the ‘Westminster model’, with its ideals of public administration,<sup>76</sup> and in its place is something of a ‘differentiated polity’,<sup>77</sup> organised in terms of ‘the New Public Management’ (NPM). These contrasts get at the heart of the state’s role in governance theory, and they are just two of the main strands in an extensive, searching, but not always consistent, governance literature.<sup>78</sup>

What a ‘governance perspective’ does, claims Gerry Stoker, in the first of five ‘propositions’, designed ‘to present a number of aspects of governance for consideration’,<sup>79</sup> is to sensitise the observer to the implications of involving a range of institutions in - in this case - the process of reforming corporate taxation.

‘Governance [Stoker first points out] refers to a complex set of institutions and actors that are drawn from[,] but also beyond[,] government’.<sup>80</sup> The term therefore highlights the ‘complexity’ created by an institutional framework that includes, not only the Treasury and HMRC, but also regulatory bodies such as the International Accounting Standards Board (IASB),<sup>81</sup> the Accounting Standards Board (ASB),<sup>82</sup> and even supranational and international institutions, such as those of the EU (especially the European Commission and

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<sup>75</sup> See Commissioners for Revenue and Customs Act 2005, s. 1(1).

<sup>76</sup> See Chapter 1 above, n. 175; also, e.g., Rosamund Thomas, *The British Philosophy of Administration: A comparison of British and American ideas 1900-1939* (Cambridge: Centre for Business and Public Sector Ethics, 1989). For the context of this work, see Rhodes, n. 18 above, pp. 166-168. See also Finer, n. 21 above, ch. 30.

<sup>77</sup> See Rhodes, n. 18 above, pp. 7-22.

<sup>78</sup> *Ibid.*, *passim*; Jon Pierre, ‘Introduction: Understanding Governance’, in *Debating Governance*, ed. by Jon Pierre (Oxford: Oxford University Press, 2000), pp. 1-10; Pierre and Peters, n. 38 above; Andrew Gamble, *Politics and Fate* (London: Polity, 2000) and ‘Economic Governance’, in *Debating Governance*, above, pp. 110-137; Jan Kooiman, ‘Societal Governance: Levels, Modes, and Orders of Social-Political Interaction’, in *Debating Governance*, above, pp. 138-164; David Richards and Martin J. Smith, *Governance and Public Policy in the UK* (Oxford: Oxford University Press, 2002), ch. 1.

<sup>79</sup> See Stoker, n. 62 above, p. 18.

<sup>80</sup> *Ibid.*, p. 19.

<sup>81</sup> See [www.iasb.org](http://www.iasb.org) (accessed 21 February 2007).

<sup>82</sup> See [www.asb.org](http://www.asb.org) (accessed 22 February 2007).



the ECJ), the OECD, the International Monetary Fund (the IMF), and the WTO. Simply reciting the range of institutions whose activities impact - in some way or other - on corporation tax reform illustrates only one level of complexity, however. At another level, the 'governance perspective' highlights the different *loci* of 'strategic decision making'.<sup>83</sup> In proposing a 'complex set of institutions and actors', Stoker does not of course have in mind the specific context of corporate taxation. Had he done so, however, he might have drawn attention to the fact that the IASB, the body responsible for formulating the 'international GAAP' that underpins the accounting theme in this study, is not an agency of HMG, and that its funding comes from a range of corporate sector and central bank sources.<sup>84</sup> Nonetheless, the various documents that it produces play a significant, though not decisive, part in shaping the corporation tax base. None of this is to detract, of course, from the point that competence in corporation tax matters remains with HMG.

Thus sensitised, both to the complexity of the institutional framework, and to the fact that strategic decisions are taken outside the institutions of HMG, we are presented with what Stoker designates 'the first dilemma of governance'.<sup>85</sup> This is that, whatever efficiency gains may result from a reliance on expertise, a division of responsibility that requires strategic decisions to be made by people other than ministers of HMG, may not be recognised as legitimate. Distrust of deliberations made in non-governmental institutions has a long history in political discourse in the UK. Recalling the seventeenth century origins of British constitutionalism,<sup>86</sup> this point can be forcefully illustrated with one of the demands made by Parliament to King Charles I in 1642:

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<sup>83</sup> See Stoker, n. 62 above, p. 18.

<sup>84</sup> See International Accounting Standards Committee Foundation, *Annual Report 2005* (London: IASCF, 2006), p. 31.

<sup>85</sup> See Stoker, n. 62 above, p. 19.

‘That the great affairs of the kingdom may not be concluded or transacted by the advice of private men, or by any unknown or unsworn councillors, but that such matters as concern the public, and are proper for the High Court of Parliament, which is your Majesty’s great and supreme council, may be debated, resolved and transacted only in Parliament, and not elsewhere : and such as shall presume to do anything to the contrary shall be reserved to the censure and judgment of Parliament ...’<sup>87</sup>

What is unusual about corporation tax reform is that the nature and scope of the involvement of a body such as the IASB is largely hidden from sight.<sup>88</sup> It may be, therefore, that, valuable as IASB assistance is, the shadowy nature of its influence, in Peters’ words, compounds the widespread difficulties ‘of citizens ... understanding and influencing the actions of their governments’.<sup>89</sup> The more that corporation tax policy comes to be seen as involving political, rather than merely technical, issues, the more the IASB’s involvement will be scrutinised.<sup>90</sup>

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<sup>86</sup> See Tomkins, n. 65 above, p. 45.

<sup>87</sup> ‘The Nineteen Propositions Sent by the Two Houses of Parliament to the King at York’, Proposition 2, reproduced in Samuel R. Gardiner, *Constitutional Documents of the Puritan Revolution 1625-1660*, 3<sup>rd</sup> edn (Oxford: Clarendon Press, 1906), pp. 249-254, 250-251 (see Tomkins, n. 65 above, p. 130); see G.E. Aylmer, *Rebellion or Revolution? England 1640-1660* (Oxford: Oxford University Press, 1986), pp. 35-36.

<sup>88</sup> Besides familiarity with FA 1998, s. 42, understanding of this point requires an appreciation of s. 42’s relationship with FA 2004, s. 50(1), and of both with CA 1985, ss. 226(2), 227(2) and 227(3) (see European Parliament and Council Regulation EC/1606/02 [2002] OJ L243 1, Art. 4); also Stephen Mayson, Derek French and Christopher Ryan, *Company Law*, 22<sup>nd</sup> edn (Oxford: Oxford University Press, 2005), pp. 282-286.

<sup>89</sup> See B. Guy Peters, ‘Managing the Hollow State’, in *Managing Public Organizations: Lessons from Contemporary European Experience*, ed. by Kjell A. Eliassen and Jan Kooiman, 2<sup>nd</sup> edn (London: Sage, 1993), pp. 46-57, 55.

<sup>90</sup> See, e.g., the arguments over IAS 39 and the subsequent adjustments to the special corporation tax code on derivatives (Chapter 1 above, n. 23): Parker, *Financial Times*, 2-3 October 2004, M6; Anon, *Financial Times*, 14 October 2004, 18 (editorial); Hargreaves, Tricks and Arnold, *Financial Times*, 18 October 2004, 1; Bolkestein, *Financial Times*, 9 November 2004, 19; Buck, *Financial Times*, 22 November 2004, 27; Anon, *Financial Times*, 24 November 2004, 20 (editorial); Felsted, *Financial Times*, 30 November 2004, 25; Croft, *Financial Times*, 20 December 2004, 21; Batchelor and Fuller, *Financial Times*, 22 December 2004, 37; Felsted, *Financial Times*, 5 January 2005, 21; Felsted, *Financial Times*, 18 January 2005, 31; Jopson and Felsted, *Financial Times*, 15 March 2005, 30; Jopson, *Financial Times*, 17 March 2005, 9; Jopson, *Financial Times*, 17 March 2005, 50; Jopson, *Financial Times*, 17 September 2005, 30 (see Julian Ghosh and Ian Johnson, *Taxation of Loan Relationships and Derivatives* (London: Butterworths LexisNexis, 1999), paras [10B.471]-[10B.521] (securitisation special purpose vehicles); [10B.861]-[10B.862] (amounts ‘recognised in determining a company’s profit or loss’)).

Within this context of complexity, of fragmented responsibility for ‘strategic decision making’, the tasks of Parliament and HMG in augmenting trust and confidence are particularly sensitive. Stoker characterises the problem in terms of the absence, as regards both the media and society, of ‘a legitimisation framework in which to place the emerging system of governance’.<sup>91</sup> At a general level, ‘tensions’ have emerged over the last decade and more about the implications of NPM for ‘separating policy and operational matters’, about ‘unaccountable quangos’ and about ‘the nature of ministerial accountability’.<sup>92</sup> These general concerns are particularised in corporation tax reform in terms of concerns about the demarcation lines between politics and administration (which can be blurred, when government is seen in terms of management); of concerns about the nature and influence of the IASB;<sup>93</sup> and of worries about the relative unaccountability of the Chancellor of the Exchequer for the conduct of fiscal policy.<sup>94</sup> If the influence of the IASB has tended to be discussed in financial reporting circles, rather than in tax circles, it may be because expertise was until recently a source of greater trust and confidence in tax circles than in other policy areas. However, to recall Tiley once more, one ‘only has to mention the name “Enron”’<sup>95</sup> to illustrate the assertion that that time may now be past.

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<sup>91</sup> See Stoker, n. 62 above, p. 20.

<sup>92</sup> *Ibid.*

<sup>93</sup> See Anon, *Financial Times*, 31 March 2004 (editorial), 17; Pierce and Knight, *Financial Times*, 7 April 2004, 16 (letter); Hargreaves and Tricks, *Financial Times*, 9 December 2004, 20; Buck, Parker and Mai, *Financial Times*, 17 January 2005, 6; Jopson, *Financial Times*, 27 January 2005, 26; Buck and Jopson, *Financial Times*, 3 February 2005, 27; Jopson, *Financial Times*, 22 February 2005, 30; Anon, *Financial Times*, 10 March 2005, 18 (editorial); Tyrrell, *Financial Times*, 17 March 2005, 42 (letter); Thal Larsen, *Financial Times*, 13 June 2005, 21; Jopson, *Financial Times*, 21 October 2005, 30; Jopson, *Financial Times*, 30 January 2006, 26; Fearnley and Hines, *Financial Times*, 25 May 2006, 12.

<sup>94</sup> See Cable, *Financial Times*, 6 December 2006, 19.

<sup>95</sup> See Tiley, n. 19 above, p. 392.

Whilst Stoker frames the problem in terms of how to ensure the ‘legitimacy’ of institutions involved in governance,<sup>96</sup> this is only a version of the point made at the end of the previous part, i.e. that, ‘to be effective in the long run power-holders must be seen to be legitimate. A legitimisation deficit undermines public support and commitment to programmes of change [,] and ultimately undermines the ability of power-holders to mobilise resources and promote co-operation and partnership’.<sup>97</sup> In other words, as we shall see later, ensuring that institutions are effective, whether because of their skill in governing, or their ability to hold other institutions to account, is a *prudential* approach, which helps to augment trust and confidence, and thus to enhance HMG’s sovereignty in tax matters. Effectiveness and capacity are closely interwoven concepts.

In essence, therefore, the governance approach alerts us, first, to the challenge that institutional complexity presents to analysing corporation tax reform, and, secondly, to how, within the context just analysed, responsibilities become ‘blurred’ as between state and non-state actors.

What Stoker asserts, in his second proposition, is that ‘[g]overnance recognises the blurring of boundaries and responsibilities for tackling ... economic issues’.<sup>98</sup> Corporation tax reform, of course, raises crucial economic issues, it being, in common with other areas of tax reform, an aspect of ‘microeconomic’ (‘supply-side’) economic policy.<sup>99</sup> Whilst the importance of this second proposition to illuminating the values and priorities of the actors in corporation tax policy may seem obscure, it does highlight an important dimension to the

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<sup>96</sup> See David Beetham, *The Legitimation of Power* (Basingstoke: Palgrave, 1991), pp. 19-20.

<sup>97</sup> See Stoker, n. 62 above, p. 20.

<sup>98</sup> *Ibid.*, p. 21.

<sup>99</sup> See H.M. Treasury, *Microeconomic Reform in Britain: Delivering Opportunities for All*, ed. by Ed Balls, Joe Grice and Gus O’Donnell (Basingstoke: Palgrave Macmillan, 2004), esp. ch. 1; also Nigel Lawson (Lord Lawson of Blaby), ‘Changing the Consensus’, in *The Chancellors’ Tales: Managing the British Economy*, ed. by Howard Davies (Cambridge: Polity, 2006), pp. 113-146, 115-116 (see also pp. viii-ix).

respective roles of the state and the corporate sector: the views of the Treasury and HMRC of their responsibilities to the corporate sector, as well as the corporate sector's views of its responsibilities to the state. Stoker sees this second proposition primarily in terms of the respective responsibilities of state and private sector in the specific context of public service provision. The 'unbundling' of utilities offers an obvious, and highly contentious, example. But the 'blurring' of responsibilities is important, too, in relation to the present area of inquiry, even though this involves the provision of services by the Crown only in some rather limited sense. This is because there is an increasing acceptance among writers on corporation tax reform of the need for greater mutual respect between the Treasury and HMRC, on the one hand, and the corporate sector, on the other. This is manifested by demands for the former to ensure that market sensitive information on big taxpayers does not become a matter of public knowledge, for instance through 'leaks' to the press, etc.;<sup>100</sup> by calls for the Treasury to justify much more carefully the introduction of statutory measures which have an obvious anti-avoidance dimension; and by suggestions for a 'much lighter touch' in compliance and enforcement matters.<sup>101</sup> The emphasis on responsibilities is no less forceful, however, in the mouths of the officials of HMRC. Companies should look to their social responsibilities, they say; companies should not go around looking to purchase tax avoidance 'products';<sup>102</sup> and they should be much more willing to disclose fully to HMRC the details of

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<sup>100</sup> See Parker and Budden, *Financial Times*, 2 April 2004, 2; also Wales, *Tax Journal*, 20 November 2006, 9-11, esp. 9.

<sup>101</sup> See Eaglesham, *Financial Times*, 6 December 2005, 4; Houlder, *Financial Times*, 31 March 2006, 5; Houlder, *Financial Times*, 21 August 2006, 3; Houlder, *Financial Times*, 17 November 2006, 3; Houlder, *Financial Times*, 25 July 2007, 4.

<sup>102</sup> See Parker, *Financial Times*, 4 May 2004, 1; Parker, *Financial Times*, 4 May 2004, 4 (FA 2002, Sched. 26, para. 22A); Croft, Jolliffe and Davies, *Financial Times*, 17 March 2005, 9; Plender, *Financial Times*, 17 March 2005, 19 (F(No. 2)A 2005, ss. 24-31); Houlder, *Financial Times*, 15 March 2006, 21; Thal Larsen, *Financial Times*, 15 March 2006, 21 (FA 2006, s. 76 and Sched. 6).

their taxation activities.<sup>103</sup> Since there is a responsibility on HMG to raise a ‘fair share’ of tax from the corporate sector, there is also a responsibility on the corporate sector not to seek to cast off that burden.

However, as Stoker says, ‘the dilemma suggested by the blurring of responsibilities is that it creates an ambiguity and uncertainty in the minds of policy-makers and public about who is responsible[,] and can lead to government actors passing off responsibility to ... [the corporate sector] when things go wrong’.<sup>104</sup> Current initiatives, therefore, such as HMRC’s Large Corporates Forum,<sup>105</sup> the assessment of high risk and low risk taxpayers, as well as the secondment of HMRC officials to individual companies, all have the capacity to build up trust and confidence between the ‘Revenue Departments’ and the corporate sector. Equally, however, they have the potential to create precisely the opposite effect. Her Majesty’s Government may stigmatise the corporate sector if corporation tax receipts suddenly drop, while the corporate sector may blame HMG for the adverse effects of tax policy on the UK’s ‘competitiveness’. Again, this is a matter of building up the foundational, political, aspect of sovereignty.

It is the debate on the types of issue just referred to that highlights another consequence of ‘blurred’ responsibilities. This is that the blurring enhances the scope for ‘[t]hose in a position to interpret and lead public debate ... [to], often with considerable effectiveness, blame others for failures and difficulties’.<sup>106</sup> Corporation tax policy provides a rather interesting context for this type of problem. It is an area of public policy where those best placed to ‘interpret and lead public debate’ are multinational corporations, especially, as we shall see in a moment, through their spokespersons in parts of the press and in the legal and

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<sup>103</sup> As envisaged by the ‘interventions’ initiative (see Hubbard, *Taxation*, 2 November 2006, 111-113).

<sup>104</sup> See Stoker, n. 62 above, pp. 21-22.

<sup>105</sup> See [www.hmrc.gov.uk](http://www.hmrc.gov.uk) (accessed 1 October 2007).

accountancy professions. In this connection, the role of the *Financial Times* cannot be underestimated. Although its subtle and studiously detached coverage (often involving interviews with leading tax professionals) strives to avoid any element of the partisan, it is extremely effective at shaping issues for debate. For instance, its policy suggestions<sup>107</sup> after the ECJ's decision in *Cadbury Schweppes*,<sup>108</sup> in September 2006, were largely adopted in the Pre-Budget Report of December that year.<sup>109</sup> Only occasionally, by contrast, does corporation tax policy achieve comparable coverage in more widely consumed media.<sup>110</sup> In this connection, too, PricewaterhouseCoopers, together with the so-called 'Hundred Group of Finance Directors' have begun to publish a striking, if somewhat crude, annual survey of 'the tax contributions made by the UK's largest businesses to government revenues'.<sup>111</sup>

The interpretative approach taken thus far should have created an impression of complexity, both as to the range and the roles of institutions involved in corporation tax reform, and as to the blurring of responsibility for the results. Each of these points raise problems of sovereignty, partly because of 'gaps' in the legitimation of power, and partly because of the tendency of each of government and corporate sector to blame the other, in the event that corporation tax reforms have unintended, and undesirable, consequences.

Problems of sovereignty also arise, however, through the power relations between institutions of government and those of the corporate sector. This brings us to the third of

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<sup>106</sup> See Stoker, n. 62 above, p. 22.

<sup>107</sup> See Anon, *Financial Times*, 14 September 2006, 16.

<sup>108</sup> See Case C-196/04, *Cadbury Schweppes plc. and Another v. Commissioners of Inland Revenue* [2007] 1 CMLR 2.

<sup>109</sup> See *Investing in Britain's potential: Building our long-term future: Pre-Budget Report December 2006* (Cm 6984) (London: TSO, 2006), para. 5.102.

<sup>110</sup> As in *The Money Programme*, 2006. 'No tax please, we're rich!'. TV, BBC 2. 2 March, discussing, inter alia, the personal tax affairs of John Caudwell, the founder of Dextra Accessories/Phones 4U (see *Macdonald (H.M. Inspector of Taxes) v. Dextra Accessories Ltd and Others* [2005] UKHL 47; [2005] STC 1111, para. 8 (Lord Hoffmann)).

<sup>111</sup> See Broadley and Collier-Keywood, *Tax Journal*, 12 February 2007, 7-8, referring to the survey's website at [www.pwc.com/uk/ttc](http://www.pwc.com/uk/ttc) (accessed 12 September 2007).

Stoker's interpretative propositions: that '[g]overnance identifies the power dependence involved in the relationships between institutions involved in collective action'.<sup>112</sup> '[G]overning is an interactive process [he contends] because no single actor, public or private, has the knowledge and resource capacity to tackle problems unilaterally'.<sup>113</sup> We have already noted one example of this phenomenon, in the apparent willingness of the Treasury to entrust part of the responsibility for shaping the corporation tax base to the IASB. This is a form of 'principal-agent' relationship<sup>114</sup> and, as we shall see, it raises classical issues of accountability. We shall, however, be noting a subtly different type of power dependency, that which involves a 'partnership' between HMG and the corporate sector, in which each negotiates 'joint projects in which by blending their capacities they are better able to meet their own ... objectives'.<sup>115</sup> This is the spirit of the various forms of enhanced co-operation suggested both by the Varney Review, of November 2006,<sup>116</sup> and by the emerging concept of 'tax governance', which is currently being fashioned at the hands of tax professionals.<sup>117</sup> Some of the issues of power and its legitimation to which they give rise are considered in the next part of the discussion. Again, our concern is with the 'generative' aspect of sovereignty, with capacity.

The fourth of Stoker's interpretative 'propositions' is closely linked to the power relationships to be examined later in the chapter. It is that partnership relationships, such as those referred to above, tend to lead to the development of 'autonomous self-governing

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<sup>112</sup> See Stoker, n. 62 above, p. 22; Colin Thain and Ross Christie, 'Treasury Power: Past, Present and Future', p. 13, available from [www.treasuryproject.org](http://www.treasuryproject.org) (accessed 22 February 2008).

<sup>113</sup> *Ibid.*, referring to Jan Kooiman, 'Social-Political Governance: Introduction', in *Modern Governance: New Government-Society Interactions*, ed. by Jan Kooiman (London: Sage, 1993), pp. 1-6, 4.

<sup>114</sup> See Stoker, n. 62 above, p. 22.

<sup>115</sup> *Ibid.*

<sup>116</sup> See *2006 Review of Links with Large Business: November 2006* (Chair, Sir David Varney) (London: HMRC, 2006).



networks of actors'.<sup>118</sup> The idea that public policy is influenced by 'policy communities', or 'issue networks' has been explored, most notably perhaps, by Marsh and Rhodes.<sup>119</sup> Two main possibilities are postulated: first, the existence of groups whose purpose is to influence policy; and, secondly, what are referred to as 'governance networks', ones whose purpose is 'not just influencing government policy but taking over the business of government'.<sup>120</sup> In the specific context of corporation tax reform, governance networks clearly exist – comprising representatives of bodies such as the Institute of Chartered Accountants in England and Wales (ICAEW),<sup>121</sup> the Law Society<sup>122</sup> and the Chartered Institute of Taxation<sup>123</sup> – all of which have both the resources and the expertise to take an active part in this particular area of public policy making. The nature of tax policy is such that, whilst reliant on such bodies for their expertise, HMG retains a more pre-eminent position than it does in the other areas of policy making discussed in the literature. Indeed, corporation tax reform has become an area in which the type of partnership just identified is a key feature of the institutional framework. This point will be underlined in Chapter 3 when the time and manner of the involvement of policy communities will be highlighted. Two illustrations will suffice at this stage: first, the discussions under 'Chatham House rules' conducted in Cambridge, involving members of the Treasury and HMRC, as well as academics and

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<sup>117</sup> See David F. Williams, *Developing the Concept of Tax Governance: A discussion paper by David F Williams of KPMG's Tax Business School* (London: KPMG, 2007).

<sup>118</sup> See Stoker, n. 62 above, p. 23; see Thain and Christie, n. 112 above, p. 13.

<sup>119</sup> See David Marsh and R.A.W. Rhodes, 'Policy Communities and Issue Networks: Beyond Typology', in *Policy Networks in British Government*, ed. by David Marsh and R.A.W. Rhodes (Oxford: Clarendon Press, 1992), pp. 249-268; also Rhodes, n. 18 above, pp. 43-45.

<sup>120</sup> See Stoker, n. 62 above, p. 23.

<sup>121</sup> See [www.icaew.co.uk](http://www.icaew.co.uk) (accessed 21 September 2007).

<sup>122</sup> See [www.lawsociety.org.uk](http://www.lawsociety.org.uk) (accessed 21 September 2007).

<sup>123</sup> See [www.tax.org.uk](http://www.tax.org.uk) (accessed 21 September 2007).

members of the practising professions; and, secondly, the regular transfer of prominent individuals between the Revenue Departments and the corporate sector.<sup>124</sup>

‘The dilemma created by such self-governing networks [Stoker correctly points out] is that of accountability’.<sup>125</sup> He analyses this as being problematic ‘at two levels’, which he formulates as ‘an accountability deficit’, both as regards ‘the individual constituent elements of the network and ... those excluded from any particular network’.<sup>126</sup> Thus, not only may members dissatisfied with the direction that ‘reform’ has taken (such as the ‘Tax Law Rewrite’) find it difficult to act, but ‘all networks are to a degree exclusive. They are driven by the self-interest of their members rather than a wider concern with the public interest or more particularly those excluded from the network’.<sup>127</sup> The recent controversy over corporation tax relief for interest payments in ‘private equity’ acquisitions may offer an example, given the nature and extent of trade union intervention in the debate.<sup>128</sup> This self-interest, or the perceptions that it generates, is a major challenge to the capacity of HMG in the particular policy area.

The fifth, and final, of Stoker’s ‘propositions’ is as follows. ‘Governance [he says] recognizes ... [a] capacity to get things done which does not rest on the power of government to command or use its authority. It sees government as able to use new techniques and tools

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<sup>124</sup> See the movements of staff between ‘professional services’ firms, on the one hand, and H.M. Treasury and HMRC, on the other: Chris Sanger, who is in charge of tax policy at Ernst and Young, was previously an adviser to H.M. Treasury (see Houlder, *Financial Times*, 4 December 2006, 3); Edward Troup, who was in charge of tax policy at Simmons and Simmons, the City law firm, moved to H.M. Treasury in 2005; Sir David Varney, Chairman of HMRC from September 2004 until September 2006, was formerly the chairman of a mobile phone company (see Adams, *Financial Times*, 14 May 2004, 3); and Richard Lambert, the Director-General of the CBI since July 2006, was formerly a member of the Monetary Policy Committee of the Bank of England (see Daneshkhu, *Financial Times*, 24 March 2006, 4).

<sup>125</sup> See Stoker, n. 62 above, p. 23.

<sup>126</sup> *Ibid.*

<sup>127</sup> *Ibid.*, p. 24.

<sup>128</sup> See Barber (TUC General-Secretary), *Financial Times*, 16 March 2007, 15; Dromey (Unite Deputy General-Secretary), *Financial Times*, 3 July 2007, 13.

to steer and guide'.<sup>129</sup> Government as 'steering'<sup>130</sup> is a key aspect of governing by 'governance'.<sup>131</sup> Stoker refers to the work of Kooiman and van Vliet in this connection,<sup>132</sup> as elaborating on the institutional aspect of NPM. Besides 'identifying key stakeholders', 'steering' involves 'influencing and steering relationships in order to achieve desired outcomes'. Most importantly, perhaps, governance is 'about what others call "system management"'. It involves thinking and acting beyond the individual sub-systems, avoiding unwanted side-effects and establishing mechanisms for effective co-ordination'.<sup>133</sup> It is in this context, possibly, that the biggest perceived failure of corporation tax (arising perhaps out of HMG's wish to bring about particular political results) has occurred, that of systemic 'complexity'.<sup>134</sup> This in turn can perhaps be attributed to mutual suspicion between the Treasury and HMRC, and the corporate sector, as well as to the inability of the two to achieve a close working relationship. That they must do so, in order for the system to work, is dictated by the need to build up the state's capacity in the area.

The purpose of this part of the discussion has been to highlight the institutional trends that have the greatest implications for sovereignty, for the ability of HMG to shape corporation tax reform and, in doing so, to augment the state. As Stoker says, however, the map constituted by his five 'propositions', 'the governance perspective', 'applies a simplifying lens to a complex reality', identifying 'key' features of that reality and posing 'significant

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<sup>129</sup> See Stoker, n. 62 above, p. 24.

<sup>130</sup> See Christopher D. Foster and Francis J. Plowden, *The State Under Stress* (Buckingham: Open University Press, 1996), pp. 46-47.

<sup>131</sup> See B. Guy Peters, 'Politics is About Governing', in *What is Politics?*, ed. by Adrian Leftwich (Cambridge: Polity, 2004), pp. 23-40, 24-27.

<sup>132</sup> See Stoker, n. 62 above, p. 24; also Jan Kooiman and Martijn van Vliet, 'Governance and Public Management', in Eliassen and Kooiman, n. 89 above, pp. 58-72.

<sup>133</sup> See Stoker, n. 62 above, p. 24.

<sup>134</sup> See Houlder, *Financial Times*, 21 October 2004, 3; Giles, *Financial Times*, 21 October 2004, 3; Howe, *Financial Times*, 22 March 2006, 17; Eaglesham and Houlder, *Financial Times*, 31 January 2006, 4; Houlder, *Financial Times*, 24 March 2006, 2; Houlder, *Financial Times*, 21 April

questions about that reality'.<sup>135</sup> The key element that now requires further elaboration is the exact nature of the challenge to sovereignty presented by the objectives and values of the corporate sector institutions visible from the London Eye.

## THE CORPORATE SECTOR AND THE STATE

If, as is likely, some of the civil servants, accountants and lawyers whose workplaces we imagined at the beginning of the chapter, were listening to the *Today* programme,<sup>136</sup> at around 6.35 on the morning of 8 March 2007, they would have heard a familiar pre-Budget exchange between Sir Digby Jones,<sup>137</sup> then famous as a former Director-General of the Confederation of British Industry (the CBI),<sup>138</sup> and Stuart Wheeler,<sup>139</sup> a City financier and major Conservative party donor. The discussion dealt with the broad outlines of some central issues of the study: the nature of the power of the corporate sector, and the extent to which it facilitates or hinders HMG in achieving its policy objectives. Although the respective contributions, inevitably perhaps, were directed at the contrasting personalities of the then Chancellor of the Exchequer, the Rt Hon. Gordon Brown, MP, and the Rt Hon. David Cameron, MP, the leader of the Opposition, they were about the extent to which Gordon Brown, as Prime Minister, would be able to rely on the constructive engagement of different

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2006, 3; Houlder, *Financial Times*, 8 November 2006, 4; Houlder, *Financial Times*, 15 August 2007, 3; Giles, *Financial Times*, 26 July 2007, 2.

<sup>135</sup> See Stoker, n. 62 above, p. 26.

<sup>136</sup> See [www.bbc.co.uk/radio4/today](http://www.bbc.co.uk/radio4/today) (accessed 21 September 2007).

<sup>137</sup> On Sir Digby Jones's generally supportive attitude to the governing party, see the acerbic observations in Hywel Williams's, *Britain's Power Elites: The Rebirth of a Ruling Class* (London: Constable, 2006), p. 185, and Monbiot, *Guardian*, 10 July 2007, 29.

<sup>138</sup> See [www.cbi.org.uk](http://www.cbi.org.uk) (accessed 21 September 2007). Duly 'ennobled' as Lord Jones of Birmingham (see Guthrie, *Financial Times*, 12 July 2007, 13), Sir Digby Jones became a Minister of State at both the Foreign and Commonwealth Office and at the newly formed Department for Business, Enterprise and Regulatory Reform, on Gordon Brown's taking office in June 2007 (see Eaglesham, *Financial Times*, 3 July 2007, 3).

corporate sector constituencies. While conceding that the Chancellor had demonstrated ‘economic competence’, the former CBI Director-General stressed Gordon Brown’s status as what he described as ‘one of the great taxing Chancellors’, and hinted at the long-stop possibility of businesses dissatisfied with the UK’s taxation climate relocating to other, more ‘business friendly’ jurisdictions. Properly interpreted, this contribution could perhaps be seen as no more than a voicing of the predictable concerns of a corporate sector operating within the governance context discussed above. Stuart Wheeler’s approach was, however, rather different. Gordon Brown may well have been a ‘taxing Chancellor’, he opined, but what was much more significant was that he was ‘not at all trusted in the City’,<sup>140</sup> and David Cameron would, in this respect, be a breath of fresh air. Moreover, the Chancellor faced the real risk that the headquarters operations of MNCs, though probably not fairly small businesses operating solely in the UK, would look to relocate in other countries, in order to avoid corporation tax.

Setting aside the inevitable media preoccupation with personalities, and bearing in mind the untheorised and partisan nature of the radio discussion, it nonetheless distilled some important realities about the relative power of corporate sector and governmental institutions. This is a huge and important topic but it is possible, even within a relatively brief compass, to elucidate it. First and foremost, it arises in the context of debates about the continuing significance of the nation state, under conditions created by that nebulous<sup>141</sup> but much-

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<sup>139</sup> Known both for his generosity to the Conservative party (he donated £5 million in 2001) and for his extravagant admiration for Lady Thatcher.

<sup>140</sup> A sally with which Sir Digby Jones would not explicitly concur although, interestingly (given the difference of perspective) one echoed by Lord Giddens, in an observation raised in questions following a lecture at Warwick University on 20 February 2007, when he said that the Chancellor was ‘not very popular in the City’.

<sup>141</sup> See Jan Aart Scholte, *Globalization: A Critical Introduction*, 2<sup>nd</sup> edn (Basingstoke: Palgrave Macmillan, 2005), pp. 15-22.

discussed idea of ‘globalisation’.<sup>142</sup> From Saskia Sassen, who maintains that ‘the major dynamics at work in the global economy carry the capacity to undo the particular form of the intersection of sovereignty and territory embedded in the modern state’,<sup>143</sup> to Hardt and Negri, who proclaim the end of the ‘centuries-long dialectic’ between capital and the state,<sup>144</sup> a succession of commentators<sup>145</sup> has asserted that governmental sovereignty has been eviscerated, or at least transformed, by global economic power. The view taken in this study is that, in the context of corporate tax policy, the state does indeed retain its importance, but that, in the global economy, new demands are made upon its sovereignty in the particular policy area. The problem is a serious one, nevertheless. If, as is suggested above, the first dilemma of the governance of corporation tax reform is taken to be that we, or – more accurately – Parliament, cannot effectively interrogate certain key areas of policy, then the possibility that those areas may be ones in which global economic power is dominant surely gives clear cause for concern. Prudent management of the corporate sector’s economic power is therefore needed for HMG to maintain the trust and confidence of the governed, and effective scrutiny of that management is required from Parliament.

Secondly, it is important in speaking of economic power, especially global economic power, to make some careful distinctions. Hobbes, as mentioned earlier, differentiated

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<sup>142</sup> See Joseph E. Stiglitz, *Globalization and its Discontents* (London: Penguin, 2002); Martin Wolf, *Why Globalization Works* (London: Yale, 2005); Joseph E. Stiglitz, *Making Globalization Work* (London: Penguin, 2007).

<sup>143</sup> See Saskia Sassen, *Losing Control? Sovereignty in an Age of Globalization* (New York: Columbia University Press, 1996), p. 5.

<sup>144</sup> See Michael Hardt and Antonio Negri, *Empire* (London: Harvard University Press, 2000), p. 306.

<sup>145</sup> See Kenichi Ohmae, *The End of the Nation State: The Rise of Regional Economies* (London: HarperCollins, 1995); Helen V. Milner and Robert O. Keohane, ‘Internationalization and Domestic Politics: A Conclusion’, in *Internationalization and Domestic Politics*, ed. by Robert O. Keohane and Helen V. Milner (Cambridge: Cambridge University Press, 1996), pp. 243-258; Susan Strange, *The retreat of the state: The diffusion of power in the world economy* (Cambridge: Cambridge University Press, 1996); Sassen, n. 143 above; John Gray, *False Dawn: The Delusions of Global Capitalism*, 2<sup>nd</sup> edn (London: Granta, 2002); (elliptically) Thomas Friedman, *The Lexus and the Olive Tree* (London: HarperCollins, 1999); Hardt and Negri, n. 144 above, pp. 306-307.

between ‘power to’ (capacity) and ‘power over’ (domination).<sup>146</sup> The idea that the corporate sector might dominate a government was a matter for concern at least as far back as the closing years of the nineteenth century.<sup>147</sup> This was unsurprising, since the joint-stock company was, in the words of Peter Drucker, ‘the first new autonomous institution in hundreds of years, the first to create a power center that was within society yet independent of the central government of the national state’.<sup>148</sup> Nonetheless, as Angus Stewart has contended,<sup>149</sup> and contrary to Talcott Parsons,<sup>150</sup> Steven Lukes,<sup>151</sup> and Hardt and Negri<sup>152</sup> (via Michel Foucault),<sup>153</sup> power is not the same as domination, and, although thinkers on the Left deplore it, there is no denying the reality of the ‘neoliberal’ economic consensus.<sup>154</sup> Keeping the confidence and trust of the governed, in corporate tax policy, as in any area, is essential to a government’s capacity,<sup>155</sup> and it involves managing the potential of the corporate sector to dominate. ‘Power to’, as Stewart says, is ‘the expression of collective autonomy, conceived as the intersubjective generation of specific forms of solidarity ...

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<sup>146</sup> See Hobbes, nn. 56 and 57 above.

<sup>147</sup> See ‘Utopia Limited or The Flowers of Progress’, in *The Complete Annotated Gilbert and Sullivan*, ed. by Ian Bradley (Oxford: Oxford University Press, 1996), pp. 969-1079, 1037-1039: ‘KING: ‘And do I understand you that Great Britain/Upon this Joint Stock principle is governed?/ MR. GOLD. We haven’t come to that, exactly – but/We’re tending rapidly in that direction./The date’s not distant.’ See also the comments attributed, in the US context, to President Rutherford B. Hayes, in John Micklethwait and Adrian Wooldridge, *The Company: A Short History of a Revolutionary Idea* (London: Phoenix, 2005), p. 2; also Hobbes, n. 31 above, p. 375.

<sup>148</sup> See Peter F. Drucker, *The Frontiers of Management* (London: Heinemann, 1987), p. 170; also, but to a different purpose, Adolf A. Berle and Gardiner C. Means, *The Modern Corporation and Private Property*, rev. edn (New York: Harcourt, Brace and World, 1967), p. 313.

<sup>149</sup> See Angus Stewart, *Theories of Power and Domination: The Politics of Empowerment in Late Modernity* (London: Sage, 2001), ch. 2.

<sup>150</sup> See Talcott Parsons, ‘On the Concept of Political Power’, in *Political Power: A Reader in Theory and Research*, ed. by Roderick Bell, David V. Edwards and R. Harrison Wagner (London: The Free Press, 1969), pp. 251-284.

<sup>151</sup> See Steven Lukes, *Power: A Radical View*, 2nd edn (Basingstoke: Palgrave Macmillan, 2005).

<sup>152</sup> See n. 144 above.

<sup>153</sup> See Michel Foucault, ‘The Subject and Power’, in Michel Foucault, *Power*, ed. by James D. Faubion (London: Allen Lane Penguin, 2001), pp. 326-348. See Loughlin, n. 20 above, p. 96.

<sup>154</sup> See Colin Leys, *Market-driven Politics: Neoliberal Democracy and the Public Interest* (London: Verso, 2001), ch. 3; also Adair Turner, *Just Capital: The Liberal Economy*, rev. edn (London: Pan Books, 2002), *passim*.

power as action in concert'.<sup>156</sup> To the profound disapproval of the Left,<sup>157</sup> HMG's commitment to private sector economic growth<sup>158</sup> is at least consistent with the corporate sector's interests. The potential for conflict is real enough,<sup>159</sup> but it is capable of being managed. If taxation policies provoke conflict, it is the 'flight' of capital that will damage economic growth;<sup>160</sup> an important aspect of HMG's task is to see that that does not happen.

Thirdly, some important distinctions need to be drawn between various constituencies of economic power. The key distinctions here are the ones implied by the radio discussion referred to earlier, between the power of MNCs and that of the City, and between MNCs and the power of firms operating exclusively in the UK. So far as MNCs are concerned, one important relationship might be that between HMG and 'foreign-owned subsidiaries' but, given certain historical factors, the relationship between HMG and 'parent firms'<sup>161</sup> might possibly be even more important.<sup>162</sup> The nature and extent of the economic power of MNCs has spawned an extensive literature,<sup>163</sup> ever since the rapid expansion into Europe of United

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<sup>155</sup> See Loughlin, n. 20 above, pp. 76-77 (Loughlin's second 'tenet' of sovereignty).

<sup>156</sup> See Stewart, n. 149 above, p. 6.

<sup>157</sup> See Leys, n. 154 above, p. 44. '[P]ost-classical endogenous growth theory' is incorrect (see Chapter 4 below); so is 'neoclassical endogenous growth theory' (see David Lipsey, *The Secret Treasury* (London: Viking, 2000), p. 27).

<sup>158</sup> See Wyn Grant, *Economic Policy in Britain* (Basingstoke: Palgrave, 2002), pp. 34-40.

<sup>159</sup> See Chapter 1 above, pp. 25-30.

<sup>160</sup> See Adam Smith (1723-1790), *An Inquiry into the Nature and Causes of the Wealth of Nations*, ed. by R.H. Campbell and A.S. Skinner (textual editor W.B. Todd), 2 vols (Oxford: Clarendon Press, 1976), I, p. 364; II, pp. 848-849, 906, 927-928.

<sup>161</sup> See Raymond Vernon, *In the Hurricane's Eye: The Troubled Prospects of Multinational Enterprises* (London: Harvard University Press, 1998), p. 2.

<sup>162</sup> Ipsos MORI, *UK Corporate Taxation and International Competitiveness* (London: Confederation of British Industry, 2006), Appendices, Section 2; also Dodwell, *Tax Journal*, 2 July 2007, 15-16, 16.

<sup>163</sup> See, e.g., Christopher Tugendhat, *The Multinationals* (Harmondsworth: Penguin, 1973), *passim*; DeAnne Julius, *Global Companies and Public Policy: The Growing Challenge of Foreign Direct Investment* (London: Pinter, 1990), esp. ch. 3; Vernon, n. 161 above, esp. chs 4 and 6; Peter J. Buckley and Mark Casson, *The Future of the Multinational Enterprise*, 3<sup>rd</sup> edn (Basingstoke: Palgrave Macmillan, 2002), esp. ch. 5.



States firms in the decades after the Second World War.<sup>164</sup> Only relatively recently, however, in the work of Nathan Jensen, has its political significance been identified with some precision.<sup>165</sup> What Jensen proposes is a certain identity, rather than an opposition, of interests, between MNCs and civil society. This is not to deny that MNCs have ‘policy preferences’, nor that their prime objective is profit-maximisation, but it does assert that ‘the consolidation and maintenance of democratic institutions’ are crucial factors in the willingness of MNCs to invest in particular states, in the UK no less than any other.<sup>166</sup> In other words, that there is little more unappealing for foreign direct investment (FDI) than wide ‘executive discretion’.<sup>167</sup> What Jensen does assert, against the arguments of Rosanne Altshuler and others,<sup>168</sup> is that ‘there is very little empirical support for claims that taxes or other forms of government fiscal policy seriously affect FDI inflows’.<sup>169</sup> Such matters are far less important, from MNCs’ viewpoint, than institutions structured in such a way as to minimise ‘political risk’: ‘Institutions affect policies, and policies affect multinational operations’.<sup>170</sup>

If the power of MNCs has given rise to extensive debate, so, too, has the power of the City of London,<sup>171</sup> and the issues raised by the possibility of ‘capital flight’. In this

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<sup>164</sup> For a famous example, at least in its day, see Jean-Jacques Servan-Schreiber’s *The American Challenge*, trans. by Ronald Steel (London: Hamish Hamilton, 1968), esp. pp. 3-7 and 199-202; also Raymond Vernon, *Sovereignty at Bay: The Multinational Spread of U.S. Enterprises* (London: Longman, 1971), esp. ch. 8. See Micklethwait and Wooldridge, n. 147 above, pp. 163-165.

<sup>165</sup> See Nathan M. Jensen, *Nation-States and the Multinational Corporation: A Political Economy of Foreign Direct Investment* (Woodstock: Princeton University Press, 2006).

<sup>166</sup> *Ibid.*, p. 153.

<sup>167</sup> *Ibid.*, p. 152.

<sup>168</sup> Rosanne Altshuler, Harry Grubert and T. Scott Newlon, ‘Has U.S. Investment Abroad Become More Sensitive to Tax Rates?’, in *International Taxation and Multinational Activity*, ed. by James R. Hines Jr (London: University of Chicago Press, 2001), pp. 9-32, 28.

<sup>169</sup> See Jensen, n. 165 above, p. xii; also Houlder, *Financial Times*, 23 July 2007, 7.

<sup>170</sup> *Ibid.*, p. 2.

<sup>171</sup> For useful descriptions of the City of London’s markets and their historical development, see, e.g., David Kynaston, *The City of London, vol. IV: A Club No More, 1945-2000* (London: Chatto and Windus, 2001), *passim*; Mike Buckle and John Thompson, *The UK Financial System: Theory and*

connection, Layna Mosley's work<sup>172</sup> provides useful complementary insights to those offered by Jensen. Mosley's analysis is not specifically concerned with the relationship between HMG and the City.<sup>173</sup> Nonetheless, it does seek to throw light on the weight given to matters such as 'the structure of a nation's tax system' '[w]hen a bond trader at Goldman Sachs, or a fund manager at Fidelity, sits at his desk, contemplating where to allocate investment'.<sup>174</sup> Just as the territory of Jensen's analysis is FDI, Mosley is concerned with 'portfolio investment',<sup>175</sup> in particular with 'the government bond market ... and ... the causal pathways associated with it'.<sup>176</sup> Her conclusion is perhaps surprising, which is that:

'[i]n the advanced capitalist democracies, market participants consider key macroeconomic indicators, but not supply-side or microlevel policies. ... So, whereas many governments have converged cross-nationally in the pursuit of lower inflation and lower government budget deficits, they have not converged in a variety of other areas, including overall government consumption, the structure of tax systems, and the role of labor market institutions within the economy'.<sup>177</sup>

Fourthly, it is clear that the corporate sector cannot legitimise itself by making decisions based on rather narrow 'economistic' calculations. Increasingly, as the 'governance' phenomena referred to earlier, as the PricewaterhouseCoopers/Hundred Group 'total tax contribution' database, and as the evolving notion of 'tax governance' illustrate, the

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*Practice*, 4<sup>th</sup> edn (Manchester: Manchester University Press, 2004), chs 7-13; William M. Clarke, *How the City of London Works: An Introduction to its Financial Markets*, 6<sup>th</sup> edn (London: Sweet and Maxwell, 2004), *passim*; Richard Roberts, *The City: A Guide to London's Global Financial Centre* (London: Profile, 2004), *passim*.

<sup>172</sup> See Layna Mosley, *Global Capital and National Governments* (Cambridge: Cambridge University Press, 2003).

<sup>173</sup> For the relationship between the City and 'New Labour', see Augar, n. 10 above, pp. 183-184; also Patrick Diamond, 'The Political Power of Economic Ideas: Understanding Relations between "New" Labour and the City in the Post-War Era', in *The City in Europe and the World*, ed. by Stephen Barber (London: European Research Forum, 2005), pp. 65-83.

<sup>174</sup> See Mosley, n. 172 above, p. 25.

<sup>175</sup> See Jensen, n. 165 above, p. 23.

<sup>176</sup> *Ibid.*, p.17.

<sup>177</sup> See Mosley, n. 172 above, p. 305.

corporate sector must seek more subtle and broader-based ways of legitimating its activities. These are usually gathered together under the umbrella term of ‘corporate social responsibility’,<sup>178</sup> an expression that is coming to include the payment of ‘appropriate’ levels of taxation.<sup>179</sup> For example, although said to be attributable to technical matters (levels of pensions contributions), reports such as that in 2007 of the retailer, J. Sainsbury, having ‘paid no corporation tax in 2005-06’,<sup>180</sup> cannot be said to enhance the firm’s reputation for corporate social responsibility. Short-term considerations over maximising shareholder value have wider implications, themselves of an economic nature.

Finally, there is an element of the experiential in interpreting the impact of corporate tax policy on levels of inward investment and incipient ‘capital flight’. Experience would suggest that, though often discussed, capital flight based on corporation tax levels has rarely, if ever, materialised in this jurisdiction. The problem for HMG is how to retain the trust and confidence of society as a whole, in circumstances such that the influence of the corporate sector appears to be so great. In so far as there is a solution, it would appear to lie in the extent to which the objectives, structure and values of the UK’s political institutions are such as to enable them to uncover the true extent to which that influence is exercised.

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<sup>178</sup> See Micklethwait and Wooldridge, n. 147 above, pp. 79-81, 153, 174; also Berle and Means, n. 148 above, *passim*; also Peter F. Drucker, *The Concept of the Corporation* (New York: Mentor, 1964), ch. 3; also Peter A. French, *Collective and Corporate Responsibility* (New York: Columbia University Press, 1984), ch. 3; also Sally Wheeler, *Corporations and the Third Way* (Hart Publishing, 2002), pp. 72-78; also *Responsible Business: Financial Times Special Report*, 3 July 2007; also Henderson Global Investors, *Responsible Tax* (London: Henderson, 2005).

<sup>179</sup> See Houlder, *Financial Times*, 22 November 2004, 9.

<sup>180</sup> See Houlder, *Financial Times*, 28 August 2007, 3.

## PARLIAMENT

For some, such as David Marquand<sup>181</sup> and Will Hutton,<sup>182</sup> the turrets and pinnacles of the Palace of Westminster have long been emblematic of a state whose political institutions are ill equipped, either to work with the corporate sector, or to safeguard the public interest against corporations' encroaching influence.<sup>183</sup> Impatience on the former count is detectable, too, in commentaries on changes to corporation tax legislation.<sup>184</sup> Having highlighted, earlier in the chapter, some of the issues arising from recent trends in governance, we next assess how well placed Parliament, the key institution of the UK's representative government, is to scrutinise the relationship between the Crown and the corporate sector.

What constitutes a representative, as opposed to a direct democracy, Bernard Manin tells us, 'is not the fact that a few govern in the place of the people, but that they are selected by election'.<sup>185</sup> However low (or high) our opinion of representative government is, therefore, we need to remember that the strength of representative institutions is that they 'subject those who govern to the verdict of those who are governed'.<sup>186</sup> It is the latter, ultimately, who will pass judgment, if not on corporation tax reform in particular, then on the 'UK economy' in general, the stability and growth of which corporation tax reform is intended to strengthen

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<sup>181</sup> See David Marquand, *The Unprincipled Society: New Demands and Old Politics* (London: Fontana, 1988), ch. 7.

<sup>182</sup> See Will Hutton, *The State We're In*, rev. edn (London: Vintage, 1996), ch. 11.

<sup>183</sup> See, e.g., Monbiot, *Guardian*, 10 July 2007, 29. For efforts to 'bridge the gap', see Muggeridge, *Financial Times*, 31 July 2007, 10 (letter). See Chapter 3 below.

<sup>184</sup> See, e.g., on reforms of another era, Malcolm Gammie's, 'Has Nigel Lawson Really Reformed Business Taxation?' (1984) FS 82-93; even more categorical is Hole [1996] BTR 347-358, 358.

<sup>185</sup> As opposed to a combination of election and lot (as in Athenian democracy). See Bernard Manin, *The Principles of Representative Government* (Cambridge: Cambridge University Press, 1997), p. 41.

<sup>186</sup> *Ibid.*, p. 234. See Sampson, n. 15 above, p. 14.

and support.<sup>187</sup> The UK's constitutional arrangements mean that the relationship between HMG and Parliament is peculiarly close, the Crown in Parliament being 'the sole representative of the person of the state'.<sup>188</sup> The fact that members of the executive both sit and vote in the legislature is, as Tomkins reminds us, Walter Bagehot's 'efficient secret' of the constitution.<sup>189</sup> The objection to the governance trends highlighted above is thus, in part at least, precisely that the non-state actors involved are not ministers, and therefore do not (by definition) have a seat in one or other of the Houses of Parliament. Although Parliament tends to be thought of as a legislative body, its real strength, as Tomkins has argued persuasively, is that it is a scrutinising body.<sup>190</sup> This scrutinising role includes, of course, Parliament's *ex ante* scrutiny of legislation,<sup>191</sup> but it also comprises its *ex post* scrutiny of governmental policy through select committees.<sup>192</sup> Parliament is the body that, in Walter Bagehot's words, 'has ... an informing function ... to inform the Sovereign what ... [is] wrong ... [and] to lay ... grievances ... before the nation'.<sup>193</sup> It is in this sense that Parliament holds HMG to account, and not precisely, as John Stuart Mill claimed, by 'watching' and 'controlling' it.<sup>194</sup> Select committees, in advising HMG of failures in policy, are thus, if Parliament is seen as the scrutinising element of the Crown in Parliament, a source of capacity, of political power. '[W]e at no time stand so highly in our estate royal',

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<sup>187</sup> See, e.g., H.M. Treasury and HMRC, *Business tax reform: capital allowances changes July 2007* (London: H.M. Treasury, 2007), p. 3.

<sup>188</sup> See Loughlin, n. 20 above, p. 84; also A.F. Pollard, *The Evolution of Parliament*, 2<sup>nd</sup> edn (London: Longmans, 1926), pp. 229-234.

<sup>189</sup> See Tomkins, n. 65 above, p. 38.

<sup>190</sup> See Adam Tomkins, 'What is Parliament for?', in *Public Law in a Multi-Layered Constitution*, ed. by Nicholas Bamforth and Peter Leyland (Oxford: Hart Publishing, 2003), pp. 53-78.

<sup>191</sup> The legislative function as expressed in 'Parliamentary sovereignty' is not therefore Parliament's 'dominant characteristic', as Dicey maintained (see Dicey, n. 52 above, p. 39). See Chapter 3 below.

<sup>192</sup> Chris Hilson's terminology (see Hilson, n. 64 above, p. 52).

<sup>193</sup> See Walter Bagehot (1826-1877), *The English Constitution* (London: Kegan Paul, 1919), p. 133.

<sup>194</sup> See John Stuart Mill (1806-1879), 'Considerations on Representative Government', in *On Liberty and Other Essays*, ed. by John Gray (Oxford: Oxford University Press, 1991), pp. 203-467, 282.

said the Tudor monarch, ‘as in the time of parliament’.<sup>195</sup> Tomkins’ proposal for interpreting the role of Parliament in this way relies on the ancient idea that more people are available to advise the Crown when Parliament is sitting than at any other time.<sup>196</sup> The ‘ancient constitution’ thus envisaged that taxation, the archetype of a measure that touches and concerns everyone, and that therefore needs political power in order to be effective, should be considered by the Crown in Parliament.<sup>197</sup> Charles I’s attempt to impose taxation in reliance on the royal prerogative, and counting on the allegiance of the judges, has long provided a salutary illustration of the consequences of ignoring this principle.<sup>198</sup> This is why the 1689 Bill of Rights, the curiously anomalous founding document of English government,<sup>199</sup> which itself invokes the principles of the ancient constitution, bans the raising of taxation ‘by pretence of prerogative’,<sup>200</sup> and requires that Parliament grant taxation (i.e. ‘supply’) to the Crown.

In case all of this sounds as though it owes too much to a Whig version of history, it is useful to reflect on the kind of representative institution that the House of Commons has become. Manin finds the principle that ‘[t]hose who govern are appointed by election at regular intervals’ as one of the key ‘constants’ of representative government.<sup>201</sup> David Judge

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<sup>195</sup> Henry VIII, in 1542, quoted in Michael A.R. Graves, *The Tudor Parliaments: Crown, Lords and Commons, 1485-1603* (London: Longman, 1985), p. 80.

<sup>196</sup> See Tomkins, n. 190 above, p. 56.

<sup>197</sup> On the *quod omnes tangit* principle (see Manin, n. 185 above, pp. 86-87); Tomkins, n. 65 above, p. 41; J.H. Baker, *An Introduction to English Legal History*, 4<sup>th</sup> edn (London: Butterworths, 2002), p. 205; Magna Carta 1215, cl. 12 (‘[n]o scutage or aid is to be levied in our realm except by the common counsel of the realm’), reproduced in J.C. Holt, *Magna Carta*, 2<sup>nd</sup> edn (Cambridge: Cambridge University Press, 1992), p. 455.

<sup>198</sup> See John Adamson, *The Noble Revolt: The Overthrow of Charles I* (London: Weidenfeld & Nicolson, 2007), pp. 7-12, 35n; also Tomkins, n. 190 above, p. 58.

<sup>199</sup> See the quotation attributed by G.M. Young to Lord Palmerston: ‘[O]ur government was founded in 1688’. (See G.M. Young, ‘The Liberal Mind in Victorian England’, in *Last Essays* (London: Rupert Hart-Davis, 1950), pp. 206-213, 211.)

<sup>200</sup> Bill of Rights 1689, fourth indent (reproduced in Geoffrey Wilson, *Cases and Materials on Constitutional and Administrative Law*, 2<sup>nd</sup> edn (Cambridge: Cambridge University Press, 1976), pp. 2-6). See Chapter 1 above, n. 337.

<sup>201</sup> See Manin, n. 185 above, p. 6.

relates Manin's insights to the contemporary House of Commons,<sup>202</sup> to show us why, even in times of disillusionment, the Commons might nonetheless be a source of trust and confidence. The situation today, Manin tells us, is not one of 'parliamentarianism', nor yet one of 'party democracy'. Instead, what we experience today is "'audience" democracy',<sup>203</sup> which nonetheless retains a key legitimating feature of those earlier models. The electorate chooses the 646 MPs because it thinks that they are 'special', and it also decides the basis on which that status is to be awarded.<sup>204</sup> This has, as we shall see, resonances for corporation tax reform when it comes to the qualities of the ministers of the Crown – the Treasury ministers – who sit on the Government front bench and deal with corporation tax matters. But it applies, too, to the individual MPs who carry out the Commons' scrutinising function in relation to this particular area of public policy: the House of Commons Treasury Select Committee.<sup>205</sup> This representativeness is lacking, to be sure, in the House of Lords Select Committee on Economic Affairs; it is very doubtful whether this is compensated by the Committee's undoubted technical expertise.<sup>206</sup>

Select committees, today Parliament's main scrutiny mechanism,<sup>207</sup> have increased in significance as ministerial responsibility has been seen to decline.<sup>208</sup> Summarising the strengths and weaknesses of select committees, in the matrix of their scrutiny, or

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<sup>202</sup> See Judge, n. 27 above, pp. 34-35.

<sup>203</sup> See Manin, n. 185 above, pp. 218-226.

<sup>204</sup> *Ibid.*, p. 236.

<sup>205</sup> Of the Committee's 14 members, as at 1 July 2007, at least 10 were graduates (eight of these from Oxbridge), and one was a Scottish aristocrat (John Thurso, MP (Caithness, Sutherland and Easter Ross, Liberal Democrats)).

<sup>206</sup> See Judge, n. 27 above, p. 76.

<sup>207</sup> See S.O.s, Nos 121-152C; *Erskine May's Treatise on The Law, Privileges, Proceedings and Usage of Parliament*, ed. by Sir William McKay *et al.*, 23<sup>rd</sup> edn (London: LexisNexis UK, 2004), ch. 26; Judge, n. 27 above, pp. 55-64; Tomkins, n. 65 above, pp. 162-164 and 166-168; John Greenwood, Robert Pyper and David Wilson, *New Public Administration in Britain*, 3<sup>rd</sup> edn (London: Routledge, 2002), pp. 175-176; Michael Rush, *Parliament today* (Manchester: Manchester University Press, 2005), pp. 225-240.

accountability, function, Tomkins has some useful comments. Reflecting on stories of the Government, via its whips, seeking to control select committee membership, he says:

‘Both positive and negative conclusions can be drawn from these stories. On the plus side, they suggest that select committees are sufficiently powerful, prestigious, and effective to be taken seriously by the government and its whips. If select committees were worthless, or ineffective, why go through the bother of seeking to manipulate their membership and direction? But on the minus side, of course, these committees are supposed to be rigorous and independent committees of inquiry. If the whips can so easily remove thorns from the government’s flesh, will that not discourage rigour? If the whips have control over membership, does that not dilute the extent to which the committees can truly be said to be independent of government?’<sup>209</sup>

Accountability, ‘[t]he rendering of accounts’, is, in Manin’s view, nothing less than ‘the democratic component of representation’.<sup>210</sup> Departmental select committees,<sup>211</sup> which date from 1979, take their cue from the Public Accounts Committee, instituted by Gladstone in 1861.<sup>212</sup> In common with other select committees, the Treasury Committee deliberates in private,<sup>213</sup> but it hears evidence in public,<sup>214</sup> and these proceedings are widely reported.<sup>215</sup> It has summarised its ‘first and most important objective’ as being ‘to examine and comment upon the economic policy of the Government’.<sup>216</sup> Treasury ministers do well to weigh the Committee’s findings carefully, since, if one thing at least is certain, it is that representative government ‘still entails that supreme moment when the electorate passes judgment on the

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<sup>208</sup> See Colin Turpin, ‘Ministerial Responsibility’, in *The Changing Constitution*, ed. by Jeffrey Jowell and Dawn Oliver, 3<sup>rd</sup> edn (Oxford: Clarendon Press, 1994), pp. 109-151.

<sup>209</sup> See Tomkins, n. 65 above, p. 164.

<sup>210</sup> See Manin, n. 185 above, p. 234.

<sup>211</sup> See S.O., No. 152; Erskine May, n. 207 above, pp. 779-782.

<sup>212</sup> See H.C.G. Matthew, *Gladstone: 1809-1874* (Oxford: Clarendon Press, 1986), p. 117; H.C.G. Matthew, *Gladstone: 1875-1898* (Oxford: Clarendon Press, 1995), p. 166.

<sup>213</sup> See Erskine May, n. 207 above, pp. 738 and 755.

<sup>214</sup> See S.O., No. 125(1); Erskine May, n. 207 above, p. 755.

<sup>215</sup> Both in the ‘print media’ and on a dedicated BBC channel (see <http://news.bbc.co.uk/tv>).

<sup>216</sup> See House of Commons Treasury Committee, *2<sup>nd</sup> Report. The 2005 Pre-Budget Report* (House of Commons Papers, Session 2005-2006, 739) (London: The Stationery Office, 2006), p. 5.



past actions of those in government'.<sup>217</sup> We can illustrate the effectiveness of the Committee by considering the success with which it has illuminated the problems raised by the governance trends in corporation tax reform discussed in the first part of the chapter.

One group of issues, it will be recalled, arises from the Chancellor's accountability for the conduct of fiscal policy, in a climate in which NPM ideas have tended to 'blur' questions of policy and administration. During the current Parliament, Gordon Brown (as Chancellor) has appeared before the Committee on at least four separate occasions, corporation tax featuring to a greater or lesser extent each time. The strengths and weaknesses of the Committee in addressing the issues on each occasion mirror those analysed in an extensive literature on select committees in general.<sup>218</sup> What is striking, first, is the limited scope of the inquiry into corporation tax. The focus tends to be on tax rates, rather than on (say) the corporation tax base,<sup>219</sup> although, as in Angela Eagle, MP's,<sup>220</sup> 2007 questioning of Gordon Brown, this can raise interesting questions about the possibly detrimental effects on the public finances of continuing to drive corporation tax rates down.<sup>221</sup> Secondly, it is noteworthy how, despite claims to the contrary, the discussion can take on a party political character. This is particularly noticeable in the attempts by a Conservative Member in 2006 to get the

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<sup>217</sup> See Manin, n. 185 above, p. 234.

<sup>218</sup> See Tomkins, n. 190 above, pp. 61-74.

<sup>219</sup> See House of Commons Treasury Committee, *4<sup>th</sup> Report. The 2006 Budget, Volume II: Oral and written evidence* (House of Commons Papers, Session 2005-2006, 994) (London: The Stationery Office, 2006), Ev. 44 (Q330) (Sally Keeble, MP (Northampton North, Labour)) and Ev. 55 (Q394-Q395) (David Gauke, MP (South West Hertfordshire, Conservative)). Mr Gauke was one of two Conservative MPs subsequently replaced on the Committee by Graham Brady, MP (Altrincham and Sale West, Conservative) and Philip Dunne, MP (Ludlow, Conservative). See Erskine May, n. 207 above, p. 742.

<sup>220</sup> Wallasey, Labour.

<sup>221</sup> See House of Commons Treasury Committee, *5<sup>th</sup> Report. The 2007 Budget, Volume II: Oral and written evidence* (House of Commons Papers, Session 2006-2007, 389) (London: The Stationery Office, 2007), Ev. 44 (Q299).

Chancellor to admit that he was manipulating tax rates for political advantage,<sup>222</sup> something the latter was never going to do, and which would have required the clearest of evidence to substantiate. Such partisanship is not peculiar to Conservative Members, however. In the same debate, Sally Keeble, MP, gave the Chancellor the opportunity to say why his approach to corporate taxation was better than Germany's,<sup>223</sup> while John McFall, MP's,<sup>224</sup> questions in 2007 seemed designed to enable the Chancellor to emphasise still further the importance of economic growth.<sup>225</sup> Such examples highlight the inadequacy of the approach of backbench Members to the Chancellor, of whom they were clearly in awe. If Sally Keeble was intent on doing more than enabling the Chancellor to justify his policies still further, it was not apparent from her failure to follow up on Gordon Brown's replies. This failure to interrogate the Chancellor's replies is a third striking feature of the Committee's discussions. It is true, too, of the very limited follow up to the Chancellor's answers to Peter Viggers, MP's,<sup>226</sup> questions in 2006,<sup>227</sup> and also of a surprising failure by the same Member to quiz a passing reference by Gordon Brown in 2007 to a large number of companies not paying tax.<sup>228</sup>

The second and third features mentioned above each illustrate two frequent criticisms of select committee hearings: that the discussion is skewed by the absence of legal

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<sup>222</sup> See House of Commons Treasury Committee, n. 219 above, Ev. 55 (Q394-Q395) (David Gauke, MP).

<sup>223</sup> *Ibid.*, Ev. 44 (Q 330).

<sup>224</sup> West Dunbartonshire, Labour (Committee Chairman).

<sup>225</sup> See House of Commons Treasury Committee, 2<sup>nd</sup> Report. *The 2006 Pre-Budget Report* (House of Commons Papers, Session 2006-2007, 115) (London: The Stationery Office, 2007), Ev. 58 (Q473-Q475). For clues, see 'Gavel Basher', *Private Eye*, No. 1194, 28 September-11 October 2007, 6.

<sup>226</sup> Gosport, Conservative.

<sup>227</sup> See House of Commons Treasury Committee, n. 216 above, Ev. 63 (Q416).

<sup>228</sup> See House of Commons Treasury Committee, n. 221 above, Ev. 36 (reply to Q248).

representation for committee Members (unlike in the United States),<sup>229</sup> and by the fact that, although the committee chairman has a role in shaping the discussion, questions from individual Members are largely uncoordinated.<sup>230</sup> The result, it might be inferred, is that Committee hearings have become little more than a further opportunity for the Chancellor to pursue familiar themes: the need to combat tax avoidance;<sup>231</sup> the overwhelming importance of promoting economic growth,<sup>232</sup> and the categorical assertion of the UK's relative 'competitiveness'. Such criticism would carry considerable weight if the Committee's role were simply the Millian one of 'controlling' and 'watching' HMG. However, if the Committee's role is seen instead, as Bagehot says, of letting the sovereign know of the problems with its governing, and of alerting the public to particular areas of concern, then the Committee's reports, rather than transcripts of its hearings (as well as HMG's responses to those reports) assume a considerable significance. Nonetheless, all is far from well. What the relatively light treatment of Gordon Brown at the hands of a Labour-dominated Select Committee indicates in what Tomkins calls a 'fault line' in the constitution, blurring the distinction between Crown and Parliament.<sup>233</sup>

Take, for instance, the problems presented by the second of Stoker's governance propositions: the 'blurring' of the respective responsibilities of state and corporate sector. These are more than questions of a possible lack of mutual respect, since they also illustrate the tendency of one to seize the initiative in order to blame the other for policy failures. The 'informing function' of the Committee is significant, it is contended, in providing a

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<sup>229</sup> For a useful, though dated, examination of the similarities and differences between the UK and US committee systems, see Kenneth Bradshaw and David Pring, *Parliament and Congress* (London: Constable, 1972), ch. 5.

<sup>230</sup> See Sampson, n. 15 above, p. 19.

<sup>231</sup> See House of Commons Treasury Committee, n. 216 above, Ev. 64 (reply to Q418); House of Commons Treasury Committee, n. 221 above, Ev. 36 (reply to Q248).

<sup>232</sup> See House of Commons Treasury Committee, n. 225 above, Ev. 58 (Q473-Q475).

<sup>233</sup> See Tomkins, n. 65 above, p. 164.

dispassionate account of the strengths and weaknesses of the arguments on either side. The ‘anti-avoidance theme’ provides an illuminating recent example of this idea in practice. When, in its report on the 2005 Pre-Budget Report, the Committee asked HMG to say ‘whether it now ... [had] any intention to introduce a general anti-avoidance rule [GAAR],’<sup>234</sup> the latter’s reply was careful not to accede to the invitation. Instead, it said simply that the ‘current approach [i.e. to anti-avoidance] ... [was] sensible, proportionate and fair’.<sup>235</sup> Conversely, the House of Lords Select Committee on Economic Affairs was able, with reservations, to commend a ‘modest step’ in the 2007 Finance Bill towards the simplification of corporation tax. Whether each of these contrasting responses, in its own particular sphere, proves to be the right one, only time will tell. The important point for present purposes is that the problem has been highlighted by the Committee (or, in the case of the latter) by the Lords Committee, and both its account of the problem, and the Chancellor’s response to it, are matters on the effectiveness of which the electorate will ultimately pass judgment. This is the paradoxical nature of parliamentary scrutiny, reflecting (as it does) the tensions of ‘Crown versus Parliament’. It is the combination of Parliament’s support for the Crown (by voting supply), and its opposition to it (through representation).<sup>236</sup> It helps to explain the strength of the two acting together, as the Crown in Parliament, to be discussed in Chapter 3.

This discussion has necessarily been somewhat selective. It has, however, underlined the point that the Treasury Committee’s role should properly be seen as an advisory one, rather

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<sup>234</sup> See House of Commons Treasury Committee, n. 216 above, p. 46.

<sup>235</sup> House of Commons Treasury Committee, *3<sup>rd</sup> Special Report. The 2005 Pre-Budget Report: Government Response to the Committee’s Second Report of Session 2005-06* (House of Commons Papers, Session 2005-2006, 1013) (London: The Stationery Office, 2006), p. 19.

<sup>236</sup> See Tomkins, n. 65 above, pp. 90-92.

than as a ‘policing’ one,<sup>237</sup> as helping to construct the story for which the government of the day will be held to account. This is what the British constitution is all about. Not the safeguarding of ‘liberty’, but the facilitation of ‘constitutional accountability’, the accountability of HMG (the Crown) to Parliament.<sup>238</sup> To be sure, the Public Accounts Committee has a similar role, but within a somewhat different remit; the Treasury Committee is the body tasked with advising HMG on the strengths and weaknesses of its corporation tax reform measures. The capacity of HMG is enhanced by Parliament’s ability to cast light on the potential for domination discussed in the previous part. Clearly, there are problems but, overall, the objectives, structure and values of Parliament go a long way to enhancing trust and confidence in corporation tax policy, not least perhaps because the discussion is that of the people’s representatives, rather than that of ‘experts’.

#### H.M. TREASURY AND H.M. REVENUE AND CUSTOMS

Effectiveness, that is, the capacity of a representative institution to advance its political objectives, means different things for different institutions. If Parliament’s scrutinising role evolved from the bloodshed of the seventeenth century, the function of the relevant Department of HMG, what Colin Thain categorises as ‘the constitutional Treasury’, is of even more ancient lineage.<sup>239</sup> For Parliament, effectiveness means the ability to construct a narrative of the Treasury’s conduct of corporation tax policy, to which the latter can react,

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<sup>237</sup> See Mathew D. McCubbins and Thomas Schwartz, ‘Congressional Oversight Overlooked: Police Patrols versus Fire Alarms’ (1984) 28 *American Journal of Political Science* 165-179.

<sup>238</sup> See Tomkins, n. 65 above, p. 47.

<sup>239</sup> See Thain, *Financial Times*, 18 February 2008, 10 (letter); Thain and Christie, n. 112 above, p. 3; Martin Loughlin, ‘Constituent Power Subverted: From English Constitutional Argument to British Constitutional Practice’, in *The Paradox of Constitutionalism: Constituent Power and Constitutional Form*, ed. by Martin Loughlin and Neil Walker (Oxford: Oxford University Press, 2007), pp. 27-48, 29.

and on the basis of which, come a General Election, the electorate can make its judgment (most likely through the ‘filter’ of the policy’s impact on the UK’s ‘economic performance’).<sup>240</sup> For the Treasury,<sup>241</sup> effectiveness means the capacity to create in the minds of the (voting) electorate the impression that the former’s actions (or inactions) matter, and that they produce optimal results in terms of the attainment of political objectives. In the corporation tax sphere, while Parliament’s task is to identify the problems with corporation tax policy, the Treasury must address the ones it considers important, discount unimportant ones, and anticipate yet others. Under the UK’s constitutional arrangements, and, as a Department whose powers originate in the royal prerogative,<sup>242</sup> the Treasury has considerable freedom of action in the initiation of policy.<sup>243</sup> The prerogative is, as Tomkins says,<sup>244</sup> the basis of executive power; it is noteworthy for its resilience to supervision by the courts.<sup>245</sup> Taxation policy is significant, because it is an aspect of the Treasury’s powers that is amenable to law, not least because of the constitutional struggles referred to above. Policy initiation, however, lies largely beyond the scope of law. ‘We may grant’, Joseph Jacob says, that the prerogative’s boundaries ‘... are defined by law and, certainly ... its scope is diminishing; but ... [at the centre of government], the rule of law does not operate’.<sup>246</sup>

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<sup>240</sup> For the period pre-1997, see Andrew Sentance, ‘UK Macroeconomic Policy and Economic Performance’, in *Britain’s Economic Performance*, ed. by Tony Buxton, Paul Chapman and Paul Temple, 2<sup>nd</sup> edn (London: Routledge, 1998), pp. 35-61; also Grant, n. 158 above, ch. 10.

<sup>241</sup> See Adam Tomkins, ‘The Struggle to Delimit Executive Power in Britain’, in *The Executive and Public Law: Power and Accountability in Comparative Perspective*, ed. by Paul Craig and Adam Tomkins (Oxford: Oxford University Press, 2006), pp. 16-51.

<sup>242</sup> *Ibid.*, p. 25; Jackson and Leopold, n. 18 above, paras 18-007-18-008; Richard A. Chapman, *The Treasury in public policy-making* (London: Routledge, 1997), ch. 2; Terence Daintith and Alan Page, *The Executive in the Constitution: Structure, Autonomy and Internal Control* (Oxford: Oxford University Press, 1999), pp. 32-39, 113-116.

<sup>243</sup> See Terence Daintith, ‘Public Law and Economic Policy’ [1974] JBL 9-22, 13.

<sup>244</sup> See Tomkins, n. 65 above, p. 78.

<sup>245</sup> *Ibid.*, pp. 81-83.

<sup>246</sup> See Joseph M. Jacob, *The Republican Crown: Lawyers and the Making of the State in Twentieth Century Britain* (Aldershot: Dartmouth), p. 1.

The reasons for this freedom of action may owe less to any lust for power, and more to some uncomfortable realities. But there is one overarching, ineluctable, difficulty. No-one knows, in this changing world, what will happen to-morrow. Or the day after. Or the day after that. Yet a government must somehow move through these radical uncertainties, to realise its political objectives. This is the fundamental difference, in the corporation tax sphere as much as any other, between Parliament and the Crown, between – in the present context - the Treasury Committee and the Treasury, between Westminster and Whitehall.<sup>247</sup> In its scrutinising role, Parliament looks over its shoulder; HMG confronts an unknown future. The latter does so, moreover, in the knowledge that, however it responds to, or anticipates, events, it must retain the trust and confidence of the governed. It is maintained in these pages that Machiavelli's account of the qualities that these uncertainties call forth from the sovereign, is as relevant now as ever it was. Machiavelli thought of these uncertainties in terms of *fortuna*,<sup>248</sup> the unpredictable woman,<sup>249</sup> what Bernard Crick synthesises as that 'sudden, awful [*sic*] and challenging piling up of ... [economic] factors and contingent political events in an unexpected way'.<sup>250</sup> Is it to be supposed, for instance, that, so soon after his appointment as Chancellor, the Rt Hon. Alistair Darling, MP, could have known the extent of the complex of issues that would be thrown up in what became known as the

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<sup>247</sup> We are right to focus on the Treasury, rather than H.M. Government as a whole, because of the 'segmented' nature of areas of policy-making identified by Richardson and Jordan (see J.J. Richardson and A.G. Jordan, *Governing under Pressure: The Policy Process in a Post-Parliamentary Democracy* (Oxford: Basil Blackwell, 1985), p. 73-74).

<sup>248</sup> See Niccolò Machiavelli, *The Prince*, trans. by Peter Bondanella (Oxford: Oxford University Press, 2005), esp. ch. XXV; see Bernard Crick, 'Introduction: So Many Machiavellis', in Niccolò Machiavelli, *The Discourses*, ed. and trans. by Bernard Crick, Leslie J. Walker and Brian Richardson (London: Penguin, 2003), pp. 57-59.

<sup>249</sup> See Machiavelli (2005), n. 248 above, pp. 86-87. If this is right, then James Naughtie and others are precisely *wrong* to suggest that *prudence* is female (see, e.g., James Naughtie, *The Rivals: The Intimate Story of a Political Marriage* (London: Fourth Estate, 2001), p. 203).

<sup>250</sup> See Crick, n. 248 above, p. 58.

‘Northern Rock crisis’?<sup>251</sup> In the face of such uncertainties, what the ruler must show, says Machiavelli, is *virtù*. It is not, as Crick again reminds us, goodness as such that is called for, but something nearer perhaps to ‘virtuosity’.<sup>252</sup> *Virtù* has many facets, the most notable, as already observed, being the facility of *prudenza*,<sup>253</sup> of ‘prudence’. It is not the same as having no policy; it is reactive, to be sure, but it is pro-active too, should circumstances demand. It is a crucial element in the generation of capacity, of sovereignty.

If, speaking interpretatively, prudence is the key to understanding the type of policy decisions to be discussed in Chapter 3, it becomes important to consider the extent to which this seems to be a characteristic of the key decision-makers in the Treasury and HMRC. Given the powers residing in individuals, the strength of their personalities, their political style, matters, no less than their policies.<sup>254</sup> Ministers, says Philip Norton, fall discernibly into one (or, more likely, a combination) of a number of different ‘styles’: ‘commanders’, ‘ideologues’, ‘managers’, ‘agents’, or ‘team players’.<sup>255</sup> The fact that they are all, at least at the Treasury, elected Members of the lower House, means that their constituents have identified in what Thain calls ‘the political Treasury’ some special quality,<sup>256</sup> which sets them apart from other people. This is one reason why it is important to maintain the difference between ministers and civil servants, between those who are elected (literally, the ‘elite’),<sup>257</sup> and those who are not. The elected are, as has long been recognised, an

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<sup>251</sup> See Porter and Reece, *Daily Telegraph*, 13 September 2007, 14.

<sup>252</sup> See Crick, n. 248 above, p. 60.

<sup>253</sup> See Chapter 1 above, n. 182.

<sup>254</sup> See Manin, n. 185 above, p. 219.

<sup>255</sup> See Philip Norton, ‘Barons in a Shrinking Kingdom: Senior Ministers in British Government’, in *Transforming British Government Volume 2: Changing Roles and Relationships*, ed. by R.A.W. Rhodes (Basingstoke: Macmillan, 2000), pp. 101-124, 109-112; also Peter Dorey, *Policy Making in Britain: An Introduction* (London: Sage, 2005), pp. 58-63.

<sup>256</sup> See n. 204 above; Thain, *Financial Times*, 18 February 2008, 10 (letter); Thain and Christie, n. 112 above, p. 4.

<sup>257</sup> See Manin, n. 185 above, p. 140.



‘aristocracy’.<sup>258</sup> Labour’s Treasury ministers amply reflect this aristocratic conception, this ‘principle of distinction’, to which reference has already been made.<sup>259</sup> For example, Kitty Ussher, MP, the Economic Secretary to the Treasury, the very model of a New Labour metropolitan intellectual,<sup>260</sup> represents the historically economically deprived, and culturally and socially diverse, constituency of Burnley and Pendle. Although it is too early to write of her ‘style’, her political skills will be tested by her part-responsibility for the 2008 Finance Bill. Alistair Darling, MP for Edinburgh South West, is socially and professionally distinguished,<sup>261</sup> though the representative of a more affluent constituency. At the time of writing, his political skills are being tested by reaction to the 2007 Pre-Budget Report and its aftermath,<sup>262</sup> but most would concede that, on Norton’s typology, he is nearest to a ‘manager’, albeit a beleaguered one.<sup>263</sup> Most importantly, there is the MP (since 1983) for Dunfermline East, Gordon Brown, who as Chancellor of the Exchequer from 1997 to 2007, has dominated the period covered by this study. Brown, working with the former *Financial Times* leader writer and special adviser, Ed Balls,<sup>264</sup> transformed a Department which, although already (in W.H. Greenleaf’s words) ‘the Department of Departments’, and

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<sup>258</sup> *Ibid.*, p. 149.

<sup>259</sup> See n. 204 above.

<sup>260</sup> See Adams, *Financial Times*, 30 July 2007, 3.

<sup>261</sup> See Paul Routledge, *Gordon Brown: The Biography* (London: Simon and Schuster, 1998), p. 297, where Darling is described as ‘a sharp Edinburgh advocate’. Darling was Chief Secretary to the Treasury, 1997-1998, and Shadow Chief Secretary to the Treasury, 1996-1997. He is ‘the great nephew of Sir William Darling, who was Conservative MP for Edinburgh South (1945-57)’ (see Rumbelow, Webster and Harding, *Times*, 22 September 2007, 6).

<sup>262</sup> See H.M. Treasury, *Meeting the aspirations of the British people: 2007 Pre-Budget Report and Comprehensive Spending Review October 2007* (Cm 7227) (London: TSO, 2007); see Wolf, *Financial Times*, 10 October 2007, 10; Strauss, *Financial Times*, 10 October 2007, 2; Brittan, *Financial Times*, 12 October 2007, 17.

<sup>263</sup> See Anon, *Financial Times*, 20 December 2007, 12 (editorial); Parker, *Financial Times*, 22-23 September 2007, 11; Rumbelow, Webster and Harding, n. 261 above; Porter and Reece, *Daily Telegraph*, 13 September 2007, 14; Barber, Blitz and Giles, *Financial Times*, 4 July 2007, 3.

<sup>264</sup> See Dorey, n. 255 above, pp. 74-78. Balls subsequently became an MP, and Economic Secretary to the Treasury (see n. 16 above).

‘basically a ministry of finance’<sup>265</sup> has become something more akin to a continental finance ministry.<sup>266</sup> ‘The Treasury’, Peter Hennessy wrote in 1990, ‘is about money [,] and money is a mighty weapon of power. [...] Knowledge, too, is power and the Treasury has a window into every ministry and departmental activity across Whitehall’.<sup>267</sup> He would have had even greater reason to reiterate these words in 2007.

‘Prudence’ is often associated with Gordon Brown, yet, as discussed in Chapter 1,<sup>268</sup> it tends not explicitly to be the prudence of Machiavelli.<sup>269</sup> This is surprising, the more so since, although commentators describe certain elements of prudence, they do not associate them directly with Machiavelli’s conception. Thus, Marquand has written of Brown’s ‘often infuriating caution’,<sup>270</sup> while Jackie Ashley has written that ‘simply to say Brown is cautious won’t do. He’s bold, too’;<sup>271</sup> and Suzanne Moore, with an interesting mixture of ideas, has written of Brown’s ‘sheer nous, cunning, cleverness, realpolitik, whatever you want to call it’.<sup>272</sup> All this is the more surprising, since there is a strong intellectual heritage of Machiavellianism in radical British Protestantism; one has only to think of James Harrington’s or Francis Bacon’s espousal of the Machiavellian view of the world to appreciate this.<sup>273</sup> It is thus no objection to say that Brown is a ‘son of the Manse’,<sup>274</sup> nor to

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<sup>265</sup> See W.H. Greenleaf, *The British Political Tradition: Volume Three: A Much Governed Nation: Part I* (London: Methuen, 1987), p. 250.

<sup>266</sup> See Philip Stephens, ‘The Treasury under Labour’, in *The Blair Effect*, ed. by Anthony Seldon (London: Little, Brown, 2001), pp. 185-207. Hence Tony Blair’s apparent plan to split it (see Wintour, *Guardian*, 9 May 2007, 1). On the pre-Gordon Brown Treasury, see Colin Thain and Maurice Wright, *The Treasury and Whitehall: The Planning and Control of Public Expenditure, 1976-1993* (Oxford: Clarendon Press, 1995).

<sup>267</sup> See Peter Hennessy, *Whitehall* (London: Fontana, 1990), p. 394.

<sup>268</sup> See Chapter 1, n. 183.

<sup>269</sup> See John Snape, ‘Corporation Tax Reform – Politics and Public Law’ [2007] BTR 374-404, 392.

<sup>270</sup> See Marquand, *New Statesman*, 24 September 2007, 36-38, 36.

<sup>271</sup> See Ashley, *Guardian G2*, 30 May 2007, 4.

<sup>272</sup> See Moore, *New Statesman*, 24 September 2007, 43-44, 43. *Nous* is an Aristotelian virtue (see Aristotle, *The Nicomachean Ethics*, ed. and trans. by J.A.K. Thomson, Hugh Tredennick and Jonathan Barnes (London: Penguin, 2004), pp. 151-152, 161).

<sup>273</sup> See James Harrington (1611-1677), *The Commonwealth of Oceana* and *A System of Politics*, ed. by J.G.A. Pocock (Cambridge: Cambridge University Press, 1992), pp. 10 and 30; R.H. Tawney,

point to Brown's 'deep moral convictions'.<sup>275</sup> H.C.G. Matthew, in describing Gladstone's approach to Irish Home Rule, reflects on Gladstone's command of *virtù*.<sup>276</sup> And this link is not an idle one, either; Marquand goes on to make a comparison, in terms of intellectual standing, between Brown and Gladstone.<sup>277</sup> Finally, and most importantly, it is no objection to identify Brown's prudence exclusively with the prudence described by Adam Smith in his *Theory of Moral Sentiments*.<sup>278</sup> Brown himself associates prudence, as Simon Lee has pointed out, with Smith in a lecture from 2004.<sup>279</sup> Brown articulates Smith's prudence, however, as an ideal characteristic.<sup>280</sup> It does not, as does Machiavelli's, seek to describe an actual mode of behaviour. '[W]e are much beholden to Machiavel and others [Bacon himself wrote], that write what men do, and not what they ought to do'.<sup>281</sup> What is claimed here is that Machiavellian prudence is as essential to corporation tax as to any other area of taxation, or public, policy, and that, as Chancellor, Brown has shown himself to be its supreme exponent.

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*Harrington's Interpretation of his Age* (London: Humphrey Milford, Oxford University Press, 1942), pp. 18-20; J.G.A. Pocock, *The Machiavellian Moment: Florentine Political Thought and the Atlantic Republican Tradition* (Princeton: Princeton University Press, 1975), pp. 317 and 390; also Paul Raffield, *Images and Cultures of Law in Early Modern England: Justice and Political Power, 1558-1660* (Cambridge: Cambridge University Press, 2004), pp. 258-260.

<sup>274</sup> See Naughtie, n. 249 above, pp. 5, 188; Routledge, n. 261 above, pp. 23-25; Robert Peston, *Brown's Britain* (London: Short Books, 2005), p. 25; William Keegan, *The Prudence of Mr Gordon Brown* (Chichester: John Wiley, 2003), p. 20; Tom Bower, *Gordon Brown* (London: HarperCollins, 2004), pp. 5-6.

<sup>275</sup> See Keegan, n. 274 above, p. 128.

<sup>276</sup> See Matthew (1995), n. 212 above, p. 237.

<sup>277</sup> See Marquand, n. 270 above, 36; also Thain and Christie, *Parliamentary Brief*, February 2008, 21-22, 21 (available from [www.treasuryproject.org](http://www.treasuryproject.org) (accessed 21 February 2008)).

<sup>278</sup> See Adam Smith (1723-1790), *The Theory of Moral Sentiments*, ed. by D.D. Raphael and A.L. MacFie (Oxford: Clarendon Press, 1976), pp. 212-217.

<sup>279</sup> See Simon Lee, *Best for Britain? The Politics and Legacy of Gordon Brown* (Oxford: Oneworld, 2007), pp. 45-47.

<sup>280</sup> *Ibid.*, pp. 46-47.

<sup>281</sup> See Francis Bacon, *The Advancement of Learning and New Atlantis*, ed. by Arthur Johnston (Oxford: Clarendon Press, 1974), p. 157.

The politicisation of corporation tax issues, something to which the discussion turns in Chapter 3, has made the prudential qualities of Treasury ministers<sup>282</sup> more important than they might have been even a decade ago. To emphasise this requirement is not, however, to diminish the importance of Treasury senior civil servants, since (irrespective of Gordon Brown's allegedly 'Stalinistic' tendencies),<sup>283</sup> it is to be presumed that at the Chancellor's elbow, at the scene of crucial decisions, has been the prudential voice of a team of the Treasury's most gifted public servants. There has, of course, been much unease about the 'politicisation' of the civil service,<sup>284</sup> given the need to ensure the accountability of individuals employed under the royal prerogative.<sup>285</sup> After all, like ministers, civil servants exercise the powers of the Crown,<sup>286</sup> although, unlike ministers, Parliament does not hold civil servants 'to constitutional account'.<sup>287</sup> So there may be good grounds for concern, especially since 'management', properly understood, is but an aspect of the art and science of government,<sup>288</sup> and it is management, rather than administration, that characterises the role of Thain's 'official' or 'permanent Treasury', as part of the contemporary civil service.<sup>289</sup> The point is indeed illustrated better by the Treasury than by any other Department of Government. Of all the buildings visible from the London Eye, the Treasury building is an

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<sup>282</sup> Currently (29 February 2008), and setting aside those mentioned in the text above, these are: the Rt Hon. Yvette Cooper, MP (Chief Secretary to the Treasury), who replaced the Rt Hon. Andy Burnham, MP, on 24 January 2008; the Rt Hon. Jane Kennedy, MP (Financial Secretary to the Treasury); Angela Eagle, MP (Exchequer Secretary to the Treasury); and Liam Byrne, MP (Minister of State 'with responsibility for revenue protection at the border').

<sup>283</sup> See Timmins, *Financial Times*, 20 March 2007, 1; Watts, *Sunday Telegraph*, 8 April 2007, 28.

<sup>284</sup> As to which, see Peston, n. 274 above, pp. 110-111; Rod Rhodes, 'The Civil Service', in Seldon, n. 265 above, pp. 97-115, 102-103, 106-107.

<sup>285</sup> Hence *A Draft Civil Service Bill: A Consultation Document: Presented to Parliament by the Minister for the Cabinet Office by Command of Her Majesty, November 2004* (Cm 6373) (London: TSO, 2004); see Timmins, *Financial Times*, 16 November 2004, 4.

<sup>286</sup> See Tomkins, n. 65 above, p. 61.

<sup>287</sup> *Ibid.*, p. 77.

<sup>288</sup> But see the argument made in Chris Dillow's, *The End of Politics: New Labour and the Folly of Managerialism* (Petersfield: Harriman House, 2007), ch. 15.

<sup>289</sup> See Rhodes, n. 284 above; Colin Thain, 'Treasury Rules OK? The Further Evolution of a British Institution' (2004) 6 BJPIR 123-130, 124; Thain and Christie, n. 112 above, p. 3.

especially powerful symbol of governance values that are traceable, in one form or another, to the development of 'New Right' ideas in the second half of the twentieth century.<sup>290</sup> Returning to the Treasury in 2004, the commentator Anthony Sampson noted how a corporate boardroom ambience had replaced the curving corridors and peeling linoleum of former days.<sup>291</sup> Emblematic of this new approach is the person of Nick Macpherson, Permanent Secretary to the Treasury since August 2005, and successor to Sir Gus O'Donnell,<sup>292</sup> who was responsible for the O'Donnell Report of 2004,<sup>293</sup> which resulted in the merging of the former Revenue Departments (the Inland Revenue and Customs and Excise),<sup>294</sup> as well as the introduction of a new budget, tax and welfare directorate in the Treasury,<sup>295</sup> which was designed to liaise more closely with the new HMRC.<sup>296</sup> Responsibility for corporation tax reform has thus been shared between the Treasury and HMRC,<sup>297</sup> the former having specialist corporation tax expertise on the Council of Economic

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<sup>290</sup> See Rodney Barker, *Political Ideas in Modern Britain* (London: Methuen, 1978), pp. 190-205. Such progressive notions were reflected in the 'shelved' Fulton report of the 1960s (see Lord Fulton (Chairman), *The Civil Service: vol. 1. Report of the Committee 1966-68* (Cmnd 3638) (London: HMSO, 1968), esp. ch. 5). On Fulton, see, e.g., Keith Dowding, *The Civil Service* (London: Routledge, 1995), pp. 20-21; Kevin Theakston, *The Civil Service since 1945* (Oxford: Blackwell, 1995), pp. 88-108; Thain, n. 289 above, p. 128.

<sup>291</sup> See Sampson, n. 15 above, p. 126; also Anthony Sampson, *Anatomy of Britain Today* (London: Hodder and Stoughton, 1965), p. 291.

<sup>292</sup> See Cameron, *FT Magazine*, 8/9 April 2006, 16-20.

<sup>293</sup> *Financing Britain's Future: Review of the Revenue Departments* (Chair, Gus O'Donnell) (Cm 6163) (London: TSO, 2004).

<sup>294</sup> For the background, see House of Commons Treasury Committee, *10<sup>th</sup> Report. Inland Revenue Matters* (House of Commons Papers, Session 2002-2003, 834) (London: TSO, 2003), pp. 3-6.

<sup>295</sup> Of which Edward Troup is a member (see n. 124 above).

<sup>296</sup> See Judge, n. 27 above, p. 158; H.M. Treasury, *HM Treasury Annual Report and Accounts 2006-2007* (House of Commons Papers, Session 2006-2007, 518) (London: TSO, 2007), p. 16; Giles, *Financial Times*, 16 January 2008, 2; HMRC, *Departmental Report 2007: HM Revenue & Customs: Presented to Parliament by the Paymaster General by Command of Her Majesty: May 2007* (Cm 7107) (London: TSO, 2007), p. 14.

<sup>297</sup> See Commissioners for Revenue and Customs Act 2005. The Commissioners for Her Majesty's Revenue and Customs are appointed by 'Letters Patent' (see CRCA 2005, s. 1(1)), the usual way of appointing Crown servants.

Advisers,<sup>298</sup> and the latter having a designated group of public servants who specialise in corporation tax (and value added tax),<sup>299</sup> and who are ‘responsible for design, specification and providing advice, carrying out technical policy work and liaising with HM Treasury and Ministers’.<sup>300</sup> Although much criticism has recently been levelled at HMRC, over operational matters such as the loss of taxpayer data, this has not been concerned specifically with corporate taxation.<sup>301</sup>

The need for prudence, whether that of elected ministers or of unelected officials, is intrinsic to the circumstances in which political institutions operate. This brings the discussion to a point of fundamental importance. The continuing pre-eminence of the political institutions whose buildings are visible from the London Eye over those whose buildings (even on a clear day) are not: those of the EU. Arguments that the UK has somehow ceded sovereignty to a supranational authority are misconceived, both because of the vision of sovereignty rehearsed above,<sup>302</sup> and because, as Helen Thompson points out, ‘[t]he Commission, except in competition policy, can only issue regulations and directives on the basis of decisions made in the Council of Ministers, and its right to initiate legislation is mediated through the largest member-states’.<sup>303</sup> Even the European Court of Justice (ECJ)

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<sup>298</sup> e.g., as in Chris Wales, who was a member of the Council of Economic Advisers from 1997 to 2003.

<sup>299</sup> See HMRC, n. 296 above, p. 14.

<sup>300</sup> *Ibid.*, p. 18.

<sup>301</sup> See *Civil Service Capability Reviews: Capability Review of HM Treasury*, available from [www.civilservice.gov.uk/capability-reviews](http://www.civilservice.gov.uk/capability-reviews) (accessed 24 February 2008); see Timmins, *Financial Times*, 18 December 2007, 3; also Christopher Wales, ‘The Implications of the O’Donnell Review for the making of Tax Policy in the UK’ [2004] BTR 543-565, esp. 544-548, 557; Christie, *The Treasury under New Labour Project Bulletin*, January 2008, Issue 3, 10-12, available from [www.treasuryproject.org](http://www.treasuryproject.org) (accessed 22 February 2008).

<sup>302</sup> See Martin Loughlin, *Sword and Scales: An Examination of the Relationship between Law and Politics* (Oxford: Hart Publishing, 2000), pp. 147-151; also Neil Walker, ‘Post-Constituent Constitutionalism? The Case of the European Union’, in Loughlin and Walker, n. 239 above, pp. 247-267.

<sup>303</sup> See Helen Thompson, ‘The Modern State and its Adversaries’ (2006) 41 *Government and Opposition* 23-42; also Colin Turpin and Adam Tomkins, *British Government and the*

may not, in reality, pose a serious threat to national sovereignty either. This is because, despite the ECJ's energy in ensuring that corporate tax law is consistent with the 'fundamental freedoms' of the European Treaty,<sup>304</sup> tax remains a matter of national competence. Moreover, as Thompson says, 'the administration of EU laws remains dependent on national judiciaries',<sup>305</sup> and even the ECJ has itself begun to show a sensitivity to the dangers to the European enterprise which would be presented by too rigid an adherence to its more uncompromising corporate taxation precedents.<sup>306</sup> This study does not therefore envisage a governance structure of which the EU institutions form either the apex or the base.<sup>307</sup> What it conceives of instead is the UK as a sovereign state, albeit with competences limited by Community law (but also GATT 1994), whose *capacity* is enhanced, rather than depleted, by membership of the EU or WTO.<sup>308</sup> This is a return to the second of the strands of the chapter referred to above. In such a world, *fortuna* appears in several guises. On the one hand, given the Treasury's role, she represents the vicissitudes of the markets, or the threats of MNCs to leave the national jurisdiction. On the other, she represents the unknowable summed up in Timothy Lyons's reiteration of Melchior Wathelet's rhetorical (and despairing) question: 'What will the ECJ decide to-morrow?'<sup>309</sup> Despite the 'legal' nature of the latter question, its very 'unpredictability' makes it

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*Constitution: Text and Materials*, 6<sup>th</sup> edn (Cambridge: Cambridge University Press, 2007), pp. 16-21; also Marsh and Rhodes, n. 119 above, p. 259.

<sup>304</sup> See, e.g., Suzanne Kingston, 'A Light in the Darkness; Recent Developments in the ECJ's Direct Tax Jurisprudence' (2007) 44 CMLRev 1321-1359.

<sup>305</sup> See Thompson, n. 303 above, p. 37, referring to J.H.H. Weiler, 'A Quiet Revolution: The European Court of Justice and its Interlocutors' (1994) 26: 4 *Comparative Political Studies* 510-534.

<sup>306</sup> See Case C-446/03, *Marks and Spencer plc. v. Halsey (H.M. Inspector of Taxes)* [2006] 1 CMLR 18; also Case C-196/04, *Cadbury Schweppes plc. and another v. Inland Revenue Commissioners* [2007] 1 CMLR 2 (discussed in Snape, n. 269 above, pp. 388-389).

<sup>307</sup> See Robert Baldwin and Martin Cave, *Understanding Regulation: Theory, Strategy, and Practice* (Oxford: Oxford University Press, 1999), ch. 12.

<sup>308</sup> See Loughlin, n. 20 above, pp. 94-95.

<sup>309</sup> See 'T.L.' [2006] BTR 399-408.

disconcertingly similar to the former one. Only the ability to move quickly, to think quickly, to prevent these unknowns from deflecting the overall policy<sup>310</sup> - in short, to behave *prudentially* - is enough to deal with them. Sovereignty is, after all, a 'generative' conception.<sup>311</sup>

Given the necessity for prudence, it is contended that, given the Treasury's need for effectiveness in reaching its twin goals of 'Raising Trend Growth' and 'Promoting Fairness and Opportunity for All',<sup>312</sup> the idea that informs all of the values at play is 'reason of state'.<sup>313</sup> This point is developed in Chapter 4; it is central to the idea that institutions must be effective, in order for them to generate trust and confidence. For the moment, we can note that what shapes these values is not 'morality' as such, but the 'advancement of the public interest',<sup>314</sup> as that is defined and shaped by ideology, perhaps, but certainly by the ideologically motivated sovereign. This might seem a case of 'double standards', but it is not that. There are only, as Crick says, two sets of standards: one applicable to the private sphere, the other applicable to the 'political realm',<sup>315</sup> the latter, as Loughlin tells us, being the field of operation of public law,<sup>316</sup> of which taxation law is so important a part.

## POLICY NETWORKS

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<sup>310</sup> See Gray, *New Statesman*, 24 September 2007, 46-47, 47.

<sup>311</sup> See, in relation to economic policy, Martin Wolf, 'Does globalisation render states impotent?' [2000] BTR 537-544. These ideas are expanded and developed in Wolf's book, n. 142 above.

<sup>312</sup> See H.M. Treasury, n. 296 above; also Chapter 3 below.

<sup>313</sup> See Loughlin, n. 20 above, pp. 148-152; Noel Malcolm, *Reason of State, Propaganda, and the Thirty Years' War: An Unknown Translation by Thomas Hobbes* (Oxford: Clarendon Press, 2007), ch. 6.

<sup>314</sup> See Gordon Brown, 'Advancing the public interest', in *Gordon Brown: Moving Britain Forward: Selected Speeches 1997-2006*, ed. by Wilf Stevenson (London: Bloomsbury, 2006), pp. 136-180. On 'interest', see Malcolm, n. 313 above, pp. 94-97.

<sup>315</sup> See Crick, n. 248 above, pp. 66-67.

<sup>316</sup> See Loughlin, n. 20 above, pp. 43-44.



Gazing out from the London Eye, at the panorama described at the beginning of the chapter, the signs of ‘policy networks’ are, as has been suggested, everywhere apparent. Corporation tax reform, in common with other areas of public policy, is so much a matter of involving policy networks, that the role and values of such bodies fall to be interpreted next.

It is important to be clear, however, about exactly the kind of organisation that we are here seeking to pinpoint. It is not, as discussed in the previous part, the totality of the relevant Departments of State, H.M. Treasury and HMRC, nor is it, as discussed in the third part of the chapter, some monolithic notion of the corporate sector as a whole. It is, rather, those individuals, or groups of individuals, who ‘mediate’ in the development of corporation tax reform proposals, those who deliberate on the ‘concerns of business’ when reforms are proposed: civil servants from the Treasury and from HMRC; lawyers; accountants; academics; members of think tanks; journalists; and coalitions of producers (most significantly the CBI). The importance of these networks, as Stoker points out, is not only that they are in a position to ‘interpret and lead public debate’, but also that they can influence policy, in some cases requiring a united front from their members, to ‘nudge’ HMG more in one direction than another.<sup>317</sup>

For the writer, the most convincing starting-point for interpreting the role of policy networks is again Manin’s dissection of the ‘principles of representative government’. Manin is not concerned to offer a complete theory of the principles and values of interest groups in the UK’s system of representative democracy. What he is concerned with, however, is the role of extra-parliamentary political discussion in such a system. Whatever influence the corporate sector may exert in the corporate ambience of Whitehall is mediated by this extra-

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<sup>317</sup> See Hobbes, n. 31 above, p. 375, where the author condemns ‘the great number of Corporations; which are as it were many lesser Common-wealths in the bowels of the greater, like wormes in the entrayles of a naturall man’.

parliamentary debate. It is in this context that policy networks fall to be considered. Explanation and interpretation of their role has fallen to Rod Rhodes and David Marsh, in a penetrating and enduringly persuasive analysis.<sup>318</sup> In this part of the chapter, elements of each analysis will be used to cast light on the other. Given the involvement in policy networks of civil servants, the context of the debate is the accountability of the Crown and its servants. There is, as discussed above, no political accountability for civil servants, nor, as we shall see, are they subject to any legal accountability by way of judicial review. Instead, their position, as individuals employed under the royal prerogative, is governed by a case-law ‘vicariousness’ principle, and by a number of executive measures falling outside parliamentary scrutiny.<sup>319</sup> Under the pragmatic *Carltona* principle,<sup>320</sup> a decision of a civil servant is, ‘of course, the decision of the minister’,<sup>321</sup> Minister and civil servant being regarded as ‘legally indistinguishable parts of a single unit, the government Department, united together in the service of the Crown’.<sup>322</sup> The executive measures include, most importantly, the 1995 Civil Service Order in Council,<sup>323</sup> and the Civil Service Management Code,<sup>324</sup> but none of them are subject to judicial or parliamentary scrutiny.<sup>325</sup> All present a significant challenge to generating trust and confidence, because they draw attention to the variability of the accountability mechanisms applicable to civil servants.

With such accountability problems firmly in mind, Rhodes and Marsh offer an interpretation of government/interest group relations that is different from both ‘corporatist’

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<sup>318</sup> See Marsh and Rhodes, n. 119 above; also Judge, n. 27 above, pp. 106-114; also Dorey, n. 255 above, ch. 5; for an overview of other approaches, see Peters, n. 22 above, ch. 7, esp. pp. 128-129; but see Hugh Pemberton, ‘Policy Networks and Policy Learning: UK Economic Policy in the 1960s and 1970s’ (2000) 78 *Public Administration* 771-792, 772-774.

<sup>319</sup> See Tomkins, n. 65 above, pp. 76-77.

<sup>320</sup> See *Carltona Ltd v. Commissioners of Works and Others* [1943] 2 All ER 560 (EWCA).

<sup>321</sup> [1943] 2 All ER 560, 563B (Lord Greene MR).

<sup>322</sup> See Tomkins, n. 65 above, p. 85.

<sup>323</sup> See [www.civilservicecommission.gov.uk](http://www.civilservicecommission.gov.uk) (accessed 22 October 2007).

<sup>324</sup> See [www.civilservice.gov.uk](http://www.civilservice.gov.uk) (accessed 22 October 2007).

and ‘pluralist’ models.<sup>326</sup> In keeping with the objectives of the study, their approach is strongly interpretative, emphasising the roles of interest groups in different policy areas,<sup>327</sup> and looking for ‘aggregations of interests’.<sup>328</sup> In the corporation tax debate, Rhodes and Marsh would accordingly distinguish between a ‘producer network’ (most importantly, here, the members of the CBI and the British Bankers’ Association (BBA)) and ‘professional networks’, such as the members of the Law Society, of think tanks such as the Institute for Fiscal Studies (IFS), of the members of the Chartered Institute of Taxation (CIOT)<sup>329</sup>). To the latter they would also add, presumably, the small group of financial journalists who have recently followed the ‘politicisation’ of corporation tax issues, most notably Vanessa Houlder of the *Financial Times*.<sup>330</sup> What the distinction serves to illustrate is the ‘relative stability’ of the professional network, as against that of the producer; the considerable reliance of the Treasury and HMRC on the former (if not the latter) ‘to get the technical detail right’<sup>331</sup> (for instance, in relation to the accounting theme discussed in the present study); and the tendency of both to further their own economic interests. Rather interesting in this latter context are the *Financial Times* journalists covering corporate tax reform, since they have ceased (as Manin might predict) to take a partisan approach, and instead have concentrated on reporting and reflecting the debate.<sup>332</sup> Marsh and Rhodes’s new typology

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<sup>325</sup> See Tomkins, n. 65 above, p. 77.

<sup>326</sup> See R.A.W. Rhodes and David Marsh, ‘Policy Networks in British Politics: A Critique of Existing Approaches’, in Marsh and Rhodes, n. 119 above, pp. 1-26; also Pierre and Peters, n. 38 above, pp. 33-35.

<sup>327</sup> Marsh and Rhodes, n. 119 above, p. 4.

<sup>328</sup> *Ibid.* p. 9.

<sup>329</sup> See Hansard HC Standing Committee A, 23 May 2006, col. 321 (Brooks Newmark, MP (Braintree, Conservative)).

<sup>330</sup> Who, as the award to her of the LexisNexis Tax Writer of the Year 2007, on 24 May 2007, indicated, is rightly respected and valued by the policy network in question.

<sup>331</sup> See Malcolm Gammie, ‘The Process of Fiscal Reform in the United Kingdom’ [1989] BTR 252-264, 253.

<sup>332</sup> See Manin, n. 185 above, pp. 228 and 232. This is what makes, say, the *Daily Telegraph*’s selective taxation coverage dinosauric.

also, however, highlights a stark contrast with the ‘issue networks’,<sup>333</sup> such as the Tax Justice Network (TJN), and (of a very different ‘stripe’ indeed) the Taxpayers’ Alliance.<sup>334</sup> What characterises these latter two is that, albeit in very different ways, their activities are directed at influencing public opinion, having ‘little or no access to government’.<sup>335</sup>

Given that, in Rhodes and Marsh’s analysis, ‘economic and professional interests dominate’ in the policy community, they also point to the limited variety of participants in professional and producer communities. Thus, although the trades unions tend not to contribute to policy debates, other names (those in the professional community) tend to recur: among law firms, Slaughter and May (commenting on what has been called in this study the European and International theme in corporation tax reform) and McGrigors, on the ‘accounting’<sup>336</sup> and the ‘compliance and enforcement’ themes, to take just two examples. Likewise, among ‘professional services’ firms, we tend to find PricewaterhouseCoopers, Deloitte and KPMG commenting on the ‘European and international’ theme. As for the producer networks, no-one would deny the monolithic status of the CBI, ready as Jonathan Guthrie has written, to comment if necessary on ‘raindrops racing down a window pane’,<sup>337</sup> but especially on corporate tax policy<sup>338</sup> and on all of the themes identified in this study. The ‘economic and/or professional interests’ of these groups, focussing recurrently on corporation tax ‘simplification’, contrast rather vividly with the corporation tax fairness issues raised by those such as the accountant, Richard Murphy, and latterly, the academic, Sol Picciotto.<sup>339</sup>

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<sup>333</sup> See Marsh and Rhodes, n. 119 above, p. 254.

<sup>334</sup> See [www.taxpayersalliance.com](http://www.taxpayersalliance.com) (accessed 10 September 2007).

<sup>335</sup> See Marsh and Rhodes, n. 119 above, p. 256.

<sup>336</sup> See Collins and Dixon, *Tax Journal*, 9 April 2007, 6-8.

<sup>337</sup> See Guthrie, *Financial Times*, 26 April 2007, 15.

<sup>338</sup> See Houlder, *Financial Times*, 21 October 2004, 3.

<sup>339</sup> See Murphy and Picciotto, *Financial Times*, 27 September 2007 (letter); also Murphy and Christensen, *Financial Times*, 12 March 2004, 18 (letter).

Reference to the contribution of Murphy and Picciotto reminds us of the aspect of personal interactions, in what Marsh and Rhodes take to be a second dimension of policy networks: ‘integration’.<sup>340</sup> Within the corporation tax policy community (that body that Tiley calls ‘tax folk’),<sup>341</sup> the same lawyers’ names recur: Stephen Edge, of Slaughter and May; Malcolm Gammie, of the tax bar (sometime of Linklaters),<sup>342</sup> and Edward Troup (now of the Treasury and formerly of Simmons and Simmons).<sup>343</sup> Among the accountants, especially prominent are, perhaps, John Whiting of PricewaterhouseCoopers; Loughlin Hickey of KPMG; and John Cullinane of Deloitte. They are all participants in an almost constant and, as mentioned in Chapter 1, sophisticated public discussion of the direction in which corporation tax reform is going. They are characterised by their longevity as participants in the debate, by (with the possible exception of Stephen Edge) their commitment to a somewhat Diceyan ideal of corporation tax law, and by values, immanent to their extensive writing, well assimilated to the broad policy objectives which corporation tax reform is seeking to attain. Gammie is in many ways representative. He writes of the ‘rule of law’ with only Dicey beside him,<sup>344</sup> and speaks in respectful tones to the House of Lords Select Committee on Economic Affairs of the familiar and faintly tedious lack of progress on tax simplification. Take, for instance, his slant on the decision in the 2007 Budget to abolish capital allowances for expenditure on industrial buildings,<sup>345</sup> which had been justified on tax simplification grounds:

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<sup>340</sup> See Marsh and Rhodes, n. 119 above, p. 251.

<sup>341</sup> See Tiley, n. 19 above, p. 62.

<sup>342</sup> See Chapter 1, n. 47.

<sup>343</sup> See n. 124 above.

<sup>344</sup> See Malcolm Gammie, ‘Tax Avoidance and the Rule of Law: a Perspective from the United Kingdom’, in *Tax Avoidance and the Rule of Law*, ed. by Graeme S. Cooper (Amsterdam: IBFD Publications, 1997), pp. 181-218, 185.

<sup>345</sup> See FA 2007, s. 36.

‘ ... *Chairman*: [Lord Wakeham] Could I just finish on this with one pretty simple question. If the Chancellor were sitting where you are sitting and we said, “Come on, tell us about this simplification, because we ain’t heard too much that has been impressive so far about simplification” what answer would he give? Why does he think what he has done is simplification?

*Mr Gammie*: To the extent that he has removed allowances for buildings, he has simplified the system. There will be a degree of repealed legislation. As I say, companies will no longer have to do all the calculations.

... *Chairman*: That is the main simplification.

*Mr Gammie*: That seems to me to be the main simplification.<sup>346</sup>

The fundamental similarity of the Diceyan approach of tax professionals, well illustrated by Gammie’s famous contempt for what Parliament provides in the exercise of its legislative function, so long as it is clear about its intentions,<sup>347</sup> nonetheless leads them to accept and work with the legislative outcomes, however flawed they may find them. With such a crushingly united front on the corporation tax policy, it is unsurprising that the chief role of the TJN is the undermining of the policy community position. One illustration is Murphy’s attempt, in the BBC’s *File on Four* programme, to move the discussion on transfer pricing away from a preoccupation with ‘anti-avoidance’ to the effect of the UK transfer pricing provisions on the economies of developing countries.<sup>348</sup>

So the corporation tax reform policy community has a tightly integrated and fairly constant membership. It also has, as the evidence would lead us to infer, considerable intellectual and economic resources. Writing of policy communities in general, Marsh and Rhodes contrast what they see as the ‘relationship of exchange’<sup>349</sup> that subsists between a

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<sup>346</sup> House of Lords Select Committee on Economic Affairs, *4<sup>th</sup> Report. The Finance Bill 2007, Volume II: Evidence* (House of Lords Papers, Session 2006-2007, 121) (London: TSO, 2007), p. 5.

<sup>347</sup> See Gammie, n. 331 above, p. 254.

<sup>348</sup> See *BBC File on Four*, 2007. ‘Companies “looting” a continent’. Radio, BBC Radio 4. 29 July. (Transcript available from [www.bbc.co.uk](http://www.bbc.co.uk).)

<sup>349</sup> See Marsh and Rhodes, n. 119 above, p. 251.

policy community and the relevant Department of HMG, and the contrasting inability of issue networks to offer any expertise that HMG is interested in acquiring. For indeed, the ‘special codes’ on corporate finance<sup>350</sup> (a fundamental component of the corporation tax code) represent an almost astonishing assimilation of professional expertise to the legislative function,<sup>351</sup> born no doubt of many a congenial meeting over coffee and biscuits in Whitehall.<sup>352</sup> Equally, there is evidently no provision in the corporation tax code capable of addressing what many would regard as the kind of rank inter-nation inequity<sup>353</sup> revealed by the *File on Four* report on transfer pricing.

The relative lack of financial resources on the issue network side is reflected in its non-hierarchical organisation. By contrast, as Marsh and Rhodes suggest, policy communities are hierarchical and, as such, are (as in the case of the CBI) able to ‘deliver [their] members’. More than that, the Law Society and the ICAEW are each in a position to discipline and exclude certain or other of their membership. The lack of resources suffered by issue networks may not endure, however. Environmental policy is perhaps the classic example of an area in which arguments once spoken to electorates over the heads of governments have gained some salience in the counsels of policy communities. The same may yet happen with corporation tax reform (especially in its international setting). However, this currently seems – at the very least – unlikely.

A criticism that might be made of the foregoing discussion is that, whatever it might rightly say about the respective positions of policy network members, it gives undue prominence to the TJN, an organisation whose salience is primarily web and media based

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<sup>350</sup> See FA 2002, ss. 69-79 and Sched. 23; FA 2002, s. 80 and Sched. 24; FA 2002, s. 81; FA 2002, s. 82 and Sched. 25; FA 2002, s. 83 and Schedules 26-28; FA 2002, s. 104.

<sup>351</sup> See Chapter 3 below.

<sup>352</sup> See also the tax treatment of property derivatives (FA 2002, Sched. 26, para. 45G; Pickard, *Financial Times*, 14 January 2005, 21).

and whose public persona has been (until Picciotto recently took up his pen) substantially confined to a single individual. If made, the point is possibly well made. The TJN is almost unique as an issue network in this policy area, however, and (unlike, possibly, the Taxpayers' Alliance), has a position widely divergent from HMG, as well as (again by comparison with the Taxpayers' Alliance) few if any powerful backers. Indeed, it is in relation to power that Marsh and Rhodes find a fourth dimension common to policy communities and issue networks. The involvement in the corporation tax reform debate of bodies such as the TJN, whilst it has the potential to lift corporation tax reform to a political significance comparable to that of – say – climate change, is hampered by the fact that, as Marsh and Rhodes point out, the involvement of members in such networks can only ever be a 'zero-sum game', since the TJN and other issue networks have disparate powers, which reflect their 'unequal resources', and the 'unequal access' of their members.<sup>354</sup> With the corporation tax reform policy community, however, there is (in Marsh and Rhodes's words) 'a balance of power among members':<sup>355</sup> although the arguments of the CIOT or the Law Society may dominate, or although both may on particular issues prevail over HMG (or *vice versa*), their constructive engagement is almost by definition a 'positive sum game', since that is why the community is found to exist in the first place. This point is well illustrated by KPMG's warning, issued through an article of Houlder's in the *Financial Times*,<sup>356</sup> that the failure of 'business' to engage with the arguments raised by the Treasury and HMRC in the

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<sup>353</sup> See Brian J. Arnold and Michael J. McIntyre, *International Tax Primer*, 2<sup>nd</sup> edn (The Hague: Kluwer, 2002), p. 4.

<sup>354</sup> See Marsh and Rhodes, n. 119 above, p. 251.

<sup>355</sup> *Ibid.*

<sup>356</sup> See Houlder, *Financial Times*, 22 June 2007, 2; Houlder, *Financial Times*, 20 July 2007, 3.



consultation paper on overseas profits,<sup>357</sup> published in June 2007, would likely result in a highly disadvantageous settlement as regarded all (corporate sector) interests concerned.<sup>358</sup>

For the moment, the biggest challenge to trust and confidence that policy networks (especially policy communities) seem to present is that of inadequate accountability. It means that the Crown, here Treasury and HMRC civil servants, is free to develop itself by self-regulation. Indeed, policy networks are a fine example of how, '[i]n the absence of both political and legal oversight and accountability, the Crown-as-executive is left free to develop and to transform itself, unsupervised and unconstrained'.<sup>359</sup> When governance is seen as a matter of 'self-organizing networks', says Rhodes, the challenge to 'governability' is that 'the networks become autonomous and resist central guidance'.<sup>360</sup> Governments are torn between using the sheer levels of expertise available, and the dangers to trust and confidence that such unaccountable advisers may bring with them.

#### HER MAJESTY'S JUDGES

The role of the judges in the reform of corporation tax is, in a number of respects, an anomalous one. Although the Special Commissioners are people who have made distinguished careers in the tax law arena,<sup>361</sup> most (if not all) of the supreme court judges and Law Lords to whom has fallen the task of interpreting corporation tax legislation were not, in

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<sup>357</sup> H.M. Treasury and HMRC, *Taxation of the foreign profits of companies: a discussion document* (London: H.M. Treasury, 2007).

<sup>358</sup> Some such warning was heeded by the United States National Foreign Trade Council, however (see Houlder, *Financial Times*, 5 October 2007, 2).

<sup>359</sup> See Tomkins, n. 65 above, p. 77.

<sup>360</sup> See R.A.W. Rhodes, 'The New Governance: Governing without Government' (1996) XLIV *Political Studies* 652-667, 667.

<sup>361</sup> e.g. Gammie himself (*passim*), a deputy Special Commissioner since 2002; Graham Aaronson, QC, counsel for the taxpayer in, e.g., *Barclays Mercantile Business Finance Ltd v. Mawson (Inspector of Taxes)* [2004] UKHL 51; [2005] STC 1: see below.

their days as members of the Bar, specialist tax lawyers.<sup>362</sup> Whether, as Tiley implies, this is to be regretted,<sup>363</sup> is a matter for debate, but it has meant that the attention of judges in corporation tax cases – as in other tax cases – has focussed (tacitly, generally) on the constitutional and administrative law problems raised. Moreover, although particular judges (Lord Brightman,<sup>364</sup> for example, and, in another age, Lords Radcliffe and Diplock<sup>365</sup>) have contributed in various capacities to the debate on the specifics of tax reform, the judiciary have not generally been involved in the *ex ante* discussion of corporation tax proposals. Instead, the judges' role has been carefully confined to the more restricted one of statutory interpretation, and may yet involve considering individual enacted provisions in hearings for judicial review.

In one sense puzzling, but in others deeply revealing of the tensions in the historical role of the higher judiciary, is the distance of the Royal Courts of Justice from Westminster, and the presence in the Palace of Westminster of the Appellate Committee of the House of Lords (soon to be reconstituted as the Supreme Court of the United Kingdom).<sup>366</sup> The panorama viewed from the London Eye is such as to make the contradictions implied extremely apparent. The role of judges in matters of taxation has always been unusually sensitive. In

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<sup>362</sup> Lord Walker of Gestingthorpe was, however, and he is therefore customarily allocated to revenue appeals (see Brice Dickson, 'The Processing of Appeals in the House of Lords' (2007) 123 LQR 571-601, 589-590).

<sup>363</sup> See 'J.T.' (John Tiley) [2000] BTR 133.

<sup>364</sup> See David Hope (Lord Hope of Craighead), 'Voices from the Past – the Law Lords' Contribution to the Legislative Process' (2007) 123 LQR 547-570, 562, 570, on Lord Brightman's extensive contribution to legislative debate (not only on tax matters); shown, too, in Joint Committee on Tax Simplification Bills, *1<sup>st</sup> Report. Capital Allowances Bill: Minutes of Evidence, 31 January 2001* (House of Commons Papers, Session 2000-2001, 175-ii) (London: HMSO, 2001), *passim*.

<sup>365</sup> See the Rt Hon. Sir Kenneth Diplock, 'The Courts as Legislators', in *The Lawyer and Justice*, ed. by Brian W. Harvey (London: Sweet and Maxwell, 1978), pp. 263-287; *Royal Commission on the Taxation of Profits and Income: Final Report: Presented to Parliament by Command of Her Majesty* (Chair, Lord Radcliffe) (Cmd 9474) (London: Her Majesty's Stationery Office, 1955); Robert Stevens, *The English Judges: Their Role in the Changing Constitution* (Oxford: Hart Publishing, 2005), p. 29.

reliance, possibly, on Bacon's idea of the 'lions under the throne',<sup>367</sup> and facing a Parliament looking for 'redress of grievances' as the price of granting taxation to the Crown, Charles I had tried to rely on the royal prerogative to levy taxation.<sup>368</sup> As might possibly be inferred from Tomkins' essay on the topic,<sup>369</sup> this has been at the forefront of the judges' minds in the contemporary closing off of the once extensive-seeming opportunities for challenging tax legislation under human rights legislation.<sup>370</sup> In between these two historical junctures is a body of case law dating (as relevant to the present study) from the late nineteenth century, and especially from 1978.<sup>371</sup> What we have in this period, as Roger Kerridge says, is a notable judicial effort to give meaning to often obscurely-directed and drafted legislative provisions, while at the same time avoiding the kinds of constitutional controversies to which reference has just been made.<sup>372</sup> 'On the whole', as Kerridge concludes, the judges, in deploying a kind of intuition, 'are to be congratulated'.<sup>373</sup> David Robertson, in his essay on the now-iconic income tax case of *Pepper v. Hart*,<sup>374</sup> writes instead of a broad 'discretion'

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<sup>366</sup> Constitutional Reform Act 2005, ss. 23-60, on and after 1 October 2009; see Diana Woodhouse, 'The constitutional and political implications of a United Kingdom Supreme Court' (2004) 24: 1 and 2 LS 134-155.

<sup>367</sup> See Francis Bacon, 'Of Judicature', in *The Essays*, ed. by John Pitcher (London: Penguin, 1985), pp. 222-225, invoking the lions under Solomon's throne (see 3 Kings, x, 19-20 (Douay Version)).

<sup>368</sup> See W. J. Jones, *Politics and the Bench: The Judges and the Origins of the English Civil War* (London: George Allen and Unwin, 1971).

<sup>369</sup> See Adam Tomkins, *Our Republican Constitution* (Oxford: Hart Publishing, 2005), pp. 67-87.

<sup>370</sup> See, e.g., *NAP Holdings UK Ltd v. United Kingdom* (1996) 22 EHRR – Comm Supp CD 114; Application No. 13013/87, *Wasa Liv Ömsesidigt, Försäkringsbolaget Valands Pensionsstiftelse and a group of approximately 15,000 individuals v. Sweden* (1988) 58 ECHRDR 163. On the sensitivity of the judicial/Crown relationship in tax, see Lord Woolf, 'Tax and Judicial Review' [1993] BTR 219-229.

<sup>371</sup> Surprisingly, the date of the first corporation tax appeal: *Willingale (H.M. Inspector of Taxes) v. International Commercial Bank Ltd* (1978) 52 TC 242 was decided in February 1978. The most recent corporation tax decision of the House of Lords is currently (29 February 2008) *Sempra Metals Ltd (formerly Metallgesellschaft Ltd) v. Inland Revenue Commissioners and Another* [2007] UKHL 34; [2007] 3 WLR 354 (although this might more properly regarded as a case on restitution).

<sup>372</sup> See Kerridge [2003] BTR 257-264.

<sup>373</sup> *Ibid.*, p. 260.

<sup>374</sup> *Pepper (Inspector of Taxes) v. Hart* [1993] AC 593.

exercised in the House of Lords,<sup>375</sup> but cannot take this much further than to explain the exercise of this discretion in terms of a rather selective judicial use of parliamentary papers.<sup>376</sup> Dicey himself, to be sure, had remarkably little to say about the constitutional position of the judiciary.<sup>377</sup> What is proposed here is an analysis of the judicial role in corporation tax appeals, as a concrete instance of judges carrying out a complementary role to that carried out by the Treasury, and by the legislature, in the particular area of corporation tax reform. The judges are, in other words, engaging in the ‘political practice’ of public law (in this case interpreting corporation tax legislation), and they are doing so in a manner that reflects the Hobbesian truth<sup>378</sup> that, as Tomkins puts it, ‘the judiciary derives its constitutional power ultimately from that of the Crown’.<sup>379</sup> Senior judges, he points out (like Cabinet ministers) are Privy Councillors,<sup>380</sup> and ‘[t]he judicial oath of allegiance is to the Crown – not to the constitution, not to the people, and certainly not to Parliament - but to the Crown’.<sup>381</sup> The truth of this is no doubt the historical reason for the attitude of circumspect submission assumed in D.C. Potter’s conclusion on *Sharkey v. Wernher* that, had the case not been decided by the House of Lords, he would have concluded that it was wrong.<sup>382</sup> It is also apparent, however, in the tendency of judges as late as the 1980s to refer to the taxpayer, not

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<sup>375</sup> See David Robertson, *Judicial Discretion in the House of Lords* (Oxford: Clarendon Press, 1998). Robertson is unusual among political scientists as taking an interest in the judges’ role in government (see David Pannick, *Judges* (Oxford: Oxford University Press, 1987), p. 10).

<sup>376</sup> See Robertson, n. 375 above, pp. 160-164. See Sedley [1999] CLJ 627-629, 628 (book review).

<sup>377</sup> See Dicey, n. 52 above, pp. 60, 410.

<sup>378</sup> See Hobbes, n. 31 above, p. 291 (see Loughlin, n. 20 above, p. 152).

<sup>379</sup> See Tomkins, n. 65 above, pp. 54-60, discussing *Proclamations* (1607) 77 ER 1352; *Prohibitions del Roy* (1611) 77 ER 1342; and *In re M.* [1994] 1 AC 377. Consistent with the functionalist approach taken in this study this approach builds on that of J.A.G. Griffith, in *The Politics of the Judiciary*, 5<sup>th</sup> edn (London: Fontana, 1997), esp. ch. 9.

<sup>380</sup> See Tomkins, n. 65 above, p. 53.

<sup>381</sup> *Ibid.*

<sup>382</sup> [1964] BTR 438-443, 439.

as such, but as ‘the subject’.<sup>383</sup> More recently, as the enterprise of the EU and its implications have become better understood, and especially with the advent of the Human Rights Act 1998 (HRA 1998), the language of ‘state’ and ‘subject’ has been suppressed. However, as will shortly become apparent, the political approach that it reflects has come to be re-asserted, albeit with much greater subtlety, and to different effect, than in former times. The attitude of the contemporary judiciary to taxation statutes is no less prudential, though manifested in different circumstances, than that in *IRC v. Duke of Westminster*.<sup>384</sup>

This first broad point can be illustrated by reference to examples within two of the four substantive themes referred to at the beginning of the study: *Barclays Mercantile v. Mawson*,<sup>385</sup> and *Revenue and Customs Commissioners v. William Grant and Sons*.<sup>386</sup> Each of these cases, the latest corporation tax decisions of the House of Lords, involve contributions by judges whose approach can be seen, in the sense discussed elsewhere in this study, as ‘prudential’, on the particular issue and at the particular historical convergence in question. Other examples, reflecting the fact that the UK retains its competence in taxation matters, are discussed in Chapter 3. In each case, the judges are enhancing the UK’s tax sovereignty by finding a ‘true’, or ‘right’, interpretation, by a prudential method.

In the later case, the judgment in which was handed down on 28 March 2007, the question (to which the judicial committee gave an affirmative answer) was the highly ‘technical’ one of whether the amount of depreciation deducted in calculating a company’s trading profits

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<sup>383</sup> See, e.g., *van den Berghs Ltd v. Clark (Inspector of Taxes)* [1935] AC 431, 439 (Lord Macmillan); *Hochstrasser (Inspector of Taxes) v. Mayes* [1960] AC 376, 389 (Viscount Simonds); *W.T. Ramsay Ltd v. IRC* [1982] AC 300, 323C, E (Lord Wilberforce).

<sup>384</sup> *Commissioners of Inland Revenue v. His Grace the Duke of Westminster* [1936] AC 1; Stevens, n. 365 above, pp. 23-24; Assaf Likhovski, ‘Tax Law and Public Opinion: Explaining IRC v Duke of Westminster’, in *Studies in the History of Tax Law: Volume 2*, ed. by John Tiley (Oxford: Hart Publishing, 2007), pp. 183-221.

<sup>385</sup> *Barclays Mercantile Business Finance Ltd v. Mawson (Inspector of Taxes)* [2004] UKHL 51; [2005] STC 1.

for accounting purposes should exclude depreciation of trading stock. If so, the company's taxable profits for the period would be reduced; if not, they would be increased. It was a classic example within the accounting theme of how far 'profits per accounts' should be aligned with taxable profit for corporation tax purposes. Of the two speeches delivered by their Lordships, the one that has attracted the greater degree of comment is that of the mercurially talented senior Law Lord, Lord Hoffmann.<sup>387</sup> He took a quintessentially prudential approach, which left various members of the corporation tax policy community reeling,<sup>388</sup> before, in a considered note, Graeme MacDonald recognised the elegance of the solution, although without describing it in terms as 'prudential'.<sup>389</sup> Indeed, viewed in Loughlin's prism of public law as a 'political practice', certain aspects of Lord Hoffmann's speech have a significance different from that ascribed by MacDonald in his extremely useful note. Thus, although, as MacDonald comments, 'many [people] were hoping for some guidance from their Lordships ... [on] the relationship between accounting practice and the law in computing taxable profits', Lord Hoffmann wisely avoided fulfilling this hope. It was the first time that the House of Lords had considered International Accounting Standards, and, in the circumstances, full discussion at this point might not have been entirely helpful. Not only might it have closed off future possibilities, but it might draw attention to the IASB's (indirect) influence on the corporation tax base, as on the question of whether, in the light of this, the GAAP deviations referred to in FA 1998, s. 42(1), were adequate to safeguard the public interest. Secondly, consistent with the delicate constitutionality of the judiciary's role in tax cases, Lord Hoffmann endorsed the comments of Sir John Pennycuik

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<sup>386</sup> *Revenue and Customs Commissioners v. William Grant and Sons Distillers Ltd; Small (Inspector of Taxes) v. Mars UK Ltd* [2007] UKHL 15; [2007] STC 680.

<sup>387</sup> [2007] UKHL 15; [2007] STC 680, 683a-688a (see Tait, *Financial Times Innovative Lawyers Report 2007*, 6 July 2007, 12-14).

<sup>388</sup> See Collins and Dixon, n. 336 above; Parry-Wingfield, *Tax Journal*, 28 May 2007, 13-15.

<sup>389</sup> MacDonald [2007] BTR 366-370.

V.-C. in *Odeon Associated Theatres v. Jones*<sup>390</sup> and of Nolan L.J., in *Gallagher v. Jones*,<sup>391</sup> that there was no room for ‘judge made’ rules on GAAP issues.<sup>392</sup> Any modifications of GAAP had thus to be made by statute, not by the judges. Whether, as MacDonald wonders, the judiciary will ever retreat from this position, is a question of prudence; not accountants’ prudence,<sup>393</sup> but the Machiavellian prudence discussed above. They may do so; they may not. It depends on the context in which the question comes to be considered next time round.

If the point decided in *William Grant* suggests a prudential approach to public law issues, in an area which might, at first sight, be thought of as merely technical, *Barclays Mercantile v. Mawson* (decided on 25 November 2004) evinces prudence in a more obviously ‘political’ area: corporation tax avoidance. Here, the question was whether capital allowances were available to a finance lessor (Barclays Mercantile), which had incurred expenditure in a complicated series of financing arrangements, the purpose of which – in Tiley’s comments on the decision – was not, as such, to avoid tax, but ‘to ensure the bank [Barclays] met the capital adequacy rules laid down by the UK banking regulatory authorities’.<sup>394</sup> In an answer that, whilst technical, had a strong element of policy, their Lordships held that capital allowances were available in such circumstances. Just as *William Grant* was a classic case on the calculation of trading profits, *Barclays Mercantile* might have seemed to be a classic tax avoidance case. In declining to treat it as such, and in thereby clarifying the application of the *Ramsay* principle, their Lordships took a highly prudential course. This feature of the decision, and hence its public law importance, did not figure in commentaries on the case, however. Tiley, for instance, commends the quality of the decision and, like MacDonald on

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<sup>390</sup> *Odeon Associated Theatres Ltd v. Jones (Inspector of Taxes)* [1971] 2 All ER 407, 414a-b.

<sup>391</sup> *Gallagher v. Jones (Inspector of Taxes)* and *Threlfall v. Jones (Inspector of Taxes)* [1993] STC 537, 560c-d.

<sup>392</sup> [2007] UKHL 15; [2007] STC 680, 685f.

<sup>393</sup> See Accounting Standards Board, *Statement of Principles for Financial Reporting*, paras 3.18-3.20 (available from [www.frc.org.uk](http://www.frc.org.uk)) (accessed 22 October 2007).

*William Grant*, describes its prudential aspects without actually characterising them in such terms. He likes the way their Lordships eschewed a ‘detailed analysis of the existing case law’,<sup>395</sup> since ‘the principles are now clear’. All that is necessary, instead, is to read the statute: ‘first [says Lord Nicholls] ... decide, on a purposive construction, exactly what transaction will answer to the statutory description and secondly, ... decide whether the transaction in question does so.’<sup>396</sup> Tiley wonders whether the House of Lords is nudging Parliament towards a GAAR, since, as a result of the decision, it may be that what we have now is ‘all the disadvantages of the uncertainty of a GAAR without the protection of an advance rulings system, the one thing that makes a GAAR for some workable’.<sup>397</sup> Finally, he praises their Lordships for reformulating the legal position in a single speech,<sup>398</sup> in response to the request from Barclays’ counsel, ‘on behalf of the profession’ for ‘definitive guidance’.<sup>399</sup> All of these comments are characteristic of the practitioner, rather than the public lawyer.

Though the precise contexts were different, both *William Grant* and *Barclays Mercantile* were cases on statutory interpretation. There is also the question, however, of how prudence might shape the response of the judiciary to the judicial review of taxation statutes. This is, in Tomkins’ terms, legal rather than political accountability, and in the present context, would tend to rely on the illegality ground famously enunciated by Lord Diplock in 1984.<sup>400</sup> Thus far, no corporation tax provision has been considered in a judicial review case, but

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<sup>394</sup> Tiley [2005] BTR 273-280, 274.

<sup>395</sup> *Ibid.*, p. 277.

<sup>396</sup> [2005] STC 1, 13b.

<sup>397</sup> See Tiley, n. 394 above, p. 280.

<sup>398</sup> *Ibid.*, p. 277.

<sup>399</sup> [2005] STC 1, 11b.

<sup>400</sup> See *Council of Civil Service Unions and Others v. Minister for the Civil Service* [1985] 1 AC 374, 410F; also Woolf, n. 370 above.



applications (as yet unsuccessful) in relation to other taxes,<sup>401</sup> indicate that it remains a real possibility. The feasibility of a challenge to a corporation tax provision by judicial review, arising through non-compliance with GATT 1994, the European Treaty, or the European Convention on Human Rights (ECHR), is certainly a constraint on ministers and civil servants when deciding to take reform measures forward.<sup>402</sup> Suffice it to say that judicial review could certainly be used for holding the Treasury to account *ex post*. What, given the absence of a Civil Service Act, is not possible, is the judicial review of the actions and decisions of civil servants, since there is as yet no ‘framework of law’ against which to test them.<sup>403</sup>

Opinions are sharply divided on the legitimacy of accountability through judicial review. Lever considers it to be necessary to protect potentially disadvantaged groups;<sup>404</sup> Waldron argues that it is ‘democratically illegitimate’.<sup>405</sup> Either way, the day of a successful challenge to corporation tax legislation must be near, not least because it looks more effective than political accountability. However, we need, as Tomkins says, to guard against the assumption that ‘no constitutional problem is solved unless or until it is judicially solved, and that there is no constitutional problem that cannot be successfully solved by the

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<sup>401</sup> See *R. (on the application of Professional Contractors Group Ltd and others) v. IRC* [2001] EWHC Admin 236; [2001] STC 629 (Burton J.); [2001] EWCA Civ 1945; [2002] STC 165 (CA); *R. (on the application of British Aggregates Association and others) v. Customs and Excise Commissioners* [2002] EWHC 926 (Admin); [2002] 2 CMLR 51 (Moses J.); *Federation of Tour Operators and Others v. Her Majesty’s Treasury and Others* [2007] EWHC 2062 (Admin); [2007] UKHRR 1210 (Stanley Burnton J.).

<sup>402</sup> See the unsuccessful challenge, subsequently referred to the ECJ under Art 234, European Treaty (ex 177), in *R. v. H.M. Treasury, ex parte Daily Mail and General Trust plc.* [1987] STC 157 (Macpherson J.); Case 81/87, *R. v. H.M. Treasury and Inland Revenue Commissioners, ex parte Daily Mail and General Trust plc.* [1988] STC 787 (notice of motion for order of mandamus).

<sup>403</sup> See Tomkins, n. 65 above, p. 77.

<sup>404</sup> See Annabelle Lever, ‘Is Judicial Review Undemocratic?’ [2007] PL 280-298.

<sup>405</sup> See Jeremy Waldron, ‘The Core of the Case Against Judicial Review’ (2006) 115 YLJ 1346-1406.

judiciary'.<sup>406</sup> Political accountability is more easily squared with the idea of a sovereign state than is the legal accountability provided by the judges.

#### SOME INTERIM OBSERVATIONS

The conclusion of the discussion of the judges' contribution to corporation tax reform is an appropriate point at which to reflect on the links between the main elements of the argument so far, and the substance of the discussion to be unfolded in the next chapter.

What the discussion in Chapter 2 has proposed is that the institutional framework of corporation tax reform relies for its effectiveness on two main intersecting tensions, each of which are both a general feature of government in the UK, and each of which bring to consciousness aspects specific to the context of corporation tax reform.

The more evident of these tensions in the literature is that between the state, and the sovereignty subsisting between it and its subjects, and global economic power and the effect on the state's sovereignty of economic globalisation. Less to the forefront of contemporary debate, however, is the tension in the UK's constitutional arrangements between the Crown (here H.M. Treasury and its junior Department, HMRC) and Parliament. In this chapter, which has concerned itself with the *ex post* scrutiny of corporation tax reform, the tension between Crown and Parliament has been depicted as one in which H.M. Treasury must use all of its prudential skills to confront the contingencies of an uncertain world. Parliament, however, with the benefit of hindsight, must use all of the analytical skills of its Members, all of its powers of compulsion, to reconstruct what effects this prudential conduct has produced and, where appropriate, to alert Treasury ministers to areas where the latter's

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<sup>406</sup> See Tomkins, n. 65 above, p. 210; also David Goldberg, QC, 'Between the Taxpayer and the Executive; Law's Inadequacy; Democracy's Failure?' [1996] BTR 9-27.

conduct of policy is producing results that are, in some sense, sub-optimal. Experience shows that the Treasury has, over the last decade at least, been much more successful in its constitutional task than has the select committee system of the House of Commons.

It is in the weaknesses of the arrangements just discussed, so critics might say, that the dangers of the other main tension, that between the corporate sector and the state, are most keenly feared. Suppose that, because of a combination of ‘gaps’ in the accountability mechanisms and the economic power of the corporate sector, the cumulative effect of apparently prudential decisions by Treasury ministers is not a promotion of the public interest, but the furtherance of the particular economic interests of MNCs. Such, with a welter of examples has been, albeit from somewhat different premises, the argument of George Monbiot.<sup>407</sup> In the next chapter, we therefore proceed to interrogate the crisis of trust and confidence thereby threatened, in the context of the process by which corporation tax reform proposals reach maturity and become law. How can we analyse what the public interest in corporation tax reform might be? Does it matter where reform proposals come from? Does the breadth and depth of the discussion and deliberation of those affected by developments in such a technical area of public law really matter? These and other questions form the subject matter of Chapter 3, which, in analysing the *ex ante* scrutiny of such proposals, complements and elaborates the discussion in the present chapter.

A significant element in what has gone before, besides the deconstruction of the tensions between corporations and the state, between Crown and Parliament, has been the interrogation of the contribution to these oppositions of the respective roles and values of, on the one hand, policy networks, and, on the other, the judiciary. In Chapter 3, against the background of the issues uncovered in Chapter 2, we shall be examining the role of policy

networks in the various corporation tax reforms of recent decades.<sup>408</sup> We shall be recalling, too, how the judiciary's role in this process can be said to have prudentially 'underpinned' these policy developments.

Finally, we should emphasise that the type of analysis pursued in these pages is facilitated by the idea of public law – including taxation law – as a 'political practice', the dominant technique in which is prudence. This does not mean, however, that the categories of law and politics collapse into one. What it does provide is a convincing analysis of the role of one in the context of the other. There is, it is maintained, a consistency between Loughlin's concept of public law as a practice of politics, and Tomkins' notion of a distinction between the political and the legal constitutions. The former is a clear manifestation of Loughlin's 'second order of the political', while the latter is Loughlin's 'third order', in which political values are shaped and prioritised in particular contexts by the logic of effectiveness.

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<sup>407</sup> See George Monbiot, *Captive State: The Corporate Takeover of Britain* (London: Macmillan, 2000), *passim*.

<sup>408</sup> See n. 350 above.

## Chapter 3

### THE PROCESS OF REFORM

#### PROLOGUE

‘It is one thing’, as the expression goes, to ask the reader to imagine the vista presented from the London Eye; it is ‘quite another’ to offer a convincing interpretation of the interactions of the various institutions in the making of corporation tax policy, of corporation tax law. Yet such is what the present chapter seeks to do. Chapter 2 analysed the objectives and values with which various institutions and groups of individuals approach the problems of corporation tax reform. The aim of that discussion was to demonstrate how far the institutional framework contributes to the augmentation of trust and confidence in H.M. Government (HMG) in the corporation tax arena. The present chapter sets about the task of analysing the extent to which HMG’s management of the different groups and institutions in the reform process also augment that trust and confidence.<sup>1</sup> The challenge presented by the latter endeavour is common to all attempts in law and political theory to show how power is consolidated in the policy-making process.

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<sup>1</sup> See John Locke, *Two Treatises of Government*, ed. by Peter Laslett (Cambridge: Cambridge University Press, 1988), pp. 381-382, ch. 19 (esp. p. 415); John Dunn, ‘Trust and Political Agency’, in John Dunn, *Interpreting Political Responsibility: Essays 1981-1989* (Cambridge: Polity Press, 1990), pp. 26-44; John Dunn, *Locke* (Oxford, Oxford University Press, 1984), ch. 2; Bernard Manin, *The Principles of Representative Government* (Cambridge: Cambridge University Press, 1997), pp. 126-127; Russell Hardin, ‘Do we want trust in government?’, in *Democracy and Trust*, ed. by Mark E. Warren (Cambridge: Cambridge University Press, 1999), pp. 22-41; Onora O’Neill, *A Question of Trust* (Cambridge: Cambridge University Press, 2002) (so many questions,

To give an imaginative dimension to the discussion, conceive that it were possible, in some Dickensian flight of fancy, to eavesdrop on the proceedings of the various institutional personnel and policy communities discussed in the previous chapter. In a lecture theatre in Whitehall, we might find, as did a reporter from the *Financial Times*, one spring morning in 2006, the head of the home civil service, giving a motivational talk to new civil service recruits, on the intrinsically worthwhile nature of a job that involves furthering the public interest rather than helping companies to avoid their corporation tax responsibilities.<sup>2</sup> Close by, one might listen in on a meeting of senior public servants from H.M. Treasury and H.M. Revenue and Customs (HMRC),<sup>3</sup> deliberating over the specifics of a new legislative measure. Across the street, in the Palace of Westminster, the House of Commons might be debating an anti-avoidance provision (one much further down the line of development), while in the chamber of the House of Lords, the judicial committee might be handing down a judgment in a corporation tax case.<sup>4</sup> Meanwhile, across the River Thames, in a glass and steel building of the City of London, a group of tax specialists from one of the large City professional services firms might be assessing the likelihood of a particular course of action crossing the elusive boundary between ‘tax planning’ and unacceptable tax avoidance<sup>5</sup> with the senior management of a merchant bank.

None of this is to suggest that tax avoidance and its regulation is the sole, or even the most important, theme in corporation tax reform. Indeed, as we shall see in the unfolding discussion, all seven of the themes introduced at the beginning of the study have some

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so few answers); Plager, *Taxation*, 1 December 2005, 227-229 (Loughlin Hickey’s 2005 Hardman lecture).

<sup>2</sup> See Cameron, *FT Magazine*, 8/9 April 2006, 16-20, 16.

<sup>3</sup> See Chapter 2 above, pp. 128-137 (‘Policy Networks’).

<sup>4</sup> See Chapter 2 above, pp. 137-146 (‘Her Majesty’s Judges’).

<sup>5</sup> See, e.g., Hansard HC Public Bill Committee, 17 May 2007, col. 215 (Ed Balls, MP, Economic Secretary to the Treasury); also Houlder, *Financial Times*, 30 July 2007, 3, referring to ‘the waning popularity of tax planning centred on day-to-day transactions’.

greater or lesser part to play. What this imaginative flight of fancy does emphasise, however, is the idea that, at any given time, individual reform proposals will be at different stages of development. There is no single process of reform, but, instead, various incremental measures,<sup>6</sup> in support of a broader set of policy objectives. There is, moreover, no single decision, but numerous decisions at various different institutional levels.<sup>7</sup>

Chapter 2 depicted institutional, group, and even individual objectives and values. In the course of introducing the ground to be covered, we remarked on the so-called ‘new institutionalism’ of authors such as March and Olsen, Tsebelis and Money, and Weaver and Rockman,<sup>8</sup> and noted that, if used as an ‘organising perspective’, as suggested by David Judge,<sup>9</sup> aspects of the new institutionalism might help us to interpret the ways in which institutions function, and mutually interact, in the reform of corporation tax. The main strands of the discussion in Chapter 2, however, concerned the ways in which the values and objectives of the institutions of the state and those of the corporate sector might differ; how, given the sovereign status of the Crown in Parliament, it is the Westminster institutions, rather than those of the EU, that are sovereign; how, following Loughlin, sovereignty is not merely a legal, but a ‘relational’, concept; and how, with some reservations, the objectives and values of the different institutions involved in corporation tax reform are indeed such as to inspire trust and confidence in their respective spheres. Chapter 2 was therefore about the question of what the various institutions bring to the reform process: interests, skill, a variable ability to hold HMG to account, etc. The present chapter is about the interaction of these institutions in the actual process of reform, on sample issues raised by the subject

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<sup>6</sup> See Hansard HC Standing Committee A, 11 May 2004, col. 114 (Rt Hon. Dawn Primarolo, MP Paymaster General).

<sup>7</sup> See Christopher Wales, ‘The Implications of the O’Donnell Review for the making of Tax Policy in the UK’ [2004] BTR 543-565, 550.

<sup>8</sup> See Chapter 2 above, nn. 23-26.

<sup>9</sup> See Chapter 2 above, n. 29.

matter of the study. However, just as Chapter 2 was concerned with institutional safeguards, and the political tensions that tend to make them effective, so Chapter 3 is devoted to the ways in which HMG's approach to corporation tax reform, and the procedural framework within which reform takes place, add to, or detract from, the trust and confidence necessary to political sovereignty. The focus of Chapter 2, as mentioned in its closing pages, was a certain *pro active* prudence, and its *ex post* scrutiny: the present chapter is about *ex ante* scrutiny, and the strengths and limitations of the processes within which that scrutiny has its place.

Students of public policy will be aware of the sheer range of theoretical possibilities that such an undertaking as the present can open up.<sup>10</sup> Indeed, the new institutionalism, a highly diluted version of which plays a subsidiary interpretative role in the present study, sets out to offer such insights. In Wayne Parsons' words, each of its distinct variants supplies:

‘... a different window or insight into how institutions shape the way in which decision-making takes place – and, especially in the case of economic institutionalism, how institutions ought to be arranged so as to ensure that they function “efficiently” (*sic*).’<sup>11</sup>

A different arrangement of institutions is not, as will now be appreciated, the main, or even a significant, object of the present inquiry. However, what the study is concerned with, in the present chapter, no less than in the previous ones, is power.<sup>12</sup> How, in other words, the institutions, processes, and outcomes of corporation tax reform augment, rather than undermine, the UK's sovereignty. Everywhere the emphasis is on power, on that understated

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<sup>10</sup> See Wayne Parsons, *Public Policy: An Introduction to the Theory and Practice of Policy Analysis* (Cheltenham: Edward Elgar, 1995), pp. 247-248. Colin Thain and Ross Christie choose Theodore Lowi's four dimensional analysis (see Colin Thain and Ross Christie, 'Treasury Power: Past, Present and Future', p. 14, available from [www.treasuryproject.org](http://www.treasuryproject.org) (accessed 22 February 2008); Theodore J. Lowi, 'Four Systems of Policy, Politics, and Choice' (1972) 32 *Public Administration Review* 298-310).

<sup>11</sup> See Parsons, n. 10 above, p. 324.



– possibly suppressed<sup>13</sup> - notion of ‘constituent power’.<sup>14</sup> Such, ultimately, is the reason for rejecting an analysis of the reform process based on some version of Luhmann’s systems theory.<sup>15</sup> It is true, as discussed in Chapter 1, that Loughlin suggested in 1992 that Luhmann’s ‘sociological theory of law’ might assist in ‘revitalizing’ the ‘functionalist style’ in public law.<sup>16</sup> By 2003, however, in propounding his ‘pure theory of public law’, he had at least postponed that possibility, relegating Luhmann’s contribution to a single point of interpretation.<sup>17</sup> Loughlin’s reasons, though not explicitly articulated, are not hard to decipher. Although Luhmann can explain why a potentially very wide range of policy alternatives are in fact narrowed down, he does so through the idea of expectations being ‘normatively’, not ‘cognitively’, closed.<sup>18</sup> Without denying the possibility that this can illuminate the role of law in certain public policy areas, the view taken in these pages is that this does not allow for the placing at the forefront of the discussion what the ‘pure theory of public law’ takes to be the central public law (here corporation tax law) technique: that of prudence. Secondly, although, through the orderly ‘structural couplings’ for which Luhmann’s theory provides, political influences, no less than other ‘outside’ influences, may play their part, as will be seen in a moment, the central contention of this study is not that corporation tax law is shaped by normative expectations (as, indeed, it may be), but that the theory and values that it embodies are conditioned by the nature and scope of the political

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<sup>12</sup> See Chapter 2 above, nn. 149-154.

<sup>13</sup> See Martin Loughlin, ‘Constituent Power Subverted: From English Constitutional Argument to British Constitutional Practice’, in *The Paradox of Constitutionalism: Constituent Power and Constitutional Form*, ed. by Martin Loughlin and Neil Walker (Oxford: Oxford University Press, 2007), pp. 27-48.

<sup>14</sup> See Chapter 2 above, n. 53.

<sup>15</sup> See Chapter 1 above, nn. 296-307.

<sup>16</sup> See Chapter 1 above, n. 297; also Martin Loughlin, ‘The Functionalist Style in Public Law’ (2005) 55 *University of Toronto Law Journal* 361-403, 402-403 (referring here, not to Luhmann but, to Gunther Teubner).

<sup>17</sup> See Martin Loughlin, *The Idea of Public Law* (Oxford: Oxford University Press, 2003), p. 97n.

<sup>18</sup> See Chapter 1 above, n. 307.

(perhaps we should say, ‘ideological’) consensus at any given time. To anticipate a more detailed discussion below, the nature of that consensus has, throughout the period covered by the study, been defined with perhaps peculiar clarity. Thirdly, between 1992 and 2003, Loughlin’s thought has become increasingly preoccupied with the role of public law in the formation and augmentation of constituent power,<sup>19</sup> that is, political sovereignty, the ‘power to model a state’, in George Lawson’s evocative words.<sup>20</sup> So, too, is the present study concerned to investigate the role of a particular species of public law – corporation tax law – in the modelling of the state of ‘the United Kingdom of Great Britain and Northern Ireland’. This role must, indeed, be an extremely important one, not just in terms of the revenue raised by the tax, but in terms of the system’s ability not to dissuade foreign direct investment, and in the manifest ability of the ‘direction’ of corporation tax reform to command the heights of public policy debate.<sup>21</sup> Fourthly, and finally, although it is not thought appropriate to characterise Luhmann’s contribution as mere ‘metaphor’, a possibility suggested by the editor of *Lloyd*,<sup>22</sup> his systems theory has to be rejected on the historical and interpretative grounds emphasised so greatly throughout the present study. What we are concerned with here is not a European or international system,<sup>23</sup> but a unique combination of national factors at a specific historical juncture.

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<sup>19</sup> See Loughlin, n. 13 above.

<sup>20</sup> See Chapter 2 above, n. 53.

<sup>21</sup> See, e.g., See Houlder, *Financial Times*, 23 December 2005, 4; Houlder, *Financial Times*, 20 June 2006, 3; Houlder, *Financial Times*, 6 October 2006, 3; Eaglesham, *Financial Times*, 10 October 2006, 4; Houlder, *Financial Times*, 17 November 2006, 3. The Institute of Directors made a ‘plea’ for ‘a “clear statement of intent” on where the corporate tax system ... [was] heading ... ’ in late 2006 (Houlder, *Financial Times*, 4 December 2006, 3).

<sup>22</sup> See *Lloyd’s Introduction to Jurisprudence*, ed. by M.D.A. Freeman, 7<sup>th</sup> edn (London: Sweet and Maxwell, 2001), pp. 701-702.

<sup>23</sup> See Niklas Luhmann, *Law as a Social System*, ed. by Fatima Kastner, Richard Nobles, David Schiff, and Rosamund Ziegert (Oxford: Oxford University Press, 2004), ch. 12; Michael King and Chris Thornhill, *Niklas Luhmann’s Theory of Politics and Law* (Basingstoke: Palgrave Macmillan, 2003), pp. 209-211.

So it is, therefore, that the discussion in the present chapter seeks to add a further dimension to the discussion in Chapter 2, and in a similar vein. It sets out to present, in Julia Black's words, another 'view of the cathedral',<sup>24</sup> or at least of the doings of those people whose working lives are spent in the buildings so visible from the London Eye. Four similar strands to those that ran through Chapter 2 run through the present chapter, although (given the concerns of Chapter 3), to a distinct purpose.

First, the significance of the state's pre-eminence, or more specifically, the pre-eminence of its representative – the Crown in Parliament – in the policy-making process, becomes, not its obligation, within the logic of the UK's constitutional arrangements, to account for the success, or failure, of its activities, to a watchful group of parliamentary select committees, but its right of legislative initiative,<sup>25</sup> in this case, in the corporation tax field. Within the logic of the UK's representative democracy, unlike – so Bernard Manin reminds us – the direct democracies of Ancient Greece,<sup>26</sup> this power of initiative is unique. Its exercise, or non-exercise, under the discretions conferred by the royal prerogative analysed in Chapter 2, calls for the qualities of prudence there discussed. Prudence dictates that, in initiating reform measures, account be taken of the possibility that the decisions surrounding the move will be scrutinised in due course by the Treasury Select Committee.

Secondly, in Chapter 2, the importance of the sovereign status of the Crown in Parliament was seen as its continuing pre-eminence over the institutions of the EU; the idea that, in tax matters especially, Westminster, not Brussels, was still the focal point of British government.<sup>27</sup> This was expressed in terms of the idea that, as regards the European and

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<sup>24</sup> See Black (1996) 16 OJLS 699-711 (Review Article).

<sup>25</sup> See Thain and Christie, n. 10 above, pp. 7 and 16 (referring to an interview with Lord Turnbull, former Permanent Secretary to the Treasury (1998-2003): see Timmins, *Financial Times*, 20 March 2007, 1); also Chapter 2 above, n. 283; also Giles, *Financial Times*, 16 January 2008, 2.

<sup>26</sup> See Manin, n. 1 above, p. 15.

<sup>27</sup> See Chapter 2 above, nn. 45 and 308.

international theme in the study, the real questions are not ones of sovereignty, but of jurisdiction and competence. A similar point applies in the present chapter. It is that, in taking the legislative initiative in particular areas of reform, HMG has first to consider its competence to act in that way. This issue needs to be taken into account, not just by HMG in initiating reform policies, but by Parliament, especially when amendments are sought to be made to legislative proposals.

The third of the strands running through Chapter 2 was how HMG's sovereignty in corporation tax matters was more than a question of its competence to act. Equally importantly, sovereignty in such matters was a question of capacity. It depended on the quality of the relationship between state and non-state actors involved in corporation tax reform.<sup>28</sup> This point remains equally valid in Chapter 3. The generation of trust and confidence is no more essential to the *ex post* scrutiny of policy than it is to the making of policy in the first place. This is why, whereas in Chapter 2, generating trust and confidence depended on a combination of the prudential qualities of Treasury ministers, and on an effective system of *ex post* accountability, in Chapter 3 it becomes a matter of how HMG consolidates its capacity in tabling and developing reform initiatives. The fourth major strand in the chapter is therefore the extent to which the process of corporation tax reform augments or detracts from trust and confidence in the specific policy area. The need to take action, or indeed not to do so, is dictated by a prudential technique, something that may require greater or lower levels of consultation, less or more pre-emptive action. Getting the 'mixture' wrong involves, not just 'losing the support of business',<sup>29</sup> but, given the purpose of reforming corporation tax, damaging the UK's economic growth in the process.

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<sup>28</sup> See Chapter 2 above, n. 59.

<sup>29</sup> See, e.g., Eaglesham and Guthrie, *Financial Times*, 25 January 2008, 4; Willman and Eaglesham, *Financial Times*, 28 January 2008, 9; Willman, *Financial Times*, 8 February 2008, 3; Parker, *Financial Times*, 12 February 2008, 2; (but see, *per contrà*, Eaglesham, *Financial Times*, 14

## PROCESSES AND INTERACTIONS

This chapter is therefore about the interactions of state and non-state actors, in the reform of corporate income tax, in the UK's developed representative democracy. While acknowledging the difficulties of unravelling the two, we are concerned here with the effectiveness of the reform process, rather than that of the institutions themselves. What characterises the policy area in question is an unusually high level of technical detail. It is thus that the first part of the discussion elaborates on the distinction between 'the technical' and 'the political', which was originally set up in Chapter 1.<sup>30</sup> Given the orientation in the present chapter towards processes, the elaboration of the issues seeks to show how these are adapted to a particular view of politics, policy and reform, conditioned by the idiosyncrasies of the UK's representative institutions. The logic of these institutions is, as ever, effectiveness, and, through this, their ability to inspire some degree of trust and confidence in the measures taken. It is thus that, just as the emphases in the discussion of the institutions, in Chapter 2, differed from a 'Sheffield school' approach, so also does the main emphasis in the present chapter. Chris Hilson's work, which provided an important inspiration for the present study, concentrates on what he calls 'ex ante accountability'.<sup>31</sup> The endorsement of this expression is reflected in its use throughout the present study.<sup>32</sup> What is crucial, however, is that it is used here to rather different effect. 'Accountability',<sup>33</sup> in Hilson's portrayal of a

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February 2008, 2); Eaglesham, *Financial Times*, 27 February 2008, 2; Willman, *Financial Times*, 29 February 2008, 2.

<sup>30</sup> See Chapter 1 above, pp. 37-43.

<sup>31</sup> See Chris Hilson, *Regulating Pollution: A UK and EC Perspective* (Oxford: Hart Publishing, 2000), p. 57.

<sup>32</sup> See Chapter 2 above, nn. 191-192.

<sup>33</sup> See Richard Mulgan, "'Accountability': An Ever-expanding Concept?" (2000) 78 *Public Administration* 555-573.

particular area of social regulation, is the key legitimating characteristic of the system.<sup>34</sup>

What we are saying here is that accountability is *a key* feature of the process of corporation tax reform, but that its legitimating capacity depends on the prudential way in which such *ex ante* accountability, through consultation and deliberation, is used. This depends, in turn, on the ‘structural’ strengths and weaknesses incident to the involvement of the corporate sector in governance through New Public Management (NPM).

As suggested above, and as discussed in detail in Chapter 2, NPM envisages particular roles for the state, on the one hand, and for the corporate sector, on the other.<sup>35</sup> The discussion in Chapter 2 examined the arguments both for, and against, the idea that corporation tax reform is just one further instance of the domination of the UK’s political institutions by MNCs and fund managers based in the City of London. The second part of the discussion in Chapter 3 seeks to examine the consequences of the perhaps surprising conclusion that, at the present juncture at least, there is some identity of interest between the state and these groups. It does so by focussing on the importance of the concept of ‘the public interest’ to HMG’s role in tax matters and on the ideological nature of the public interest concept. As will be explained, the (problematic) ideology is that economic growth can be combined with social justice, that efficiency and fairness can go hand in hand. This is the ‘Third Way’ ideology, or at least New Labour’s vision of it, to which brief reference has already been made.<sup>36</sup> That corporation tax reform has a decisive part to play in this vision has been emphasised by HMG on many occasions, although its implications have not been fully developed in the literature, either in terms of its implications for issues such as

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<sup>34</sup> See Hilson, n. 31 above, pp. 57-68 and ch. 5.

<sup>35</sup> See the overview of NPM change in Christopher Hood, *Explaining Economic Policy Reversals* (Buckingham: Open University Press, 1994), ch. 7, esp. p. 130 (table).

<sup>36</sup> See Chapter 1 above, nn. 187-189.

corporation tax avoidance (as to which see Chapter 4), or of the problems and opportunities thereby presented for the critique of policy.

The emphasis placed on the ideological nature of the public interest, and on its importance in understanding corporation tax reform, has two main implications for the present study. First, it helps us to isolate the relevance of economics, as well as the particular type of economics involved. On one view, economic values are the *only* values running through corporation tax reform (corporation tax being, as was said elsewhere, a form of economic regulation),<sup>37</sup> so some clarification of their nature and scope is clearly extremely important. What is not regarded as important here, however, is an ‘economistic’, or ‘public choice’, view of the motives for, and outcomes of, the actions of the individuals and institutions involved in corporation tax reform.<sup>38</sup> It is not simply that it is the sphere of activity of the economist rather than the public lawyer. It is that, although parties and politicians may indeed ‘make excessive promises to win votes’,<sup>39</sup> one characteristic of the New Labour government after 1997 has been that, given its historically large parliamentary majority, it has not generally had ‘to cut deals so as to secure support’,<sup>40</sup> nor, in all of the examination of the sources involved in the study, is there any obvious sign that an inquiry based on the tendency of ‘bureaucrats’ to maximise ‘their own self-interest’<sup>41</sup> would be justified. This does not rule out criticism of the coherence or consistency of decisions taken on other grounds, nor does it obviate the idea that public choice might have a role in other

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<sup>37</sup> See Chapter 1 above, n. 352.

<sup>38</sup> See Arye L. Hillman, *Public Finance and Public Policy: Responsibilities and Limitations of Government* (Cambridge: Cambridge University Press, 2003), ch. 6; Richard A. Musgrave and Peggy B. Musgrave, *Public Finance in Theory and Practice*, 5<sup>th</sup> edn (New York: McGraw-Hill, 1989), ch. 7; John Tiley, *Revenue Law*, 5<sup>th</sup> edn (Oxford: Hart Publishing, 2005), p. 15.

<sup>39</sup> See Parsons, n. 10 above, p. 307.

<sup>40</sup> *Ibid.*

<sup>41</sup> *Ibid.*

areas of policy.<sup>42</sup> It is simply to say that, as an analytical tool, its suitability is not borne out, or even suggested, by the facts.

The second main implication of placing emphasis on an ideological view of the public interest is the clue that it provides to the nature of the power being wielded in the reform process. It is no part of the present discussion to suggest power relations based on any of those themes that have proved so enduring in Western political writing. Thus, for instance, there is no suggestion that the process of corporation tax reform has proved to be an illustration of ‘the power of organized interests’<sup>43</sup> (as ‘corporatist’ theories would suggest);<sup>44</sup> of technocrats (since the argument is specifically that whatever levels of technical expertise are involved, corporation tax reform raises important political issues);<sup>45</sup> or of elites (as C. Wright Mills suggested in the America of the 1950s,<sup>46</sup> and as Hywel Williams has sought to suggest in relation to the Britain of the early years of the twenty-first century).<sup>47</sup> The reason is that all three, as well as any ‘neo-Marxist’ position we might care to adopt, would portray power as a matter of some form of domination.<sup>48</sup> Throughout the study, we have been very careful to avoid that suggestion. Instead, we seek to portray the policy-making process in the

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<sup>42</sup> *Ibid.*, pp. 306-323; Robert Baldwin and Martin Cave, *Understanding Regulation: Theory, Strategy, and Practice* (Oxford: Oxford University Press, 1999), pp. 21-25; also Christopher D. Foster and Francis J. Plowden, *The State Under Stress: Can the Hollow State be Good Government?* (Buckingham: Open University Press, 1996), pp. 33-34.

<sup>43</sup> See Parsons, n. 10 above, pp. 257-262.

<sup>44</sup> On corporatism, see Wyn Grant, *Economic Policy in Britain* (Basingstoke: Palgrave, 2002), p. 219; Chapter 2 above, n. 325; also Jon Pierre and B. Guy Peters, *Governance, Politics and the State* (Basingstoke: Macmillan, 2000), pp. 34-35, 80-83.

<sup>45</sup> See Parsons, n. 10 above, pp. 265-271; also Claudio M. Radaelli, *Technocracy in the European Union* (London: Longman, 1999), pp. 111-112.

<sup>46</sup> See C. Wright Mills, *The Power Elite* (New York: Oxford University Press, 1959); Steven Lukes, *Power: A Radical View*, 2<sup>nd</sup> edn (Basingstoke: Palgrave Macmillan, 2005), pp. 66 and 76; also Parsons, n. 10 above, pp. 265-271.

<sup>47</sup> See Hywel Williams, *Britain's Power Elites: The Rebirth of a Ruling Class* (London: Constable, 2006), pp. 217-226 (xi-xiv).

<sup>48</sup> See Angus Stewart, *Theories of Power and Domination: The Politics of Empowerment in Late Modernity* (London: Sage, 2001), pp. 46-53.



corporation tax field as being a manifestation of the augmentation of constituent power.<sup>49</sup> True it is that corporation tax reform has a strong technical dimension, but, as the public prominence of the discussions referred to earlier on demonstrate, its political dimension is no less salient. Constituent power is ‘power to’, in Thomas Hobbes’s famous dichotomy, rather than ‘power over’.<sup>50</sup> So our question is therefore, interpretatively speaking, how is it that, despite massive criticism of the length and ‘complexity’ of corporation tax legislation, the tax seems to work, that it continues to raise sufficient receipts,<sup>51</sup> that there is little evidence (if any) that it either discourages inward investment or promotes ‘capital flight’?<sup>52</sup> The answer, insofar as it can be captured within the dimensions of this work, is that it is through prudent decision making, allowing for participation by technically well-informed groups, by those affected, and by lobbyists, but which decision-making cannot in the end be dominated by them. In case this may seem naive, consider the responses to some key objections. We may wish politics to be practised differently, yet what we have is what political history has bequeathed us. Economic growth is now the key element in the ‘neo-liberal’ ideological consensus.<sup>53</sup> The views of George Monbiot,<sup>54</sup> Colin Leys,<sup>55</sup> and others, to be discussed

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<sup>49</sup> See Chapter 2 above, nn.20 and 53; also nn. 14 and 19 above (this Chapter).

<sup>50</sup> See Chapter 2 above, nn. 56, 57 and 146.

<sup>51</sup> Corporation tax receipts were sluggish between 2001 and 2004, when they began to rise rather steadily: see Giles, *Financial Times*, 21 October 2004, 3; Daneshkhu, *Financial Times*, 19 November 2004, 2; Plender, *Financial Times*, 17 March 2005, 19; Giles, *Financial Times*, 19 August 2005, 3; Giles and Daneshkhu, *Financial Times*, 27 March 2006, 1; Giles, *Financial Times*, 21 November 2006, 4. There was a ‘sharp decline’ in receipts in autumn 2007 (see Rozenberg, *Times*, 25 September 2007, 44; Strauss and Briscoe, *Financial Times*, 25 September 2007, 4; Giles, *Financial Times*, 21 November 2007, 4). Receipts rallied again, however, in early 2008 (see Giles, *Financial Times*, 22 February 2008, 1).

<sup>52</sup> See Ipsos MORI, *UK Corporate Taxation and International Competitiveness* (London: Confederation of British Industry, 2006), Appendix, Section 2; Houlder, *Financial Times*, 20 June 2006, 3; Eaglesham, *Financial Times*, 10 October 2006, 4; Houlder, *Financial Times*, 17 November 2006, 3; Willman, *Financial Times*, 23 March 2007, 3; Houlder, *Financial Times*, 14 May 2007, 3.

<sup>53</sup> See John Schwarzmantel, *Ideology and Politics* (London: Sage, 2008), p. 42.

<sup>54</sup> See George Monbiot, *Captive State: The Corporate Takeover of Britain* (London: Macmillan, 2000), *passim*.

below, may (possibly rightly) suggest another way, but their views represent merely the reality of an ideological debate,<sup>56</sup> and are not necessarily an accurate interpretation of what has actually happened. Corporation tax reform, though it is undoubtedly a highly technical undertaking, will be judged by its economic results, and, so far at least, these have been remarkably encouraging.

All of these issues are intended to pave the way, with a little anticipation of the conclusions, for the analysis in the third to sixth parts of the discussion. The argument rather carefully unfolded in Chapter 2 was that the institutional framework within which corporation tax reform takes place is designed to ensure a certain freedom of (prudent) action by HMG, subject to close scrutiny (albeit *ex post*) by Parliament, a scrutiny that, overall, is rather successful, although it shines rather an intermittent beam on the taxation of companies. The object of the arrangements is the holding of the Crown (in Parliament) to account by Parliament. The third to sixth parts of the present discussion apply this historical, institutional, logic to the corporation tax reform process, and they do so by taking up the division of the tax policy-making process that, basing himself on O'Donnell,<sup>57</sup> Christopher Wales, a former member of the Council of Economic Advisers,<sup>58</sup> suggested in a 2004 paper: 'initiation'; 'development'; 'presentation' and 'delivery'.<sup>59</sup> The unique value of Wales's paper hardly needs to be underlined. What does need to be emphasised, however, is that, although not theorised in such terms, what each of the four stages involves is the need for HMG to judge the nature of reform proposals, the timing and extent of consultation, the

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<sup>55</sup> See Colin Leys, *Market-driven Politics: Neoliberal Democracy and the Public Interest* (London: Verso, 2001).

<sup>56</sup> See Liam Murphy and Thomas Nagel, *The Myth of Ownership* (Oxford: Oxford University Press, 2000), p. 173.

<sup>57</sup> See *Financing Britain's Future: Review of the Revenue Departments* (Chair, Gus O'Donnell) (Cm 6163) (London: TSO, 2004).

<sup>58</sup> See David Lipsey, *The Secret Treasury* (London: Viking, 2000), p. 46.

<sup>59</sup> See Wales, n. 7 above, pp. 549-551.

nature and detail of explanatory material, and the issue of practical guidance on new measures. In a word, although Wales does not express it thus, HMG must use different ways of behaving ‘prudently’. In the third to sixth parts of the discussion, what this has entailed in practice is analysed in detail. Suffice it to say at this stage that, although the fourfold division of the process tends to mask the point, the crucial stage is that part of the process, in the ‘development’ phase, which involves the detailed debating of Finance Bill (FB) clauses by the relevant standing committee of the House of Commons. This is the (almost ‘sacred’) point at which, by historical necessity, tax legislation is approved by Parliament, the ‘Gothic prudence’ of the system. True it is that debate may be short; that consultation may have been brief (or even non-existent); that MPs are not (in the main) tax professionals. Within the logic of the system, none of these matters is as relevant as the mere fact that the FB clauses have been argumentatively scrutinised by the democratically elected representatives of the people. The method, in the third to sixth parts of the discussion, is largely to use the examples given in Chapter 1, but not there discussed in detail, to illustrate further the three ‘non-substantive’ themes in corporation tax reform: the consultation, the technical and the Departmental themes. Each of these examples in turn concerns aspects of the four ‘substantive’ themes: accounting, anti-avoidance, compliance and enforcement and European and international developments. Augmenting trust and confidence in corporation tax reform is more complex, and more widespread, than the casual reader of the newspapers or professional journals might imagine.

In the light of the choices involved in this approach, including the rejection of an interpretation based on systems theory,<sup>60</sup> we now need to develop two aspects of the discussion originally introduced in Chapter 1: the question of the political dimension to

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<sup>60</sup> See the Prologue above.

corporation tax reform; and, within the practice of the politics that seeks to manage the implications of this political element, the question of the nature and scope of the public interest in the reform of corporation tax.

#### THE 'POLITICAL' ELEMENT IN CORPORATION TAX REFORM

In Chapter 1, it was maintained that the reform of corporation tax had, over recent years, been transformed from a technical, or technocratic, enterprise, and into a political one.<sup>61</sup> By way of a preliminary justification for this contention, the discussion in that chapter sought to characterise the political nature of the issues thereby raised, mainly in terms of their potential to create conflict. In the corporation tax context, this entailed threats of capital flight, dissuading inward investment, and scaring fund managers away from the jurisdiction.<sup>62</sup> But there were potentially other 'lower level' antagonisms, too. Hence, for instance, traces of conflicts of interest, albeit skilfully averted, were to be found in the textures of the loan relationships code,<sup>63</sup> and, more generally, in the ability of the economic issues involved in corporation tax reform to energise the potential for conflict. In this part of the chapter, we need to broaden and deepen those preliminary points in three, interrelated, ways: first, by contrasting the conflictual view of 'the political' posited so far, with its deliberative counterpart, to produce a synthesis suitable for deployment in the rest of the discussion; secondly, by pointing up the subtle distinction between politics and 'policy', especially the idea of 'reform' itself; and, thirdly, by illustrating the link between politics and political economy, the discipline with which tax policy is customarily most closely associated.

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<sup>61</sup> See Chapter 1 above, pp. 37-43.

<sup>62</sup> See Chapter 1 above, nn. 146-148.

<sup>63</sup> See Chapter 1 above, n. 130.

An analysis of these three sets of relationships is crucial to an understanding of what the public interest in corporation tax reform might be, and to the relationship between (and relative significance of) the stages of the reform process identified above. The thread that binds them together is the nature of power and how it differs from mere domination.

### **Ideas of ‘the political’**

The author has written elsewhere of the different ways in which ‘the concept of the political’ has been envisaged over the centuries, and of how these might illuminate the political dimension to the reform of corporation tax.<sup>64</sup> It is not, therefore, necessary to do more here than to reflect on the main aspects of that analysis, and to indicate the issues that are of the greatest relevance to the present inquiry.

First, it is possible to conceive of political issues in two distinct ways.<sup>65</sup> On the one hand, the Aristotelian mode could be adopted,<sup>66</sup> and a political issue could be imagined as one which is within the ‘public domain’, and which is subjected to discussion within a ‘set of institutions which ... allow space for deliberation, negotiation, [and] the representation of interests’.<sup>67</sup> This mode is new to the present study, but it has a rather obvious appeal, since it seems to offer a correspondence to what we find if we look at the engagements between, say, members of policy communities, when reform proposals have been made. It reflects, broadly speaking, the assumptions running through Claudio Radaelli’s 1997 and 2003 examinations

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<sup>64</sup> See John Snape, ‘Corporation Tax Reform – Politics and Public Law’ [2007] BTR 374-404, 382-389.

<sup>65</sup> See Erik Oddvar Eriksen and Jarle Weigård, *Understanding Habermas: Communicative Action and Deliberative Democracy* (London: Continuum, 2003) pp. 6-9; Andrew Gamble, *Politics and Fate* (Cambridge: Polity, 2000), pp. 3-5.

<sup>66</sup> See Aristotle, *The Politics*, ed. by Stephen Everson (Cambridge University Press: Cambridge, 1988); also Aristotle, *The Nicomachean Ethics*, ed. and trans. by J.A.K. Thomson, Hugh Tredennick and Jonathan Barnes (London: Penguin, 2004).

<sup>67</sup> See Gamble, n. 65 above, p. 3.

of the approach of the European Commission to corporate tax policy in the EU.<sup>68</sup> What makes the Aristotelian vein rather pallid and unconvincing, however, is its tendency not to see political issues as ones involving ‘power, conflict and antagonism’,<sup>69</sup> something that the tradition of Machiavelli would have us do.<sup>70</sup> Given the corporation tax context, however, the deliberative dimension might nonetheless be very insightful. Secondly, writers in the Aristotelian tradition tend to work in a ‘normative’ mode, rather than an interpretative one. The issues of which they speak concern matters as they ought to be rather than as they are.<sup>71</sup> Writers such as Thomas Aquinas,<sup>72</sup> Michael Sandel,<sup>73</sup> John Rawls,<sup>74</sup> and Jürgen Habermas,<sup>75</sup> although they point us towards a better way of living, are unlikely to be able to help us understand the conflictual reality of programmes of legislative reform as convincingly as ones such as Machiavelli,<sup>76</sup> Hobbes,<sup>77</sup> Carl Schmitt,<sup>78</sup> and

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<sup>68</sup> See Claudio M. Radaelli, *The Politics of Corporate Taxation in the European Union: Knowledge and International Policy Agendas* (London: Routledge, 1997); Claudio M. Radaelli, ‘The Political Economy of EU Direct Tax Policy’, in *Contemporary Issues in Taxation Research*, ed. by Andy Lymer and David Salter (Aldershot: Ashgate Publishing, 2003), pp. 145-165.

<sup>69</sup> See Chantal Mouffe, *On the Political* (London: Routledge, 2005), p. 9.

<sup>70</sup> See J.G.A. Pocock, *The Machiavellian Moment: Florentine Political Thought and the Atlantic Republican Tradition* (Princeton: Princeton University Press, 1975), pp. 423, 491.

<sup>71</sup> The elision that Hume observed: see David Hume, *A Treatise of Human Nature*, ed. by L.A. Selby-Bigge, 2<sup>nd</sup> edn by P.H. Nidditch (Oxford: Clarendon Press, 1978), pp. 469-470.

<sup>72</sup> See St Thomas Aquinas, *Summa Theologiae, Volume 28: Law and Political Theory (1a2ae. 90-97)*, ed. and trans. by T. Gilby, O.P. (London: Eyre and Spottiswoode, 1966). The writer would like to thank Dr Michael Sutton for drawing Aquinas to his attention in this context.

<sup>73</sup> See Michael J. Sandel, *Liberalism and the Limits of Justice*, 2<sup>nd</sup> edn (Cambridge: Cambridge University Press, 1998). Sandel seems to have been an important ideological influence on Gordon Brown (see *Gordon Brown: Moving Britain Forward: Selected Speeches 1997-2006*, ed. by Wilf Stevenson (London: Bloomsbury, 2006), pp. 145, 272).

<sup>74</sup> See John Rawls, *A Theory of Justice*, rev. edn (Oxford: Oxford University Press, 1999); John Rawls, *Political Liberalism* (New York: Columbia University Press, 1993).

<sup>75</sup> See Jürgen Habermas, *Between Facts and Norms*, trans. by William Rehg (Cambridge: Polity Press, 1997).

<sup>76</sup> See Niccolò Machiavelli, *The Prince*, trans. by Peter Bondanella (Oxford: Oxford University Press, 2005); also Niccolò Machiavelli, *The Discourses*, ed. and trans. by Bernard Crick, Leslie J. Walker and Brian Richardson (London: Penguin, 2003) (see Chapter 1 above, nn. 179, 182 and 190).

<sup>77</sup> See Thomas Hobbes, *Leviathan, or The Matter, Forme, & Power of a Common-wealth Ecclesiasticall and Civill*, ed. by C.B. Macpherson (London: Penguin, 1985); Thomas Hobbes, *On the Citizen*, ed. and trans. by Richard Tuck and Michael Silverthorne (Cambridge: Cambridge University Press, 1998).

(contemporaneously) Chantal Mouffe.<sup>79</sup> For the purposes of the present study, we really do need to have some such understanding of this reality. This is why, in the author's view, there is a lack of realism to Radaelli's account of corporate tax reform in the European context. Thirdly, the point of deliberating on political issues, in the Aristotelian tradition, is to see which side of the argument helps to promote 'the common interest',<sup>80</sup> the creation of a just society. In the Machiavellian tradition, however, although expressions such as 'the common interest' are used, more frequent are 'the public interest' or 'the public good',<sup>81</sup> expressions whose primary focus is not, as such, the just society, but the building up of a powerful state.<sup>82</sup> Again, for reasons to be discussed in the next part, it is the latter, rather than the former, which on balance seems to capture the mainspring of corporation tax reform. Again, too, Radaelli does not seem in general to take sufficient account of national interests in his account of European corporate tax reform.<sup>83</sup> Fourthly, in its emphasis on the state, the Machiavellian tradition regards political issues as ones that affect the *building up* of the state, rather than ones that presuppose its existence.<sup>84</sup> If corporation tax revenues are taken to be so crucial to the UK's continued prosperity that their loss or diminution would threaten the

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<sup>78</sup> See Carl Schmitt, *The Concept of the Political*, trans. by George Schwab (Chicago: University of Chicago Press, 1996).

<sup>79</sup> See Chantal Mouffe, *The Return of the Political* (London: Verso, 1993); also Mouffe, n. 69 above.

<sup>80</sup> See Aristotle (1988), n. 66 above, p. 68.

<sup>81</sup> Different from the concept of 'public goods' or 'common goods' (see Hume, n. 71 above, p. 539; Adam Smith, *An Inquiry into the Nature and Causes of the Wealth of Nations*, ed. by R.H. Campbell and A.S. Skinner (textual editor W.B. Todd), 2 vols (Oxford: Clarendon Press, 1976), II, pp. 689, 708, 723), both relating back to Hobbes's jobs of government (see Chapter 1 above, n. 169); Murphy and Nagel, n. 56 above, pp. 86ff.; Martin Wolf, *Why Globalization Works* (London: Yale, 2005), pp. 61-64; O'Donnell, n. 57 above, p. 93; Russell Hardin, *David Hume: Moral and Political Theorist* (Oxford: Oxford University Press, 2007), pp. 77-78, 121-123.

<sup>82</sup> See Hannah Arendt, *The Human Condition*, 2<sup>nd</sup> edn (Chicago: University of Chicago Press, 1998), p. 182; Samuel Pufendorf, *On the Duty of Man and Citizen*, ed. by James Tully (Cambridge: Cambridge University Press, 1991), pp. 133, 175; Machiavelli (2003), n. 76 above, pp. 100-138; Quentin Skinner, *Machiavelli* (Oxford: Oxford University Press, 1981), pp. 54-55, 58-67.

<sup>83</sup> But see Radaelli (2003), n. 68 above, p. 148.

<sup>84</sup> See Schmitt, n. 78 above, p. 19; also Gamble, n. 65 above, p. 4.

state's 'stability',<sup>85</sup> then the Machiavellian emphasis, at an interpretative level at least, can be said to be all the more useful than the Aristotelian one. This is a point, in fact, which even Radaelli recognises. Fifthly, as if to underscore the importance of Hobbes's 'state of nature' in the Machiavellian tradition, of the 'ever present possibility of conflict',<sup>86</sup> it places centre stage, not the public-private dichotomy essential to Aristotelian thought,<sup>87</sup> but the opposition of (political) 'friend' and (political) 'foe'.<sup>88</sup> As discussed in Chapter 1, it is only necessary to reflect on the tone of much public debate in the corporation tax field to see that this latter is an essential ingredient in the interpretation of its reform.<sup>89</sup> Finally, it does not matter that the issues raised by the reform of corporation tax involve some clash of economic interests; economic interests, as we have said, are quite capable of energising political issues.<sup>90</sup>

In what follows, the idea of corporation tax reform as involving political issues seeks to draw on elements of both traditions. First, we accept that all of the interactions discussed in the study, between state and corporate sector, and between the corporate sector and the rest of society, imply the constant potential for conflict. If we look at the five 'dilemmas' of corporation tax reform as governance, discussed in Chapter 2, the existence of the strand is plain: the involvement of bodies outside HMG itself, such as the European Commission, the European Court of Justice (the ECJ) and the International Accounting Standards Board (the IASB), suggests the constant possibility of conflict over competences, if not over capacity; the existence of influential opinion-formers in the media and in special interest groups suggests the constant possibility of sections of the corporate sector being ready to enlist in an

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<sup>85</sup> See Chapter 4 below.

<sup>86</sup> See Chapter 1 above, n. 139.

<sup>87</sup> See Arendt, n. 82 above, pp. 29 and 31; also Gamble, n. 65 above, pp. 3-5.

<sup>88</sup> See Hobbes (1985), n. 77 above, p. 185; Schmitt, n. 78 above, p. 90 (note by Leo Strauss).

<sup>89</sup> Understated in Radaelli's brief account of the reform of corporation tax in the 1980s (see Radaelli (1997), n. 68 above, pp. 125-136).

<sup>90</sup> See Chapter 1 above, n. 149.



‘us’ and ‘them’ struggle against HMG,<sup>91</sup> especially in the event of some serious failure of corporation tax policy; and even the fact of involving policy networks creates the constant possibility of conflict over the inclusion of some professional, or producer, networks, to the exclusion of others. Secondly, we acknowledge the public and deliberative nature of much of the debate on corporation tax reform, although (as the discussion in this chapter will make clear), the nature and scope of the deliberative dimension is seriously restricted by British ideas of what the ‘art and science of government’ involves. Thirdly, and perhaps most importantly, the constant possibility of conflict encompasses, not just groups within the UK, but also the UK, on the one hand, and other EU Member States and the EU institutions, on the other.

What we end up with, therefore, is an idea of the political that owes something to the Aristotelian tradition, for sure, but which is defined primarily by the uncomfortable realities of the Machiavellian world view.

### **Politics, policy and reform**

It will be apparent from what has just been said why, in choosing an idea of what Loughlin calls ‘the second order of constitutional law’, i.e. the business of politics, this study has opted for the (Machiavellian) tradition of politics as the ‘art of government’.<sup>92</sup> It is not simply a matter of taking a pessimistic view of human relations. This view of politics also commends itself because of the representative nature of British government. Governing, in Britain, as has been highlighted in Chapter 2, has been seen as a matter of ‘prudence’ at least since

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<sup>91</sup> A reflection of the (political) ‘friend’ and (political) ‘enemy’ distinction in Schmitt, which Leo Strauss regards as characteristic (see Schmitt, n. 78 above, p. 90).

<sup>92</sup> See Chapter 1 above, pp. 31-37.

1688.<sup>93</sup> Although, as we shall see in the next part, prudence has a place in the Aristotelian tradition of politics,<sup>94</sup> it is most closely associated with the tradition of Machiavelli<sup>95</sup> and Hobbes.<sup>96</sup> The rest of the chapter will show how thoroughly this pervasive notion is worked through in the UK policy-making process. For the moment, it is necessary only to carve out from the notion of prudence the kind of fiscal prudence most closely associated with the Rt Hon. Gordon Brown, MP, as Chancellor of the Exchequer. What this study seeks to do is to highlight the relationship between fiscal prudence - discussed in the next part of the Chapter – and the prudence that is the most essential ‘tool’ in British government. Each consolidates the other; a big mistake (possibly Alistair Darling’s mistake) is to confound one with the other.

Some European languages make little, if any, distinction between ‘politics’ and ‘policy’.<sup>97</sup> Even the English of Marlowe<sup>98</sup> and of Milton<sup>99</sup> seemed not to emphasise such a divergence. Modern commentators in English do make a distinction, however.<sup>100</sup> In Hecló’s words, ‘[a]s commonly used’, policy is ‘usually considered to apply to something “bigger” than particular decisions, but “smaller” than general social movements’;<sup>101</sup> it is purposeful

<sup>93</sup> See George Savile, ‘The Character of a Trimmer’, in *The Works of George Savile Marquis of Halifax*, vol. 1, ed. by Mark N. Brown (Oxford: Clarendon Press, 1989), pp. 178-249, 187; (see Loughlin, n. 17 above, p. 151, on the crucial importance of Savile to English attitudes to government); also Chapter 2 above, n. 199.

<sup>94</sup> See Aristotle (2004), n. 66 above, pp. 150-157, 159-166.

<sup>95</sup> See Chapter 2 above, nn. 268-281.

<sup>96</sup> See Hobbes (1985), n. 77 above, p. 169; also Art Vanden Houten, ‘Prudence in Hobbes’s Political Philosophy’ (2002) 23 *History of Political Thought* 266, esp. 267-279.

<sup>97</sup> e.g. French, German or Italian (see Parsons, n. 10 above, pp. 13-14).

<sup>98</sup> See, e.g., Christopher Marlowe, ‘The Jew of Malta’, Act I, Scene 1, line 138; Act I, Scene 2, lines 160-162, in *Doctor Faustus and Other Plays*, ed. by David Bevington and Eric Rasmussen (Oxford: Oxford University Press, 1998), pp. 256, 262, 454.

<sup>99</sup> See, e.g., John Milton, ‘The Ready and Easy Way to Establish a Free Commonwealth’, in *John Milton: The Major Works*, ed. by Stephen Orgel and Jonathan Goldberg (Oxford: Oxford University Press, 1991), pp. 330-353, 341.

<sup>100</sup> See, e.g., Blitz, *Financial Times*, 12 July 2007, 2.

<sup>101</sup> See H. Hugh Hecló, ‘Review Article: Policy Analysis’ (1972) 2 *British Journal of Political Science* 83-108, 84.

(‘policy’ being the antonym of ‘aimlessness’);<sup>102</sup> and it is, as Harold Lasswell said, ‘commonly used to designate the most important choices made ... in organized ... life ... [, being] free of many of the undesirable connotations clustered about the word *political*, which is often believed to imply “partisanship” or “corruption”’.<sup>103</sup> Parsons puts it well when he says that, ‘[t]o have a policy is to have rational reasons or arguments which contain both a claim to an understanding of a problem and a solution’.<sup>104</sup> Policy, then, is the ‘big picture’, the ‘vision’, that vision whose realisation requires the practices, the craft, of politics.<sup>105</sup> Arthur Smithies, writing in 1950, on the death of Joseph Schumpeter, attributed a saying to him that explicitly recognises this relationship:

‘Only in a very special sense can we speak of a nation’s policy or policies. In general declared policies are nothing but verbalizations of group interests and attitudes that assert themselves in the struggle of parties for points in the political game, though every group exalts the policies that suit it into eternal principles of a “common good” that is to be safeguarded by an imaginary kind of state. Nobody has attained political maturity who does not understand that policy is politics. Economists are particularly apt to overlook these truths.’<sup>106</sup>

Policy making, therefore, is quintessentially a prudential activity – quick, clever reactions, ones that weigh ends and means, are necessary to keep the ‘vision’ alive.<sup>107</sup>

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<sup>102</sup> See Parsons, n. 10 above, p. 13.

<sup>103</sup> See Harold D. Lasswell, ‘The Policy Orientation’, in *The Policy Sciences: Recent Developments in Scope and Method*, ed. by Daniel Lerner and Harold D. Lasswell (Stanford: Stanford University Press, 1951), pp. 3-15, 5. ‘Political’ is used here, of course, in its popular sense, which is excluded from the discussion above (for the reasoning, see Snape, n. 64 above, pp. 388-389).

<sup>104</sup> See Parsons, n. 10 above, p. 15; in the tax context, see, e.g., John R. King, ‘Debt and Equity Financing’, in *Tax Policy Handbook*, ed. by Parthasarathi Shome (Washington, D.C.: IMF, 1995), pp. 158-161.

<sup>105</sup> See Chapter 1 above, n. 156.

<sup>106</sup> See Arthur Smithies, ‘Memorial: Joseph Alois Schumpeter 1883-1950’ (1950) 40: 4 *American Economic Review* 628-648, 644.

<sup>107</sup> See Parsons, n. 10 above, p. 42; Loughlin, n. 17 above, p. 151 (referring to Savile, n. 93 above).

Reform, in turn, is a species of policy making.<sup>108</sup> The vastness of the tax reform literature<sup>109</sup> no doubt owes something to the fact that all public policy issues involving taxation are, in an important sense, concerned with tax reform, rather than ‘tax design’.<sup>110</sup> Some of its broad outlines, so far as it relates to the taxation of corporate income, will be discussed in Chapter 4. Here it is simply necessary to note four distinct, although interrelated, points. First, at least so far as its application to corporation tax over the past 15 years or so is concerned, the fact that reform is incremental, often reactive, in nature. Responding to successive ECJ decisions has been an important part of this process.<sup>111</sup> So incremental has reform been, in fact, that, although many would date the ‘vision’ to a consultation document of July 2001,<sup>112</sup> intellectually, the case seems far stronger for reaching back to the earliest systematic corporation tax consultation, that of 1989, on foreign exchange (FOREX) gains and losses.<sup>113</sup> Secondly, reform is, by its very nature, never finished, a point that has been underlined by Joel Slemrod,<sup>114</sup> unconsciously perhaps reflecting some thoughts of Michael Oakeshott on ‘reform’ in general.<sup>115</sup> Thirdly, whilst all reform is difficult to manage, tax reform is perhaps especially so: ‘[o]ne should bear in mind [as Machiavelli himself wrote] that there is nothing more difficult to execute, nor more

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<sup>108</sup> See Shome, n. 104 above, *passim*.

<sup>109</sup> See Simon James and Christopher Nobes, *The Economics of Taxation: Principles, Policy and Practice*, 7<sup>th</sup> edn (Harlow: Financial Times Prentice Hall, 2000), pp. 285-287; Radaelli (1997), n. 68 above, p. 55; also *Tax Law Design and Drafting*, ed. by Victor Thuronyi (Washington, DC: IMF, 1996).

<sup>110</sup> See Murphy and Nagel, n. 56 above, p. 128; also Martin Feldstein, ‘On the Theory of Tax Reform’ (1976) 6 *Journal of Public Economics* 77-104, 90-98.

<sup>111</sup> See Snape, n. 64 above, pp. 397-403; also Frans Vanistendael, ‘The role of the European Court of Justice as the supreme judge in tax cases’ [1996] *EC Tax Review* 114-122, esp. 122.

<sup>112</sup> See H.M. Treasury and Inland Revenue, *Large Business Taxation: The Government’s strategy and corporate tax reforms: A consultation document* (London: H.M. Treasury, 2001). See Chapter 4 below.

<sup>113</sup> See Inland Revenue, *Tax Treatment of Foreign Exchange Gains and Losses: A Consultative Document* (London: Inland Revenue, 1989) (see Chapter 1 above, n. 49).

<sup>114</sup> See Joel Slemrod, ‘The economic impact of the tax reform act of 1986’, in *Do Taxes Matter? The Impact of the Tax Reform Act of 1986*, ed. by Joel Slemrod (Cambridge, Mass.: MIT Press, 1990), p. 1, quoted in Radaelli (1997), n. 68 above, p. 55.

dubious of success, nor more dangerous to administer, than to introduce new political orders'.<sup>116</sup> Finally, it is at least arguable that describing this incremental process as one of 'reform' may not only be misleading, but, if it is, it may damage the political acceptability of the measures taken. Most people, unconsciously perhaps, harbour a 'Burkean' idea of 'reform' as a process that retains something of the subject matter's 'true' substance.<sup>117</sup> What has been at work here, as we shall see presently, is, instead, a radical reworking of the nature and purposes of the tax.

### **Politics and political economy**

Finally, the relationship between politics and economics, as Hannah Arendt pointed out,<sup>118</sup> has an oxymoronic quality: the political, on an Aristotelian view, relates to the public space ('the realm of the *polis*'),<sup>119</sup> whereas the economic relates to the private sphere ('the "household" (*oikia*)').<sup>120</sup> As late as the time of James Mill, economists were comparing the economy of a state with that of a household.<sup>121</sup> However, although Adam Smith asserted that what was 'prudent' for a household must, of necessity, be good for a country,<sup>122</sup> and although economists like to use the imagery even today,<sup>123</sup> its use beyond mere metaphor,

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<sup>115</sup> See Michael Oakeshott, *On Human Conduct* (Oxford: Clarendon Press, 1975), pp. 55-57.

<sup>116</sup> See Machiavelli, n. 76 above, p. 22.

<sup>117</sup> See Edmund Burke, 'A Letter to a Noble Lord', in *The Portable Edmund Burke*, ed. by Isaac Kramnick (New York: Penguin Books, 1999), pp. 213-229, 218-219; Francis P. Canavan, S.J., *The Political Reason of Edmund Burke* (Durham, N.C.: Duke University Press, 1960), p. 177.

<sup>118</sup> See Arendt, n. 82 above, p. 29.

<sup>119</sup> *Ibid.*, p. 30.

<sup>120</sup> *Ibid.*, p. 33.

<sup>121</sup> *Ibid.*, p. 33n, referring to Gunnar Myrdal, *The Political Element in the Development of Economic Theory*, trans. by Paul Streeten (London: Routledge and Kegan Paul, 1953), pp. 140-143.

<sup>122</sup> See Smith, n. 81 above, I, p. 457.

<sup>123</sup> See Wolf, n. 81 above, p. 77.

said Rousseau, was a mistake.<sup>124</sup> In fact, like David Hume, Smith regarded political economy as part of politics.<sup>125</sup> Indeed, it is Smith's crucial definition of political economy that marks out the designing of taxes as a practice of political economy and thus of politics. Political economy, says Smith, is that 'branch of the science of a statesman or legislator' which relates to providing, not simply 'a plentiful revenue or subsistence for the people', by ensuring that they can 'provide such a revenue or subsistence for themselves', but also supplying 'the state or commonwealth with a revenue sufficient for the publick services'.<sup>126</sup>

Political economy therefore includes the art and science of designing taxes, and its use as such is supported by Schmitt's analysis of the relationship between political and other phenomena such as economics.<sup>127</sup> They do not, contrary to Luhmann and earlier systems theorists, run alongside each other, in their own self-constructing 'environments'.<sup>128</sup> Rather, the political creates the conditions in which the economic can function,<sup>129</sup> and (as mentioned above), the economy can provide the energising force behind the political.<sup>130</sup> The best way of achieving the ends that Smith regarded as desirable is, of course, a matter of ideology, the ideology of the 'public interest'.

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<sup>124</sup> See Jean-Jacques Rousseau, *Discourse on Political Economy and The Social Contract*, trans. and ed. by Christopher Betts (Oxford: Oxford University Press, 1994), pp. 3-6 (see Chapter 1 above, n. 372).

<sup>125</sup> See Hume, n. 71 above, p. xv; Adam Smith, *The Theory of Moral Sentiments*, ed. by D.D. Raphael and A.L. MacFie (Oxford: Clarendon Press, 1976), pp. 186-187 (see Donald Winch, *Adam Smith's Politics: An Essay in Historiographic Revision* (Cambridge: Cambridge University Press, 1978), pp. 12-13 (also Myrdal, n. 121 above, p. 143; Arendt, n. 82 above, p. 33n).

<sup>126</sup> See Smith, n. 81 above, I, p. 428. But note changes in usage: see Charles S. Maier, 'Introduction: Political economy and history', in *In search of stability: Explorations in historical political economy*, ed. by Charles S. Maier (Cambridge: Cambridge University Press, 1987), pp. 1-16, esp. 2-6.

<sup>127</sup> See Schmitt, n. 78 above, p. 37.

<sup>128</sup> See Luhmann, n. 23 above, p. 357.

<sup>129</sup> See Schmitt, n. 78 above, p. 88 (note by Leo Strauss); also Hobbes (1985), n. 77 above, p. 186.

<sup>130</sup> See Schmitt, n. 78 above, p. 38 (see Chapter 1 above, n. 149).

## THE PUBLIC INTEREST IN CORPORATION TAX REFORM

What the public interest in corporation tax reform might be, as distinct from ‘what business wants’, has rarely, if ever, entered into the corporation tax reform debates of recent years.<sup>131</sup> Yet some idea of its nature and implications, which goes beyond the political decision as to how much of the total ‘tax take’ is required in the first instance from the corporate sector, is crucial: first, because, given the concept of politics embraced above, it is essential to the conception of corporation tax as public law, to which we shall return in Chapter 4. Secondly, because the very idea of the public interest, one whose fortunes have been distinctly varied,<sup>132</sup> is ideological, not least because of what it says about the relative roles of state and corporate sector. And, thirdly, because, in the last decade or so, corporation tax, in common with many other areas of law, has been put to work in the service of a particular view of the public interest, some elements of which had already been grasped in the work of the Thatcher and Major administrations, but which have been developed and articulated most fully in the writings of ‘Britain’s most prolific author’,<sup>133</sup> erstwhile Chancellor and current Prime Minister, Gordon Brown.

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<sup>131</sup> But see, e.g., Case C-324/00, *Lankhorst-Hohorst GmbH v. Finanzamt Steinfurt* [2003] STC 607, 627a-b; also COM (2007) 785 final, *The application of anti-abuse measures in the area of direct taxation – within the EU and in relation to third countries*, 10 December 2007, pp. 2, 3.

<sup>132</sup> For some observations on its historical significance in the tax context, see Carolyn Webber and Aaron Wildavsky, *A History of Taxation and Expenditure in the Western World* (New York: Simon and Schuster, 1986), pp. 142-147, 296-297, 356-357.

<sup>133</sup> See Anon, *Private Eye*, No. 1197, 9 November-22 November 2007, 5.

### **‘The public interest’ and ‘the common good’**

‘Let the welfare of the people be the first of laws’, that most famous of Cicero’s injunctions, was introduced in Chapter 1: ‘*salus populi suprema lex esto*’.<sup>134</sup> In that discussion, we noted the ambiguity of the expression, ‘*salus populi*’,<sup>135</sup> while linking it with Hobbes’ idea that one of the fundamental duties of the state was to provide the conditions under which subjects could make money honestly,<sup>136</sup> and also with what Michael Oakeshott calls the ‘unresolved tension’ between the idea that states exist for ‘the promotion of some specified enduring interest’,<sup>137</sup> or simply to ensure the ‘loyalty’ of subjects to each other.<sup>138</sup> If, as is contended throughout this study, the purpose (albeit an understated one) of corporation tax is to assist in the promotion of the ‘public interest’,<sup>139</sup> it is important to reflect briefly on what the idea of the public interest may imply that other, apparently similar, concepts, such as ‘the common interest’, and, especially, ‘the common good’, may not.

The first point we can make is that, although the usage is so far from consistent that the point may be a misleading generalisation, the public interest is perhaps more closely identified with the Machiavellian tradition in political thought than with the Aristotelian one. The latter tends to talk about ‘the common interest’, or, possibly, the ‘common good’,<sup>140</sup> rather than about the public interest, the ‘public good’, the ‘general interest’, or the ‘national

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<sup>134</sup> See Chapter 1 above, n. 164; on ‘welfare’, see Brian Barry, *Political Argument: A Reissue with a New Introduction* (Berkeley: University of California Press, 1990), pp. 187-189, 224-225.

<sup>135</sup> *Ibid.*, n. 166.

<sup>136</sup> *Ibid.*, n. 169.

<sup>137</sup> *Ibid.*, n. 400.

<sup>138</sup> *Ibid.*

<sup>139</sup> See Application No. 21319/93, *National and Provincial Building Society and Others v. United Kingdom* [1997] STC 1466 (ECtHR); see Arendt, n. 82 above, p. 182, on the literal significance of ‘inter-est’ (also Stewart, n. 48 above, pp. 36-38).

<sup>140</sup> See Milton, n. 99 above, p. 345; Rousseau, n. 124 above, p. 63 (in ‘The Social Contract’); John Stuart Mill, ‘Considerations on Representative Government’, in *On Liberty and Other Essays*, ed. by John Gray (Oxford: Oxford University Press, 1991), p. 255.



interest’.<sup>141</sup> Thus, Hannah Arendt draws attention to the fact that Aquinas, writing in the Aristotelian tradition, recognised, not a political realm as such, but the common spiritual and material interests of individuals, interests whose furtherance was possible only if one of those individuals took it upon himself to ‘look out’ for them all.<sup>142</sup> Within the same tradition, John Finnis describes the common good as:

‘... a set of conditions which enables the members of a community to attain for themselves reasonable objectives, or to realize reasonably for themselves the value(s), for the sake of which they have reason to collaborate with each other (positively and/or negatively) in a community.’<sup>143</sup>

In doing so, Finnis underestimates the virulence of controversy when he goes on to say that ‘[t]he common good is a frequent or at least a justified meaning of the phrases “the general welfare”<sup>144</sup> or “the public interest”.’<sup>145</sup> Again, Rawls says that the common good consists of ‘conditions and ... objectives that are ... to everyone’s advantage’,<sup>146</sup> and ‘[t]he common good I think of as certain general conditions that are in an appropriate sense equally to everyone’s advantage’.<sup>147</sup>

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<sup>141</sup> ‘General interest’ is used in Application No. 13013/87, *Wasa Liv Ömsesidigt, Försäkringsbolaget Valands Pensionsstiftelse and a group of approximately 15,000 individuals v. Sweden* (1988) 58 ECHRDR 163, 187; Application No. 15375/89, *Gasus-Dosier-und Fördertechnik GmbH v. Netherlands* (1995) 20 EHRR 403 (ECtHR), para. 61; see Barry, n. 134 above, p. 203; Adam Smith referred to ‘the general interest’ (see Smith, n. 81 above, I, pp. 144, 265, 266, 529; II, p. 613), Burke ‘the general *good* [emphasis added]’ (see Edmund Burke, ‘Speech at Mr. Burke’s Arrival in Bristol’, in Kramnick, n. 117 above, pp. 155-157, 156). See Gertrude Himmelfarb, *The Roads to Modernity: The British, French and American Enlightenments* (London: Vintage, 2008), pp. 56-59.

<sup>142</sup> See Arendt, n. 82 above, p. 35.

<sup>143</sup> See John Finnis, *Natural Law and Natural Rights* (Oxford: Clarendon Press, 1980), p. 155.

<sup>144</sup> See Murphy and Nagel, n. 56 above, *passim*, who use this expression.

<sup>145</sup> See Finnis, n. 143 above, p. 156.

<sup>146</sup> See Rawls (1999), n. 74 above, p. 205; see Samuel Freeman, *Rawls* (London: Routledge, 2007), pp. 216-219.

<sup>147</sup> See Rawls (1999), n. 74 above, p. 217.

Machiavelli, by contrast, although he was not entirely consistent, spoke of the public good and the public interest.<sup>148</sup> More explicitly still, Hobbes (as Rawls himself told his students) rejected the idea that ‘people ... [had] any agreed notion about what is good ... [advocating] some agency, some impartial arbitrator or impartial judge, to decide what is in the common good’<sup>149</sup> and, in doing so, talked about the ‘good of the people’.<sup>150</sup> Likewise, Samuel Pufendorf held that laws were to ensure that the conduct of citizens served ‘to preserve and promote the public good’,<sup>151</sup> while, in the famous judicial decision that forms the basis of the modern ‘purposive’ tradition in statutory interpretation,<sup>152</sup> Sir Edward Coke significantly reports the Exchequer barons as speaking of the legislative purpose being ‘*pro bono publico*’, rather than ‘*pro summa bonum*’.<sup>153</sup>

The second point is that the idea of the public interest is more realistic than that of the common good, more interpretatively useful, since it is more consonant with the idea of representative government than is the idea of the common good, which has a strongly deliberative dimension. This is not to say that a political discussion cannot take place in a deliberative mode, just that, in reality, many political decisions are taken by the few on behalf of the many, without wider deliberation. This is reflected in the point that

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<sup>148</sup> See Skinner, n. 82 above, p. 85.

<sup>149</sup> See John Rawls, *Lectures on the History of Political Philosophy*, ed. by Samuel Freeman (Cambridge, Mass: Belknap Press, 2007), p. 84.

<sup>150</sup> See Loughlin, n. 17 above, p. 141.

<sup>151</sup> See Pufendorf, n. 82 above, p. 133.

<sup>152</sup> See Tiley, n. 38 above, pp. 52-57; also Hansard HC Public Bill Committee, 17 May 2007, col. 217 (Ed Balls, MP, Economic Secretary to the Treasury)

<sup>153</sup> See *Heydon’s Case* (1584) 76 ER 637: ‘... the office of all the Judges is always to make such construction as shall suppress the mischief, and advance the remedy, and to suppress subtle inventions and evasions for continuance of the mischief, and *pro privato commodo*, and to add force and life to the cure and remedy, according to the true intent of the makers of the Act, *pro bono publico* ((1584) 76 ER 637, 638); see Barry, n. 134 above, p. 202; also Locke, n. 1 above, p. 377 (see Dunn, n. 1 above, p. 51); Note also idea of ‘public interest law’ (see Rajeev Dhavan, ‘Whose Law? Whose Interest?’, in *Public Interest Law*, ed. by Jeremy Cooper and Rajeev Dhavan (Oxford: Basil Blackwell, 1986), pp. 17-48).

Machiavelli's prudence is the prudence of the 'virtuous' sovereign.<sup>154</sup> In the Aristotelian tradition, whilst 'prudence', as a 'cardinal virtue', is an important quality in shaping the common good, it is not the province of government alone, but of every individual.<sup>155</sup>

Thirdly, the common good, of course, refers to the common good of mankind. It is not, in other words, related specifically to the nation state.<sup>156</sup> The public interest, by contrast, is an interest in the building up of a powerful state, able to defend itself, both economically and militarily, against other states.

Fourthly, the public interest, unlike the common good, has a recognised place in the 'welfare economics' literature, which, in a contemporary and revived form, has animated HMG's economic policy since 1997.<sup>157</sup> This point is made clear in a contribution from Richard Musgrave from 1962. Welfare economics, he says, is what economists 'have to say about "the public interest"'.<sup>158</sup> Welfare economics is, in other words, about 'correcting for' economic inefficiencies, which can of course include 'spillover costs' (e.g. in the form of pollution),<sup>159</sup> but they can also include 'spillover benefits' (e.g. in the form of technical innovations), an idea crucial to New Labour's ideology of the public interest as the

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<sup>154</sup> See Chapter 2 above, n. 252.

<sup>155</sup> See *Catechism of the Catholic Church*, rev. edn (London: Geoffrey Chapman, 1999), p. 400.

<sup>156</sup> *Ibid.*, pp. 416-419; Bill Jordan invokes a similarly 'frontier-less' conception of 'the common good', although not from a specifically Christian standpoint (see Bill Jordan, *The Common Good: Citizenship, Morality and Self-Interest* (Oxford: Basil Blackwell, 1989), pp. 174-184).

<sup>157</sup> See, most importantly, H.M. Treasury, *Reforming Britain's Economic and Financial Policy: Towards Greater Economic Stability*, ed. by Ed Balls and Gus O'Donnell (Basingstoke: Palgrave, 2002); H.M. Treasury, *Microeconomic Reform in Britain: Delivering Opportunities for All*, ed. by Ed Balls, Joe Grice and Gus O'Donnell (Basingstoke: Palgrave Macmillan, 2004).

<sup>158</sup> See R.A. Musgrave, 'The Public Interest: Efficiency in the Creation and Maintenance of Material Welfare', in *Nomos V: The Public Interest*, ed. by Carl J. Friedrich (New York: Atherton Press, 1962), pp. 107-114; also Murphy and Nagel, n. 56 above, p. 136 (theory of 'optimal taxation' as owing much to welfare economics).

<sup>159</sup> Which provides the economic justification for instruments such as pollution taxes: see H.M. Treasury and Inland Revenue, n. 112 above, para. 1.17; also Balls, Grice and O'Donnell, n. 157 above, p. 10.

furtherance of economic growth<sup>160</sup> in combination with ‘societal fairness’. It is a perception of the public good that goes beyond ‘Smith’s attempt to reconcile public good with individual interest – a problem that for Smith was moral and economic at the same time’.<sup>161</sup>

### **The ideological nature of the public interest**

It is one of the central arguments of this study, already heavily underscored, that what has sustained corporation tax reform, especially in the decade since 1997, has been its supporting role in the advancement of a particular conception of the public interest. Decisions as to the levels of taxation to be collected, in the first instance, from the corporate sector,<sup>162</sup> are only part of that process. Of more importance, analytically speaking, is what conception HMG has of the economic and social role of corporation tax. What is unusual, perhaps, is that this conception has been set out particularly fully, both by Gordon Brown himself, and by his main advisers, and that, to some extent at least, it has even taken a public law form.

Gordon Brown has consistently referred to the public interest, rather than to the common good,<sup>163</sup> on various occasions dating back even before 1997. It will be recalled from Chapter 1 that his view of the public interest – his ideology – has attempted to blend ‘enterprise’ with ‘fairness’.<sup>164</sup> With what success this has been achieved, only time will tell, but it is clearly within this framework that the incremental process<sup>165</sup> of corporation tax reform must be understood. Thus, in a speech of March 2003, he emphasised the close interrelationship of

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<sup>160</sup> See Diane Coyle, *The Soulful Science: What Economists Really Do and Why it Matters* (Princeton: Princeton University Press, 2007), p. 51; Murphy and Nagel, n. 56 above, pp. 50-53; Joel Slemrod and John Bakija, *Taxing Ourselves: A Citizen’s Guide to the Debate over Taxes*, 3<sup>rd</sup> edn (Cambridge, Mass.: MIT Press, 2004), pp. 114-120.

<sup>161</sup> See Don Slater and Fran Tonkiss, *Market Society: Markets and Modern Social Theory* (Cambridge: Polity Press, 2001), p. 41; also Himmelfarb, n. 141 above, ch. 2.

<sup>162</sup> See Chapter 1 above, pp. 67-68.

<sup>163</sup> See Brown, n. 73 above, pp. 136-180.

<sup>164</sup> See Chapter 1 above, n. 188; also Balls, Grice and O’Donnell, n. 157 above, p. 6.

efficiency and ‘social justice’, and characterised the role of business tax reform as being to support business.<sup>166</sup> What he was clearly interested in, as a matter of ideology,<sup>167</sup> was cementing a certain identity of interest between the state and the corporate sector, such as that identified in Chapter 2 above. He said:

‘Britain has a unique opportunity to be, once again, a beacon to the world, advancing enterprise and fairness together – a dynamic, vibrant economy that is the first economy in the new era of globalisation to match flexibility with fairness and, in doing so, to attain the high levels of growth and employment that are the best route to prosperity for all.’<sup>168</sup>

Since this passage is concerned with building a ‘modern economy’, it sets out some of the key intersections in the ideological debate over the public interest in corporation tax reform. First, it reflects a clear desire to put British interests first,<sup>169</sup> thus reinforcing a public interest, rather than a common good, approach to corporation tax policy: ‘[t]he way forward [said the Chancellor earlier in the speech] is mutual recognition of national practices[,] not harmonised regulations; and tax competition not tax harmonisation’.<sup>170</sup> This is an approach which, as we shall see, has permeated the European and international theme in corporation tax reform. Secondly, in its reference to ‘high levels of growth’,<sup>171</sup> the passage underlines the

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<sup>165</sup> See Hansard HC Standing Committee A, 11 May 2004, col. 114 (Rt Hon. Dawn Primarolo, MP, Paymaster General).

<sup>166</sup> See Brown, n. 73 above, p. 119.

<sup>167</sup> See Thain and Christie, n. 10 above, p. 11.

<sup>168</sup> See Brown, n. 73 above, p. 135; also Murphy and Nagel, n. 56 above, pp. 181-188, whose ideology is remarkably similar.

<sup>169</sup> But see Murphy and Nagel, n. 56 above, p. 198, n. 7.

<sup>170</sup> See Brown, n. 73 above, p. 118; also Hansard HC Standing Committee A, 11 May 2004, col. 112 (Rt Hon. Dawn Primarolo, MP, Paymaster General); also Kitty Ussher, *The spectre of tax harmonisation* (London: Centre for European Reform, 2000), pp. 47-48 (see Chapter 2 above, n. 260).

<sup>171</sup> See the 1944 White Paper on the independence of the Bank of England (referred to in Brown, n. 73 above, p. 91).

ideological espousal of the ‘post-neoclassical endogenous growth theory’<sup>172</sup> that had gained ground since the 1980s. The impact of this theory on the values immanent to the changing corporation tax code will be discussed in Chapter 4. For the moment, it is sufficient to note that, in macroeconomic terms,<sup>173</sup> it has involved putting the conquest of inflation before full employment, while in microeconomic terms,<sup>174</sup> it has entailed attempting to use the corporation tax system to encourage for instance investment in research and development.<sup>175</sup>

Ideological conflict, in terms of differing perceptions of the public interest, is the third notable feature of the passage above. Hence the emphasis on fairness, and the pairing of ‘high levels ... [of] employment’ with economic growth. All debates about corporation tax reform, especially as they relate to corporation tax avoidance, are about differing conceptions of the requirements of fairness, and its prioritisation relative to some version of ‘efficiency’. Thus, Philip Gillett is precisely right to regard anti-avoidance measures as involving a political calculation,<sup>176</sup> since they are fundamentally about HMG’s ability to strike the right balance between fairness and efficiency. But there is no jurisprudential reality beyond that, no legalistic way of testing whether, and when, an anti-avoidance measure is a step too far. So far as those affected are concerned, views on such measures are a matter of personal ideologies about the role of the state in creating fairness,<sup>177</sup> while, as regards HMG, their

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<sup>172</sup> See Coyle, n. 160 above, pp. 48-52; also David Coates, *Models of Capitalism: Growth and Stagnation in the Modern Era* (Cambridge: Polity Press, 2000), pp. 48-49, 265-273.

<sup>173</sup> As redefined: see Balls and O’Donnell, n. 157 above, ch. 1; Balls, Grice and O’Donnell, n. 157 above, ch. 1 (also see Nigel Lawson (Lord Lawson of Blaby), ‘Changing the Consensus’, in *The Chancellors’ Tales*, ed. by Howard Davies (Cambridge: Polity, 2006), pp. 113-146, 115-116 (see also pp. viii-ix)).

<sup>174</sup> See Thain and Christie, *Parliamentary Brief*, February 2008, 21-22, 21 (available from [www.treasuryproject.org](http://www.treasuryproject.org) (accessed 21 February 2008)).

<sup>175</sup> See Coyle, n. 160 above, pp. 48-52.

<sup>176</sup> See Houlder, *Financial Times*, 13 September 2006, 3.

<sup>177</sup> See Gerhart Niemeyer, ‘Public Interest and Private Utility’, in Friedrich (ed.), n. 158 above, pp. 1-13.

introduction is a matter of political judgment. These are issues to which we shall return in Chapter 4.

In case this sounds something of a truism, it is worth noting a lawyer's response to a public law manifestation of these principles. An important tool in getting the balance right between efficiency and fairness is the famous 'prudence ... for a purpose',<sup>178</sup> already alluded to in Chapter 1. As explained subsequently, this is comprehended by, though not coincident with, Machiavellian prudence.<sup>179</sup> In this context, the obligation in FA 1998, s. 155, for H.M. Treasury 'to prepare and lay before Parliament' a 'code for fiscal stability', is, rightly interpreted, of the first importance. We shall have occasion to return to it in Chapter 4. For present purposes, however, we need to focus on one aspect of an analysis of section 155 by Edward Troup.<sup>180</sup> What he questions is the very premise that Gillett correctly acknowledges, the way in which the ideas discussed above were reflected in the 1997 Budget Report.<sup>181</sup> It was there claimed that the 'tax system should ... be well designed, *to meet the objectives of the government of the day*, without generating undesirable side effects'.<sup>182</sup> Troup's evident dismay at the 'strong implication ... that taxation has a part to play in social and economic engineering'<sup>183</sup> completely misses the ideological nature of the public interest, as well as the conception of public law embraced throughout this study, the latter, it is submitted, being a broadly accurate reflection of the reality. Troup also does not seem to appreciate the importance of the code to 'constrained discretion', the idea that economic policy discretion must be available to HMG, but subject to institutional safeguards.<sup>184</sup>

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<sup>178</sup> See Chapter 1 above, n. 184.

<sup>179</sup> See Chapter 2 above, nn. 279-280.

<sup>180</sup> See Troup [1998] BTR 490; also Chapter 2 above, n. 124.

<sup>181</sup> See *Equipping Britain for our long-term future: Financial Statement and Budget Report July 1997* (House of Commons Papers, Session 1997-1998, 85) (London: The Stationery Office, 1997).

<sup>182</sup> *Ibid.*, para. 1.68. (Emphasis added.)

<sup>183</sup> See Troup, n. 180 above, p. 491.

<sup>184</sup> See Balls and O'Donnell, n. 157 above, pp. 30-35.

In his review of the stages in the making of taxation policy, Christopher Wales identifies the first such stage as ‘policy initiation’. In the rest of the chapter, we seek to show how each of these stages has invoked one or more of the seven themes drawn out at the beginning of the study.

#### INITIATING REFORM MEASURES

If what has been said convincingly establishes the premises, much of the writing on the process of corporation tax reform is more insightful in certain respects, while being less so in others, than might be anticipated. More insightful than might be expected is the fact that it is generally willing to accord a rather privileged status to experts in the particular policy area. Less insightful, however, is the fact that writing on reform is in general insufficiently discriminating as to what different strands of corporation tax reform may require. Two documents illustrate the truth of these points. One of them is the paper to which reference has already been made,<sup>185</sup> in which Wales, with considerable flair, conceives of the corporation tax policy process in terms of the four stages considered here. The other is a rather austere discussion paper, produced by a working party under the chairmanship of Sir Alan Budd,<sup>186</sup> and published in 2003 by the Institute for Fiscal Studies (IFS).<sup>187</sup> The two documents are quite different. The value of the former, as has already been mentioned, is that it sets out the public views of a long-serving member of Gordon Brown’s Council of

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<sup>185</sup> See Wales, n. 7 above.

<sup>186</sup> Now provost of Queen’s College, Oxford, Sir Alan Budd was head of the Government Economic Service and Chief Economic Adviser to the Treasury from 1991 to 1997.

<sup>187</sup> See Tax Law Review Committee, *Making Tax Law: Report of a Working Party on the Institutional Processes for the Parliamentary Scrutiny of Tax Proposals and for the Enactment of Tax Legislation chaired by Sir Alan Budd* (London: Institute for Fiscal Studies, 2003).



Economic Advisers.<sup>188</sup> Indeed, it was to the offices of Chris Wales, then still a City accountant,<sup>189</sup> that Ed Balls<sup>190</sup> wended his way early on the morning of New Labour's Election victory in 1997. The importance of the latter document is that the working party consisted of a distinguished group of tax practitioners, including Malcolm Gammie, QC,<sup>191</sup> Edward Troup<sup>192</sup> and John Whiting,<sup>193</sup> as well as several academics and parliamentarians. That said, the text of the IFS document does bear the unmistakable literary stamp, familiar from earlier work on the consultation theme, of the first of the three.<sup>194</sup> It goes without saying that both documents are extremely valuable in the present context:<sup>195</sup> the Wales paper because it reflects on the findings of the 2004 O'Donnell Report as they relate to tax policy-making; the IFS document because it sets out the considered views of some of those practitioners who have been most closely involved with the reform of corporation tax.

The present study concentrates on four reform themes: the greater alignment of 'commercial profits' with 'taxable profits', which we have designated 'the accounting theme'; the prevention of unacceptable manipulations of the corporation tax base (designated 'the anti-avoidance theme'); the reshaping of the mechanisms for determining and collecting the tax due ('the compliance and enforcement theme'); and, most intriguingly, perhaps, the need to react effectively to the activities of international and EU institutions, especially the

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<sup>188</sup> See Chapter 2 above, n. 298. On the Council of Economic Advisers, see Thain and Christie, n. 10 above, p. 12.

<sup>189</sup> See Hugh Pym and Nick Kochan, *Gordon Brown: The First Year in Power* (London: Bloomsbury, 1998), p. 44; also Lipsey, n. 58 above, p. 126, for Wales's contribution.

<sup>190</sup> See Chapter 2 above, nn. 16 and 264; Chapter 4 below, n. 199.

<sup>191</sup> See Chapter 1 above, n. 47.

<sup>192</sup> See above. Then still in private practice, as a partner in the City law firm, Simmons and Simmons (see Chapter 2 above, n. 124).

<sup>193</sup> See p. 133 above.

<sup>194</sup> Gammie was the working party's secretary (see the list in Tax Law Review Committee, n. 187 above, p. v).

<sup>195</sup> Older, still interesting, studies include: Ann Robinson and Cedric Sandford, *Tax Policy-Making in the United Kingdom: A Study of Rationality, Ideology and Politics* (London: Heinemann, 1983); Michael Rush, 'Influencing the 1986 Budget', in *Parliament and Pressure Politics*, ed. by

ECJ ('the European and international theme'). A key strand in the present chapter is that each of these four themes has invoked subtly different ideas of what prudence requires, and that, since prudential decision-making in individual cases cannot be reduced to a formula, each of the two documents just mentioned, valuable as they are, underestimates this element of spontaneity and contextuality.

One of the ways in which both documents are less incisive than might be anticipated is in their relation of corporate tax reform proposals to the institutions, and also to the processes, of representative democracy. In the IFS document, the authorial viewpoint is distorted, something that puts the critical emphasis of the work in the wrong place.<sup>196</sup> There is also, as we shall see, some misunderstanding of the UK's constitutional arrangements. Likewise, although the Wales paper has particular strengths, it too makes some fundamental constitutional errors, some of which it shares with the IFS document. Overall, there is less emphasis on how we reached the present situation, than on how matters might be improved for the future. One of the conclusions of the present study is that greater light would be shone on the latter if the analysis of the former were somewhat sharpened.

The initiation of reform proposals, the first of Wales's four stages, is a useful (and indeed logical) place to begin analysing the strengths and weaknesses of the literature of which the two documents under discussion are taken as exemplars. Recall the institutional structure evoked in Chapter 2 above. There are two cross cutting tensions: between the corporate sector and the state, and between the Crown (represented here by H.M. Treasury and its junior department(s)),<sup>197</sup> and Parliament. These tensions inform the options for initiating

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Michael Rush (Oxford: Clarendon Press, 1990); B. Guy Peters, *The Politics of Taxation: A Comparative Perspective* (Oxford: Blackwell, 1991); and Hood, n 35 above, ch. 6.

<sup>196</sup> See Tax Law Review Committee, n. 187 above, para. 3.5.

<sup>197</sup> For most of the relevant period, there were two junior departments, the relevant one being the Inland Revenue (see Chapter 1 above, p. 13).

reform measures.<sup>198</sup> The Crown has considerable freedom of initiative, at least when ‘the rules of the game’ are simply recited. In order to act authoritatively, however, as ‘the Crown in Parliament’, it must at all times strive for prudence in taking forward the public interest. If it acts imprudently, its sovereignty begins to drain away, in part because of the difficulty of enforcing party discipline when a measure is brought before the House of Commons, and in part because the trust and confidence of the electorate is thereby undermined. The relationship between the Commons and opinion outside Parliament is an important one, to which we shall return. That such imprudent proposals have not generally figured in corporation tax reform (unlike, arguably in other policy areas),<sup>199</sup> is an indication that the course taken has usually been the right one. Indeed, it is not too much to say that the personal qualities of the individuals, the ministers, who hold this major competence, are never more important than at the initiation of policy. Prudence, first and foremost, is about the weighing of ends and means,<sup>200</sup> the end defined by the ideology of the public interest that the governing party has embraced (in our case, a combination of efficiency and fairness), and the means by the choice of measures (including corporation tax measures) needed to bring this about. As Manin says, if our system is viewed as something nearer to ‘audience democracy’ than to ‘party democracy’,<sup>201</sup> the apparent ‘aptitude’ of the responsible minister ‘for making good decisions’<sup>202</sup> is all-important. More difficult to believe now he is Prime Minister, but

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<sup>198</sup> The Treasury’s role as a policy initiator has been lamented by Lord Turnbull, who was Permanent Secretary to the Treasury from 1998 to 2002 (see Timmins, *Financial Times*, 20 March 2007, 1). Thain and Christie date this policy role to the Southgate review of 1994 (see *Fundamental Review of H M Treasury’s Running Costs: A report to the Chancellor of the Exchequer by Sir Colin Southgate et al.* (London: no named publisher, 1994), p. 86: Thain and Christie, n. 10 above, p. 12.

<sup>199</sup> e.g., possibly, anti-terrorism legislation, or educational reform.

<sup>200</sup> See Chapter 1 above, pp. 34-35; Smith, n. 125 above, p. 216 (quoted in Chapter 5 below, n. 32); (see Winch, n. 125 above, p. 159).

<sup>201</sup> Already touched on at Chapter 2 above, nn. 203-204.

<sup>202</sup> See Manin, n. 1 above, p. 221.

certainly as Chancellor, Gordon Brown had this quality in abundance, just as his successor, Alistair Darling, seems to lack it.<sup>203</sup>

The fact that, in the UK's representative democracy, it is HMG, and not anyone else, which has the right of policy initiative,<sup>204</sup> places a particularly heavy accent on the coherence and consistency of the corporation tax policy choices embodied in each of the four substantive themes referred to above. Wales writes:

'Policy initiation requires a particular blend of skills and knowledge. It requires an understanding of macro and micro-economic policy<sup>205</sup> and the key elements that underpin the government's strategy. It requires a deep understanding of the tax system, an understanding of how the system functions and where it is dysfunctional; and it requires an appreciation of how policy change might be engineered to reduce the risks that change itself can create.'<sup>206</sup>

The need for rigorous rationality in policy initiation can be underlined all the more forcefully by taking account of four further factors. First, the point that, theoretically, the system places absolute discretion over the initiation of proposals in the hands of ministers of the Crown, there being no doctrine of mandate and recall in a representative system, and no binding electoral pledges in the UK system.<sup>207</sup> Secondly, the fact that it is perfectly legitimate, in a representative system, for the choice of one reform proposal rather than another to lie with the relevant minister, on the advice of her civil servants (and, possibly, her policy adviser(s)), and for that decision to be made behind closed doors.<sup>208</sup> This applies both to 'strategic

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<sup>203</sup> See, e.g., Anon, *Financial Times*, 25 January 2008, 12 (editorial); Parker, *Financial Times*, 12 February 2008, 2; Parker, *Financial Times*, 13 February 2008, 2.

<sup>204</sup> See Tax Law Review Committee, n. 187 above, para. 6.3; for sources of proposals in the 1980s, see Leonard Beighton, 'Tax Policy and Management: The Role of the Inland Revenue' (1987) 8 FS 1-16, 5-6.

<sup>205</sup> [See Balls and O'Donnell, n. 157 above; Balls, Grice and O'Donnell, n. 157 above.]

<sup>206</sup> See Wales, n. 7 above, p. 549 (a most Machiavellian passage!).

<sup>207</sup> See Manin, n. 1 above, p. 163.

<sup>208</sup> *Ibid.*, p. 167. This reflects Benedetto Croce's point about the 'aristocratic' nature of modern government (see Benedetto Croce, 'Elements of Politics', in *Politics and Morals*, trans by

policy’ (big) choices and to (smaller) decisions involved in ‘policy maintenance’,<sup>209</sup> although, as Wales perceptively points out, ‘[t]he corporate tax reform programme is a prime example of strategic policy that has swept up a range of maintenance issues’.<sup>210</sup> Thirdly, a point of relevance to the New Labour government, the fact that a conference resolution of 1907 gave the leaders of the Parliamentary Labour Party the competence to decide on the priorities between different policy options.<sup>211</sup> Fourthly, the fact that, as Wales points out, one of the consequences of the merger of the Inland Revenue and Customs and Excise has been that the ‘strategic policy advice’ of civil servants will be ‘single-sourced’.<sup>212</sup> ‘A future Chancellor [Wales writes] may well regret having had her sources of advice narrowed to such an extent’.<sup>213</sup> In the light of these four observations, and with the public interest as the starting point, we can reflect on the strengths and weaknesses of the initiatives behind each of the four substantive reform themes.

Although the accounting theme ranges across at least three main areas (the use of GAAP under FA 1998, s. 42, the special codes on corporate finance, and the treatment of intangibles), the decision to proceed in each case was prudential because of its consistency with New Labour’s ideology of the public interest. We shall return to a much fuller analysis of these points in Chapter 4. For the moment, however, we simply need to point out that, whatever the temptations to act differently, there was in each case a clear commitment to the free market. For example, in its fundamental reaffirmation in 2002 of the Conservatives’ approach in 1993, 1994 and 1996, HMG acknowledged that the pre-1996 corporation tax

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Salvatore J. Castiglione (London: George Allen and Unwin, 1946), pp. 7-43, 17-18; Loughlin, n. 17 above, p. 83).

<sup>209</sup> See O’Donnell, n. 57 above, pp. 95-96.

<sup>210</sup> See Wales, n. 7 above, p. 549.

<sup>211</sup> See Manin, n. 1 above, p. 214.

<sup>212</sup> See Wales, n. 7 above, p. 556; and so, apparently, it came to pass (see Houlder, *Financial Times*, 11 February 2008, 3). For the pre-merger position, on the Inland Revenue side, see Beighton, n. 204 above, 2-3.

treatment of corporate debt was both anomalous<sup>214</sup> and helped to create tax avoidance opportunities,<sup>215</sup> as well as the fact that there had been no serviceable law on the tax treatment of FOREX<sup>216</sup> or financial instruments,<sup>217</sup> leaving the vacuum to be filled by GAAP, which already had a conceptual framework for such items.<sup>218</sup> Specifically, the 2002 reaffirmation of the essentials of the loan relationships code was a reflection of an ideological commitment to the continued facilitation of the ‘gilt strips’ market<sup>219</sup> and, more importantly (though less commented on), to the Private Finance Initiative (PFI),<sup>220</sup> something which Gordon Brown has always strongly affirmed to be in the public interest.<sup>221</sup> Initiation, or reaffirmation, of the policy in each of these cases was the prudent course, not least because a barely-noted effect of the introduction of the loan relationships code in 1996

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<sup>213</sup> See Wales, n. 7 above, p. 556.

<sup>214</sup> See Southern, *Tax Journal*, 23 November 1995, 6; Doran and Greenbank, *The Times*, 11 April 1996, available from <http://global.factiva.com/ha/default.aspx> (accessed 12 March 2008); Elizabeth Keeling, ‘Taxing Foreign Exchange Gains and Losses – Past Doubts and Future “Solutions”’ [1995] BTR 122-136, 122-129; Judith Freedman, ‘The Role of Realisation: Accounting, Company Law and Taxation’, in *The Influence of Corporate Law and Accounting Principles in Determining Taxable Income*, ed. by Per Thorell (London: Kluwer Law, 1997), pp. 29-48, 43-46.

<sup>215</sup> See, e.g., ICTA 1988, s. 74(1)(m); ICTA 1988, ss. 337(2)(b); ICTA 1988, s. 337(3) (see *Cairns v. MacDiarmid* [1983] STC 178 (the so-called “non-deposit” scheme)); ICTA 1988, s. 338 (see *Wilcock v. Frigate Investments Ltd* [1982] STC 198; *Macniven (H.M. Inspector of Taxes) v. Westmoreland Investments* [2001] UKHL 6; [2001] 2 WLR 377); TCGA 1992, ss. 251, 253, 254 (*Cleveley’s Investment Trust Co. v. IRC* (1971) 47 TC 300; *Aberdeen Construction Group Ltd v. IRC* [1977] STC 302; *WT Ramsay Ltd v. IRC* [1979] STC 582, 587 (Templeman L.J.)).

<sup>216</sup> See Pagan [1993] BTR 276-278.

<sup>217</sup> See Freshfields, ‘Taxation of Financial Instruments’ (1991) 5 *Corporate Briefing* 284-286; Cook [1993] BTR 429-434; more generally, see Alvin C. Warren, Jr., ‘Commentary: Financial Contract Innovation and Income Tax Policy’ (1993) 107 Harv. L. Rev. 460-492; Julian S. Alworth, ‘Taxation and Integrated Financial Markets: The Challenges of Derivatives and Other Financial Innovations’ (1998) 5 *International Tax and Public Finance* 507-534; and David Southern, ‘The Taxation of Derivatives’ [1998] BTR 348-363.

<sup>218</sup> See, e.g., David Southern, *Tolley’s Taxation of Corporate Debt and Financial Instruments*, 2<sup>nd</sup> edn (Croydon: Tolley Publishing, 1998), ch. 13.

<sup>219</sup> See David Hole, ‘The Taxation of Gilts and Bonds’ [1995] BTR 511-522, 511-512.

<sup>220</sup> See Inland Revenue, *The Taxation of Gilts and Bonds: A Consultative Document* (London: Board of Inland Revenue, 1995), p. 7.

<sup>221</sup> See Brown, n. 73 above, p. 167. For an alternative viewpoint, see Allyson M. Pollock, David Price and Stewart Player, ‘An Examination of the UK Treasury’s Evidence Base for Cost and Time Overrun Data in UK Value-for-Money Policy and Appraisal’ *Public Money and Management* April 2007 1-7.

had been a broadening out of the tax base.<sup>222</sup> Imprudent, given New Labour's commitment to the market, would have been the suggestion, which was actually referred to at the Committee Stage of the FOREX code in 1993,<sup>223</sup> that a 'Tobin tax'<sup>224</sup> would be the appropriate means of taxing transactions in currencies. It was not that such an innovation would have been bad in itself (in fact, there were arguments for it under an economic policy designed to tackle 'spillover costs').<sup>225</sup> It was simply that it would not have been seen as consistent with New Labour's developing ideology of the public interest.

A similar kind of prudence, although to subtly different ends, was the touchstone for the measures making up the compliance and enforcement theme in the present study. The great strength of the introduction of corporation tax self-assessment (CTSA) in FA 1998,<sup>226</sup> was that the bringing-in of quarterly interim payments of corporation tax could be taken as the *quid pro quo* for the abolition of what by the late 1990s had become the much resented advance corporation tax (ACT).<sup>227</sup> This 'up front' payment of corporation tax had been a key feature of the tax since it was remodelled in 1972.<sup>228</sup> Because there was a cap on the amount of ACT that could be set against 'mainstream corporation tax',<sup>229</sup> and because overseas tax

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<sup>222</sup> See Southern, n. 214 above, p. 7.

<sup>223</sup> See Hansard HC Standing Committee A, 18 May 1993, cols 11-12 (Alistair Darling, MP, Edinburgh Central, Labour).

<sup>224</sup> See Inge Kaul, Isabelle Grunberg and Mahbub ul Haq, 'Overview', in *The Tobin Tax: Coping With Financial Volatility*, ed. by Mahbub ul Haq, Inge Kaul and Isabelle Grunberg (New York: Oxford University Press, 1996), pp. 1-12.

<sup>225</sup> See Ruth Kelly, *Fabian Society Discussion Paper No 15: Taxing the Speculator: the route to forex stability* (London: Fabian Society, 1993), pp. 18-22; Leys, n. 55 above, p. 27; Barry Eichengreen, 'Conclusion: The Tobin Tax: What Have We Learned?', in ul Haq, Kaul and Grunberg, n. 224 above, pp. 273-287, 279-281.

<sup>226</sup> See Chapter 1 above, n. 37.

<sup>227</sup> *Ibid.*, n. 85.

<sup>228</sup> See FA 1972, ss. 84-92; H.M. Treasury, *Reform of Corporation Tax: Presented to Parliament by the Chancellor of the Exchequer* (Cmnd 4630) (London: HMSO, 1971); *Report from the Select Committee on Corporation Tax, together with minutes of evidence, appendices and index* (House of Commons Papers, Session 1970-1971, 622) (London: HMSO, 1971). David Marquand (Chapter 2, n. 181 above) was a member of the Select Committee.

<sup>229</sup> See ICTA 1988, s. 239(2) (FA 1972, s. 85(2)).

on foreign dividends had to be relieved before ACT,<sup>230</sup> many companies by the time of its abolition were carrying ‘ACT mountains’. So, whilst it was a risky strategy to begin a process of introducing interim corporation tax payments under CTSA, it was obviously the right one.<sup>231</sup> Not only was criticism reasonably muted<sup>232</sup> (the problem of ‘shadow’ ACT possibly apart),<sup>233</sup> but CTSA has remained one of the more ‘stable’ components of the corporation tax code.

As we shall see, the most recent manifestations of the European and international theme have involved the need to react effectively to the potential for disruption resulting from a number of high-profile decisions of the ECJ. In such cases, policy choices are of course very limited, but, again, a convincing case could be made, given the public interest imperative, for (as has happened) preferring the risk of challenge under Community law to the certainty of leakage from the corporation tax base. The need for such effective reactions is not the only relevance of the European and international theme, however. The 1980s saw a growing literature produced by the Organisation for Economic Co-operation and Development (the OECD) on the arguments for, and against, marrying tax and accounting.<sup>234</sup> Against this background, it became quite easy for HMG to argue that the public interest was best served by initiating reform measures based on the ‘policy transfer’ involved in adopting these ideas.

None of the three themes just discussed can be said to present particularly serious problems for the somewhat secretive process of corporation tax policy initiation within the

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<sup>230</sup> See ICTA 1988, s. 797(4)(a); see Chris Whitehouse, Loraine Watson, Lakshmi Narain and Natalie Lee, *Revenue Law – principles and practice*, 18<sup>th</sup> edn (Croydon: Butterworths Tolley, 2000), para. [33.44]; the problem had been mitigated by FA 1994, s. 138 and Sched. 16, but it was still a real one (*ibid.*, paras [33.46]-[33.70]).

<sup>231</sup> Given the impact on pensions of the withdrawal of ‘payable’ ACT credits, it was also an illustration of how, in a contest between efficiency and fairness, efficiency would tend to win.

<sup>232</sup> See Lipsey, n. 58 above, p. 130.

<sup>233</sup> See Chris Whitehouse, Lakshmi Narain, Loraine Watson and Natalie Lee, *Revenue Law – principles and practice*, 19<sup>th</sup> edn (Croydon: Tolley Lexis Nexis, 2001), paras [33.76]-[33.100].



UK's representative institutions. Their logic, if not their precise form, commends itself on the terms discussed above. The same cannot be said, unfortunately, for the anti-avoidance theme. Initiating measures that could be avoided by opportunistic corporation tax planning must logically be done in secret, that is, without prior consultation.<sup>235</sup> The acceptability of such measures over the long term, if not when they are announced, depends on the care with which they are explained, argued, adjusted and justified,<sup>236</sup> as well as on the number and range - cumulatively speaking - of the measures involved. Of all the tests for the prudential conduct of corporation tax reform, none has proved more difficult for HMG to manage. An illustration is provided, indeed, by the fairly cursory way in which HMG announced measures to prevent deals in 'overseas losses' following the ECJ's decision in *Marks and Spencer*.<sup>237</sup> The challenge has been all the greater because the impetus for a number of corporation tax anti-avoidance measures, as Chapter 4 will show, has been, at the very least, a highly contestable one.

If the absence of the recognition of the need for prudence, and of the constraints of representative democracy more generally, is a weakness of the corporation tax reform literature, a considerable strength is its (largely tacit) recognition of the relative roles of expertise and debate in such a system. This touches on issues to be further developed in the next section about the role of Parliament in a representative democracy. Its importance here is what it says about the role of experts in such a system. Although the writer would disagree with the central proposition of the IFS discussion paper, that Parliament should have greater

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<sup>234</sup> See, e.g., Organisation for Economic Co-operation and Development, *The Relationship between Taxation and Financial Reporting: Income Tax Accounting* (Paris: OECD, 1987), pp. 12-13.

<sup>235</sup> See John Isaac, 'Development of Tax Policy Formulation and Presentation: a Retrospect' [2006] BTR 222-228, 223.

<sup>236</sup> *Ibid.*

<sup>237</sup> See Case C-446/03, *Marks and Spencer plc. v. Halsey (H.M. Inspector of Taxes)* [2006] 1 CMLR 18, discussed in Snape, n. 64 above, pp. 398-399.

resources and more time to scrutinise tax legislation earlier,<sup>238</sup> he would endorse the assumption that the drafting of legislative proposals is a matter for experts in consultation with those affected. Likewise, the need for strong expertise in tax policy making is a constant refrain in the Wales paper.<sup>239</sup> The reason is that all that representative government requires is for legislative proposals to be subjected to ‘argumentative scrutiny’.<sup>240</sup> This is not, as is sometimes claimed, ‘rule by experts’; it does not amount to a technocracy.<sup>241</sup> Moreover, HMG, as the initiator of corporation tax legislation, knows that its actions will be subject to ‘the retrospective judgment’ of the electorate, and this ‘counts in ... [its] deliberations’.<sup>242</sup> ‘Prudence dictates ... that ... [HMG act] now in preparation for that day of popular judgment.’<sup>243</sup> It is rational for HMG to get advice on such technical matters. That is what prudent people, prudent governors, do. Overall, it might be that, because of this, in the corporation tax area at least, the governance issues discussed in Chapter 2 are more prudent than problematic. If so, it follows that much soul-searching in the governance literature might be misplaced. We consider this next. So, too, might be the yearning in both the IFS document and Wales’s paper for what each call ‘effective [parliamentary] scrutiny’ of legislative texts.<sup>244</sup> Moreover, to anticipate Chapter 4 slightly, the prudential element is evidence that ‘liberal normativism’<sup>245</sup> cannot help us to understand how public law develops in the UK.

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<sup>238</sup> See Tax Law Review Committee, n. 187 above, para. 1.4.

<sup>239</sup> See Wales, n. 7 above, pp. 551, 559-560.

<sup>240</sup> See Manin, n. 1 above, p. 191.

<sup>241</sup> See Frank Fischer, *Technocracy and the Politics of Expertise* (London: Sage, 1990), pp. 21-26; also Claudio M. Radaelli, *Technocracy in the European Union* (London: Longman, 1999), p. 149 (sets ‘technocracy’ in opposition to ‘democracy’).

<sup>242</sup> See Manin, n. 1 above, p. 181.

<sup>243</sup> *Ibid.*, p. 237.

<sup>244</sup> See Tax Law Review Committee, n. 187 above, para. 6.8; Wales, n. 7 above, p. 563.

<sup>245</sup> See Chapter 1 above, nn. 283-287.

## DEVELOPING THE MEASURES

Having taken matters thus far, it is useful to reiterate the basis of the interaction of Crown and Parliament in the process of corporation tax reform. Hobbes's point, it will be recalled, was that 'LEVIATHAN',<sup>246</sup> in our day the 'United Kingdom of Great Britain and Northern Ireland', is external to the people. It is the '*Mortall God*, to which wee owe under the *Immortall God*, our peace and defence',<sup>247</sup> and HMG is its representative.<sup>248</sup> It is not Parliament that is the sovereign, but HMG, and HMG is the Crown in Parliament.<sup>249</sup> All of this is apparent, not from Dicey, but from the close analysis to which Martin Loughlin has subjected the historical material, especially Hobbes.<sup>250</sup> To extrapolate Loughlin's analysis a little, HMG retains its sovereignty so long as it continues to make prudent decisions in the public interest. Such decisions do not always have to work; they do not always have to be effective. When accounts come to be rendered, however, they have to be found to have been the prudent, or most prudent, decision, in the public interest, at the relevant time. It is not the people who are, in a general sense, sovereign.<sup>251</sup> They become sovereign, however, when they re-elect or dismiss the governing party at a General Election, the regularity of which is one of a small number of principles that, for three centuries, have been a constant feature of representative government.<sup>252</sup>

It might be wondered why we need to underscore these points at this juncture. The reason is that they help to give a shape and a significance to the development stage of corporation tax reform proposals, especially as regards the true role of Parliament in the process. Since

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<sup>246</sup> See Chapter 2 above, n. 39.

<sup>247</sup> See Hobbes (1985), n. 77 above, p. 227.

<sup>248</sup> See Chapter 2 above, n. 35.

<sup>249</sup> *Ibid.*

<sup>250</sup> See Loughlin, n. 17 above, *passim*.

<sup>251</sup> See Manin, n. 1 above, p. 234.

the IFS document concentrates on only one aspect of the development stage, that of ‘parliamentary scrutiny’, admittedly with some regard to what we have called ‘the consultation theme’, we need to turn to Wales’s characterisation of the second stage elements. Policy development is the stage of the widest scope, since it is made up (he says) of ‘the entire process of translating the [policy] vision into law’.<sup>253</sup> Given the preoccupations of the present study, therefore, it is about how the prudence of the initial decision to proceed with a particular course of action needs to be replicated in the prudence of public servants, either working alone or in co-operation with Treasury ministers. As someone with considerable experience of the demands of the development stage on the individuals involved,<sup>254</sup> Wales’s points are particularly important, and we need to subject the most relevant ones to rather close analysis. Before doing so, however, we need to emphasise the link between the prudence of politicians and officials in managing tax proposals in our time, and the prudence of the architects of the institutional framework within which they operate. Montesquieu wrote of the English system as being a ‘fine system’, albeit one that ‘was found in the forests’.<sup>255</sup> ‘[T]he [forests] ... of *Germania*, that is, [rejoins Manin] which had also given birth to “Gothic” customs and the feudal system’.<sup>256</sup> The English system has what James Harrington called ‘the Gothic prudence’,<sup>257</sup> a strength born of experience and of history, and with a logic of its own. There have been changes since the eighteenth century, to be sure, but - as Chapter 2 has shown - the British system is still fundamentally that which

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<sup>252</sup> *Ibid.*, p. 6.

<sup>253</sup> See Wales, n. 7 above, pp. 549-550.

<sup>254</sup> See Lipsey, n. 58 above, p. 126.

<sup>255</sup> See Charles de Secondat, baron de Montesquieu, *The Spirit of the Laws*, trans. and ed. by Anne M. Cohler, Basia Carolyn Miller and Harold Samuel Stone (Cambridge: Cambridge University Press, 1989), p. 166.

<sup>256</sup> See Manin, n. 1 above, p. 90.

<sup>257</sup> *Ibid.* (quoting James Harrington’s ‘The Prerogative of Popular Government’, in *The Political Works of James Harrington*, ed. by J.G.A. Pocock (Cambridge: Cambridge University Press, 1977), pp. 389-499, 477).

was created in the bloodshed of the seventeenth- and early eighteenth centuries.<sup>258</sup> These points are not merely quaint or eccentric. They provide the logic by which all proposals, including those of the IFS and of Wales, in this context and in a functionalist mode, must be judged. Without a strong sense of history, we cannot make sense of Treasury policy, as Thain and Christie emphasise.<sup>259</sup> This point is especially applicable, perhaps, to the IFS proposals, which lack a certain historical sensitivity. It also applies to Wales's, however, since, although his analysis of the Treasury's role, and the functions of the old 'Revenue Departments', reflects a keen awareness of how that part of HMG works, his discussion of the role of Parliament quickly dissolves into the kind of platitudes set out so fully in the IFS document.

Drawing on his experience at the centre of the corporate tax reform process, to Chris Wales, the development stage has a particular aura, and it makes exacting and specific demands, especially on expertise. It is not intended here to set up a black-and-white contrast between his paper and the IFS document, but there is, it seems to the writer, an insightfulness, and a truth, about this part of Wales's discussion, which makes parts of the IFS document seem at best naïve, and at worst, ideologically highly charged. Wales first identifies the importance of discussions between senior Treasury and HMRC civil servants and Treasury ministers (and also, presumably, special advisers) about translating the ideological vision into policy materials.<sup>260</sup> It is to be inferred that there is some overlap, some inter-fertilisation here, with the policy initiation stage, although, in Wales's typology, this first part of the development stage makes particular demands, both on the ministers involved, and especially on the officials. The demands on civil servants become particularly

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<sup>258</sup> Either, or both of 1688 (see Palmerston: Chapter 2 above, n. 199) or 1707 can be seen as Britain's 'constitutive moment'.

<sup>259</sup> See Thain and Christie, n. 10 above, *passim*.

prominent in what Wales identifies as ‘the iterative process with the ministerial team[,] to consider how the proposals fit with the government’s broader policy objectives’.<sup>261</sup> The key passage is as follows:

‘... [T]he policy development process requires a very broad range of skills. It requires an understanding that spans the vision and the detail; to identify how the vision can be made to work within the framework of the existing system and to see where further change will be needed to allow the old and the new to work effectively together. It requires the skills of the analysts and statisticians to take the detailed proposals and assess their effect on behaviour and yield and, of course, a system that traps the necessary information and allows it to be manipulated to identify and quantify the effects of change.’<sup>262</sup>

Every part of this extract demands our closest attention in the context of the present study. This is not only because it demonstrates an analytical subtlety far beyond the somewhat ‘box-like’ assumptions on which the IFS document relies. It is unnecessary to highlight, but we should certainly note, Wales’s encapsulation of the Machiavellian prudence in emphasising the need for skills that can comprehend the ‘vision’ and ‘the detail’. What the opening words of the extract disclose, however, is more than this, since Wales writes of ‘the vision’ and its being put to work within the existing system. Although Samuel Brittan and others might want to be spared ‘the vision thing’,<sup>263</sup> Wales emphasises, in a way which is almost completely absent from the IFS discussion, the fact that what is undertaken here is the use of the corporation tax system to bring about a specific (democratically sanctioned) conception of the public interest. Supreme technical ability is needed to achieve this, but it is a political, not a technocratic, project. It is about harnessing a mass of technical material to an agreed political end. This point is drawn out particularly strikingly where Wales stresses

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<sup>260</sup> On relations between elected and non-elected officials, see Lord Healey of Riddlesden, ‘Why the Treasury is so difficult’, in Davies, n. 173 above, pp. 52-75, 53-57.

<sup>261</sup> See Wales, n. 7 above, p. 550.

<sup>262</sup> *Ibid.*

<sup>263</sup> See Brittan, *Financial Times*, 23 November 2007, 15.

the importance of technical skill in making ‘the vision’ work within the ‘existing system’, and seeing where further change will be needed. Building on New Labour’s ideological construct of the public interest, Chapter 4 will demonstrate in detail how radical New Labour’s plans for the corporation tax system have been. The accounting theme, for example, has had an important role in this process, as too has the anti-avoidance theme. Suffice it to say, for the moment, that it has been radical in intent and, it seems, in effect. This may be the reason why Wales refers to the ‘effect’ of policies ‘on behaviour’.

Making ‘the vision’ work within ‘the existing system’ is something rather poorly understood by those who comment on tax reform in general and on the need for simplicity in the system in particular. This is not simply a matter of issues such as the formal constraints on competence imposed by GATT 1994/WTO and/or the Community law. One of many memorable points made by Murphy and Nagel, in *The Myth of Ownership*,<sup>264</sup> one to which we shall return, is that tax policy is never about ‘tax design’, it is always about reform, because it always has to take account of the existing system. In placing emphasis on the history, this study seeks to reflect an understanding of this insight. What Murphy and Nagel do not say, however, is that reform creates avoidance opportunities, something that has encouraged governments to hold back from large-scale reform of their tax systems.<sup>265</sup> Secondly, to the extent that radical political change must for all these good reasons be accommodated within existing institutional and conceptual structures, ‘complexity’ is inevitable. Only lack of change, lack of intervention, makes things simple. This is why ‘simplification’ arguments have often come from ‘minimum-statists’ on the libertarian Right of politics.<sup>266</sup>

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<sup>264</sup> (Oxford: Oxford University Press, 2000). See Chapter 1 above, n. 359.

<sup>265</sup> See Tiley, n. 38 above, p. 16.

<sup>266</sup> See Sir Geoffrey Howe, ‘Reform of Taxation Machinery’ [1977] BTR 97-104; also Lord Howe of Aberavon, ‘Simplicity and Stability: the Politics of Tax Policy’ [2001] BTR 113-123. (For the

In relation to the foregoing extract from Wales's paper, we might finally draw attention, again harking back to Murphy and Nagel, to the emphasis in the last part of the extract on the importance of information in weighing ends and means. Murphy and Nagel rightly speak, in an engaging phrase, of 'large empirical uncertainties about the economic consequences of [the] different choices'<sup>267</sup> involved in tax policy-making. That is not, however, to deny the importance of such information as there is. This strand is drawn out by Wales in his reference to 'the skills of the analysts and statisticians',<sup>268</sup> whose findings are so important (in the prudential mode) in the weighing of ends and means. John McEldowney has written persuasively about the contribution to the development of public law of 'the statistical movement',<sup>269</sup> and we may note in passing the link between 'political arithmetick'<sup>270</sup> and political economy on which rests, in a sense, the whole matter of the present study. It is in this part of the corporation tax policy development process, in the weighing of ends and means, however, that statistical work comes into its own.

The end towards which statistical information and modelling techniques, and, indeed, the technique of prudence, are directed, of course, is effectiveness.<sup>271</sup> All the corporate tax reform proposals in the world are nothing if they do not work towards the realisation of the vision of the public interest that the governing party has put before the electorate at the General Election. It is this (Wales's reference to making 'the old and the new ... work

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ideological context, see Lord Howe of Aberavon, 'Can 364 Economists all be Wrong?', in Davies, n. 173 above, pp. 76-112, esp. pp. 101-102.) See Chapter 4 below.

<sup>267</sup> See Murphy and Nagel, n. 56 above, p. 4.

<sup>268</sup> See Cabinet Office, *The 46<sup>th</sup> Civil Service Year Book* (London: TSO, 2007), pp. 233-235.

<sup>269</sup> See John F. McEldowney, *Public Law*, 3<sup>rd</sup> edn (London: Sweet and Maxwell, 2002), paras 8-058a-8-067; John F. McEldowney and Sharron McEldowney, *Environmental Law and Regulation* (London: Blackstone Press, 2001), pp. 21-23; see Sir William Petty, 'A Treatise of Taxes & Contributions', in *The Economic Writings of Sir William Petty: together with the Observations upon the Bills of Mortality* more probably by Captain John Graunt, ed. by Charles Henry Hull, 2 vols (New York: Augustus M. Kelley, 1963 and 1964), I, pp. 1-97.

<sup>270</sup> See Pocock, n. 70 above, p. 425n.



effectively together’) that encapsulates the significance of the remaining elements in ‘policy development’. These are the importance of effective parliamentary liaison, and (rather less prominent in Wales than in the IFS document) consultation. The need for Treasury and HMRC to work effectively with ‘Parliamentary counsel[,] to ensure that the legislation, when enacted, will achieve the policy intent’,<sup>272</sup> ‘the handling of the Parliamentary process itself[,] and the provision of support for ministers in the House’,<sup>273</sup> is something the analysis of which we shall defer until we consider the role of Parliament in the development stage. As to consultation, however, this does require some close consideration at the present juncture. There are two reasons for this. First, the relativity, the contextuality, of its importance to effectiveness, and, secondly, its significance as a *locus* for the ‘governance dilemmas’ already examined.

Wales does not ‘major’ on the consultation theme, although he does acknowledge the special nature of the ‘presentational skills’ involved in ‘a formal process of public consultation’.<sup>274</sup> Gammie, if he was indeed responsible for drafting the findings of the IFS working party, does do so, however, and in the process evinces a slight change of position from his earlier work on the importance of consultation. The IFS document promulgates the view that the emphasis on consultation places Parliament too far back in the process, and that proposals are too far down the line by the time they reach the House of Commons.<sup>275</sup> As will be shown below, this seems to betray a fundamental misunderstanding of the constitutional role of Parliament. The IFS document laments most of all a lack of ‘uniformity’ in the

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<sup>271</sup> This is even true in relation to the importance of prudence in furthering the common good in the catechism: see *Catechism of the Catholic Church*, n. 155 above, pp. 400, 418.

<sup>272</sup> See Wales, n. 7 above, p. 550.

<sup>273</sup> *Ibid.*

<sup>274</sup> *Ibid.*

<sup>275</sup> See Tax Law Review Committee, n. 187 above, para. 4.5.

consultation process,<sup>276</sup> but, in a slightly obscure passage, also concedes that consultation periods and forms need to be ‘tailored’.<sup>277</sup> We shall return to the constitutional misunderstanding presently. But there is also a failure to appreciate that the only reason for consultation is prudence, to make provisions work effectively, and that effectiveness might actually require less consultation in some cases, and more in others.

The former point, which is related to the governance point to be discussed in a moment, is in a way acknowledged, because the IFS is interested in making tax legislation work better, although (arguably) with insufficient emphasis on its political purpose. The latter point, however, is elided. Given that the watchword is ‘prudence’, how best to attain the political end, the reform project in question might not be such as to lend itself to consultation. If we consider the issues raised by the accounting theme, or, indeed, by the compliance and enforcement theme, or the technical theme, what is prudent is the building up of a broad base of support over a long period of time, in an atmosphere of as much transparency as supports the public interest.<sup>278</sup> All of the initiatives in these three reform themes have been successful (some, like CTSA, conspicuously so),<sup>279</sup> and this broad, deep, form of consultation, being prudent in the circumstances, has worked. The examples given in Chapter 1 above illustrate this. In other cases, however, especially those involving anti-avoidance measures, the activities that HMG seeks to curtail will be the province of opportunists, for whom transparency would merely make matters easier.<sup>280</sup> In such cases, prudence declares for no consultation, effectiveness requiring swift action. Not all cases are easy to judge, however. The current Chancellor’s capital gains tax reform is an indication of how spectacularly

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<sup>276</sup> *Ibid.*, para. 3.3.

<sup>277</sup> *Ibid.*, paras 3.4, 5.2.

<sup>278</sup> See Lipsey, n. 58 above, p. 88.

<sup>279</sup> See Giles, *Financial Times*, 21 October 2005, 3.

<sup>280</sup> Especially, perhaps, non-residents.

situations can be misjudged, and there is some evidence<sup>281</sup> that a similar lack of prudence was to be detected in the abolition (without consultation) of industrial buildings allowances<sup>282</sup> under Alistair Darling's predecessor.

Failing to match the length and depth of consultation to the prudential requirements of the situation is only part of the way in which the discussion in the IFS document is skewed. Prudence has a part to play in another area, although it is a slightly different one. We have touched briefly on this point at the end of the previous section. The consultation stage, it is suggested, is the point at which the five 'governance dilemmas' discussed in Chapter 2 come into play. The reasoning in an individual case might go as follows. H.M. Treasury might approve of what, say, the International Accounting Standards Board (the IASB) has to say about profits measurement, and it might be convenient to translate it into tax law, but the (informed) electorate might not approve if they knew the influence of this non-elected, relatively unaccountable body. The matter probably will not become important, provided there is no risk, and there is unlikely to be if it legislates to modify the IASB's rules where necessary.<sup>283</sup> H.M. Treasury might, in the process of adopting this solution, become over-reliant on the accountancy profession, but, if it listens to them, H.M. Treasury might gain their influential support. To do so, H.M. Treasury will have to work within a policy network, but, again, in a relatively low-risk policy area, so the unaccountability of some of the individuals involved is probably not overly important. There is some risk, nonetheless, that any added technical complexity might discredit the policy, but in an already complex area, this is unlikely to make much difference. At each stage, as Manin might infer, the questions are: is the decision a prudent one, and is it in the public interest? If not, on either count, and

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<sup>281</sup> See Houlder, n. 212 above.

<sup>282</sup> See FA 2007, s. 36.

<sup>283</sup> See FA 1998, s. 42.

there are serious consequences, HMG's credibility will be affected. Such must be the considerations going through the mind of the minister signing a - usually very brief - regulatory impact assessment (the RIA), once the process of consultation on corporation tax reform measures is complete.

The part of the development stage to which Wales gives the least detailed consideration (and one that O'Donnell did not consider) is the one that is weakest in Wales's analysis, namely the role of Parliament in the development stage. Much more consideration is given to this by the IFS, however. This is also weak, and for generally similar reasons. The yardstick of strength or weakness here is not the prudence of today's decision-makers, nor yet of some exogenous norm, but the prudence of the ages: the prudence that was found 'in the forests of Germany'. Before exploring this issue in detail, we should refer to the fact that Wales places much more emphasis than does the IFS on the contribution of effective mutual understanding, and close co-operation, between officials in the relevant department, and parliamentary counsel,<sup>284</sup> both in terms of the drafting of instructions to counsel, and their interpretation.<sup>285</sup> The IFS has nothing complimentary to say about the drafting of tax legislation. Secondly, Wales obliquely pays tribute to the accumulated experience (in 2004) of the Treasury ministers.<sup>286</sup> The IFS makes no mention of them. But anyone who has read the contributions to Standing Committee debates by the minister involved (Conservative as well as Labour) would be impressed by the intellectual grasp of people who do not always have legal training,<sup>287</sup> and on the effectiveness of the public servants briefing them.

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<sup>284</sup> See Terence Daintith and Alan Page, *The Executive in the Constitution: Structure, Autonomy and Internal Control* (Oxford: Oxford University Press, 1999), p. 221; also Cabinet Office, n. 268 above, pp. 237-238.

<sup>285</sup> See Wales, n. 7 above, pp. 557-558.

<sup>286</sup> *Ibid.*, p. 560; also Thain and Christie, *Parliamentary Brief*, February 2008, 21-22, 22 (available from [www.treasuryproject.org](http://www.treasuryproject.org) (accessed 21 February 2008)).

<sup>287</sup> The Treasury Ministers 'sacked' in 2007, on Gordon Brown's taking office as Prime Minister, had considerable combined experience, all having been long-serving. Dawn Primarolo, in Lipsey's

The first of the ways in which both Wales's contribution, and that of the IFS, underestimates the constitutional theory, is in relation to the 'effective [parliamentary] scrutiny' of legislation. Wales thinks it is 'weak';<sup>288</sup> the IFS, chancing its arm, claims that 'the House of Commons fails to scrutinise the rules (if not the levels) of taxation in any real sense at all'.<sup>289</sup> Within the logic of the system, it has to be said that neither comment is justified. It is not simply the fact that in each parliamentary session for the last decade many columns of Hansard have been devoted to FB debate.<sup>290</sup> It is, more importantly, that representative democracy requires only that legislative proposals be subject to 'argumentative scrutiny'.<sup>291</sup> More fully, what representative democracy insists on is that 'no measure can be adopted unless a majority deems it *justified* after argumentative scrutiny'.<sup>292</sup> Although the IFS deprecates both the nature and the scope of argument in the Commons, not to say the 'scrutiny', involved, Wales obviously regards FB debates as a significant challenge to the ministers and public servants involved, because he earlier emphasises the gruelling nature of the exchanges:

'In our Parliament's confrontational process, the officials involved [i.e. civil servants advising ministers] need to be able to identify the issues that the Opposition are likely to target and prepare and provide appropriate briefing and support. ... [T]his is a matter of

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words (see n. 58 above), 'a former left-winger who looks and sounds like a faintly flustered Sunday-school teacher' was nonetheless a 'safe pair of hands' (*ibid.*, p. 25) and 'bore the bulk of the burden' of 'tax responsibilities' as Paymaster General (*ibid.*, p. 126) throughout most of the period covered by this study.

<sup>288</sup> See Wales, n. 7 above, p. 563.

<sup>289</sup> See Tax Law Review Committee, n. 187 above, para. 2.4.

<sup>290</sup> Statistics on the length of standing committee debates on FBs in *Hansard* are striking: FB 1997, nine sittings, 509 cols; F(No. 2)B 1998, 23 sittings, 1063 cols; FB 1999, 19 sittings, 787 cols; FB 2000, 26 sittings, 1051 cols; FB 2001, seven sittings, 221 cols; FB 2002, 16 sittings, 579 cols; FB 2003, 15 sittings, 633 cols; FB 2004, 21 sittings, 777 cols; FB 2005, eight sittings, 319 cols; F(No. 2)B 2005, 21 sittings, 785 cols; FB 2007, 14 sittings, 525 cols. It would not therefore be correct to say that there is no scrutiny of FB clauses.

<sup>291</sup> See Manin, n. 1 above, p. 191.

<sup>292</sup> *Ibid.*

linking policy objectives to detail. Technical analysis on its own is not sufficient and neither is pure policy advice.<sup>293</sup>

As Manin says, the ‘English aristocrats and French lawyers’<sup>294</sup> who invented representative government, ‘certainly did not confuse a parliament with a learned society’.<sup>295</sup> Occasionally, it is true, debate seems somewhat perfunctory, but often (such as in the case of the Standing Committee debate on the FB 1998 measures on CTSA),<sup>296</sup> this is explained by the context (there, the continuing legislative euphoria following the 1997 landslide election victory). More frequently, as in the case of the Standing Committee proceedings on the F(No. 2)B 2005<sup>297</sup> clauses on the intra-Community surrender of group losses, both the knowledge and engagement of the participants rather impresses.<sup>298</sup> More of a problem, little underscored in the literature, is the use of the ‘guillotine’ to curtail debate,<sup>299</sup> but the institution itself recognises this as an expedient, which is why the occasions on which the ‘guillotine’ is used are carefully minuted.<sup>300</sup>

The crux of the matter appears, as Manin explains, in the following words of Emmanuel Joseph Sieyès, who explains why the will of the majority in Parliament is an expression of the public interest:

‘Without doubt the general interest<sup>301</sup> is nothing if it is not the interest of someone: it is that particular interest that is common to the greatest number of voters. From this comes the necessity of the competition of opinions.’<sup>302</sup>

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<sup>293</sup> See Wales, n. 7 above, p. 550.

<sup>294</sup> See Manin, n. 1 above, p. 234.

<sup>295</sup> *Ibid.*, p. 190.

<sup>296</sup> See Hansard HC Standing Committee E, 9 June 1998, cols 704-712.

<sup>297</sup> F(No. 2)B 2005 became FA 2006.

<sup>298</sup> See Hansard HC Standing Committee A, May 16, 2006, cols 159-179.

<sup>299</sup> See S.O.s, Nos 83, 83A-83I; see *Erskine May's Treatise on The Law, Privileges, Proceedings and Usage of Parliament*, ed. by Sir William McKay *et al.*, 23<sup>rd</sup> edn (London: LexisNexis UK, 2004), pp. 466-481; also Ferrier [2003] Conv. 346-347.

<sup>300</sup> See House of Commons Information Office Factsheet P10, *Programming of Government Bills* (London: UK Parliament, 2004), available from [www.parliament.uk](http://www.parliament.uk) (accessed 4 April 2008).

<sup>301</sup> [See n. 141 above.]

The point only needs to be read for its importance to be clear. ‘Public decision’ is the result of ‘trial by discussion’, plus ‘majority consent’.<sup>303</sup> For Manin, it means that:

‘(1) parliamentary debate does not constitute a disinterested activity, oriented solely by the search for the truth, but a process that aims to identify the interest common to the greatest number,<sup>304</sup> and (2) the general interest, unlike Rousseau’s “general will”,<sup>305</sup> does not transcend particular interests and is not of a different nature than [*sic*] them.’<sup>306</sup>

To similar effect had been the conclusion of John Locke, in the seventeenth century,<sup>307</sup> and Jeremy Waldron in the twentieth.<sup>308</sup> If the idea of the sanctity of argumentative scrutiny indeed reflects the logic of the system, then few of the arguments put forward by the IFS seem relevant: that the House of Commons lacks the time to scrutinise FBs adequately; that it lacks the ‘inclination’ to do so; and (most perversely) that it lacks the requisite ‘expertise’.<sup>309</sup> If it is objected, even in the face of so many pages of Hansard devoted to debating corporation tax reform proposals, that scrutiny is nonetheless inadequate, it is necessary to turn only to John Stuart Mill. Mill, in Manin’s analysis:

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<sup>302</sup> See Emmanuel Joseph Sieyès, *Vues sur les moyens d’exécution dont les représentants de la France pourront disposer en 1789* (Paris: anonymous publisher, 1789), p. 92 (quoted in Manin, n. 1 above, p. 188); also Burke, n. 141 above, p. 156 (see Manin, n. 1 above, p. 187n).

<sup>303</sup> See Manin, n. 1 above, p. 190.

<sup>304</sup> [See Arendt, nn. 82 and 139 above, on the significance of ‘inter-est’; also Barry, n. 134 above, ch. 10.]

<sup>305</sup> For Rousseau, ‘the general will’ was ‘the first principle of the public economy and the fundamental rule of government’ (see Jean-Jacques Rousseau, *Discourse on Political Economy and The Social Contract*, trans. and ed. by Christopher Betts (Oxford: Oxford University Press, 1994), p. 9 (in ‘Discourse on Political Economy’), 73-74 (in ‘The Social Contract’). Rousseau deplored (England’s) representative government: *ibid.*, p. 127.

<sup>306</sup> See Manin, n. 1 above, p. 188n.

<sup>307</sup> *Ibid.*, p. 189n, quoting Locke, n. 1 above, pp. 331-332.

<sup>308</sup> See Jeremy Waldron, *The Dignity of Legislation* (Cambridge: Cambridge University Press, 1999), ch. 4.

<sup>309</sup> See also Wales, n. 7 above, p. 563; also Isaac, n. 235 above, p. 224-225. But it is not expertise that qualifies an MP.

‘ ... suggested that propositions of laws [*sic*] be drafted by a commission of experts appointed by the Crown and then brought before Parliament only for discussion and approval. He even went so far as to deny Parliament the right to amend the commission’s propositions in the course of discussion. Mill wrote: “[The bill] once framed, however, Parliament should have no power to alter the measure, but only to pass or reject it; or, if partially disapproved of, remit it back to the Commission for reconsideration.” According to Mill, the principal function of the debating body should be to grant or withhold “the final seal of national assent” after a public exchange of arguments, not to conceive and formulate legislative measures.’<sup>310</sup>

This obviously contrasts with the IFS’s disapproval of legislative proposals being brought before Parliament as ‘*faits accomplis*’,<sup>311</sup> and it sits ill, too, with its rather dogmatic assertion that ‘consultation is not and should not become a substitute for Parliamentary scrutiny’.<sup>312</sup> It does, however, fit well with the kind of debate referred to above, on the surrender of losses between EU Member States, and the *Marks and Spencer* litigation that had just been before Park J. in the Chancery Division.<sup>313</sup> There, Mark Hoban, MP,<sup>314</sup> made a carefully analytical and measured contribution to the debate, and even the Opposition backbench disagreement on the point of principle<sup>315</sup> is a vivid illustration of the ‘argumentative scrutiny’ that representative democracy requires.<sup>316</sup>

That first group of arguments mounted by both Wales and the IFS is about the nature and extent of Parliamentary scrutiny. Both go on to argue that each aspect would be facilitated by the allocation of greater resources to this aspect. Wales advocates the introduction of an ‘adaptation’ of the US Congressional Budget Office, which provides ‘the Congress with the objective, timely, non-partisan analyses needed for economic and budget decisions’,<sup>317</sup>

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<sup>310</sup> See Manin, n. 1 above, p. 191, quoting Mill, n. 140 above, pp. 203-467, 280 and 283.

<sup>311</sup> See Tax Law Review Committee, n. 187 above, para. 3.8.

<sup>312</sup> *Ibid.*, para. 3.9.

<sup>313</sup> See Snape, n. 64 above, pp. 399-400.

<sup>314</sup> Fareham, Conservative.

<sup>315</sup> See Snape, n. 64 above, pp. 395-396.

<sup>316</sup> See Hansard HC Standing Committee A, May 16, 2006, cols 159-179.

<sup>317</sup> See Wales, n. 7 above, p. 563, quoting the Congressional Budget Office’s Mission Statement, available from: [www.cbo.gov/aboutcbo/factsheet.shtml](http://www.cbo.gov/aboutcbo/factsheet.shtml) (accessed 18 March 2008).



suggesting that ‘it would surely improve the process of scrutiny that tax proposals undergo in Parliament’.<sup>318</sup> Somewhat less ambitiously, the IFS argues for more resources, including the institution of a new select committee, and a ‘team’ to work on ‘tax structure’.<sup>319</sup> There is, however, an historical and logical objection to these superficially sensible suggestions. Unlike ‘the US Congress, Parliament is not the forum of public discussion. Each party is grouped around a leading figure, and each parliamentary party votes in a disciplined manner in support of its leader’.<sup>320</sup> In short, therefore, sensible as it sounds, this suggestion ignores the significance of the (still crucial) concept of party discipline.

If, on this historical and interpretative basis, Wales and the IFS are wrong on each of the foregoing questions, then perhaps a third argument, somewhat common to both, might stand further analysis. Wales offers for consideration the idea that the House of Lords could perhaps undertake ‘a greater level of scrutiny’ of FBs, arguing that ‘the problem of a lack of effective scrutiny of tax law proposals in the Commons has been compounded by the convention that the House of Lords has a very limited role in relation to Finance Bills’.<sup>321</sup> On this point, the IFS is rather more cautious: it suggests that a joint committee of Lords and Commons ‘would not infringe the current prerogatives of the House of Commons in tax legislation’,<sup>322</sup> but goes on to suggest that, even if such a committee was constituted solely from the House of Commons, this ‘would not prevent the House of Lords establishing its own Committee on Taxation’.<sup>323</sup> The problem, however, is that the House of Lords is not

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<sup>318</sup> See Wales, n. 7 above, p. 564.

<sup>319</sup> See Tax Law Review Committee, n. 187 above, paras 1.4, 6.2 and 7.6.

<sup>320</sup> See Manin, n. 1 above, p. 231.

<sup>321</sup> See Wales, n. 7 above, p. 564.

<sup>322</sup> See Tax Law Review Committee, n. 187 above, para. 6.3.

<sup>323</sup> *Ibid.*, para. 6.5.

elected.<sup>324</sup> Election (that is, representation) is the *quid pro quo* for taxation, not taxation expertise. In this light, it is encouraging that the rather obfuscatorily named House of Lords Select Committee on Economic Affairs<sup>325</sup> has encountered difficulties in enlisting co-operation from officials on tax matters, and rather surprising that Wales should find this state of affairs so unsatisfactory.<sup>326</sup> He may be right that ‘a reformed House of Lords might be in a position to make a stronger claim’,<sup>327</sup> but this too would depend on the Lords being an elected representative assembly.<sup>328</sup> Furthermore, it is a little disingenuous for the IFS to suggest that the taxation sub-committee of the House of Lords Select Committee on Economic Affairs might provide some kind of antecedent for its proposed committee.<sup>329</sup> The Lords Committee, as its name suggests, is a Select Committee and, as such, is concerned only with the *ex post* scrutiny of tax legislation.<sup>330</sup>

Wales puts one other argument that, did it not illustrate so well Loughlin’s point that sovereignty is not competence alone, but constituent power (competence enlarged by capacity),<sup>331</sup> we might put aside. Although he does not make it a large part of his argument, Wales makes the point that ‘in the last twenty years, there have been very few Finance Bills that meet all the requirements of the definition as [*sic*] a money bill.’<sup>332</sup> So, in reality, if the House of Lords had wanted to intervene in FB debates, it would probably have been able to

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<sup>324</sup> Except in the limited sense provided for by the House of Lords Act 1999 (see Ministry of Justice, *The Governance of Britain* (Cm 7170) (London: TSO, 2007), p. 41); see Eaglesham, *Financial Times*, 20 July 2007, 2.

<sup>325</sup> See Chapter 2 above, nn. 206 and 346.

<sup>326</sup> See Wales, n. 7 above, p. 564.

<sup>327</sup> *Ibid.*, p. 564.

<sup>328</sup> See Ministry of Justice, n. 324 above, p. 42.

<sup>329</sup> See Tax Law Review Committee, n. 187 above, para. 6.5.

<sup>330</sup> See Chapter 2 above, n. 206.

<sup>331</sup> *Ibid.*, nn. 49-54.

<sup>332</sup> See Parliament Act 1911 (as amended by Parliament Act 1949), s. 1(2) (see *O. Hood Phillips & Jackson: Constitutional and Administrative Law*, ed. by Paul Jackson and Patricia Leopold, 8<sup>th</sup> edn (London: Sweet and Maxwell, 2001), para. 8-034); see Erskine May, n. 299 above, pp. 928-931.

do so'.<sup>333</sup> Even allowing that the premise is true, the reader who has followed the argument of the study so far will appreciate that precisely the opposite is the case. In *theory*, the House of Lords might have been able to intervene. '[I]n reality', any such intervention might have precipitated the abolition of the Chamber.

What the present writer finds so strange in both the Wales and the IFS accounts is that both betray a fundamental unwillingness to entrust tax legislation to the House of Commons, and a commensurate willingness (without any obvious basis, especially not an historical one) to enlist the help of the House of Lords. This, combined with the Lords' difficulties in establishing a legitimate claim to interfere, not just in corporate taxation matters, but in tax matters generally, would explain both Gammie's demeanour, already noted, before the Lords' Economic Affairs Committee,<sup>334</sup> and the Committee's own fulsome appreciation of his contribution to their deliberations.<sup>335</sup> Distinguished and influential as Gammie is, it is very difficult to understand the foundations of his sympathies on this question. The same comment applies to Wales's views on the Lords' role. What we see in the debates on the FBs is democracy in action. Or, more accurately (and rather significantly), representative democracy in action. The right of elected representatives of the people to argue about matters of taxation applies even, perhaps especially, to corporate taxation.

#### PRESENTATION OF REFORM MEASURES

With the conclusions of the previous section in mind, it is possible to make some relatively brief comments on Wales's own rather concise treatment of the third and fourth stages of the

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<sup>333</sup> See Wales, n. 7 above, p. 564.

<sup>334</sup> See Chapter 2 above, n. 346.

reform process. '[A] significant omission', in Wales's view, from the O'Donnell Report, was its failure to identify 'policy presentation as an important part of the [reform] process'.<sup>336</sup> In practice, the presentation of reform measures, allowing (as it does) for 'a more detailed engagement between officials and those affected by the new policy', has been a common feature of the reform process 'over the last few years'.<sup>337</sup>

Perceptively, Wales sees both the Pre-Budget Report (PBR), and the Budget Report itself, not as part of the legislative process, but as part of the process, the 'political' process, of presenting reform proposals to the electorate.<sup>338</sup> It is certainly possible to infer that one effect of combining successive announcements of increases in economic growth with publishing decisions on corporate tax reform, has been that the former has energised the latter. In other words, that the combined announcements on either occasion are a crucial way of building up HMG's capacity in relation to taxation policy. Whilst the IFS document takes the PBR as the start of the legislative process,<sup>339</sup> Wales's analysis of its significance as a presentational one therefore seems the more persuasive. It also, somewhat paradoxically, squares with the more general idea that Parliament is not 'a learned society'.<sup>340</sup> Wales is surely right, too, in his premise as to the administrative significance of the presentation stage. In terms of the requirements of representative government, confronting the electorate with the legislation itself has a crucial importance. Manin regards the interaction of Parliament with the world outside as being a function of whether our current system is viewed primarily

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<sup>335</sup> House of Lords Select Committee on Economic Affairs, *4<sup>th</sup> Report. The Finance Bill 2007, Volume II: Evidence* (House of Lords Papers, Session 2006-2007, 121) (London: TSO, 2007), p. 5.

<sup>336</sup> See Wales, n. 7 above, p. 548.

<sup>337</sup> *Ibid.*, p. 550.

<sup>338</sup> *Ibid.*; see also Lipsey, n. 58 above, ch. 7 (esp. pp. 120, 130).

<sup>339</sup> See Tax Law Review Committee, n. 187 above, para. 4.1.

<sup>340</sup> See Manin, n. 1 above, p. 190.

as a ‘party democracy’, or as an ‘audience democracy’.<sup>341</sup> If the former, then there is a sense in which the law is ‘handed down’ to the people most closely affected by the reform measure in question. If the latter, then, ‘[t]he extra-parliamentary voice of the people ... made ... more peaceful and rendered commonplace’,<sup>342</sup> there is a sense in which it is ‘passed across the table’. As already suggested, the UK’s system now has features both of ‘party democracy’ and ‘audience democracy’, and much may depend on the potential for conflict suggested by the measures in question. Measures within the anti-avoidance theme, especially when previously unannounced, fall into the former category, with matters in the accounting theme falling into the latter. It would be tempting to push the point too far but, as will become apparent from the next chapter, to the extent that anti-avoidance measures purport to further a particular, and contentious, concept of fairness, they bear the hallmark of party democracy, one that is held up for inspection by a constituency more used to being treated with a degree of respect.

In either case, judging what prudence requires, in terms of ‘a more detailed engagement between officials and ... [taxpayers]’, or ‘ministerial visits and speeches’,<sup>343</sup> is clearly of crucial importance. It may be a prudence of a lesser scope, involving conversation and dialogue, but it too has the objective of advancing the public interest.

#### DELIVERY OF REFORM MEASURES

With this final stage in the evolution of corporate tax reform measures, the spotlight falls, in administrative terms, exclusively on the contribution of the junior Department to H.M.

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<sup>341</sup> See Chapter 2 above, nn. 203-204.

<sup>342</sup> See Manin, n. 1 above, p. 231.

<sup>343</sup> See Wales, n. 7 above, p. 550.

Treasury, HMRC. We are here edging towards the parameters of the study, but we can nonetheless comment usefully on one or two aspects.

An experiential and practical stage,<sup>344</sup> the chief element here is ‘the issue of detailed guidance for taxpayers and the revenue department’s own network’.<sup>345</sup> It is therefore where the technical theme comes into its own, but it may also involve, as Wales mentions, ‘audit and investigation’ in the case of a new anti-avoidance measure.<sup>346</sup> Furthering the public interest, as sanctioned by Parliament, can indeed be the only justification for time spent in audit, or in settling HMRC guidance documents, and without which, it is to be suspected, the system would not work. It still involves management, though, and with this a certain prudence, since it entails engaging with the practising tax profession. Delivery involves myriad prudential calculations about the priorities and interests of professional society (who, after all, have mortgages and school fees to pay),<sup>347</sup> as well as the standing of the legal and accountancy professions in society. The former is the subject of a considerable literature; the taxation context of the latter is beginning to be noted.<sup>348</sup> Tax professionals’ expertise is at one and the same time useful to the Department, and mystifying to people in general. The professionals themselves, though often despised at a societal level, are valued by those who understand what they do. These factors together are the raw materials of prudential calculation.

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<sup>344</sup> *Ibid.*, p. 551.

<sup>345</sup> *Ibid.*

<sup>346</sup> See Wales, n. 7 above, p. 551.

<sup>347</sup> See Harold Perkin, *The Rise of Professional Society: England since 1880* (London: Routledge, 1989), pp. 457, 461-462 (1960s to 1980s); Harold Perkin, *The Third Revolution: Professional elites in the modern world* (London: Routledge, 1996), p. 210 (of the 1990s); more generally, Richard Sennett, *The Corrosion of Character: The Personal Consequences of Work in the New Capitalism* (New York: W.W. Norton, 1998), ch. 3, esp. pp. 52-53; and Jeff Schmidt, *Disciplined Minds* (Oxford: Rowman and Littlefield, 2000), ch. 13.

<sup>348</sup> See Erica Stary, ‘The March of the Tax Profession’ [2006] BTR 249-266.

We might finally note that, although the fourth stage is largely the province of HMRC, the judiciary's role, in interpreting and applying corporate tax legislation to specific cases, can most usefully be considered in this light. The importance of judicial prudence in this area has already been discussed in detail,<sup>349</sup> and the writer has analysed elsewhere its crucial role in sustaining a consistent vision of the public interest in particular (and rare) cases where the ECJ (but not, at the relevant time, Parliament) has had an opportunity to intervene.<sup>350</sup> There is no need here to rehearse the details of *William Grant*<sup>351</sup> or *Barclays Mercantile*,<sup>352</sup> in the House of Lords, or *Marks and Spencer* before Park J.<sup>353</sup> or the Court of Appeal.<sup>354</sup> What each decision demonstrates, however, is a clear grasp, on the judges' part no less than that of HMG, to make prudent decisions in the public interest, in 'delivering' tax policy in particular areas.

#### SOME CONNECTIONS

We are now at the stage of the analysis of 'theory' and 'values' in the reform of corporation tax, to make some important interpretative connections. Specifically, it is possible to overlay Chapter 2's examination of institutional claims to trust and confidence with aspects of the current chapter's discussion of how the process of reforming corporation tax may inspire these essential elements of sovereignty in the corporation tax context.

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<sup>349</sup> See Chapter 2 above, pp. 137-146.

<sup>350</sup> See Snape, n. 64 above, pp. 399-400.

<sup>351</sup> See *Revenue and Customs Commissioners v. William Grant and Sons Distillers Ltd; Small (Inspector of Taxes) v. Mars UK Ltd* [2007] UKHL 15; [2007] STC 680.

<sup>352</sup> See *Barclays Mercantile Business Finance Ltd v. Mawson (Inspector of Taxes)* [2004] UKHL 51; [2005] STC 1.

<sup>353</sup> See *Marks and Spencer plc. v. Halsey (Inspector of Taxes)* [2006] EWHC 811 (Ch); [2006] STC 1235 (Park J.).

<sup>354</sup> See [2007] EWCA Civ 117; [2007] 2 CMLR 21.

Just as the physical manifestations of the institutions involved in corporation tax reform might present themselves vividly to the interested observer, especially in the spring sunshine, so the ways in which they interact in the reform process remain, by comparison, rather dark. Various, generic, explanations are possible, an obvious one being a Luhmannian systems theory analysis. In the preceding pages, however, we have sought to find the thread of an historically informed interpretation, based on the idea of corporation tax law as a species of ‘political jurisprudence’.<sup>355</sup> From such a perspective, it has been essential to uncover what the ‘political’ element in the reform of corporation tax might be. This chapter has sought to characterise that element, in a word, as ‘conflict’, or at least as the constant potential for conflict, and, following Loughlin, the policy-making process has been portrayed as being, to a very high degree, a demanding process of managing conflict, in the intellectual tradition of Hobbes and of Machiavelli. And it has done so in the context of the seven themes introduced at the beginning of the study. It is thus that, in examining the values immanent to the corporation tax base, in Chapter 4, we may expect to find, as mentioned in Chapter 1, ‘signs of conflict averted’, in the very textures of the corporation tax code itself. It is thus, too, as Chapter 4 explains, that we can expect to find values, not of a distinctively ‘legal’ nature (except to the extent that they live within the rules and exceptions embodied in the corporation tax code itself), but of a political kind, in the sense delineated above.

If we can expect the corporation tax base to be characterised by the skilful prioritisation of political values, we can anticipate, too, that it will embody a particular vision, or visions, of the public interest. Chapter 3 has sought to show that, understated as it is in debates on corporation tax reform, the importance of the public interest is heavily underscored by the present study’s conception of corporation tax law as a type of ‘political practice’, as that term

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<sup>355</sup> See Loughlin, n. 17 above, p. 134.



is applied to public law in general, in Loughlin's functionalist account of what public law involves. Chapter 4 will therefore illustrate, in cumulative fashion, how the corporation tax base embodies a particular ideology of the relationship between state and corporate sector. Taken together, Chapters 3 and 4 demonstrate tellingly how, within the kind of functionalist critique undertaken in this study, public law can embody no public interest separate from political choices. Whilst it is certainly possible to argue that things should not be falling out in this way, it cannot sensibly be contended that the existing state of affairs represents a domination of government by the corporate sector. There is not, in any sensible interpretative sense, a 'corporate takeover of Britain'.<sup>356</sup> What there is, instead, is an ideological consensus in which strong economic growth is a core element, perhaps the main element, of the public interest.

The truth of the idea that the shape of the corporation tax base represents conscious political choices, and that it is a reasonably accurate depiction of the contribution of the corporate sector to the UK's representative democracy, is illustrated both by the stages of the reform process analysed in the current chapter, and by the values disclosed by the corporation tax code itself. This is because the four stages described by Wales, and their prudential management, embody an idea of the appropriate role of corporate taxation within the UK's representative democracy.

Imagine a picture projected onto a screen, and built up in stages, by the use of images on transparent slides. Placed over the insights offered in Chapter 2, to build up a picture of the corporation tax system of which Chapter 4 forms the final layer, Chapter 3 has sought to illuminate exactly why it is that, despite political controversies, the system still has the capacity to inspire a high degree of trust and confidence. It is therefore quite misleading to

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<sup>356</sup> See Chapter 2 above, n. 407.

opine, as William E. Simon once did, that ‘the nation should have a tax system which looks like someone designed it on purpose’.<sup>357</sup> There is not one purpose, but many; and they are worthy of respect as the outcomes of conscious political choices, of prudential decisions in a complex world.

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<sup>357</sup> See David F. Bradford *et al.*, *Blueprints for Basic Tax Reform*, 2<sup>nd</sup> edn (Arlington, Va.: Tax Analysts, 1984).

## Chapter 4

### THE EVOLVING CORPORATION TAX BASE

#### PROLOGUE

At the end of the previous stage of the discussion, the reader was asked to imagine each chapter of the study as if it were a transparent slide, on which were depicted successive aspects of a progressively fuller interpretation of the material. Each ‘slide’, it is hoped, has added some greater light or shade, or some subtler, some more delicately etched, detail, to an ever more finished picture. This fourth chapter, which forms the picture’s ‘top layer’, is concerned with the theory and values immanent to the corporation tax base, or to the corporation tax code, at a particular point in its recent history.<sup>1</sup> We take ‘the corporation tax code’, a deceptively tidy expression, to refer (as elsewhere in the study) to non-statutory material, as well as to the legislative texts themselves.<sup>2</sup>

In characterising the subject matter in this way, these two terms, ‘the code’, and ‘the base’, although capable of signifying rather different concepts, are alike in at least one significant respect: to the extent that the corporation tax base – what is, and what is not, taxed – is constructed by the legislative code (and constitutional expectations insist that this will be the case),<sup>3</sup> then, rationally, the theory and values immanent to one will correspond to

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<sup>1</sup> i.e. 29 February 2008.

<sup>2</sup> Consolidated in, e.g., *The Red Book*, ed by Loughlin G. Hickey and David Milne, 6 vols (Kingston-upon-Thames: Wolters Kluwer, 2007): see Chapter 2 above, n. 8.

<sup>3</sup> See Chapter 1 above, n. 337; Chapter 2 above, nn. 197-200.

those immanent to the other. However, without relying on an explicit distinction between substance and form, there is still considerable merit in concentrating for certain purposes on the code, on the printed page, on the form taken by the constitutive elements of corporation tax. This is because much discussion of the reform of the tax has concentrated on the volume, on the changeability, and on the extreme ‘complexity’, of corporation tax legislation.

Whilst the reader is urged to engage with the pictorial element in the discussion, such an intellectual embrace should be mindful of one, crucial, point: the fleetingness of the picture presented. The discussion in Chapter 3 has illustrated how, following the logic of prudential government, much corporation tax reform is reactive. Here, in Chapter 4, it is necessary to bring out the fast moving, electronic, and often ‘closed’ nature of the economic activities the aggregate gains on which the system seeks to tax.<sup>4</sup> All relevant commentaries give prominence to the speed of financial markets in general, and the pace of change in the City of London’s markets in particular.<sup>5</sup> It is the work of moments, for instance, for Layna Mosley’s Goldman Sachs-based bond trader or the fund manager working at Fidelity, sitting in front of her computer screen, to allocate investments to one jurisdiction rather than to

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<sup>4</sup> See ICTA 1988, ss. 15 (Schedule A) and, more importantly, 18 (Schedule D); generally, see Ken Messere, Flip de Kam and Christopher Heady, *Tax Policy: Theory and Practice in OECD Countries* (Oxford: Oxford University Press, 2003), pp. 115-117; on radical reform, see Stephen R. Bond, ‘Levelling up or levelling down? Some reflections on the ACE and CBIT proposals, and the future of the corporate tax base’, in *Taxing Capital Income in the European Union: Issues and Options for Reform*, ed. by Sijbren Cnossen (Oxford: Oxford University Press, 2000), pp. 161-179, 172-175.

<sup>5</sup> See, e.g., Mike Buckle and John Thompson, *The UK Financial System: Theory and Practice*, 4<sup>th</sup> edn (Manchester: Manchester University Press, 2004), pp. 149-151 (‘electronic trading’); William M. Clarke, *How the City of London Works: An Introduction to its Financial Markets*, 6<sup>th</sup> edn (London: Sweet and Maxwell, 2004), pp. 12, 120-125; David Kynaston, *The City of London, vol. IV: A Club No More, 1945-2000* (London: Chatto and Windus, 2001), ch. 22; Richard Roberts, *The City: A Guide to London’s Global Financial Centre* (London: Profile, 2004), ch. 3; William E. Scheuerman, *Liberal Democracy and the Social Acceleration of Time* (London: Johns Hopkins University Press, 2004), pp. 5, 159-164.

another.<sup>6</sup> Not only that, but she has an increasing range of financial instruments at her disposal for hedging against investment risks.<sup>7</sup> More generally, however, we know that multinational corporations (MNCs) have the capability, if commercial considerations so dictate, to move operations relatively quickly from one country to another, and that they, too, can hedge in ever more elaborate ways against currency and interest rate risks. Thus, in looking for the theory and values immanent to the corporation tax code, we need to be mindful of the dimension of impermanence, occasioned by the need to respond to a rapidly changing financial and commercial reality. Indeed, it is possible to assert with some cogency that a tax that relies so fundamentally on concepts of ‘residence’, ‘source’, and ‘profits’, is uniquely vulnerable, in a world of instantaneous, or at least very rapid, investment decisions, and largely without exchange controls.<sup>8</sup>

If impermanence is, paradoxically, the one constant feature of the corporation tax code, so too is what the code says about how taxation legislation consolidates political power, that is, sovereignty,<sup>9</sup> in this particular area of public policy. An important question in what follows is therefore how, despite the charges of change and of complexity, corporation tax legislation remains effective, and the ways in which, for the most part, it continues to command trust and confidence from those affected by it. Equally important, however, are the ways in which certain features of the code tend to undermine that trust and confidence. Recent debates on corporation tax reform have understandably tended to focus on the latter rather than on the former.

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<sup>6</sup> See Layna Mosley, *Global Capital and National Governments* (Cambridge: Cambridge University Press, 2003), p. 25; see Chapter 2 above, n. 174.

<sup>7</sup> See Buckle and Thompson, n. 5 above, chs 13 and 14; Clarke, n. 5 above, ch. 13; Roberts, n. 5 above, p. 73.

<sup>8</sup> See H.M. Treasury, *Reforming Britain's Economic and Financial Policy: Towards Greater Economic Stability*, ed. by Ed Balls and Gus O'Donnell (Basingstoke: Palgrave, 2002), p. 35; also Bond, n. 4 above, pp. 171-172.

<sup>9</sup> See Chapter 2 above, nn. 47-57.

What Chapter 3 depicted was the ongoing, dynamic, interaction of the institutions whose objectives and values had been discussed in Chapter 2. Shaping the discussion in this way has allowed the emergence of some important, evolving, conclusions about the way that power – constituent power – is consolidated within this system of taxation. First, that the tensions between the corporate sector and the state have been managed in the context of a government whose ideology places a high premium on the importance of the corporate sector in promoting the public interest, and whose commercial success is *in itself* part of that public interest. Chapter 3 afforded various examples of this process. One, particularly telling, example, was HMG's refusal, after 1997, to reshape the foreign exchange (FOREX) rules to reflect the idea of the Tobin tax, a prospect which Alistair Darling, MP, had himself alluded to in Opposition, when the accounting-based FB 1993 provisions had reached the Committee Stage. The present chapter, in offering a snapshot of the main values in the corporation tax code at a particular historical juncture, shows how this ideology is reflected across the code as a whole, and how the politically contentious mixture of efficiency and fairness significantly contributes to dissatisfaction with the code. Secondly, Chapters 2 and 3 have shown that the premium placed on the co-operation of the corporate sector has underlined the managerial, that is to say, the governance, dimension to HMG's approach to corporation tax reform. Statecraft of this kind has been well illustrated by the use of policy communities to take the reform process forward. Chapter 4 seeks to show how, within the corporation tax code itself, there is much evidence of this managerial approach. A major example, already referred to in various connections, is the use of accounting terminology and concepts, in the drafting of the special codes on the tax treatment of corporate finance. Thirdly, Chapters 2 and 3 have shown that, although this governing ideology, and this managerial approach, each present certain challenges to the structure of the UK's representative institutions, they also

display to advantage the historical strengths of those institutions. Despite the ‘gaps’ in the possibilities for bringing responsible individuals before the House of Commons Treasury Select Committee, and, despite the only intermittent beam that the Committee is able to bring to bear on corporation tax, some important initiatives have nonetheless been scrutinised fairly effectively. Furthermore, as Chapter 3 has shown, the debate on individual reform measures is both fuller and, within the logic of the institutional structure of representative government in the UK, more effective than some (especially, perhaps, corporate tax lawyers) may lead us to believe.

Our task in Chapter 4, therefore, is to analyse the theory of, and the main values immanent to, the corporation tax code produced by the institutions and the processes analysed earlier in the study. The theory is, as ever, about effectiveness, about prudence. Although much has been said on different aspects of this already, we shall build later on, on one or two points, as they relate to the theory. For the moment, we should briefly return to the values immanent to the code.

It will be recalled from Chapter 1 that the present study accepts that certain values are ‘immanent’ to corporation tax law. They are political, not ‘rule of law’ values, and they are to be discerned by close examination of the legislative texts and policy documents, bringing to bear a sense of historical awareness, an acute sense of what is coherent, what is non-contradictory, and what is consistent.<sup>10</sup> This is Loughlin’s critical method, based on Isaiah Berlin,<sup>11</sup> and traceable ultimately to the immanent critique of G.W.F. Hegel:<sup>12</sup>

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<sup>10</sup> See Chapter 1 above, p. 68.

<sup>11</sup> See Isaiah Berlin, ‘Does political theory still exist?’, in *The Proper Study of Mankind: An Anthology of Essays*, ed. by Henry Hardy and Roger Hausheer (London: Pimlico, 1998), pp. 59-90, 76.

‘Immanent critique [says Loughlin] stems from a philosophical idealism which tries to examine experience in a coherent and comprehensive manner in order to reveal the logic and rationality immanent in this experience ... truth always lies ahead; at any moment it is immanent but never realised.’<sup>13</sup>

We are looking, therefore, for how the practice of corporation tax law, as embodied in the corporation tax code, and given the overwhelming need for effectiveness (something discussed below) shapes and prioritises, in particular cases, the values immanent to this area of law. As Loughlin says, elsewhere, we are therefore developing an ‘explanatory framework’, with a view to revealing ‘the value of assumptions, the causal relations and the dominant features’ of corporation tax law as a political practice.<sup>14</sup>

Different aspects of the same four strands as those that occurred in previous chapters therefore appear in Chapter 4. Thus, rather than HMG’s liability to account for the success or failure of its corporation tax reform measures, and instead of HMG’s right of legislative initiative, we are concerned with how, and how far, the corporation tax code reflects the state’s pre-eminence. Secondly, we are interested, not in the formal constraints on corporation tax reform spelt out in the European Treaty, but in how the corporation tax code and its accompanying policy statements, reveals an intergovernmentalist<sup>15</sup> view of the relationship of the UK’s corporation tax base with those of the rest of Europe, and also with those of OECD and GATT 1994/WTO members. Thirdly, we are concerned, not with how

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<sup>12</sup> See Dudley Knowles, *Hegel and the Philosophy of Right* (London: Routledge, 2002), pp. 71-73; Martin Loughlin (1988) 51 MLR 531-548 (‘Review Article’), p. 533, quoting Berlin, n. 11 above, p. 76; also Chapter 2 above, n. 72.

<sup>13</sup> See Loughlin, n. 12 above, pp. 533-534, quoting Hegel’s *Philosophy of History*; this is different, he points out, from the immanent critique developed by the Frankfurt school (*ibid.*, pp. 535-536).

<sup>14</sup> See Martin Loughlin, *Public Law and Political Theory* (Oxford: Clarendon Press, 1992), p. 35; also Martin Loughlin, ‘Theory and Values in Public Law: An Interpretation’ [2005] PL 48-66, 59.

<sup>15</sup> See Alan S. Milward, *The European Rescue of the Nation-State*, 2<sup>nd</sup> edn (London: Routledge, 2000), ch. 1; John Snape, ‘Corporation Tax Reform – Politics and Public Law’ [2007] BTR 374-404, *passim*; Michelle Cini, ‘Intergovernmentalism’, in *European Union Politics*, ed. by Michelle Cini (Oxford: Oxford University Press, 2003), pp. 93-108; Hansard HC Standing Committee A,



the processes of reform augment or detract from confidence in the tax, but with the role of the code in mediating the relationship between HMG and the corporate sector, and possibly with society more widely. The final strand, therefore, in the discussion is the extent to which the form and content of the corporation tax code militates in favour of, or against, its effectiveness.

### ECONOMICS, REALISM AND POLITICS

The aim of the present chapter is to develop the implications of the idea that it is the public law status of the corporation tax code that dictates its constant propensity for change, its complexity, and the prioritisation of the political values within it. Given the nature and role of public law, as ‘a set of practices concerned with the establishment, maintenance and regulation of the activity of governing the state’,<sup>16</sup> whose ‘even handedness’ helps to ‘create intimacy, shape identity, generate trust, and strengthen allegiance’,<sup>17</sup> it would indeed be surprising if corporation tax law did not respond to the commercial and financial developments sketched out above.<sup>18</sup> It is the contention of this study that much, if not most, of the scholarly writing on corporation tax, fails, for one reason or another, to take sufficient account of this point. Some reference was made to this state of affairs in Chapter 1 above,

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16 May 2006, col. 166 (Mark Hoban, MP (Fareham, Conservative)) and col. 167 (Rob Marris, MP (Wolverhampton South-West, Labour)); also Rifkind, *Financial Times*, 13 December, 2006, 15.

<sup>16</sup> See Loughlin (2005), n. 14 above, p. 58; see Chapter 1 above, n. 317.

<sup>17</sup> See Martin Loughlin, ‘Constitutional Law: the Third Order of the Political’, in *Public Law in a Multi-Layered Constitution*, ed. by Nicholas Bamforth and Peter Leyland (Oxford: Hart Publishing, 2003), pp. 27-51, 40-41; see Chapter 1 above, n. 325.

<sup>18</sup> See Hansard HC Public Bill Committee, 17 May 2007, col. 216 (Ed Balls, MP, Economic Secretary to the Treasury); also the Rt Hon. Gordon Brown’s Foreword to H.M. Treasury and Inland Revenue, *Large Business Taxation: The Government’s strategy and corporate tax reforms: A consultation document* (London: H.M. Treasury, 2001).

where it was contended that the theoretical discussion of corporation tax tends primarily to be of an economic nature.<sup>19</sup>

To redress the imbalance somewhat, the chapter unfolds in a sequence designed to illustrate the importance of recognising the public law nature of the corporation tax code; the implications of this for the code's 'complexity' and 'instability'; and the consequences of its public law nature for the values that the corporation tax code embodies, and their prioritisation in particular areas. It is therefore important to be clear, both about the nature of the economics learning on corporation tax, and the strengths and limitations that it presents for the issues under consideration in the chapter.

The first, possibly the most important, point, to be made about the economic analysis of corporation tax, is that it has a strongly 'normative' character. This comment might seem surprising to an economist of taxation. James and Nobes, for example, in their classic study, say, when discussing fairness in taxation, that economists 'are inclined to leave the definition of equity to others', since they 'are trained from an early age to steer clear of normative arguments'.<sup>20</sup> Two points can be made about this claim. First, that the term 'normative' is not, as it is in the present study, set up in disjunction with 'functionalist'.<sup>21</sup> James and Nobes may not, in other words, have thought through the possible range of connotations of the term that they are invoking. Secondly, and more importantly, there are grounds for believing that, try as they might, economists do think in normative terms when they write about taxation.<sup>22</sup> Normativism in the study of public law, and as used in this study, is 'rooted in a belief in the

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<sup>19</sup> See Chapter 1 above, n. 94.

<sup>20</sup> See Simon James and Christopher Nobes, *The Economics of Taxation: Principles, Policy and Practice*, 7<sup>th</sup> edn (Harlow: Financial Times Prentice Hall, 2000), p. 78.

<sup>21</sup> See Chapter 1 above, n. 274.

<sup>22</sup> See Liam Murphy and Thomas Nagel, *The Myth of Ownership* (Oxford: Oxford University Press, 2000), p. 136.

ideal of the separation of powers and in the need to subordinate government to law'.<sup>23</sup> In economics, as in public law, at least as far as its liberal variant is concerned, one of the chief advocates of normativism has been F.A. Hayek.<sup>24</sup> In the study of economics, Gunnar Myrdal has associated it with the making of unwarranted assumptions about what taxation should and should not seek to achieve.<sup>25</sup> Allowing for the vintage of Myrdal's work, and also for the intellectual tradition to which it belongs,<sup>26</sup> we may nonetheless concede that he has a point.<sup>27</sup> These judgments are unwarranted in the sense that they are neither the outcome of an ideological struggle, nor are they based on intense empirical observation of the incidence of taxes.<sup>28</sup> What they have in common with the normative tradition in public law is that they clearly separate economics from both the politics and the law disciplines, and close off a more profound, distinctively political, debate, about what the tax system is actually *for*. There are many examples of such attempts.<sup>29</sup> So, in 1978 and 1982 respectively, the Meade Committee<sup>30</sup> and the authors of the Green Paper on corporation tax reform,<sup>31</sup> each wondered whether bringing in a 'flow-of-funds' corporation tax would make taxing corporate profits

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<sup>23</sup> See Chapter 1 above, n. 270.

<sup>24</sup> See Chapter 1 above, n. 263.

<sup>25</sup> See Gunnar Myrdal, *The Political Element in the Development of Economic Theory*, trans. by Paul Streeten (London: Routledge and Kegan Paul, 1953), ch. 7.

<sup>26</sup> It is referred to with approval by Hannah Arendt (in *The Human Condition*, 2<sup>nd</sup> edn (Chicago: University of Chicago Press, 1998), p. 44n), and his work more generally by Joseph A. Schumpeter, in *History of Economic Analysis*, ed. by Elizabeth Boody Schumpeter (London: George Allen and Unwin, 1954), p. 1173.

<sup>27</sup> See Daniel M. Hausman and Michael S. McPherson, *Economic analysis and moral philosophy* (Cambridge: Cambridge University Press, 1996), pp. 211-220.

<sup>28</sup> See Myrdal, n. 25 above, pp. 185-186; also Greenspan's engaging idea of Adam Smith's lucky guess (see Alan Greenspan, *The Age of Turbulence: Adventures in a New World* (London: Allen Lane, 2007), pp. 262-263).

<sup>29</sup> See John Tiley, *Revenue Law*, 5<sup>th</sup> edn (Oxford: Hart Publishing, 2005), pp. 815-823.

<sup>30</sup> See *The Structure and Reform of Direct Taxation: Report of a Committee chaired by Professor J.E. Meade*, ed. by J.E. Meade (London: George Allen and Unwin, 1978), ch. 12.

<sup>31</sup> See *Corporation Tax: Presented to Parliament by the Chancellor of the Exchequer by Command of Her Majesty January 1982* (Cmnd 8456) (London: HMSO, 1982), ch. 7.

more neutral. Again, in 1991, the Institute for Fiscal Studies (IFS)<sup>32</sup> suggested improving neutrality by the making of an ‘allowance for corporate equity’ (an ACE)<sup>33</sup> in the taxation of corporate profits.<sup>34</sup> Even now, a working group of the European Commission is considering the advantages of a ‘common consolidated corporate tax base’ (a CCCTB) for Europe. Intellectual feats though each of these are, they do not help us to interpret the process of corporation tax reform. At the very most, they tend to betray the ideological stance of their progenitors, a point to which we return below.

The second point that might be made about the economic analysis of corporation tax is that it lacks a certain realism, a charge that can certainly not be levelled against the interpretative turn in political writing. It is impossible to illustrate this point more vividly than by reference, not to academic writing, but to the rich and illuminating memoirs of Lord Lawson of Blaby, who, as the Rt Hon. Nigel Lawson, MP, was Chancellor of the Exchequer in the early years of the Thatcher administration, and who had been responsible for commissioning the 1982 Green Paper referred to above. He describes how, whilst admiring the intellectual beauty of its recommendations, he had contemplated with horror the political consequences of proceeding down that line:

‘We [Lawson and Arthur, later Lord, Cockfield]<sup>35</sup> looked into the theoretically attractive switch from an income tax to an expenditure tax system, and had a long session with

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<sup>32</sup> See Institute for Fiscal Studies, Commentary No. 26, *Equity for Companies: A Corporation Tax for the 1990s: A Report of the IFS Capital Taxes Group chaired by Malcolm Gammie* (London, 1991), developing arguments made in Michael Devereux and Harold Freeman, ‘A General Neutral Profits Tax’ (1991) 12:3 FS 1-15.

<sup>33</sup> See John R. King, ‘Debt and Equity Financing’, in *Tax Policy Handbook*, ed. by Parthasarathi Shome (Washington, DC: IMF, 1995), pp. 158-161, 161; also Bond, n. 4 above, *passim*.

<sup>34</sup> See Bond, n. 4 above, pp. 164-169.

<sup>35</sup> Cockfield was a distinguished official, who had been a Commissioner of Inland Revenue between 1951-1952, and who eventually became an EC Commissioner, before quarrelling with Margaret Thatcher (see Nigel Lawson, *The View from No. 11: Memoirs of a Tory Radical* (London: Bantam Press, 1992), pp. 17, 22, 31, 35-36, 336, 894-898; *WW*; Margaret Thatcher, *The Downing Street Years* (London: HarperCollins, 1993), p. 547).

Professor James Meade, its foremost exponent, but (in my view rightly) shrank from the upheaval and practical problems that would have been involved.’<sup>36</sup>

Lawson, in many respects an extremely successful practitioner of the ‘art and science of government’, collides beautifully in this extract with the ‘Aristotelian’ mindset of the economist, the mentality Lady Thatcher so famously resented in the Whitehall civil service.<sup>37</sup> There is no need to elaborate further on this here; suffice it to say that, insofar as they pinpoint the gulf ‘[b]etween the idea [a]nd the reality’,<sup>38</sup> the cleavage between the Aristotelian and the Platonic view of politics,<sup>39</sup> Lawson’s comments remain as relevant today as they were in the 1980s.

The third point that we can make about the economics writing is that, as an enterprise of political economy, the very technicality of corporation tax reform tends to remove its difficulties from public debate, despite the fact that, as shown in Chapter 3, the most important corporation tax issues are eminently political.<sup>40</sup> To the extent that corporation tax reform thereby becomes the province of experts, of technocrats,<sup>41</sup> it is a neat illustration of the range and importance of the issues that, given the involvement of policy networks, and the vagaries of the Select Committee system, are outside effective parliamentary scrutiny. It is not necessary to develop this point here, since the accountability issues raised have already been discussed.<sup>42</sup> All that it is necessary to affirm at this stage is that the inaccessibility of

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<sup>36</sup> See Lawson, n. 35 above, p. 17 (also 344-345).

<sup>37</sup> See Thatcher, n. 35 above, p. 46 (although Thatcher does not herself identify this mindset as ‘Aristotelian’).

<sup>38</sup> See T.S. Eliot, ‘The Hollow Men’, in *Collected Poems 1909-1962* (London: Faber and Faber, 1974), pp. 91-92.

<sup>39</sup> See Cleinias’s recognition of the potential for strife, and the legislator’s response, in the state of Crete (Plato, *The Laws*, ed. by Trevor Saunders (London: Penguin, 2004), pp. 5-6 (discussed in Martin Loughlin, *The Idea of Public Law* (Oxford: Oxford University Press, 2003), p. 34n).

<sup>40</sup> See Chapter 3 above, p. 164; also Snape, n. 15 above, p. 382.

<sup>41</sup> See Chapter 3 above, n. 241.

<sup>42</sup> See Chapters 2 (*ex post*) and 3 (*ex ante*) above.

the relevant policy material, together with its potentially influential nature, can hardly be regarded as a contribution to prudential governance.

The final point is linked to the point made above about the normative nature of much of the economics writing. It is also, so far as it draws in questions of legislative simplicity, relevant to the concerns about ‘complexity’, ‘instability’ and ‘the rule of law’ discussed below. This is part at least of the point made by Jürgen Habermas, that, once policy issues become characterised as ones of political economy, ‘the category of law ... [loses] its central role in theoretical analysis’.<sup>43</sup> Although this may serve as a lament for scholars whose ‘home discipline’ is law, it is much more important than this, for two reasons: first, it means that the usefulness of the economics literature for the lawyer is diminished by its understatement of the crucial importance of law; and, secondly, which is a related point, it involves assumptions about the nature of law, and of legal studies, which, in the light of trends in public law scholarship, are increasingly unjustifiable.

Aspects of each of these four points inform the developing discussion in the present chapter. Our attention turns first to the expansion, in the light of these comments, of elements of the theory of public law, as it relates to corporate taxation. This is a fuller examination of why the values of the corporation tax code are political values, and why, and how, the code must be analysed as a manifestation of a ‘political practice’. The discussion is illustrated by reference to a number of cases in which the public law nature of the judicial technique in tax law cases has been in evidence. The issues are related to, and shaped by, the governance issues raised in Chapter 2, and the portrayal of the political dimension to corporation tax reform offered in Chapter 3. What it is sought to stress is the theory of effectiveness, and the paramount status of the technique of prudence.

From an elaboration of the public law nature of the corporation tax code in the first part of the chapter, the second part moves to a consideration of the implications of this characterisation of corporation tax law for what is ubiquitously, but inaccurately, referred to as ‘the rule of law’. The contention here is that much of the debate on corporation tax reform misses the significance of legitimate divergences of opinion on the nature and consequences of ‘the rule of law’,<sup>44</sup> and the implications of this for ‘complexity’ in the code, as well as for perceptions of its ‘instability’. Unless we move beyond these outdated and unrealistic, Hayekian, preconceptions, it is argued, we shall never properly be able to understand what is going on, nor assess the viability of routes to improvement.

The foregoing lays the groundwork for the extended discussion of the values immanent to the changing corporation tax code, in the third and final part of the chapter. This consists of extended, and complementary, analyses of the values of efficiency and fairness. What vision of each of these terms does the code embody? How far are these values and their prioritisation a reflection of the institutions and processes discussed in Chapters 2 and 3? What are the strengths and weaknesses of the concepts thus deployed? Why, despite everything, do they seem in reality, just now, to be fairly robust? As a basis for shedding light on these issues, in the rest of the third part of the chapter, there is an extended discussion of the importance of a theory of effectiveness in giving shape and content to the values themselves.

We continue, therefore, by building outwards the implications of the idea of corporation tax as public law, with the aims suggested above firmly in mind.

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<sup>43</sup> See Jürgen Habermas, *Between Facts and Norms*, trans. by William Rehg (Cambridge: Polity Press, 1997), p. 45.

<sup>44</sup> See *Deutsche Morgan Grenfell Group plc v. Inland Revenue Commissioners and the Attorney General* [2006] UKHL 49; [2007] STC 1, 41h-42c (Lord Walker of Gestingthorpe).

## FURTHER IMPLICATIONS OF THE PUBLIC LAW NATURE OF CORPORATION TAX

Previous chapters have emphasised that, properly understood, corporation tax law is to be seen as a form of public law. The truth of this contention is apparent, not only from the fact that taxation in general is the exercise of one of the most fundamental ‘prerogatives of the state’,<sup>45</sup> but also from the essentially political nature of the issues with which it has, as a ‘practice of politics’, to contend. In the next several pages, it is sought to justify the importance of this argument in understanding the textures of the corporation tax code itself, especially in the light of the nineteenth and twentieth century hostility of English lawyers<sup>46</sup> and political philosophers<sup>47</sup> to any distinction between public and private law.<sup>48</sup> In making out this justification, we follow Loughlin’s discussion of public law ‘method’,<sup>49</sup> reflecting on the specific implications of that method for the reform of corporation tax law.

First and foremost, the corporation tax code is more than a highly detailed, and extremely complicated, collection of what Loughlin refers to as ‘the edicts of the supreme authority in the state’.<sup>50</sup> It is that, of course, since, as was mentioned above, it is, like all effective UK tax legislation, a manifestation of the pre-eminence of the state, and its representative, the Crown in Parliament (i.e. HMG). ‘Juridification’,<sup>51</sup> what Loughlin calls (drawing on Habermas) ‘the

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<sup>45</sup> See Chapter 2 above, n. 43. The judges of the Council of Europe have evidently read their Bodin (see *Ferrazzini v. Italy* [2001] STC 1314); Oliver, QC, evidently has not (see *N. Ali and S. Begum and Others v. Commissioners of Customs and Excise* [2002] VATDT No. 17681).

<sup>46</sup> Most famously, of course, Dicey and Lord Hewart: see A.V. Dicey, *Introduction to the Study of the Law of the Constitution*, ed. by E.C.S. Wade, 10<sup>th</sup> edn (London: Macmillan, 1965), pp. 202-203; the Rt. Hon. Lord Hewart of Bury, *The New Despotism* (London: Ernest Benn, 1929), chs 3 and 4.

<sup>47</sup> See Michael Oakeshott, *On Human Conduct* (Oxford: Clarendon Press, 1975), p. 151.

<sup>48</sup> See Chapter 1 above, pp. 38-39.

<sup>49</sup> See Loughlin, n. 39 above, ch. 8.

<sup>50</sup> *Ibid.*, p. 131.

<sup>51</sup> *Ibid.*



tendency to conceptualize extensive spheres of public life in legal terms',<sup>52</sup> will not help us to see what this extra dimension might be, since it underestimates 'the social dimension' of the 'normative authority'<sup>53</sup> contained within the highly detailed prescriptions of the code. Neither, Loughlin would argue, will certain reactions to juridification, namely the (liberal) normativism of Habermas and of Dworkin,<sup>54</sup> help us to identify this additional quality. Each of these (albeit for very different reasons) underestimates the distinctiveness of public law, and is 'unable to supply critical standards against which governmental action is to be measured'.<sup>55</sup> It is, we may infer, the Aristotelian impetus behind Habermas and Dworkin that so limits their interpretative potential when confronted with legislation such as the corporation tax code.<sup>56</sup> No, instead, the code must be analysed for what it is, as 'an aspect of political practice', part of the 'third order of the political'.<sup>57</sup> The corporation tax code is an expression, in other words, of HMG's sovereignty, its tax sovereignty, the term being used, not in the sense of competence only, but in its fullest, 'generative', sense,<sup>58</sup> sovereignty as 'capacity', as 'constituent power'.<sup>59</sup> Viewed thus, at any one stage in its detailed development, the corporation tax code marks out, with great precision and exactitude, the exercise of the sovereign power of HMG in taxing corporate income.

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<sup>52</sup> *Ibid.*

<sup>53</sup> *Ibid.*

<sup>54</sup> This does not however preclude Freedman's use of Dworkinian analysis in the context of a 'GANTIP' (see Judith Freedman, 'Defining Taxpayer Responsibility: In Support of a General Anti-Avoidance Principle' [2004] BTR 332-357).

<sup>55</sup> See Loughlin, n. 39 above, p. 132.

<sup>56</sup> But see John F. Avery Jones, 'Tax Law: Rules or Principles?' [1996] BTR 580-600; John Prebble, 'Should Tax Legislation be Written from a Principles and Purpose Point of View or a Precise and Detailed Point of View?' [1998] BTR 112-123; also Chapter 3 above, n. 245.

<sup>57</sup> Hence the present writer's comment that corporation tax reform solutions are matters of constitutional law (see Snape, n. 15 above, p. 379).

<sup>58</sup> See Chapter 2 above, n. 50.

<sup>59</sup> *Ibid.*, n. 53.

Secondly,<sup>60</sup> the corporation tax code must, in the light of the foregoing, be viewed as ‘political jurisprudence’.<sup>61</sup> This might seem worrying, as it might suggest few, if any, limitations on what the code might come to contain. This is the ‘paradox’ to which Loughlin, finding its origins in Jean Bodin,<sup>62</sup> attaches fundamental weight, however: ‘it is precisely because limits are disabling, that they are enabling’,<sup>63</sup> or, to put it another way, ‘authority is enhanced when competence is limited’.<sup>64</sup> Loughlin draws strength from Stephen Holmes’s analogy with grammar – grammatical rules enable greater clarity of expression, not less. Thus, if we look at the corporation tax code as a whole, we can draw at least three related conclusions about its status as ‘political jurisprudence’. First, especially as it consists of primary legislation, which has been tested in the *fora* analysed in Chapter 3 (i.e. expert discussion in policy communities, and ‘argumentative scrutiny’ by elected representatives of the people), it reflects the enabling power of constraint or, perhaps, restraint: ‘[P]rohibition on taxation without consultation’ is specifically identified by Holmes as a hallmark of the enabling power of institutional restraint.<sup>65</sup> We can, without doing violence to the idea, read ‘consultation’ here as encompassing, not only the consultation of Parliament, but the consultation of experts prior to the parliamentary stage. That is why Malcolm Gammie was absolutely right to focus on the absence of proper consultation (in appropriate circumstances, at least) as a major problem with tax measures of the 1980s.<sup>66</sup> Secondly, however, we can draw contrasting conclusions about those parts of the code which result from the conferring on H.M. Treasury of wide delegated powers, or measures that, even though they appear in

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<sup>60</sup> We are here following the structure of Loughlin’s argument on ‘method’ (Loughlin, n. 39 above, p. 134).

<sup>61</sup> *Ibid.*

<sup>62</sup> *Ibid.*, p. 137.

<sup>63</sup> *Ibid.*

<sup>64</sup> *Ibid.*, p. 138.

<sup>65</sup> Quoted in Loughlin, n. 39 above, p. 137.

<sup>66</sup> See Chapter 1 above, n. 48.

primary legislation, were not subject to full consultation before Parliament argued over them, in circumstances such that it would have been prudent so to do. The 1965 introduction of corporation tax itself provides interesting material for consideration, so far as this last point is concerned. Would it have been more prudent for the then Labour government to have consulted widely on its introduction,<sup>67</sup> or was the prudent course the ‘Crippsian’<sup>68</sup> one that was actually taken?<sup>69</sup> Difficult as it is to reconstruct the circumstances of the decision,<sup>70</sup> it is interesting to note that we are fast approaching the point at which every major structural feature of the 1965 tax has been reconstructed, albeit over four decades. Thirdly, although this is a point to which we return later in the chapter, with the code viewed as political jurisprudence, the complicated and detailed plethora of reliefs and exemptions begins to look as though they reflect what is politically possible, and desirable, in the furtherance of government policy.

With this concept of the corporation tax code in mind (as ‘political jurisprudence’), we can consider further the conception of law, and the purpose of law, that the code therefore embodies.<sup>71</sup> First, it is an idea of law explicitly as a means of ‘advancing the public interest’.<sup>72</sup> Full discussion of how the code seeks to do this is reserved to the last part of the chapter. For the moment, it is enough to recall the discussion of the public interest in Chapter 3, and especially the idea that the promotion of the public good will be ideological (indeed, that it has been); that the pursuit of an ideology can be an entirely legitimate objective for law; and that much of the disagreement about the pros and cons of corporation tax reform

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<sup>67</sup> *Ibid.*

<sup>68</sup> i.e. Sir Stafford Cripps (see Loughlin, n. 14 above, p. 236); Peter Clarke, *The Cripps Version: The Life of Sir Stafford Cripps 1889-1952* (London: Allen Lane, 2002), pp. 57-61.

<sup>69</sup> Ferrier (see Chapter 3 above, n. 299) states that FB 1965 was debated on the floor of the House.

<sup>70</sup> But see Kynaston, n. 5 above, pp. 300-301, 304, 307, 311-312; also Richard Holt, *Second Amongst Equals: Chancellors of the Exchequer since the Second World War* (London: Profile Books, 2002), pp. 14-15.

<sup>71</sup> We are here still following Loughlin, n. 39 above, p. 140.

fails to take proper account of this point. Secondly, the code enshrines an idea of law as what is created by the state (or its representative), that is, by ‘those forms and institutions that establish and regulate the exercise of governmental authority’,<sup>73</sup> and which create ‘conditions for maintaining state authority’.<sup>74</sup> The corporation tax code is thus the creation of the person differentiated from other persons because it is instituted ‘precisely for the purpose of creating law’;<sup>75</sup> of an established set of procedures, which help to create trust and security;<sup>76</sup> and, as Bodin says, of the state’s unique and nearly fundamental prerogative, the right to raise taxes.<sup>77</sup>

To recapitulate. We can say, even before we begin to look for the values immanent to the code, that the corporation tax code is a precise indicator of the boundaries of the sovereign power of the state to tax corporate income. Secondly, that, as such, the code is an example of political jurisprudence, whose strength is drawn, paradoxically, from the constraints under which it constantly evolves. Thirdly, that, as political jurisprudence, it is designed to further the public interest, as that idea is conceived of by ‘the government of the day’.<sup>78</sup> Fourthly, that it has been promulgated through established channels, a point the full significance of which will become apparent when we consider the code’s relationship with ‘the rule of law’. Finally, that the code represents the unique and basic power of the state, the power of levying taxes. This leaves for consideration the relevance of the final component in Loughlin’s depiction of public law method: the technique of public law that the corporation tax code

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<sup>72</sup> *Ibid.*, pp. 140-141, although he does not use the expression ‘the public interest’.

<sup>73</sup> *Ibid.*, p. 141.

<sup>74</sup> *Ibid.*

<sup>75</sup> See Chapter 2 above, n. 36.

<sup>76</sup> See Loughlin, n. 39 above, p. 142.

<sup>77</sup> See Chapter 2 above, n. 43.

<sup>78</sup> An expression also used by Gammie (see Malcolm Gammie, ‘The Process of Fiscal Reform in the United Kingdom’ [1989] BTR 252-264, 253).

illustrates.<sup>79</sup> In this study, we shall avoid detailed consideration of a possible fifth stage in the method, which is the code's relationship with morality. It is not simply that the code is an example (albeit a monumental one) of economic regulation. More fundamentally, it is that the political conditions managed by the code, and, within them, the economic conditions,<sup>80</sup> are themselves the basis of 'moral life'.<sup>81</sup> We here put aside the idea of the primacy of morality in Rawls and in Dworkin on the basis that misunderstands the reality of politics.<sup>82</sup>

This final point about the nature of the corporation tax code, what it says about the techniques of public law, is its role in managing that 'brokenness',<sup>83</sup> that potential for conflict which, throughout the study, has been taken to characterise 'the concept of the political'.<sup>84</sup> In Chapter 3, this was related to the potential for conflict that arises out of the five dilemmas of governance identified in Chapter 2.<sup>85</sup> These are potential conflicts between HMG and the corporate sector; between HMG and other EU Member States (as well as the EU institutions); and between conflicting interests within the corporate sector itself. Since there is 'no authoritative morality' through which these conflicts, or potential conflicts, can be resolved (neither Dworkin nor Rawls is in a position to help much here), we cannot expect to find either moral values, or a moral ordering of values, within the code. Instead, we find that the theory running through the code is 'reason of state',<sup>86</sup> and that its method is prudence,<sup>87</sup> albeit in juristic form. Given the objectives and values of the institutions

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<sup>79</sup> See Loughlin, n. 39 above, pp. 148-152.

<sup>80</sup> See Carl Schmitt, *The Concept of the Political*, trans. by George Schwab (Chicago: University of Chicago Press, 1996), p. 88 (note by Leo Strauss).

<sup>81</sup> See Loughlin, n. 39 above, p. 145; see Chapter 1 above, nn. 252 and 287; Chapter 3 above, nn. 74 and 149 (Rawls); Chapter 1 above, nn. 283 and 358; n. 54 above, this chapter (Dworkin).

<sup>82</sup> *Ibid.*, p. 147.

<sup>83</sup> *Ibid.*, p. 148.

<sup>84</sup> See Chapter 3 above, pp. 177-178.

<sup>85</sup> See Chapter 2 above, pp. 99-112.

<sup>86</sup> *Ibid.*, pp. 139-140.

<sup>87</sup> See Loughlin, n. 39 above, p. 149.

discussed in Chapter 2, as well as the logic of the reform process itself (in Chapter 3), neither point should be in any way surprising.

The idea of ‘reason of state’ being ‘the reason of’ the corporation tax code<sup>88</sup> may strike the reader as ‘un-British’.<sup>89</sup> Yet, as Loughlin shows, reason of state is the underlying idea of one of the foundational documents of British government, the Bill of Rights of 1689. The ban on ‘the levying of money for or to the use of the Crown by pretence of prerogative without grant of Parliament’<sup>90</sup> is itself, as has already been emphasised, a prudential one. This predisposition to prudence runs through, not just the corporation tax code itself, but also, as indicated in Chapter 2, the way in which the judiciary (also obliged to be prudent)<sup>91</sup> interpret its injunctions, sometimes (one infers), disingenuously, or even in ignorance of the label. The juristic prudence of the code is the subject matter of the next part of the discussion, and, by extension, the rest of the chapter as well.

At the level of judicial activity, we may note the following points. First, the existence of the well-known exclusion of the securing of the ‘payment of taxes or other contributions’ from the right to possession of property under the European Convention on Human Rights (ECHR), Protocol 1, Article 1, reinforces the prudential nature of judicial reasoning in cases that might involve challenges to reform measures;<sup>92</sup> however, even if some future case were to fall outside the exception, Loughlin’s notion of rights as the ‘positivization’ of ‘political

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<sup>88</sup> *Ibid.*, p. 151.

<sup>89</sup> See *Deutsche Morgan Grenfell Group plc v. Inland Revenue Commissioners and the Attorney General* [2006] UKHL 49; [2007] STC 1, 41h-42c (Lord Walker of Gestingthorpe).

<sup>90</sup> See Chapter 1 above, n. 337.

<sup>91</sup> See Chapter 2 above, pp. 151-152.

<sup>92</sup> See, albeit in different contexts, Application No. 13013/87, *Wasa Liv Ömsesidigt, Försäkringsbolaget Valands Pensionsstiftelse and a group of approximately 15,000 individuals v. Sweden* (1988) 58 ECHRDR 163; Application No. 21319/93, *National and Provincial Building Society and Others v. United Kingdom* [1997] STC 1466 (ECtHR) (civil claim originating in tax is a civil right within ECHR, Art 6); *Eagerpath Ltd v. Edwards (Inspector of Taxes)* [2001] STC 26.

claims’<sup>93</sup> would mean that the reasoning would still have to be of a prudential kind, since human rights adjudication itself involves ruling on political norms.<sup>94</sup> Falling outside the exception in Protocol, Article 1, is not an escape from the political into a reassuringly certain realm of law. Secondly, European judges seem much better at understanding the public law nature of the taxation function than are certain of their English counterparts.<sup>95</sup> Thirdly, although the outer limits of the public law nature of taxation need still to be fully charted,<sup>96</sup> cases clearly of a public law nature show much evidence of judges using a prudential technique.<sup>97</sup> Finally, as recent cases on claiming repayment of tax paid under a mistake of law, and on the nature of interest awards illustrate, a prudential approach may require the application of private law principles, especially where the amounts in question can be quantified.<sup>98</sup> These cases might possibly be regarded as contributing to marking out the boundaries of the public law of taxation. The better view, it is argued, is that the use of private law principles is itself a prudential response to a public law problem,<sup>99</sup> since it tends to augment trust and confidence, not merely in the judiciary, but also in the ‘creditworthiness’ of the state itself.<sup>100</sup>

<sup>93</sup> See Loughlin, n. 39 above, pp. 125, 130.

<sup>94</sup> *Ibid.*, p. 162.

<sup>95</sup> Contrast *Ferrazzini v. Italy* [2001] STC 1314 (ECtHR) and Application No. 73053/01, *Jussila v. Finland* (2006) 9 ITL Rep 662, with *N. Ali and S. Begum and Others v. Commissioners of Customs and Excise* [2002] VATDT No. 17681 (Stephen Oliver, QC (Chairman)), as yet unreported.

<sup>96</sup> See Lord Woolf, ‘Tax and Judicial Review’ [1993] BTR 219-229; Ian Saunders, *Taxation: Judicial Review and Other Remedies* (Chichester: John Wiley, 1996), pp. 103-106, 153-155.

<sup>97</sup> See Case C-446/03, *Marks and Spencer plc. v. Halsey (H.M. Inspector of Taxes)* [2006] 1 CMLR 18; [2006] EWHC 811; [2006] STC 1235 (Park J.); affirmed [2007] EWCA Civ 117; [2007] 2 CMLR 21; *Revenue and Customs Commissioners v. William Grant and Sons Distillers Ltd; Small (Inspector of Taxes) v. Mars UK Ltd* [2007] UKHL 15; [2007] STC 680; and *Barclays Mercantile Business Finance Ltd v. Mawson (Inspector of Taxes)* [2004] UKHL 51; [2005] STC 1.

<sup>98</sup> See *Deutsche Morgan Grenfell Group plc v. Inland Revenue Commissioners and the Attorney General* [2006] UKHL 49; [2007] STC 1; *Sempra Metals Ltd (formerly Metallgesellschaft Ltd) v. Inland Revenue Commissioners and Another* [2007] UKHL 34; [2007] 3 WLR 354.

<sup>99</sup> i.e. in that it applies ‘private law’ principles.

<sup>100</sup> As in the foundational constitutional law case of *John Entick v. Nathan Carrington and others* (1765) 95 ER 807 (Court of King’s Bench).

## ‘COMPLEXITY’ AND ‘INSTABILITY’ IN THE CORPORATION TAX CODE

If the characterisation of the corporation tax code in the terms just invoked is maintainable, then there are important consequences for the significance of current political debates over the ‘complexity’ and the ‘instability’ of the code. Such debates tend to be framed by reference to ‘the rule of law’, so we next need to consider what the implications of ‘the rule of law’, if any, may be for the idea of the corporation tax code as political jurisprudence.

John Cullinane, writing in the *Financial Times*, in April 2006, set out the key elements of the current debate with particular clarity.<sup>101</sup> His contribution, though brief, merits serious consideration, since it appeared in what has become one of the leading *fora* for tax policy, and it comes from the pen of a leading member of the corporation tax policy community.<sup>102</sup> Cullinane’s ‘hammering on the doors of representative government’, to adapt Bernard Manin’s phraseology, is thus apt to carry particular resonance. The corporation tax code,<sup>103</sup> he says, is ‘complicated’ (for instance, because there are still many exceptions to the accounting theme); it is ‘unclear’ (among the exceptions to accounting treatment for corporation tax purposes are research and development allowances and reliefs,<sup>104</sup> and these are notoriously difficult to apply to individual cases); and, finally, the code (like its counterparts in other jurisdictions) is subject to frequent, and often retrospective, change.

What is wrong with each of these tendencies, says Cullinane, is that they run contrary to ‘the rule of law, the ‘idea’ of which is, apparently, that ‘people and businesses know where

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<sup>101</sup> See Cullinane, *Financial Times*, 20 April 2006, 11; also Cullinane, *Taxation*, 11 May 2006, 147-150.

<sup>102</sup> See Chapter 2 above, p. 133. Cullinane was, at the time of writing the article, deputy president of the Chartered Institute of Taxation (CIOT), and is now its president.

<sup>103</sup> In fact, Cullinane refers to ‘tax’ in general, but it is clear from the context that corporation tax is intended.



they stand and can make decisions accordingly'.<sup>105</sup> What is needed is a 'return' to the 'rule of law', something which would, he argues, have very specific consequences for the corporation tax code: the augmentation of what has in this study been called 'the accounting theme' (marrying 'taxable profits' with 'profits per accounts'); assessing more accurately the costs that businesses will have to bear in order to comply with reforms to the code (which would include, presumably, reducing its 'complexity'); and, finally, 'keeping the rules as stable and comprehensive as possible'.

If the view of the corporation tax code presented in this study commends itself to the reader, it will be apparent that, while Cullinane's conclusions might be maintainable, his reasoning certainly is not. This is because the characteristics that he attributes to 'the rule of law' are at best contentious, and because his conclusions are nonetheless supportable within a conception of corporation tax law as a 'political practice', as 'political jurisprudence'. The second part of this statement is discussed under the second and third sub-headings below. What we need to consider next is the contentious nature of 'the rule of law'.

### **'The rule of law'**

Judith Shklar,<sup>106</sup> the elegance of whose argument is vastly underestimated both by Brian Tamanaha,<sup>107</sup> in his recent monograph, and by Lord Bingham, in a lecture at Cambridge in 2006,<sup>108</sup> centres the rule of law on Montesquieu, and its significance on (in this case) the corporation tax code's origins in the well-established institutions and processes through

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<sup>104</sup> See below in this chapter.

<sup>105</sup> See Cullinane (April 2006), n. 101 above.

<sup>106</sup> Shklar, who died in 1992, was a powerful commentator on the relationship of politics and law.

<sup>107</sup> See Brian Z. Tamanaha, *On the Rule of Law: History, Politics, Theory* (Cambridge: Cambridge University Press, 2004), p. 59.

<sup>108</sup> See Lord Bingham, 'The Rule of Law' [2007] CLJ 67-85, 67.

which taxation law in the UK is created.<sup>109</sup> The historical and interpretative nature of Shklar's analysis makes it essential to a functionalist view of the corporation tax code as political jurisprudence.

Montesquieu, says Shklar, provides the rule of law with its later historical signification, as 'the rule of institutions', the earlier (fatally circumscribed and much-abused) one being Aristotle's 'rule of reason'.<sup>110</sup> Cullinane's aspirations for the corporation tax code coincide with neither of these, but with Lon Fuller's post-Hayekian,<sup>111</sup> Aristotle-twisting view of the 'rule of law',<sup>112</sup> Fuller maintaining that, in accordance with 'the rule of law', law must be *inter alia* 'clear', 'enduring', and 'promulgated'. As Shklar says, acidly: 'as a legal ideal for us there is little either to accept or reject in this conventional list of lawyerly aspirations'.<sup>113</sup> Although Fuller does not say in what kind of society such characteristics might obtain,<sup>114</sup> they could be compatible even with a 'repressive and irrational government'.<sup>115</sup> What Montesquieu offers is an analysis of the rule of law as protection from 'the fear of violence, the insecurity of arbitrary government and the discrimination of injustice'.<sup>116</sup> In describing the English system of the eighteenth century, Montesquieu conceived of the rule of law as a means of ensuring, via institutional controls, the personal security of the individual.<sup>117</sup> As

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<sup>109</sup> See Judith Shklar, 'Political Theory and the Rule of Law', in *The Rule of Law: Ideal or Ideology?*, ed. by A.C. Hutchinson and P. Monahan (Toronto: Carswell, 1987), pp. 1-16.

<sup>110</sup> *Ibid.*, p. 5; see Aristotle, *The Nicomachean Ethics*, ed. and trans. by J.A.K. Thomson, Hugh Tredennick and Jonathan Barnes (London: Penguin, 2004), pp. 187-189, 215-216 (see Martin Loughlin, *Sword and Scales: An Examination of the Relationship between Law and Politics* (Oxford: Hart Publishing, 2000), pp. 69-71, 183-184).

<sup>111</sup> *Ibid.*, p. 7 ('no social end in view').

<sup>112</sup> See Lon L. Fuller, *The Morality of Law*, rev. edn (London: Yale University Press, 1969), pp. 46-91 (the eight 'desiderata that make up the internal morality of the law', *ibid.*, p. 81).

<sup>113</sup> See Shklar, n. 109 above, p. 13.

<sup>114</sup> Shklar describes Fuller's notion of the 'rule of law' as 'political and historical fantasizing' (*ibid.*, p. 14).

<sup>115</sup> See Shklar, n. 109 above, p. 13.

<sup>116</sup> *Ibid.*, p. 16; see Charles de Secondat, baron de Montesquieu, *The Spirit of the Laws*, trans. and ed. by Anne M. Cohler, Basia Carolyn Miller and Harold Samuel Stone (Cambridge: Cambridge University Press, 1989), pp. 156-166.

<sup>117</sup> See Shklar, n. 109 above, p. 4.

E.P. Thompson concluded,<sup>118</sup> ‘England was not [in the eighteenth century] a gulag society[,] and its political classes had to some degree shackled themselves’.<sup>119</sup> That was the method of prudence;<sup>120</sup> the foundation of the very system, analysed in Chapters 2 and 3, which is, in our own days, producing the corporation tax code.<sup>121</sup>

If this is right, the significance of the rule of law to the corporation tax code is simply that it is the product of those institutions and processes discussed in previous chapters. This has already been identified as a characteristic of political jurisprudence.<sup>122</sup> What it means is that the corporation tax code, in all its ‘instability’ and ‘complexity’, is a vivid illustration of Loughlin’s point, closely aligned to Shklar’s (via Montesquieu), that the rule of law, in this system, means no more (but, equally importantly, no less) than ‘that authority can only be wielded through recognized legal forms and that the legal machinery of the state exists to ensure the compliance of office-holders with these forms ...’.<sup>123</sup>

So, if Cullinane is wrong about the premises, but supportable, possibly, in his conclusions, what is the true significance of ‘complexity’ and ‘instability’ in the corporation tax code itself?

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<sup>118</sup> See E.P. Thompson, *Whigs and Hunters: The Origin of the Black Act* (London: Penguin, 1990), pp. 258-269.

<sup>119</sup> See Shklar, n. 109 above, p. 5.

<sup>120</sup> See Chapter 3 above, n. 93; also Mark N. Brown, ‘The Character of a Trimmer’, in *The Works of George Savile Marquis of Halifax*, vol. 1, ed. by Mark N. Brown (Oxford: Clarendon Press, 1989), pp. 33-68.

<sup>121</sup> See Loughlin, n. 110 above, pp. 183-185.

<sup>122</sup> See above in this chapter.

<sup>123</sup> See Loughlin, n. 39 above, pp. 132-133 (this might be what Lord Bingham (see n. 108 above) is saying, albeit indirectly, in reference to the Constitutional Reform Act 2005).

## ‘Complexity’

Cullinane pinpoints the ‘complexity’ of the corporation tax code as one of its most undesirable characteristics,<sup>124</sup> and, as discussed, grounds this argument in the requirements of a version of ‘the rule of law’. Are we therefore to conclude, with Tiley, that the corporation tax code, along with the rest of UK taxation law, is merely a ‘shambles’,<sup>125</sup> or, that its ‘complexity’ denotes something more?<sup>126</sup> Certainly much of the political debate on corporation tax is currently focussing on the phenomenon of ‘complexity’.<sup>127</sup> A report sponsored by the Confederation of British Industry (the CBI), and published in 2006, refers to the perception, on the part of its members, of hitherto undreamt-of levels of ‘complexity’.<sup>128</sup> These political debates ascribe the significance of ‘complexity’, not to a breach of ‘the rule of law’, but to international ‘competitiveness’ issues, although as Martin Wolf<sup>129</sup> and Samuel Brittan<sup>130</sup> would insist, this is properly to be regarded, not as ‘competitiveness’ between states, but between individual firms in different states. The argument maintained in the present study is that, given the institutional and procedural

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<sup>124</sup> The complaint has often been made about UK taxation law in general: see *Great Western Railway Company v. Bater (Surveyor of Taxes)* (1922) 8 TC 231, 255 (Lord Wrenbury); Hubert Monroe, QC, *Intolerable Inquisition? Reflections on the Law of Tax* (London: Stevens, 1981), pp. 23-24; Maurice Parry-Wingfield, ‘The Chicken or the Egg?’ [2000] BTR 597-601, 598; on the need for simplicity, see Meade, n. 30 above, pp. 18-21.

<sup>125</sup> See Tiley, n. 29 above, p. 49.

<sup>126</sup> Rather like (which is not an original point), Oliver Cromwell’s description of English real property law as an ‘ungodly jumble’, i.e. as law whose ‘values’ are ‘ungodly’ (quoted, e.g., in J.H. Baker, *An Introduction to English Legal History*, 4<sup>th</sup> edn (London: Butterworths, 2002), p. 289).

<sup>127</sup> See Houlder, *Financial Times*, 24 March 2006, 2; also ‘Memorandum submitted by the Institute of Chartered Accountants in England and Wales’, in House of Commons Treasury Committee, 5<sup>th</sup> Report. *The 2007 Budget, Volume II: Oral and written evidence* (House of Commons Papers, Session 2006-2007, 389) (London: TSO, 2007), pp. Ev 61-63, Ev 62.

<sup>128</sup> See Ipsos MORI, *UK Corporate Taxation and International Competitiveness* (London: Confederation of British Industry, 2006), 2 (see Snape, n. 15 above, p. 383).

<sup>129</sup> See Martin Wolf, *Why Globalization Works* (London: Yale, 2005), pp. 80-81.

<sup>130</sup> See Brittan, *Financial Times*, 31 August 2007, 11.

background, and, given the status of corporation tax law as public law, such ‘complexity’ is unavoidable.<sup>131</sup> The most we can say is that it can be more or less prudently managed.

With ‘complexity’, we are not talking about the sheer technical intricacy of issues that thereby become difficult to relate to the democratic process,<sup>132</sup> nor about the ‘complexity’ of ‘complexity science’, with its tendency to describe opaquely what might be rendered realistically.<sup>133</sup> We are talking instead about the ‘complexity’ that has often resulted from the need to make corporation tax legislation effective.<sup>134</sup> The ‘complexity’ of all tax legislation arises from the prudential need to make difficult decisions and careful distinctions between situations.<sup>135</sup> Three types of distinction have a particularly important part to play in the corporation tax code. First, there is the need to devise provisions suitable for a wide range of different service industries, ones as diverse as banking and life assurance.<sup>136</sup> Secondly, there is the need to maintain fairness in the system, by combating tax avoidance, a process that needs to address the difficulties exacerbated by the historically ‘literal’ approach of the judges to the difficulties of interpreting parts of the corporation tax code.<sup>137</sup> Thirdly, there is

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<sup>131</sup> See Deborah L. Paul, ‘The Sources of Tax Complexity: How Much Simplicity Can Fundamental Tax Reform Achieve?’ (1997) 76 *North Carolina Law Review* 151-221; also Hansard HC Public Bill Committee, 17 May 2007, col. 215 (Ed Balls, MP, Economic Secretary to the Treasury).

<sup>132</sup> See Danilo Zolo, *Democracy and Complexity: A Realist Approach*, trans. by David McKie (Cambridge: Polity Press, 1992); James Bohman, *Public Deliberation: Pluralism, Complexity, and Democracy* (Cambridge, Mass.: MIT Press, 1996).

<sup>133</sup> See Elizabeth McMillan, *Complexity, Organizations and Change* (London: Routledge, 2004), pp. 25-28.

<sup>134</sup> Although not always: see Hansard HC Standing Committee A, 11 May 2004, cols 118-119 (Rt Hon. Dawn Primarolo, MP, Paymaster General); the need for effectiveness is ‘glossed’ in the Tax Law Review Committee’s, *Making Tax Law: Report of a Working Party on the Institutional Processes for the Parliamentary Scrutiny of Tax Proposals and for the Enactment of Tax Legislation chaired by Sir Alan Budd* (London: Institute for Fiscal Studies, 2003), para. 8.2.

<sup>135</sup> See John Prebble, ‘Why is Tax Law Incomprehensible?’ [1994] BTR 380-393; Joel Slemrod and John Bakija, *Taxing Ourselves: A Citizen’s Guide to the Debate over Taxes*, 3<sup>rd</sup> edn (Cambridge, Mass.: MIT Press, 2004), pp. 163-172; on casuistry and the importance of drawing distinctions ‘in kind’ when state-building, see Loughlin, n. 39 above, pp. 131 and 152.

<sup>136</sup> See Monroe, n. 124 above, p. 23. On the life assurance industry, see H.M. Treasury, *Microeconomic Reform in Britain: Delivering Opportunities for All*, ed. by Ed Balls, Joe Grice and Gus O’Donnell (Basingstoke: Palgrave Macmillan, 2004), p. 278.

<sup>137</sup> See Monroe, n. 124 above, p. 32.

the need prudently to address the legitimate concerns of interest groups over corporation tax reform measures, particularly within the corporate sector.<sup>138</sup> It may be that current difficulties over the capital allowances ‘simplification’ in relation to industrial buildings illustrate the antithesis of this, the ‘complexity’ of effectiveness, with a relatively new phenomenon, the ‘simplicity’ of ineffectiveness. Perhaps this was what Oliver Wendell Holmes meant in saying: ‘I do not care about the simplicity that lies this side of complexity’.<sup>139</sup>

The logic of the statutory response to each of these three areas of difficulty has been prudence, that is, juristic prudence. Such a reading of the suggestions in the tax simplification literature may put the current ‘complexity’ of the corporation tax code, as well as the feasibility of the proposed solutions,<sup>140</sup> in a more realistic perspective. What is ironic is that the prudential nature of the Tax Law Rewrite may be being undermined, both by the volume of the rewritten legislation, and by the impression of vastness created by its operation alongside the legislative texts that it will eventually replace.<sup>141</sup>

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<sup>138</sup> *Ibid.*, pp. 31, 34.

<sup>139</sup> Quoted in Southern, *Tax Journal*, 23 November 1995, 6-9, 8.

<sup>140</sup> Most importantly, the Tax Law Rewrite (see Chapter 1 above, n. 88); see FA 1995, s. 160 (a ‘one-off’ measure only); Inland Revenue, *The Path to Tax Simplification: A background paper* (London: HMSO, 1995), assessed in David Salter, ‘Pre-Parliamentary Procedure, Consultation and the Tax Law Rewrite’ (1997) 16 CJQ 294-299, and David Salter, ‘Towards a Parliamentary Procedure for the Tax Law Rewrite’ (1998) 19 Stat LR 65-79. Specifically on the corporation tax rewrite, see Houlder, *Financial Times*, 25 February 2008, 4.

<sup>141</sup> See Houlder, *Financial Times*, 24 March 2006, 2; Houlder, *Financial Times*, 8 November 2006, 4; Houlder, *Financial Times*, 15 August 2007, 3, citing the following numbers as the ‘average number’ of pages in FBs since the early 1980s: ‘153 in 1980-84; 209 in 1985-89; 266 in 1990-94; 312 in 1995-99 and 463 in 2000-07’; H.M. Treasury, *Meeting the aspirations of the British people: 2007 Pre-Budget Report and Comprehensive Spending Review October 2007* (Cm 7227) (London: TSO, 2007), paras 4.49-4.53; also Malcolm Gammie, ‘Tax Simplification’, in *The IFS Green Budget: January 2008*, ed. by Robert Chote, Carl Emmerson, David Miles and Jonathan Shaw (London: The Institute for Fiscal Studies, 2007), pp. 260-267, who seems to have lost much of his appetite for rewritten tax legislation.

## ‘Instability’

Of the criticisms made by Cullinane (and indeed by others), the charge of ‘instability’ in the corporation tax code needs particularly careful consideration. Again, we need to decide what its significance is, once we have excluded it from the conception of the ‘rule of law’ chosen as relevant to the present study.

The first, perhaps the most important, point, is the need to highlight the long-standing, almost instinctive, hold on the Western imagination that the idea of ‘stability’ has. John Pocock relates how, when once the reality of a post-classical city republic had emerged in fifteenth century Italy, writers (of whom Machiavelli is only the most well-known) fell to wondering how, having come into existence, such an institution might meet its end.<sup>142</sup> *La stabilità*, keeping the ‘ship of state’ afloat and on course, was as important to its constituent policies as to the enterprise as a whole. Some proximate sense of ‘stability’, it is suggested, pervades discussions on the need for stability in laws, but especially in economic growth. When Chancellors of the Exchequer, most notably the Rt Hon. Gordon Brown, MP, talk about ‘economic stability’, this is the kind of imagery that they seem to invoke. Tax, moreover, has an important role in economic stabilisation.<sup>143</sup>

In artificially unpicking economic from legal considerations, however, we need to distinguish carefully between a concrete notion of the role of taxation in general in economic ‘stabilisation’,<sup>144</sup> and more imaginative notions of the city on the sea. Reference has already been made to Edward Troup’s critique of the 1998 *Code for Fiscal Stability*. In the course of

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<sup>142</sup> See J.G.A. Pocock, *The Machiavellian Moment: Florentine Political Thought and the Atlantic Republican Tradition* (Princeton: Princeton University Press, 1975), pp. 99-103.

<sup>143</sup> See Richard A. Musgrave, *The Theory of Public Finance: A Study in Public Economy* (New York: McGraw-Hill Book Company, 1959), pp. 5-6; Richard A. Musgrave and Peggy B. Musgrave, *Public Finance in Theory and Practice*, 5<sup>th</sup> edn (New York: McGraw-Hill, 1989), pp. 11-13; H.M. Treasury and Inland Revenue, *Corporation Tax Reform: A Consultation Document* (London: Inland Revenue, 2003), para. 1.11.

his commentary, he commends the (then) newly elected Labour government for its formal commitment to ‘the worthy, if slightly Calvinistic aims, of “transparency, stability, responsibility, fairness and efficiency”’.<sup>145</sup> However, Troup is careful to emphasise that, despite its name, the Code relates to the ‘key principles to the formulation and implementation of – (a) fiscal policy, and (b) policy for the management of the National Debt’.<sup>146</sup> It is about ‘Government borrowing (*i.e.* the excess of spending over taxation)’, in other words, not about tax levels *per se*, and certainly not about the ‘stability’ of tax legislation.<sup>147</sup> Without mentioning the technique of prudence, Troup nonetheless acknowledges that no government would commit itself to stasis in this way. Does this mean that the corporation tax code is inherently ‘unstable’, therefore?

Well, no, not necessarily. ‘Stability’ is an important element in prudential governance. We can see this from Hobbes’s acceptance that the purpose of the ‘art and science of government’ is the need for men ‘to conforme themselves into one firme and lasting edifice’,<sup>148</sup> with the penalty of failure, one might say of ‘imprudence’, being destruction:

‘[F]or want, both of the art of making fit Lawes, to square their actions by, and also of humility, and patience, to suffer the rude and combersome points of their present greatnesse to be taken off, they<sup>149</sup> cannot without the help of a very able Architect,<sup>150</sup> be

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<sup>144</sup> See Plowden Report, *Control of Public Expenditure* 1961 (Cmnd 1432), para. 10; James and Nobes, n. 20 above, ch. 6.

<sup>145</sup> See FA 1998, s. 155(2); H.M. Treasury, *The Code for Fiscal Stability*, 1998 (available from [www.hm-treasury.gov.uk](http://www.hm-treasury.gov.uk) (accessed 10 December 2007)).

<sup>146</sup> See FA 1998, s. 155(1).

<sup>147</sup> See Troup [1998] BTR 490, 491.

<sup>148</sup> See Thomas Hobbes, *Leviathan, or The Matter, Forme, & Power of a Common-wealth Ecclesiasticall and Civill*, ed. by C.B. Macpherson (London: Penguin, 1985), p. 363 (see Loughlin, n. 39 above, pp. 140-141).

<sup>149</sup> [i.e. ‘men ... at last weary of irregular jostling, and hewing one another ...’ (Hobbes, n. 148 above, p. 363.)]

<sup>150</sup> See D.M. Palliser, *The Age of Elizabeth: England under the later Tudors 1547-1603* (London: Longman, 1983), p. 369, on ‘architects’ before Sir Christopher Wren.



compiled, into any other than a crasie building, such as hardly lasting out their own time, must assuredly fall upon the heads of their posterity.’<sup>151</sup>

Although Hobbes is speaking here both of the state and of the particular laws it creates, we may conclude that prudence is the essential technique in the framing of such laws. Stability is a prudential quality, no doubt. There is a recognition of this in the commitment to ‘stability of direction in legislation’, over the long term, in the corporation tax policy documents.<sup>152</sup> Given an objective of economic growth, prudential lawmaking will require stability in laws, to encourage investment.<sup>153</sup> Hence, Cullinane is right to advocate ‘keeping the rules as stable ... as possible’, but the reason is prudence, rather than the ‘rule of law’. The use of the phrase ‘stable ... as possible’ indeed acknowledges that absolute stability may not always be realisable. A Conservative MP spoke well in pointing out, when the provisions of the ‘loan relationships’ code were under consideration in Standing Committee, in February 1996, that tax law was subject to ‘evolutionary development’: ‘[i]t is constantly necessary [he said] to revise, amend, improve and bring up to date the corpus of tax law’.<sup>154</sup>

None of this is to underplay the economic importance of stability.<sup>155</sup> We return to this point once we have considered the significance of a theory of effectiveness in shaping the values contained in the corporation tax code itself.

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<sup>151</sup> See Hobbes, n. 148 above, p. 363 (see Loughlin, n. 39 above, pp. 140-141).

<sup>152</sup> See, e.g., H.M. Treasury and Inland Revenue, n. 18 above, para. 1.3; Sanger, *Tax Adviser*, April 2002, 12.

<sup>153</sup> See Meade, n. 30 above, p. 21; also H.M. Treasury and Inland Revenue, n. 18 above, para. 1.13.

<sup>154</sup> See Hansard HC Standing Committee E, 29 February 1996, col. 596 (Nigel Forman, MP (Carshalton and Wallington, Conservative)).

<sup>155</sup> See Musgrave and Musgrave, n. 143 above, ch. 30, pp. 531-532; James and Nobes, n. 20 above, ch. 6; Balls and O'Donnell, n. 8 above, ch. 1; Colin Thain, ‘Economic Policy’, in *Developments in British Politics 6*, ed. by Patrick Dunleavy, Andrew Gamble, Ian Holliday and Gillian Peele (Basingstoke: Macmillan, 2002), pp. 219-237; Colin Thain, ‘Economic Policy’, in *Developments in British Public Policy*, ed. by Peter Dorey (Cambridge: Sage, 2005), pp. 24-45.

## THE PRIORITISATION OF POLITICAL VALUES IN THE CORPORATION TAX CODE

The reader should, by this stage in the chapter, be persuaded that most theoretical discussions of the current state of corporate taxation have little, if any, interpretative value. This is not, of course, to deny their normative usefulness, or their undoubted intellectual rigour. What it does assert, however, is that arguments for reform that do not explicitly address the deep implications of the public law nature of the corporation tax code, or that do not recognise the political significance of its complexity, are to some greater or lesser extent inadequate, in interpretative terms. The present study is not, of course, concerned with constructing a normative theory, but it is appropriate to stress that any such theory would be much the stronger for building on robust interpretative foundations.

These points made, we are now in a position to etch in the final details of the picture that this study seeks to create. They are concerned with the reality: what ‘configuration’ of theory and values have the institutions and processes discussed in previous chapters in fact helped to create? What are the strengths and weaknesses of that structure? And how is it that such weaknesses as there are, are nonetheless outweighed, for the present at least, by the system’s strengths?

We continue by referring to two, roughly contemporaneous, theoretical pieces, which help to underline the stance taken in the study as a whole. The former is part of Loughlin’s ‘archaeological’ labours on the origins of modern public law;<sup>156</sup> the latter is from Sol Picciotto’s work on the establishment of a social, economic and political context for the ‘principles’ of the taxation of international business.<sup>157</sup> What Loughlin is at pains to point

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<sup>156</sup> See Loughlin (1992), n. 14 above.

<sup>157</sup> Sol Picciotto, *International Business Taxation* (London: Weidenfeld and Nicolson, 1992), p. 83.

out, an idea to which brief reference has already been made,<sup>158</sup> is that Adam Smith's *The Wealth of Nations*,<sup>159</sup> which is nearly always referred to in theoretical discussions of taxation,<sup>160</sup> is not, properly understood, to be read as laying down a series of exogenous 'norms' about what taxes and tax systems should, or should not, do. If so, the much quoted 'canons of taxation',<sup>161</sup> would provide no clue as to the weight to be attached to one canon, relative to that to be attached to the others, either generally, or in a particular case. Instead, the canons, as indeed Smith's work as a whole, should be regarded as a 'manual', albeit a highly sophisticated one, of the 'science of legislation'.<sup>162</sup> These are the points that the legislator ('the prince') needs to bear in mind, Smith is saying, if he or she is to create a tax (system) that will *work*.<sup>163</sup> It is not that taxes, or tax systems, which fail to reflect some or all of these principles, are in some sense immoral, or 'unfair', or 'bad'. Rather, it is simply that they will tend not to work; they will create resentment, and damage the economy, and, in damaging the economy, they will fail to raise the funds that the prince needs to create the

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<sup>158</sup> See Chapter 1 above, n. 260.

<sup>159</sup> See Adam Smith, *An Inquiry into the Nature and Causes of the Wealth of Nations*, ed. by R.H. Campbell and A.S. Skinner (textual editor W.B. Todd), 2 vols (Oxford: Clarendon Press, 1976).

<sup>160</sup> But, interestingly, not in Meade, n. 30 above.

<sup>161</sup> See Smith, n. 159 above, II, pp. 825-828: 'All nations have endeavoured, to the best of their judgment, to render their taxes as equal as they could contrive; as certain, as convenient to the contributor, both in the time and in the mode of payment, and, in proportion to the revenue which they brought to the prince, as little burdensome to the people' (p. 827). This had been prefigured in Smith's earlier (1766), *Lectures on Jurisprudence*, ed. by R.L. Meek, D.D. Raphael and P.G. Stein (Oxford: Clarendon Press, 1978), pp. 530-535; in part, by a work attributed to Henry Home (Lord Kames) (1696-1782), the slightly earlier *Sketches of the History of Man* (Edinburgh: Creech, 1774), vol. 1, pp. 474-481; and, in part, by Montesquieu, n. 116 above (see Smith, n. 159 above, II, 827n). Adam Smith's 'four maxims or principles' are revisited in John Stuart Mill's, *Principles of Political Economy and Chapters on Socialism*, ed. by Jonathan Riley (Oxford: Oxford University Press, 1994), pp. 167-169.

<sup>162</sup> See Loughlin (1992), n. 14 above, p. 4; Donald Winch, 'Adam Smith's "enduring particular result": a political and cosmopolitan perspective', in *Wealth and Virtue: The Shaping of Political Economy in the Scottish Enlightenment*, ed. by Istvan Hont and Michael Ignatieff (Cambridge: Cambridge University Press, 1983), pp. 253-269; Donald Winch, *Adam Smith's Politics: An Essay in Historiographic Revision* (Cambridge: Cambridge University Press, 1978), esp. p. 159.

<sup>163</sup> *Ibid.*; Roy Porter, *Enlightenment: Britain and the Creation of the Modern World* (London: Penguin, 2000), pp. 188ff; Montesquieu, n. 161 above.

conditions to sustain his Scottish Enlightenment conception of ‘the public good’.<sup>164</sup> This prudential logic of effectiveness is what, in turn, provides the ‘grammar’, which shapes the ‘vocabulary’,<sup>165</sup> which the canons of taxation contain. As Smith says, it is by the non-observance of ‘some one or other’ of the canons ‘that taxes are frequently so much more burdensome to the people than they are beneficial to the sovereign’.<sup>166</sup> The instrumental and prudential spirit in which the canons are laid down was well understood by John Stuart Mill, in his *Principles of Political Economy*,<sup>167</sup> and, later on, by the Whitehall civil servant, Sir Josiah Stamp,<sup>168</sup> in his remarkable *Principles of Taxation*.<sup>169</sup> This understanding was, however, rather less apparent in the justly famous 1978 Meade Committee Report,<sup>170</sup> and also in the rather fatuous arrogance<sup>171</sup> of the 10 ‘tenets’ advanced by the various contributors to the Institute of Chartered Accountants in England and Wales’s *Pathways to Tax Reform* of 2000.<sup>172</sup>

It is in the prudential Smithian vein just described, although without explicit reference to Smith’s canons, that Picciotto has delineated, albeit briefly, the implications of ideas such as

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<sup>164</sup> *Ibid.*, pp. 394-396; also Don Slater and Fran Tonkiss, *Market Society: Markets and Modern Social Theory* (Cambridge: Polity Press, 2001), pp. 41-43 (see Chapter 3 above, n. 161, in relation to the ‘public good’ as ‘harmony’ of self-interests).

<sup>165</sup> See Chapter 1 above, n. 329.

<sup>166</sup> See Smith, n. 159 above, II, p. 827.

<sup>167</sup> See Mill, n. 161 above.

<sup>168</sup> Stamp was killed in an air raid in 1941 (see Rosamund Thomas, *The British Philosophy of Administration: A comparison of British and American ideas 1900-1939* (Cambridge: Centre for Business and Public Sector Ethics, 1989), p. 251).

<sup>169</sup> See Sir Josiah Stamp, *The Fundamental Principles of Taxation in the Light of Modern Developments* (The Newmarch Lectures for 1919) (London: Macmillan and Co., 1921), esp. ch. 4; also A.C. Pigou, *A Study in Public Finance*, 3<sup>rd</sup> edn (London: Macmillan, 1962), pp. 40-45, esp. p. 43.

<sup>170</sup> See Meade, n. 30 above, p. 23, which is rather vague on what is the most important practical question (see also Cedric Sandford, *The Economics of Public Finance: An Economic Analysis of Government Expenditure and Revenue in the United Kingdom*, 4<sup>th</sup> edn (Oxford: Pergamon Press, 1992), p. 112-113, which is similarly vague on this point).

<sup>171</sup> See Michael Oakeshott, ‘Rationalism in politics’, in *Rationalism in politics and other essays* (Indianapolis: Liberty Fund, 1991), pp. 5-42, esp. 15-16.

those just discussed, for the legitimacy of taxes and tax systems. Independently of Loughlin's interpretation of Smith, but also in 1992, Picciotto draws out some strikingly similar conclusions to those of Loughlin.<sup>173</sup> He emphasises, as does Loughlin in relation to public law generally,<sup>174</sup> the point that tax law is a practical art, the 'overriding aim' of which is 'effectiveness', an aim that will be frustrated, as it is in relation to other forms of regulation, if a system lacks 'fairness':

'Taxation is not an abstract exercise in political or economic philosophy, but a practical matter of raising state finance for the public good. The overriding aim is therefore effectiveness, which must be predicted, based on estimations of the patterns of compliance, non-compliance and avoidance. It is in this sense that the question of *legitimacy* is central to the evaluation of taxation, as well as other types of legal regulation of economic activity.<sup>175</sup> Legitimacy in this sense combines the interrelated issues of equity and effectiveness. To the extent that a regulatory system lacks fairness it fails in political acceptability, and will also tend to fail in effectiveness as enforcement becomes difficult and non-compliance grows. Equally, a system which has problems of enforceability and therefore of effectiveness will tend to lose political acceptability.'<sup>176</sup>

Note the similarity to Loughlin's position here. First, although Picciotto does not relate the practical art of taxation to the 'power of practical reason' that is prudence,<sup>177</sup> the idea of tax legislation as a 'practice' is surely implied.<sup>178</sup> Secondly, Picciotto places the emphasis on 'effectiveness'. Unlike in the 'Sheffield school'<sup>179</sup> scheme of things, where 'effectiveness' is

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<sup>172</sup> See Institute of Chartered Accountants in England and Wales, *Towards a better tax system: Practical consideration of the ten tenets* (London: ICAEW, 2000); also Sandford, n. 170 above, p. 112.

<sup>173</sup> See Picciotto, n. 157 above, p. 83.

<sup>174</sup> See Loughlin, n. 39 above, esp. pp. 148-152, 163.

<sup>175</sup> [See Chapter 1 above, n. 352; also Murphy and Nagel, n. 22 above, p. 162 ('tax legislation is, in general, distinct from expenditure legislation').]

<sup>176</sup> See Picciotto, n. 157 above, p. 83.

<sup>177</sup> See Chapter 1 above, n. 182.

<sup>178</sup> See above in this chapter, pp. 243-244.

<sup>179</sup> See Chapter 1 above, n. 115.

presented as a ‘rule of law value’ along with all the others,<sup>180</sup> in Picciotto’s summation, as in Loughlin’s ‘pure theory of public law’,<sup>181</sup> effectiveness is not merely an immanent value, but the theory that shapes and prioritises such values in particular situations. Thirdly, and finally, like Loughlin, Picciotto sees the significance of tax fairness, not as some absolute quality, but as a value the presence of which makes a tax the more likely to succeed, and the absence of which will tend to undermine its effectiveness.

The intellectual strand common to both Loughlin’s portrayal of ‘the science of legislation’, and to Picciotto’s summation of the demands of tax policy-making is, of course, the need for tax policy to be effective.<sup>182</sup> That effectiveness has to be judged by reference to what the first ‘Brown Budget’, that of July 1997, referred to as ‘the objectives of the government of the day’.<sup>183</sup> What shapes these objectives, and their relationship to a particular view of the ‘public interest’ has already been discussed in Chapter 3. The only point that we need to underscore at this late stage in the study is the analogous position of ‘the prince’, in Smith’s world-view, and the Crown in Parliament in the depiction of the British constitution in the present study.<sup>184</sup> Both are ‘the sovereign’, but the sovereignty that subsists in the relationship of government and governed depends, in the world of today, on the maintenance of trust and confidence between the two. This, in turn, depends on constantly prudential political choices. To say it is about ‘trade-offs’ between values, as

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<sup>180</sup> See, e.g., Chris Hilson, *Regulating Pollution: A UK and EC Perspective* (Oxford: Hart Publishing, 2000), pp. 127-129.

<sup>181</sup> See Loughlin, n. 39 above, ch. 9.

<sup>182</sup> This does, of course, have an administrative dimension, which is outside the scope of the study: see Christopher Wales, ‘The Implications of the O’Donnell Review for the making of Tax Policy in the UK’ [2004] BTR 543-565, 548.

<sup>183</sup> See n. 78 above (also Chapter 1 above, n. 380; Chapter 3 above, n. 181); *Equipping Britain for our long-term future: Financial Statement and Budget Report July 1997* (House of Commons Papers, Session 1997-1998, 85) (London: The Stationery Office, 1997), para. 1.68.

<sup>184</sup> See Chapter 2 above, nn. 35 and 52.

Troup expresses it,<sup>185</sup> gets somewhere near, but this is too leaden an expression for conveying what is essentially a quicksilver ability.<sup>186</sup> What is clear, in corporation tax more perhaps than any other area of taxation policy, is that HMG's ability to make prudential decisions, to 'deserve' the trust and confidence of the electorate, is enhanced by the relatively low salience of the tax. In coolly analytical terms, it is indeed the mass of individuals that eventually bears the burden of corporation tax.<sup>187</sup> In politics, however, that is much less important than the fact that the tax is initially laid on the companies themselves.<sup>188</sup>

Two main consequences flow from these observations, consequences that are of the first importance to the study as a whole. First, that the values immanent to the corporation tax code at any particular moment, and the way in which they appear to have been prioritised, reflect, not only the view of the public interest taken by the current administration, but also the public interest ideology of previous ones. Thus, we might say, do legislative codes proclaim their histories. Secondly, it is necessary to be extremely sceptical of certain types of adverse, especially 'journalistic' and other 'professional', criticism of the current state of corporate taxation. When people disagree about corporation tax reform, they do so, not by reference to some 'objective' reality, but by reference to their own (often tacit) perceptions of the public interest, that is to say by reference to their own political, or ideological, viewpoints. In other words, they are arguing about the values themselves, possibly, and certainly about their prioritisation. No-where is this phenomenon more apparent than in relation to anti-avoidance legislation and its implications for the concept of 'fairness' in taxation.

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<sup>185</sup> See Troup, n. 147 above, p. 491.

<sup>186</sup> See Chapter 2 above, n. 252.

<sup>187</sup> See Kay, *Financial Times*, 25 October 2005, 19; John Kay and Jadu Sen, 'The Comparative Burden of Business Taxation' (1983) 4:3 FS 23-28, 23); also Malcolm Gammie, 'Reforming Corporate Taxation: An Evaluation of the United States Treasury Integration Proposals and other Corporate Tax Systems in an International Context – Part 1' [1992] BTR 148-173, 149.

We can explore the implications of the propositions just advanced by unravelling the main values which are most obvious from the corporation tax code, as it is currently framed: efficiency and fairness. Not only do nations want to be wealthier, it is the duty of governments, if not to make them wealthier, to create the conditions under which they can become so.<sup>189</sup> Convincing the UK's electorate, both of the promising nature of its ideology, and of its ability to formulate and implement policies to enhance national wealth, through 'credible socialism',<sup>190</sup> has been the present government's priority since 1997. By the time of the New Labour landslide in the early summer of that year, the traditional party of the Left, had, through a combination of miscalculation and dogmatism, been away from the 'corridors of power' for the best part of two decades.<sup>191</sup> 'To be socialist and at the same time credible', to repeat the aspiration voiced by Gordon Brown in a 1997 speech,<sup>192</sup> was New Labour's solution to ('Old') Labour's long absence from government.<sup>193</sup> The implications of these ideas for tax reform were expressed thus in the July 1997 Budget report:

'It is essential that tax policy is based on clear principles. These are to encourage work, savings and investment, and fairness. A tax system should also be well designed, to meet the objectives of the government of the day,<sup>194</sup> without generating undesirable side effects; it must keep taxpayers' compliance costs to a minimum; it should avoid the less well off bearing an unfair burden; and attention must be paid to any implications for the United Kingdom's international competitiveness.'<sup>195</sup>

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<sup>188</sup> See Snape, n. 15 above, pp. 403-404.

<sup>189</sup> See Chapter 1 above, n. 169, referring to Thomas Hobbes, *On the Citizen*, ed. and trans. by Richard Tuck and Michael Silverthorne (Cambridge: Cambridge University Press, 1998), p. 144; also Smith, n. 159 above, I, p. 428 (see Chapter 3 above, n. 126).

<sup>190</sup> See Chapter 1 above, n. 187.

<sup>191</sup> See William Keegan, *The Prudence of Mr Gordon Brown* (Chichester: John Wiley, 2003), chs 2-3.

<sup>192</sup> See Chapter 1 above, n. 187; see Colin Thain and Ross Christie, 'Treasury Power: Past, Present and Future', p. 11, available from [www.treasuryproject.org](http://www.treasuryproject.org) (accessed 22 February 2008).

<sup>193</sup> See Gordon Brown, *Fabian Pamphlet 563: Fair Is Efficient – a socialist agenda for fairness* (London: Fabian Society, 1994), *passim*.

<sup>194</sup> See Chapter 3 above, pp. 196-197.



The corporation tax code, as will become apparent, has been a crucial instrument in the achievement of these two objectives, ‘credible’ policies and ‘socialist’ values. Within its intricate provisions, we can trace the uneasy reconciliations that giving effect to the two objectives sometimes involve. In this part of the discussion, we shall be concentrating on the ‘credibility’ dimension, which, for reasons also to become apparent, is in essence a question of efficiency. In the next section, the emphasis will be on what we might, albeit rather crudely, think of as the ‘socialist’ component, the value of fairness. The untangling of the values in this way is not entirely satisfactory, since there is much interpenetration,<sup>196</sup> but it is nonetheless maintainable,<sup>197</sup> and it highlights the substantial differences immanent to each.

### **Efficiency**

That HMG places considerable emphasis on efficiency in corporate taxation is everywhere apparent in the policy documents. The fullest statement of its importance, although not the earliest, appears in two substantial volumes,<sup>198</sup> in which Ed Balls<sup>199</sup> and Gus O’Donnell,<sup>200</sup> two individuals very closely associated with corporation tax reform, set out HMG’s economic policy objectives, and the place of efficiency within them. The background is the distinction, already alluded to,<sup>201</sup> between macroeconomic and microeconomic policy. We have already seen how, in the hands of Balls and O’Donnell, macroeconomic policy is about keeping inflation steady, at very low levels, ‘over the long term’, to generate ‘high and stable

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<sup>195</sup> See House of Commons Papers, Session 1997-1998, 85, n. 183 above, para. 1.68.

<sup>196</sup> See Balls, Grice and O’Donnell, n. 136 above, p. 7.

<sup>197</sup> *Ibid.*, p. 5.

<sup>198</sup> See Balls and O’Donnell, n. 8 above; Balls, Grice and O’Donnell, n. 136 above.

<sup>199</sup> See Chapter 2 above, nn. 16 and 264; David Lipsey, *The Secret Treasury* (London: Viking, 2000), p. 27; also Thain and Christie, *Parliamentary Brief*, February 2008, 21-22, 22 (available from [www.treasuryproject.org](http://www.treasuryproject.org) (accessed 21 February 2008)).

<sup>200</sup> See Chapter 1 above, nn. 81, 375; Chapter 2 above, n. 293; Chapter 3 above, n. 2.

<sup>201</sup> See Chapter 2 above, n. 177; Chapter 3 above, n. 83.

levels of growth and employment'.<sup>202</sup> With such stability as the goal of macroeconomic policy, the conditions are created under which the second and third 'pillars' of economic policy, 'tackling the supply-side barriers to growth and delivering employment and economic opportunities for all',<sup>203</sup> can be worked on too. Reforming corporation tax, as well as other areas of taxation, is part of the second pillar, the 'tackling' of 'supply-side barriers to growth', but it also has implications for the third. It is a key example of the post-1997 role of H.M. Treasury as an economics ministry.<sup>204</sup>

Curtailing 'supply-side barriers to growth' means, in the case of the corporation tax code, using it to assist 'firms [to] reach their full potential',<sup>205</sup> that is, making the tax more efficient. However, as we shall see, this is not simply the efficiency of the fourth of Smith's 'canons of taxation'. What we have, in 2008, is a corporation tax code that has had provisions shorn from it which are seen to be inconsistent with enhancing efficiency; older provisions which are consistent with that objective retained; and new provisions introduced that are designed to enhance efficiency. Three of the themes introduced at the beginning of the study are efficiency themes in this sense. First, the accounting theme, reflected in the large areas of the code now based on accounting practice. Secondly, the European and international theme, which is illustrated by those features of the code (mainly relating to the availability of reliefs within corporate groups) that reflect the principles of the European Treaty and GATT 1994, as well as the 'best practice' disseminated by the OECD.<sup>206</sup> Thirdly, the compliance and enforcement theme, which, for the purpose of the study, is taken to be

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<sup>202</sup> See Chapter 3 above, n. 83; also Gordon Brown, 'Advancing the public interest', in *Gordon Brown: Moving Britain Forward: Selected Speeches 1997-2006*, ed. by Wilf Stevenson (London: Bloomsbury, 2006), p. 91, on the 1944 origins of this expression (see also Chapter 3 above, n. 171).

<sup>203</sup> See Balls, Grice and O'Donnell, n. 136 above, p. 5.

<sup>204</sup> See Thain and Christie, n. 192 above, p. 8.

<sup>205</sup> See Balls, Grice and O'Donnell, n. 136 above, p. 6.

embodied in the rules on corporation tax self-assessment (CTSA). How each of these reflect the circumstances of their introduction, and the extent to which they are consistent, or inconsistent, with their proffered objective, will be addressed later in the discussion. For the moment, it is just necessary to return to the policy documents on corporation tax reform, and to relate the ideas they contain to economic thinking more generally.

The efficiency imperative within the code, according to Balls, Grice and O'Donnell, and the need thereby to address 'market failures', is driven by one crucial factor, already discussed at some length: the need to 'make ... [markets] work better in the public interest'.<sup>207</sup> 'Markets are [as they re-emphasise] a powerful means of advancing the public interest',<sup>208</sup> and this is reflected in the four 'major microeconomic goals' set out by Balls, Grice and O'Donnell, in what is essentially a highly detailed explanation of New Labour's microeconomic policy. Two of these goals relate to 'high quality public services' delivery, and to the maintaining of unprecedentedly high levels of employment. Whilst generally relevant, in the sense that the code's effectiveness impacts directly on these goals, the two of most importance here are 'building a fair society', discussed below in conjunction with fairness, and, what we need to consider next, 'raising the sustainable rate of UK productivity growth'.<sup>209</sup>

The key word in the microeconomic goal of raising 'productivity growth' is 'sustainability', the idea that it can be achieved consistently over the long term. Although this is a use of the expression 'sustainability' that environmentalists deplore, it focuses attention on two key implications of the goal: the need to favour competition, so as to encourage innovation and creativity, and the need to eliminate 'market failures'.

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<sup>206</sup> See, e.g., Organisation for Economic Co-operation and Development, *Taxing Profits in a Global Economy: Domestic and International Issues* (Paris: OECD, 1991), ch. 1.

<sup>207</sup> *Ibid.*, p. 6. See also Chapter 3 above.

<sup>208</sup> *Ibid.*

To the extent, therefore, that the corporation tax code lacks any element of protectionism, in the form of tax subsidies, it is reflecting one aspect of efficiency. The UK's membership of the EU and GATT 1994/WTO, are major drivers for this, and we shall have occasion to return to it below. It is not merely the absence of tax subsidies that can be seen to reflect this ideal of efficiency, however. Insofar as the code promotes, or at least does not undermine, either access to capital, or the 'free mobility of capital and labour',<sup>210</sup> it can also be said to disclose this particular vision of efficiency. Again, we shall return to this later in the discussion. Both of these manifestations of efficiency are illustrations of HMG's perception that its role 'is not only to support but [to] positively enhance markets in the public interest'.<sup>211</sup> The ideas underlying these elements are also contained in three policy 'orientation documents', as they might be called: *Large Business Taxation: The Government's strategy and corporate tax reforms: A consultation document*, which appeared in July 2001;<sup>212</sup> *Reform of Corporation Tax: A Consultation Document*, published in August 2002;<sup>213</sup> and *Corporation Tax Reform: A Consultation Document*, published exactly a year later, in August 2003.<sup>214</sup> The 2001 document emphasises that the corporation tax code needs to contribute 'to creating the best possible location for investment', that it must embody rates of tax which are 'as low as possible', and that it must reflect 'the realities of the modern business environment'.<sup>215</sup> On this footing, '[t]he key principles for corporate tax reform are'

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<sup>209</sup> *Ibid.*, p. 7.

<sup>210</sup> *Ibid.*, p. 8.

<sup>211</sup> *Ibid.*

<sup>212</sup> See H.M. Treasury and Inland Revenue, n. 18 above.

<sup>213</sup> See H.M. Treasury and Inland Revenue, *Reform of Corporation Tax: A Consultation Document* (London: Inland Revenue, 2002).

<sup>214</sup> See H.M. Treasury and Inland Revenue, n. 143 above.

<sup>215</sup> See H.M. Treasury and Inland Revenue, n. 18 above, para. 1.5.

fairness (discussed below) and ‘competitiveness’.<sup>216</sup> Increasing efficiency enhances competitiveness, as the document goes on to make clear:

‘[T]o create the best possible location for investment, the tax system should complement business competitiveness, not stifle it [it reads]. This means: removing tax distortions, facilitating decision-making that is driven by commercial factors, rather than by tax considerations. Businesses, not government, are best placed to judge how to operate and structure themselves.’<sup>217</sup>

Rather, therefore, than taking a doctrinaire stance, the 2001 document confronts ‘head on’ the fact ‘that multinational businesses are likely to increase in importance’,<sup>218</sup> and, in an oblique reference to Nigel Lawson’s corporation tax reforms of the 1980s,<sup>219</sup> emphasises how the world has moved on since then.<sup>220</sup> This being so, it is ‘fair tax competition’ between countries that will allow ‘business to exploit real commercial opportunities’.<sup>221</sup> Key to this are the maintenance of ‘a low rate, broad base system’, and the better alignment of commercial profits and tax profits.<sup>222</sup> However, it also involves the removal from the code of ‘outdated and ineffective restrictions’,<sup>223</sup> as illustrated, for instance, by the deletion of certain restrictions on ‘the transfer of assets and the use of tax losses within multinational groups’,<sup>224</sup> and the abolition of withholding tax on interest payments.<sup>225</sup>

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<sup>216</sup> *Ibid.*

<sup>217</sup> *Ibid.*, para. 1.6.

<sup>218</sup> *Ibid.*, para. 1.8.

<sup>219</sup> *Ibid.*

<sup>220</sup> See Louis MacNeice’s, *Autumn Journal: a Poem* (London: Faber and Faber, 1939), p. 39.

<sup>221</sup> See H.M. Treasury and Inland Revenue, n. 18 above, para. 1.11.

<sup>222</sup> *Ibid.*, paras 1.12 and 1.14-1.15.

<sup>223</sup> *Ibid.*, paras 1.12 and 1.19.

<sup>224</sup> *Ibid.*, para. 1.19 (see ICTA 1988, s. 402(3A), added by FA 2000, s. 97, and Sched. 27, para. 1).

<sup>225</sup> See HM Treasury News Release BN2J, *Withholding tax on international bond interest abolished*, 21 March 2000 (reprinted at [2000] SWTI 458-460); H.M. Treasury Press Release, *A more competitive environment for business*, 8 November 2000 (reprinted at [2000] SWTI 1588-1594); Budget Note 13/01, *Withholding tax on intra-UK corporate interest etc*, 7 March 2001 (reprinted at [2001] SWTI 442-444); FA 2001, s. 85; FA 2002, s. 94; FA 2004, ss. 98-106 (but see now ITA 2007, s. 874). See *Taxation of Companies and Company Reconstructions*, ed. by Richard

Besides removing distortions, the elimination of ‘market failures’ is also detectable in the code. According to Balls, Grice and O’Donnell, these exist ‘when the competitive outcome of markets is not efficient from the point of view of the economy as a whole’.<sup>226</sup> In the 2001 document, the 1999 removal from the corporation tax code of the obligation to pay advance corporation tax (ACT), and its replacement by payments of corporation tax on account, under CTSA, is seen as one example of the removal of distortion,<sup>227</sup> while the introduction of ‘a new research and development (R&D) tax credit’<sup>228</sup> ... aimed at encouraging innovation by large companies in recognition of the wider benefits to the economy that flow from R&D expenditure’,<sup>229</sup> is a way to remedy a significant ‘market failure’.<sup>230</sup>

It will be appreciated from all of this that a particular, highly developed, idea of efficiency runs as a key value through the corporation tax code. Before examining the accounting theme and the European and international theme in more detail, as offering specific examples, it is important to locate these features of the code, if only briefly, in economic thinking more generally, and to spell out some implications for this highly complex public law example of economic regulation.

If we try to match the idea of efficiency as just outlined with Smith’s four ‘canons’, albeit as filtered through Meade, we find mainly divergences. Smith, in his fourth ‘canon’, famously related efficiency – tax efficiency – to the yield from the tax. A prince would not be prudent to impose an unprofitable tax, one which required ‘a great number of officers’,<sup>231</sup> or which subjected people over-much ‘to the frequent visits, and ... odious examination of

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Bramwell, Alun James, Mike Hardwick and John Lindsay, 8<sup>th</sup> edn (London: Sweet and Maxwell, 2002), section A3.10 (new law); App 1.6 (old law).

<sup>226</sup> See Balls, Grice and O’Donnell, n. 136 above, p. 8.

<sup>227</sup> See H.M. Treasury and Inland Revenue, n. 18 above, para. 1.16.

<sup>228</sup> See FA 2002, s. 53 and Sched. 12.

<sup>229</sup> See H.M. Treasury and Inland Revenue, n. 18 above, para. 1.17.

<sup>230</sup> *Ibid.* (environmental incentives).

<sup>231</sup> See Smith, n. 159 above, II, p. 826.

the tax-gatherers',<sup>232</sup> or which, in the language of today, imposed an 'excess burden of taxation',<sup>233</sup> because it was such as to 'obstruct the industry of the people'.<sup>234</sup> No, he should rather ensure that:

'[e]very tax ... be so contrived as both to take out and to keep out of the pockets of the people as little as possible, over and above what it brings into the publick treasury of the state.'<sup>235</sup>

Allowing for the fact that the policy documents speak of the need for corporation tax, like all taxes, to 'raise sufficient revenue for the Government to fund public services and to service debt',<sup>236</sup> and without entering here into speculation, in an area of 'large empirical uncertainties',<sup>237</sup> on how far corporation tax may impose unduly high administrative costs (for HMG)<sup>238</sup> and compliance costs (for the corporate sector),<sup>239</sup> it is plain that something more significant is contained in the corporation tax code than either Smith or Meade can capture. It is true that neutrality, as an aspect of efficiency,<sup>240</sup> is a guiding principle of the code, since the idea that commercial, not tax, considerations should drive corporate decision-making, is a recurrent theme.<sup>241</sup> Nonetheless, it is not a complete description.

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<sup>232</sup> *Ibid.*, p. 827.

<sup>233</sup> See James and Nobes, n. 20 above, pp. 20-21.

<sup>234</sup> See Smith, n. 159 above, II, pp. 826-827.

<sup>235</sup> *Ibid.*, p. 826.

<sup>236</sup> See H.M. Treasury and Inland Revenue, n. 18 above, para. 1.4.

<sup>237</sup> See Chapter 3 above, n. 181.

<sup>238</sup> 0.96 pence per pound (for 2004/2005), as against 0.76 pence per pound (for 1999/2000) (see *Revenue Law - Principles and Practice*, ed. by Natalie Lee, 24th edn (Haywards Heath: Tottel, 2006), para. [1.5]).

<sup>239</sup> See, e.g., Cedric Sandford, Michael Godwin and Peter Hardwick, *Administrative and Compliance Costs of Taxation* (Bath: Fiscal Publications, 1989), pp. 140-148 (figures for 1986-1987); PricewaterhouseCoopers LLP and World Bank Group, *Paying Taxes: The global picture* (London: PricewaterhouseCoopers, 2006); see Houlder, *Financial Times*, 8 November 2006, 4.

<sup>240</sup> Neutrality is a counter to the danger of the 'excess burden of taxation' (see James and Nobes, n. 20 above, pp. 302, 303); also Barry Bracewell-Milnes, 'A Liberal Tax Policy: Tax Neutrality and Freedom of Choice' [1976] BTR 110-121.

<sup>241</sup> See H.M. Treasury and Inland Revenue, n. 18 above, para. 1.6.

What is missing from, not only Smith's conception of efficiency, but also from most contemporary assessments of New Labour's public interest view of corporate tax policy, is an appreciation of the impact on the corporation tax code of the burgeoning, in the 1980s, of 'post-neoclassical endogenous growth theory'.<sup>242</sup> Some specific implications of this will be examined later in the discussion. For the moment, it is sufficient to note that, at the pen of its main exponents, Robert Barro,<sup>243</sup> Robert Lucas,<sup>244</sup> and Paul Romer,<sup>245</sup> it offers a way of understanding how nations get wealthier. As explained and contextualised by Diane Coyle, it goes beyond Smith's classical assessment of growth as the result of the 'invisible hand' of the market,<sup>246</sup> and beyond Robert Solow's<sup>247</sup> idea that 'the growth of outputs depends on the growth of inputs, and on how effectively these inputs are used'.<sup>248</sup> This is because, rather than regarding technical innovation and the increase of 'human capital' as exogenous to growth, post-neoclassical endogenous growth theory requires them to be factored in ('made endogenous').<sup>249</sup> The idea is that human capital (Lucas and Barro) and 'technology and the process of innovation' (Romer), once 'endogenized',<sup>250</sup> can be shown to create positive 'spillovers' that contribute to growth: 'the same bit of knowledge [as Coyle explains] can be used repeatedly without being used up; and one bit becomes the foundation for the next'.<sup>251</sup> The obvious link to the corporation tax code is with the introduction of research and

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<sup>242</sup> See Diane Coyle, *The Soulful Science: What Economists Really Do and Why it Matters* (Princeton: Princeton University Press, 2007), ch. 2.

<sup>243</sup> See Robert J. Barro, 'Economic Growth in a Cross Section of Countries' (1991) 106 *Quarterly Journal of Economics* 407-443.

<sup>244</sup> See Robert E. Lucas, 'On the mechanics of economic development' (1988) 22 *Journal of Monetary Economics* 3-42.

<sup>245</sup> See Paul M. Romer, 'Increasing Returns and Long-Run Growth' (1986) 94 *Journal of Political Economy* 1002-1037.

<sup>246</sup> See Coyle, n. 242 above, pp. 39-40; Smith, n. 159 above, I, p. 456.

<sup>247</sup> Robert M. Solow, 'A Contribution to the Theory of Economic Growth' (1956) 70 *Quarterly Journal of Economics* 65-94.

<sup>248</sup> See Coyle, n. 242 above, p. 42.

<sup>249</sup> *Ibid.*, p. 48.

<sup>250</sup> *Ibid.*, p. 51.



development credits,<sup>252</sup> but, as we shall see, its influence is more pervasive than this. With Gordon Brown having been taunted for it,<sup>253</sup> and Barro himself having been satirised by the former Conservative Chancellor, the Rt Hon. Kenneth Clarke, MP, it is hardly surprising that ‘new growth theory’ has not figured more prominently in discussions of corporation tax reform, even though O’Donnell and Balls expressly recognise its influence.<sup>254</sup>

It is thus easy to see how the corporation tax code might be a scene of conflict or potential conflict. It is not now a creature of classical, nor yet neoclassical, political economy (as before New Labour came to power, arguably, it was). It has become an instrument of post-neoclassical political economy. It is, as such, a vast regulatory instrument, an economic instrument<sup>255</sup> for encouraging growth. Efficiency here is not, as such, about creating a profitable tax; it is about economic efficiency more generally, efficiency in output. The corporation tax code is a scene of conflict, therefore, because it has been put to work in the service of economic growth, as part of a project to mould and sustain output.<sup>256</sup> It is not simply seeking to collect the fruits of growth. Once again is the truth of Carl Schmitt’s analysis being demonstrated: the political precedes and underlies the economic, and the economic energises the political.<sup>257</sup>

We can develop these points if we look at their implications for the accounting theme, and the European and international theme, incidentally nodding in the direction of compliance and enforcement. Compliance and enforcement is not a big part of this study, but we need to include it because it underpins the others. It has both a classical significance (in

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<sup>251</sup> *Ibid.*; also Brown, n. 193 above, p. 21.

<sup>252</sup> See Coyle, n. 242 above, p. 51.

<sup>253</sup> See Lipsey, n. 199 above, p. 27.

<sup>254</sup> See Balls and O’Donnell, n. 8 above, p. 30.

<sup>255</sup> See, e.g., Anthony Ogus, ‘Corrective Taxes and Financial Impositions as Regulatory Instruments’ (1998) 61 MLR 767-788.

<sup>256</sup> See *Financing Britain’s Future: Review of the Revenue Departments* (Chair, Gus O’Donnell) (Cm 6163) (London: TSO, 2004), p. 94.

helping to make the tax profitable) and a (post-) neoclassical one, in representing the removal from the system of the distortions caused by ACT.<sup>258</sup> More than this, however, we need not say.

The same is not true, however, for those parts of the corporation tax code that seek to marry tax law and accounting practice, or that seek to support the neutrality of the system in European and international markets. There are at least three different strands to the accounting theme, and their introduction in Chapter 1 sought to isolate them as follows: the two (formerly three) ‘distinct but overlapping, independent but interdependent’, separate but integrated,<sup>259</sup> special codes on corporate finance; the use, in calculating trading profits under Schedule D, Case I, of generally accepted accounting practice (GAAP); and the assimilation, in broad terms, of the taxation treatment of intangibles, including intellectual property, to their accounting treatment.

The most general of these three, the corporation tax code’s co-option of GAAP in the calculation of trading profits, serves as a way of putting the other two in context. The essence of what is at stake here is as follows. Generally accepted accounting practice helps to shape the corporation tax base because section 42(1), FA 1998, as amended first by FA 2004,<sup>260</sup> and then by Companies Act 2006 (CA 2006),<sup>261</sup> requires trading profits to be ‘computed in accordance with generally accepted accounting practice’. For the purposes of the kind of company or corporate group covered by the present study, this will be the International Accounting Standards (IASs) already encountered in the context of *Revenue and Customs Commissioners v. William Grant and Sons*,<sup>262</sup> since these have been compulsory for listed

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<sup>257</sup> See Chapter 3 above, nn. 129-130.

<sup>258</sup> See H.M. Treasury and Inland Revenue, n. 18 above, para. 1.16.

<sup>259</sup> See Chapter 1 above, n. 17.

<sup>260</sup> See FA 2004, s. 50.

<sup>261</sup> See note in Hickey and Milne, n. 2 above, 1A, pp. 3,622-3,623.

<sup>262</sup> See Chapter 2 above, n. 384.

companies since January 2005.<sup>263</sup> However, section 42(1) goes on to provide that calculation in accordance with GAAP is ‘subject to any adjustment required or authorised by law’,<sup>264</sup> the very proviso which, in *William Grant*, Lord Hoffmann declined to take as giving a green light to introduce further ‘judge-made rules’ into the interpretation of the code.<sup>265</sup>

Section 42 indicates the extent to which the corporation tax code now favours efficiency, and invites comment on the prudence of its salience. Its attractiveness is acknowledged by Judith Freedman who, while referring to the assumptions in the 2002 and 2003 policy documents, does not expressly make the link with new growth theory.<sup>266</sup> Balls, Grice and O’Donnell explicitly make the point that ‘better aligning taxable and commercial profits’<sup>267</sup> is an important way of turning the ideal of neutrality (‘that decision-making is driven by commercial factors rather than by tax considerations’)<sup>268</sup> into reality. Freedman herself points out, elsewhere, that ‘aligning taxable and commercial profits’ had been one of a small number of early business tax aspirations professed by New Labour prior to its General Election victory in 1997.<sup>269</sup> The contention in the present study is that, if the depiction of the corporation tax code as public law, as a political practice, is maintainable, then it is easy to see why a number of the key arguments against alignment (including, possibly, Freedman’s own), have been so readily discounted in the fabric of the code itself. For instance, one objection is that using the tax system to create incentives is somehow inconsistent with

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<sup>263</sup> See CA 2006, ss. 399(2)-399(3), 403(1)-403 (formerly CA 1985, s. 227); see European Parliament and Council Regulation EC/1606/02 (2002) OJ L243 1.

<sup>264</sup> See FA 1998, s. 42(1).

<sup>265</sup> See Chapter 2 above, n. 390.

<sup>266</sup> See Judith Freedman, ‘Aligning Taxable Profits and Accounting Profits: Accounting standards, legislators and judges’ (2004) 2 *eJournal of Tax Research* 71-99, 74-75.

<sup>267</sup> See Balls, Grice and O’Donnell, n. 136 above, p. 71.

<sup>268</sup> *Ibid.*, pp. 70-71; also Sanger, n. 152 above, p. 13.

<sup>269</sup> See Judith Freedman, ‘Defining Taxable Profit in a Changing Accounting Environment’ [1995] BTR 434-444, 444.

aligning commercial and taxable profits.<sup>270</sup> That may be so, but it is clear from the policy documents that alignment is consistent with a policy that relies on incentivisation, and, moreover, all that Balls, Grice and O'Donnell argue for is 'better' alignment, not complete alignment. The system of capital allowances on plant and machinery, for example, after consultation, has been retained. Furthermore, if HMG regards the corporation tax system as creating only a 'conventional' set of property rights, as is argued in the next section, one of the other main objections to alignment, its importation into the code of accountants' discretion,<sup>271</sup> will seem much less important. Much more compelling will be arguments from efficiency, and the idea that the very fact of complete alignment would, given the function of accounts, create a major disincentive to depressing profits for tax purposes.

In considering the parts of the code devoted to intellectual property and other intangibles,<sup>272</sup> on the one hand, and corporate finance, on the other, it is important to recognise that, although efficiency is again to the fore, they raise important issues additional to those raised by section 42. This is because, whilst section 42 relates only to the calculation of trading profits, leaving untouched the distinction between income and capital (including capital allowances),<sup>273</sup> the special codes cut through it, completely assimilating capital and income.<sup>274</sup> An important, though little-noted consequence of this, as David Southern says (speaking only of the special codes on corporate finance) is that, in the areas to which the special codes relate, the corporation tax base has been changed from profits to expenditure,

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<sup>270</sup> See Freedman, n. 266 above, p. 75.

<sup>271</sup> *Ibid.*

<sup>272</sup> See the excellent overview in Sue Whiting, *Corporation Tax 2005/2006* (Kingston upon Thames: CCH, 2005), para. 3.20.2.

<sup>273</sup> See H.M. Treasury and Inland Revenue, n. 213 above; H.M. Treasury and Inland Revenue, n. 214 above.

<sup>274</sup> See Whiting, n. 272 above (intangibles regime applies only to intangibles acquired, or created, after 31 March 2002).

as in the case of VAT.<sup>275</sup> The reason, as Southern trenchantly points out, is that '[a]ny measure of income requires that capital be maintained',<sup>276</sup> something which occurs only if an 'accounts based approach' does not (inconsistently) try to assimilate capital to income. Efficiency is evidently seen as so important in these parts of the code that it is preferred to consistency.

Discussion of the impact of the special codes on the corporation tax base, and our focus on the latter, takes us back to the role of efficiency in the European and international theme. This involves an exploration of the uneasy boundary between the public interest as the furthering of economic growth, through membership of the EU and GATT 1994/WTO,<sup>277</sup> and the public interest as the protection of the national tax base. The latter touches on fairness issues, and one of its specific applications, in relation to transfer pricing, is therefore discussed below. We can approach the relevant issues in stages, by moving from the limited legislative intervention by EU institutions countenanced by the UK, to the highly prudential embodiment in the corporation tax code of the consequences of the various 'milestone' decisions of the European Court of Justice (ECJ).

The limited legislative impact on the UK's corporation tax base of the five directives<sup>278</sup> so far adopted has often been noted.<sup>279</sup> They are reflected in the now long-standing amendments to the corporation tax code, in the code's provisions on corporate

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<sup>275</sup> See David Southern, *Taxation of Corporate Debt, Foreign Exchange and Derivative Contracts*, 7<sup>th</sup> edn (London: Lexis Nexis, 2004), p. 2.

<sup>276</sup> *Ibid.*

<sup>277</sup> See the ECJ's discussion of Member State and Community membership in Cases C-21 to 24/72, *International Fruit Company NV v. Produktschap voor Groenten en Fruit* [1975] 2 CMLR 1, para. 18.

<sup>278</sup> See Chapter 1 above, n. 38; see Ben J.M. Terra and Peter J. Wattel, *European Tax Law*, 4<sup>th</sup> edn (The Hague: Kluwer Law, 2005), chs 16, 10, 9, 11, 14 and 13; Paul Farmer and Richard Lyal, *EC Tax Law* (Oxford: Clarendon Press, 1994), chs 11-16; David W. Williams, *EC Tax Law* (London: Longman, 1998).

<sup>279</sup> See, e.g., Farmer and Lyal, n. 278 above, pp. 246-247; Williams, n. 278 above, chs 8 and 10.

reconstructions, intra group dividends, and interest and royalty payments.<sup>280</sup> Adopting the analysis used throughout the study, it can be seen that these various manifestations of EU public law<sup>281</sup> represent, as incorporated in the corporation tax code, the outer limits of prudent legislative endeavour on matters specifically involving Community law and (corporate) taxation. We have to remember that even the Lisbon Treaty contains no mandate for direct tax harmonisation,<sup>282</sup> and that what energises and makes the rights and obligations spelt out in these fragmentary pieces of paper real, are the successive judgments of HMG as to where the UK's national interest lies, and the temporally limited acceptance by the British public that HMG has balanced the relevant ends and means correctly. That some, especially those perhaps of a technocratic or Aristotelian frame of mind,<sup>283</sup> find this disappointing,<sup>284</sup> goes without saying. Prudence may require a new approach, in the public interest, in due course. For the moment, however, it stands for the (often rather uncomfortable) reality. The reality can be observed both at the level of the practice of politics, as in Gordon Brown's idea that the public interest is served, not by tax harmonisation, but by free and open (i.e. 'fair') tax competition, and also at the level of theory, or at least at the level of those theories likely to be translated into practice. Unless even the optional adoption of the proposed common consolidated corporate tax base (CCCTB) can convincingly be shown to serve the

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<sup>280</sup> See, e.g., TCGA 1992, Chapter 2 (ss. 126-140G) ('Reorganisation of Share Capital, Conversion of Securities, etc.').

<sup>281</sup> See Chapter 1 above, nn. 210 and 211.

<sup>282</sup> See *A guide to the Treaty of Lisbon: European Union insight January 2008*, available from [www.lawsociety.org.uk](http://www.lawsociety.org.uk) (accessed 17 March 2008).

<sup>283</sup> See Claudio M. Radaelli, *The Politics of Corporate Taxation in the European Union: Knowledge and International Policy Agendas* (London: Routledge, 1997) (see Chapter 1 above, n. 127; Chapter 3 above, n. 68); Claudio M. Radaelli, *Technocracy in the European Union* (London: Longman, 1999) (see Chapter 1 above, n. 198; Chapter 2 above, n. 45; Chapter 3 above, n. 241); Claudio M. Radaelli, 'The Political Economy of EU Direct Tax Policy', in *Contemporary Issues in Taxation Research*, ed. by Andy Lymer and David Salter (Aldershot: Ashgate Publishing, 2003), pp. 145-165 (see Chapter 1 above, n. 199; Chapter 3 above, n. 68).

<sup>284</sup> See, e.g., Stephens, *Financial Times*, 15 January 2008, 17.

British national interest,<sup>285</sup> it has no chance of becoming a reality as far as the UK is concerned.

The legislative interventions just discussed (actual or proposed) reflect the efficiency value in the code in different ways. They have tended to become and remain realities only insofar as they have assisted HMG in its professed aim of using the EU to enhance competition and promote innovation, in the push for a 'sustainable' rise in 'the rate of UK productivity growth'.<sup>286</sup> This is why, despite HMG's wariness of the EU, the occasional arguments made in favour of export subsidies for small manufacturers<sup>287</sup> (whatever technical possibilities may arise under state aid law or WTO subsidies rules) remain thoroughly out-with the mainstream of political and economic debate.<sup>288</sup>

It is in the context of the legislative impasse illustrated by the corporate tax directives that the balance between efficiency and the protection of the tax base, embodied in the code's responses to ECJ decisions, should be considered. Whatever else may be said, there is no evidence to suggest that the ECJ's activity in this area is seen in either Whitehall or Westminster as anything other than a source of apprehension and irritation. The prudential nature of the response, both of HMG and of the judiciary, to the *Marks and Spencer* and *Cadbury Schweppes* rulings, has already been referred to in Chapter 3.<sup>289</sup> It is only necessary here to draw out two further points. First, as already suggested, the provisions of the code

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<sup>285</sup> See Chapter 3 above, n. 72.

<sup>286</sup> See Balls, Grice and O'Donnell, n. 136 above, p. 8.

<sup>287</sup> An idea that occasionally forms the subject matter of radio interviews with managing directors of small engineering companies around Budget time.

<sup>288</sup> See, notoriously, the US Foreign Sales Corporation scheme (noted by Minder and Alden, *Financial Times*, 1-2 October 2005, 7; Beattie and Minder, *Financial Times*, 14 February 2006, 6); for background, see Raymond H.C. Lujala, 'WTO Agreements versus the EC Fiscal Aid Regime: Impact on Direct Taxation' (1999) 27 *Intertax* 207-225, 212-216; Yarif Brauner, 'National Report The United States', in *WTO and Direct Taxation*, ed. by Michael Lang, Judith Herdin and Ines Hofbauer (The Hague: Kluwer Law, 2005), pp. 727-760; for the UK's situation, see Caroline Våljemark, 'National Report United Kingdom', *ibid.*, pp. 685-725.

<sup>289</sup> See Chapter 3 above, nn. 349-353.

designed to embody ECJ decisions on the European Treaty's 'fundamental freedoms' trace a delicate boundary between efficiency and, as will be seen below, a species of fairness customarily referred to as 'inter-nation equity'. Secondly, this being so, the solutions that they embody will always be contentious, the more so since they temper the opportunities offered by the single market with a concern for the integrity of the UK's corporate tax base, a compromise usually manifested by the prudent and studiously lawful nature of the relevant legislative conditions.<sup>290</sup>

The foregoing should leave us with a sense both of the dream and of the reality. Before taking up the threads of fairness, it is therefore appropriate to take stock. Efficiency, in the corporation tax code, is clearly the motor of fairness. Balls, Grice and O'Donnell sum this up thus:

‘ ... [T]he Government has ... sought to promote, on the one hand, competition, innovation, and the enterprise economy, and on the other hand, a modern welfare state and world class public services as the routes to an efficient and fair Britain in which individuals can realise their potential.’<sup>291</sup>

This, of course, is an ideology. What it suggests, however, is not simply that fairness has a political dimension, something we would expect, but that efficiency does so too. In the context of this ideology, the efficiency value embedded in the corporation tax code is not simply a technical, or technocratic, one. Were the code still to be in its pre-1993 shape,<sup>292</sup> such an argument might wash, but now in 2008 the code has been transformed. No, the particular idea of efficiency that it both embodies, and is intended to serve, is, potentially at least, highly conflictual. It is not simply the efficiency of a tax that, within the fourth of

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<sup>290</sup> See Snape, n. 15 above, p. 404n.

<sup>291</sup> See Balls, Grice and O'Donnell, n. 136 above, pp. 5-6.

<sup>292</sup> i.e. the date the FOREX rules were introduced under the Conservative Government of the Rt Hon. John Major, MP.



Smith's 'canons', is profitable to the sovereign. Instead, it is the efficiency of what might be envisaged as an attempt to create a vast economic instrument for increasing output over the long haul. That there has been massive economic growth since 1997 no one could seriously deny<sup>293</sup> and, although it is impossible to link the corporation tax code directly with that process, the informing idea of the code is certainly broadly consistent with it. The inconsistency may lie in its inevitable 'complexity'. Conclusive judgments are difficult, but it may be that the use of the code as a regulatory instrument has put the satisfaction of Smith's fourth 'canon' very difficult to realise. The fact that the code seems to work is an indication that the particular balance that it strikes continues, for all its 'complexity', to reflect a measure of constituent power. With this in mind, we need to ask what the fairness value can be said to add to this analysis.

## **Fairness**

If we read closely into the corporation tax code, and compare certain provisions with the relevant policy statements, we find that each contains a highly particularised conception of fairness. More obviously than efficiency, fairness can be seen as one of W.B. Gallie's 'essentially contested concepts',<sup>294</sup> in William Connolly's words, a concept that describes a 'valued' state of affairs, which 'involves reference to several dimensions', and enables people 'to interpret even ... shared values differently as new and unforeseen situations arise'.<sup>295</sup> Not 'radically confused', but a concept whose 'original exemplar' has an 'authority

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<sup>293</sup> See Brittan, *Financial Times*, 23 March 2007, 15.

<sup>294</sup> See W.B. Gallie, 'Essentially Contested Concepts' (1955-1956) 56 *Aristotelian Society (Proceedings)* 167-198.

<sup>295</sup> See William E. Connolly, *The Terms of Political Discourse*, 3<sup>rd</sup> edn (Oxford: Blackwell, 1993), p. 10.

... acknowledged by all the contestant users of the concept',<sup>296</sup> fairness in the corporation tax context needs to be very carefully situated.

It is the first task of this part of the discussion to isolate the characteristics of the idea in this context, and to situate them relative to ideas of fairness that are ubiquitous in the taxation literature.<sup>297</sup> That this will give us a clearer sense of this, the second main value immanent to the code, goes without saying. What it will also do, however, is to enable us to reflect, as with efficiency, on how the use of the idea has been shaped by the institutions and processes discussed in previous chapters. Such conclusions as we are able to draw on this question will in turn enable us to assess the strengths and weaknesses of the fairness immanent to the corporation tax code, and, as with efficiency, to suggest why, despite concerns over its 'complexity' and its 'instability', the code has so far proved effective.

Corporation tax policy documents have contained a consistent statement of the constituent elements of fairness ever since the present government took office in 1997. The tensely prepared Budget report, of July that year,<sup>298</sup> placed fairness in the context of the various dimensions of efficiency discussed above. As will be recalled, encouraging fairness was one of the 'clear principles' on which tax policy in general had to be based,<sup>299</sup> and it meant that the tax system 'should avoid the less well off bearing an unfair burden'.<sup>300</sup> Recalling the discussion in Chapter 3 above,<sup>301</sup> it will be noted that these statements were clearly central to the ideology of the public interest that the incoming New Labour government espoused. Fairness is a value, 'essentially contested' though it may be, and it is

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<sup>296</sup> See Gallie, n. 294 above, p. 180; John Rawls, *A Theory of Justice*, rev. edn (Oxford: Oxford University Press, 1999).

<sup>297</sup> See James and Nobes, n. 20 above, ch. 5; Musgrave, n. 143 above, p. 160.

<sup>298</sup> See House of Commons Papers, Session 1997-1998, 85, n. 183 above; see Chapter 1 above, n. 380; see Hugh Pym and Nick Kochan, *Gordon Brown: The First Year in Power* (London: Bloomsbury, 1998), pp. 54-58, ch. 5.

<sup>299</sup> See House of Commons Papers, Session 1997-1998, 85, n. 183 above, para. 1.68.

<sup>300</sup> *Ibid.*, paras 1.66-1.69.

at least as important as efficiency. Its ‘contestedness’ means, however, that how it applies to particular situations may not, however, be self-evident. Its importance is apparent, too, from the reform documents of 2001, 2002 and 2003, already discussed in the efficiency context.<sup>302</sup> In the 2001 document, HMG fleshed out this earlier statement of the importance of fairness, again relative to that of efficiency. Fairness had two functions, one of which was that of ‘ensuring [that] individual businesses pay their fair share of tax in relation to their commercial profits and compete on a level playing field’.<sup>303</sup> Stripping away the metaphor, and replacing it with something like ‘without unfair advantage’, deciding what is fair in this context plainly involves a process of comparing a company’s commercial profit level with the amount of corporation tax that it is paying, and, possibly, of comparing those tax levels with other, similar, companies. The other function of fairness disclosed by the 2001 document, one framed in specifically (welfare) economics terminology, was that of utilising corporation tax ‘to correct market failures that impose wider costs on society’,<sup>304</sup> always provided of course that ‘the tax system is the best policy instrument’<sup>305</sup> for this purpose. Conceived in terms of these two functions, fairness was viewed as being on a par with efficiency as a value shaping the corporation tax code. These formulae were repeated in relation to the specific reform proposals contained in the 2002 document and (by reference) the 2003 document.<sup>306</sup>

For anyone familiar with the theoretical literature, these recurrent formulations of fairness present certain rather surprising features. First, they make only implicit reference to

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<sup>301</sup> See pp. 193-197 above.

<sup>302</sup> See nn. 18, 213 and 143 above.

<sup>303</sup> See H.M. Treasury and Inland Revenue, n. 18 above, para. 1.7.

<sup>304</sup> *Ibid.*; also Balls, Grice and O’Donnell, n. 136 above, p. 6.

<sup>305</sup> See H.M. Treasury and Inland Revenue, n. 18 above, para. 1.7; also Wales, n. 182 above, p. 549.

<sup>306</sup> See H.M. Treasury and Inland Revenue, n. 213 above, para. 1.5; also H.M. Treasury and Inland Revenue, n. 143 above, para. 1.4.

those long-established components of fairness, ‘vertical equity’ and ‘horizontal equity’.<sup>307</sup> In the hands of Smith (read as argued in the earlier part of the chapter), who based his argument on Hobbes,<sup>308</sup> Locke and Pufendorf,<sup>309</sup> fairness – or ‘equality’ in taxation – is encapsulated by the ‘benefit principle’,<sup>310</sup> which was subsequently taken up by Hayek<sup>311</sup> and rendered thus by Smith himself:

‘The subjects of every state ought to contribute towards the support of the government, as nearly as possible, in proportion to their respective abilities; that is, in proportion to the revenue which they respectively enjoy under the protection of the state.’<sup>312</sup>

What Smith was postulating here, of course, was the prudential need for a ruler to ensure, so far as it could, not necessarily that taxpayers contribute according to their ‘ability to pay’,<sup>313</sup> but that they ‘contribute in proportion to the benefit they derive from government’.<sup>314</sup> Although the benefit principle is reflected to a degree in the 2001 policy document’s second ‘principle’, the need to ‘ensure fairness between all stakeholders in the UK economy, so all sections make a fair contribution to the future of the UK’,<sup>315</sup> it is not as prominent as the need to combat tax avoidance. The ‘brokenness’ of the fairness concept, its ‘essentially

<sup>307</sup> See, especially, Murphy and Nagel, n. 22 above, ch. 2; Musgrave and Musgrave, n. 143 above, ch. 13.

<sup>308</sup> See Hobbes, n. 148 above, pp. 386-387; Dudley Jackson, ‘Thomas Hobbes’ Theory of Taxation’ (1973) 21 *Political Studies* 175-182, 176-177.

<sup>309</sup> See Edwin R.A. Seligman, *Progressive Taxation in Theory and Practice*, 2<sup>nd</sup> edn (Princeton, N.J.: American Economic Association, 1908); Musgrave, n. 143 above, pp. 61-68; Murphy and Nagel, n. 22 above, pp. 192-193. On Seligman, see Ann Mumford, *Taxing Culture: Towards a theory of tax collection law* (Aldershot: Ashgate Dartmouth, 2002), ch. 3.

<sup>310</sup> But see Jane Frecknall Hughes, ‘The Concept of Taxation and the Age of Enlightenment’, in *Studies in the History of Tax Law: Volume 2*, ed. by John Tiley (Oxford: Hart Publishing, 2007), pp. 253-286, quoting D.P. O’Brien, *The Classical Economists* (Oxford: Clarendon Press, 1975), p. 241.

<sup>311</sup> See F.A. Hayek, *The Constitution of Liberty* (London: Routledge and Kegan Paul, 1960), pp. 315-316 (see Murphy and Nagel, n. 22 above, pp. 192-193).

<sup>312</sup> See Smith, n. 159 above, II, p. 825.

<sup>313</sup> See Mill, n. 161 above, pp. 169-187; but see Pigou, n. 169 above, pp. 43-44.

<sup>314</sup> See Murphy and Nagel, n. 22 above, p. 16.

<sup>315</sup> See H.M. Treasury and Inland Revenue, n. 18 above, para. 1.4.

contested' nature, is thus easily illustrated. Even on the Left it is 'contested', since it is a substitution for the sharply progressive levels of personal income tax that R.H. Tawney had thought that fairness – or, in his word, 'equality' – required.<sup>316</sup> The startling contrasts still reported by the IFS as to inequality in the UK ensure that the argument on the Left will continue.<sup>317</sup>

Secondly, the concept of fairness invoked in the corporation tax policy documents suggests an idea, not of tax fairness as such, but of the role of corporation tax in creating a fairer society.<sup>318</sup> The discussion in Chapter 3 illustrated how HMG views corporation tax reform as a means of advancing the public interest. In assessing the fairness implications of the role thereby assigned to the tax, it is argued here that the ideology that corporation tax serves owes much to the analysis of taxation in general set forth in Liam Murphy and Thomas Nagel's, *The Myth of Ownership*.<sup>319</sup> When we first encountered Murphy and Nagel's work in Chapter 1, it was to place the accent on their notion of the 'conventionality of property', and to ascribe the work to the 'liberal normativist' tradition of Rawls and Dworkin.<sup>320</sup> Here, we need to stress the work's emphasis on taxation as the key instrument in distributive justice, or 'political morality',<sup>321</sup> and to show its practical realisation of a 'conventional' idea of property, 'as what is created by the tax system, rather than what is disturbed or encroached on',<sup>322</sup> by it. Indeed, Murphy and Nagel's concluding chapter could almost have served as a normative 'blueprint' for income tax policy under the Brown

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<sup>316</sup> See R.H. Tawney, *Equality*, 4<sup>th</sup> edn (London: George Allen and Unwin, 1952), pp. 165-167.

<sup>317</sup> See Mike Brewer, Alissa Goodman, Michal Myck, Jonathan Shaw and Andrew Shephard (eds), *Poverty and inequality in Britain: 2004* (London: The Institute for Fiscal Studies, 2004), pp. 9-22; Mike Brewer, Luke Sibieta and Liam Wren-Lewis, *Racing away? Income inequality and the evolution of high incomes* (London: Institute for Fiscal Studies, 2008); Giles, *Financial Times*, 18 January 2008, 3.

<sup>318</sup> See Balls, Grice and O'Donnell, n. 136 above, p. 7.

<sup>319</sup> Oxford: Oxford University Press, 2002.

<sup>320</sup> See Chapter 1 above, nn. 364 and 365.

<sup>321</sup> This term is being used here in a 'Dworkinian' sense (see Murphy and Nagel, n. 22 above, p. 12).

Chancellorship.<sup>323</sup> The apparent correspondence may also reflect something of Gordon Brown's well-known predilection for Rawls's thought<sup>324</sup> and for American political (and also economic) theory in general.<sup>325</sup> The idiosyncrasies of the reality are perhaps a neat illustration of the limitations of the political morality of Rawls and Dworkin in practice.<sup>326</sup> What we have in the code, therefore, is a fairness that is contentious, that seems to place a greater emphasis on anti-avoidance than on 'progressivity', and that relies on the 'conventionality' of property to implement a version of societal fairness,<sup>327</sup> rather than tax fairness as such. Illustrations of the last of these points, admittedly a particularly controversial one, will be examined in a moment.

In the corporation tax policy documents of 2001 to 2003, the conception of fairness as societal fairness, along the lines just analysed, is thus closely aligned with the curtailment of corporation tax avoidance. This is significant because, in Murphy and Nagel's account, the impact on fairness of tax avoidance is barely touched on. Part of the reason for the omission may be that Murphy and Nagel's discussion does not specifically address corporation tax issues, and corporation tax in the UK is the area in which anti-avoidance measures have become particularly prevalent. 'Countering artificial<sup>328</sup> tax avoidance in the UK corporate tax environment will remain a priority',<sup>329</sup> the 2001 document promised, and, although

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<sup>322</sup> *Ibid.*, p. 175.

<sup>323</sup> *Ibid.*, pp. 181-188.

<sup>324</sup> See Robert Peston, *Brown's Britain* (London: Short Books, 2005), p. 30, who recounts Gordon Brown's fondness for Rawls's "'maximin" rule' (see Amartya Sen, *On Economic Inequality*, enlarged edn (Oxford: Clarendon Press, 1997), pp. 22-23).

<sup>325</sup> See Simon Lee, *Best for Britain? The Politics and Legacy of Gordon Brown* (Oxford: Oneworld, 2007), pp. 55-56 (Sandel's 'moral limits of markets': see Chapter 3 above, n. 73); also Keegan, n. 191 above, pp. 12-13; Pym and Kochan, n. 298 above, pp. 98 (Reich), 113 (Reich ('the Third Way') and Summers); Brown, n. 202 above, pp. 145, 272 (Sandel) and 84 (Greenspan).

<sup>326</sup> See above, n. 58.

<sup>327</sup> See Balls, Grice and O'Donnell, n. 136 above, p. 7.

<sup>328</sup> See the use of the expression 'fictitious or artificial transaction', in F(No. 2)A 1915, s. 44(3) (noted by Southern, n. 275 above, p. 490), a criminalising measure relating to excess profits duty.

<sup>329</sup> See H.M. Treasury and Inland Revenue, n. 18 above, para. 1.20.

similarly forthright general statements do not appear in the 2002 or 2003 documents, the importance of anti-avoidance legislation to fairness does.<sup>330</sup> The result of the emphasis on corporation tax anti-avoidance measures in the pursuit of fairness is that this is what, in the real world of representative institutions and corporate power, and allowing for adjustments in the name of prudence, a ‘Rawlsian’ distributive justice might look like. There is a strong sense of tax law as ‘moulding’ a fairer society, rather than of it as something with which the unwary may be unfortunate enough to collide.<sup>331</sup>

With these points in mind, we turn to four aspects of the corporation tax code that, at the beginning of the study, we used to exemplify what has been called ‘the anti-avoidance theme’ in corporation tax reform.<sup>332</sup> These elements address four types of problem, each of which is an almost inevitable consequence of a tax that uses corporate profits as its base,<sup>333</sup> and which relies on the time-honoured distinction between ‘income and chargeable gains’.<sup>334</sup> The first, second and fourth measures deal with attempts to manipulate deductions from the corporation tax base, while the third addresses attempts to allocate profits between companies in a group.

First, there is the broad ‘general anti-avoidance rule’, which, since 2002, has been common to each of the special codes on the tax treatment of loan relationships, FOREX and financial instruments.<sup>335</sup> The well known ‘paragraph 13’ prevents deductions which are attributable to ‘unallowable purposes’,<sup>336</sup> and, so far as it concerns loan relationships, it

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<sup>330</sup> See H.M. Treasury and Inland Revenue, n. 213 above, paras 1.5 and 1.6; also H.M. Treasury and Inland Revenue, n. 143 above, para. 1.4.

<sup>331</sup> See Shklar, n. 109 above, p. 7; also Adam Tomkins, ‘In Defence of the Political Constitution’ (2002) 22 OJLS 157-175.

<sup>332</sup> See Chapter 1 above, nn. 27-36.

<sup>333</sup> *Ibid.*, n. 9; see ICTA 1988, s. 8(1).

<sup>334</sup> See ICTA 1988, s. 6(4)(a).

<sup>335</sup> See Chapter 1 above, n. 23.

<sup>336</sup> *Ibid.*, n. 30.

states that deductions<sup>337</sup> are to be disregarded to the extent that, ‘on a just and reasonable apportionment, [they are] ... attributable to ... [an] unallowable purpose’.<sup>338</sup> An ‘unallowable purpose’, meanwhile, is one ‘which is not amongst the business or other commercial purposes of the company’.<sup>339</sup> This wording has a number of features that, prior to its introduction, were, if not unprecedented, then certainly unusual.<sup>340</sup> The novelty lay in HMRC’s competence to make a ‘just and reasonable apportionment’ of the deductions, and in the competence given to the judges to define the outer limits of an ‘unallowable purpose’. The positing of the rule, as we have seen, provoked a reaction that, given the concept of fairness explained above, seems predictable.<sup>341</sup> Even today, Bramwell hints at the difficulties of interpretation that the rule presents;<sup>342</sup> Ghosh and Johnson assert that it ‘has caused, since its inception, inevitable uncertainty and controversy’;<sup>343</sup> and Southern considers it to be of ‘limited [practical] application’, given its ‘inherent limitations and ... the law of diminishing returns’.<sup>344</sup> A Tory backbencher, Mark Field, MP,<sup>345</sup> whose early training was as a City solicitor, neatly linked these uncertainty concerns to the idea of fairness reflected in paragraph 13, as well as to the ideological difference implied, when the rule was confirmed and extended in 2002:

‘The City of London is an important financial centre and a centre of invisible earnings for this country. I have a philosophical concern that a feeling exists that taxes must be raised,

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<sup>337</sup> Called ‘debits’ in the legislation (see FA 1996, Sched 9, para. 13(1)).

<sup>338</sup> See FA 1996, Sched. 9, para 13(1).

<sup>339</sup> See FA 1996, Sched. 9, para. 13(2).

<sup>340</sup> See Southern, n. 275 above, pp. 490-491; also Hole [1996] BTR 347-358, 355-356.

<sup>341</sup> The original FB 1996 draft clauses, which became FA 1996, Sched. 9, para 13(1), referred to companies becoming parties to transactions ‘otherwise than in good faith’ (see Edge, *Tax Journal*, 14 December 1995, 4-5, 4).

<sup>342</sup> See Bramwell, n. 225 above, para. A3.9.

<sup>343</sup> See Julian Ghosh and Ian Johnson, *Taxation of Loan Relationships and Derivatives* (London: Butterworths LexisNexis, 1999), para. [6.31].

<sup>344</sup> See Southern, n. 275 above, p. 498.

<sup>345</sup> Cities of London and Westminster, Conservative.



and that banks and other financial institution [*sic*] must go about their business ensuring that they pay a fair amount of tax; it is somehow seen as illegitimate to avoid tax and utilise the tax system. The idea that financial institutions should be willing to take everything on the chin and not use the system to their benefit is a matter of concern.’<sup>346</sup>

In the same debate, Ruth Kelly, MP, the Economic Secretary to the Treasury,<sup>347</sup> reiterated the values underlying paragraph 13, as well as the ideological gulf:

‘I do not for a moment share the philosophical doubts of the hon. Member for Cities of London and Westminster about the legitimacy of raising a fair share of taxation from particular individuals or companies. I take the principled view, which I think is shared on the Labour Benches, that we should create a level playing field where everyone pays a fair share of tax. That is what the clause is designed to do.’<sup>348</sup>

Paragraph 13 is thus one of those provisions that highlight especially clearly both the ideology, and the configuration of power, immanent to the corporation tax code. The alignment of parties in the House of Commons, as well as its institutional organisation, have, in other words, given the corporation tax code a strong undertow of societal fairness. It seems, moreover, that paragraph 13 applies this idea to loan relationships in a way that reflects a ‘conventional’ view of property, and that, in so doing, tax law is being put to work to mould a fairer society. People may disagree about what fairness requires, but that is not relevant here. What is relevant is that the institutions of representative democracy have accorded it a particular nature and scope, and, in doing so, have recognised that property rights are ‘conventional’ rather than ‘moral’ or ‘natural’.<sup>349</sup> That a loan relationship may not be caught by paragraph 13 is not quite a case of being, in Walton J.’s aphorism, ‘untaxed by

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<sup>346</sup> See Hansard HC Standing Committee F, 11 June 2002, col. 323.

<sup>347</sup> See Chapter 1 above, n. 24.

<sup>348</sup> See Hansard HC Standing Committee F, 11 June 2002, col. 325.

<sup>349</sup> See Murphy and Nagel, n. 22 above, p. 175 (see Chapter 1 above, n. 363); also Loughlin, n. 39 above, ch. 7, on rights generally.

concession’,<sup>350</sup> but the conceptualisation of tax law embodied in paragraph 13 is equally not the Diceyan view of tax law implicit in the MP for London and Westminster’s comments. The wording of paragraph 13 has hardly ever been judicially tested,<sup>351</sup> but, when the testing comes, judges will have competence to remould the property rights created by a loan relationship. The extent to which they calculate that they have the capacity so to do remains to be seen.

Deductions from the corporation tax base have been restricted, too, under an entirely separate provision, introduced in 2003, which applies to contributions to employee trusts.<sup>352</sup> This provision is rather less well known than paragraph 13, but it highlights an equally important point, and its existence highlights that not all of the anti-avoidance measures in the code raise anti-avoidance issues as controversial as those of paragraph 13. Schedule 24 to FA 2003<sup>353</sup> prevents a company from making a deduction from its profits when, without there being a receipt by the employee, the company makes a contribution to an employee benefit trust (an EBT).<sup>354</sup> In doing so, Schedule 24 removes a corporation tax avoidance opportunity, by denying the company a deduction until the employee is actually paid. The corporation tax treatment of contributions to EBTs is thereby ‘squared’ with the situation when the employee is remunerated directly. The issue had arisen because contributions to EBTs had been used to remunerate the directors of Dextra Accessories/Phones 4U, including

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<sup>350</sup> See *Vestey and Others v. IRC* [1979] Ch. 177 (‘one should be taxed by law, and not be untaxed by concession’ ([1979] Ch. 177, 197 (Walton J.)); also Hansard HC Public Bill Committee, 17 May 2007, cols 212-213 (Mark Hoban, MP (Fareham, Conservative)); also Chartered Institute of Taxation, *Taxed by Law, Untaxed by Concession* (London: CIOT, 2005). A later *Vestey* case, in which Walton J. also inveighed against ESCs is noted above (see Chapter 1 above, n. 321; Chapter 2 above, n. 73).

<sup>351</sup> But see *Prudential plc v. Revenue and Customs Commissioners*, analysed by Ghosh and Johnson, n. 343 above, paras. [6.121]-[6.140] (discussing now repealed FA 1994, s. 168A and similar wording (see FA 2002, ss. 83(2), 141 and Sched. 40)).

<sup>352</sup> See Chapter 1 above, n. 31.

<sup>353</sup> See FA 2003, s. 143.

<sup>354</sup> FA 2003, Sched. 24, para. 9(1), uses ‘employee benefit scheme’, which includes a trust.

its founder, John Caudwell,<sup>355</sup> and the Special Commissioners had held that the technique was not frustrated by FA 1989, s. 43(11).<sup>356</sup> Schedule 24 to FA 2003 was HMG's response to Dextra Accessories' success before the Special Commissioners, and it pre-dated HMG's subsequent successful appeal to the House of Lords.<sup>357</sup> Lord Hoffmann, delivering the only full speech, encapsulated the prudence of both the Law Lords' unanimous decision, and HMG's own legislative response:

‘ ... [T]here would be other anomalies in the construction favoured by the Special Commissioners .... By setting up a trust such as this, the taxpayer could achieve immediate deductibility of payments into the trust and postpone indefinitely the liability of employees to tax on the emoluments for which, in part, the money was eventually applied. That would enable the purpose of section 43 to be easily frustrated.’<sup>358</sup>

The logic of this point seems to have eluded the author of a short article in the *Tax Journal*,<sup>359</sup> Jonathan Levy, who had advised the taxpayer in the litigation. He wrote of the continuing ‘uncertainty’ that the Law Lords’ decision presented, and, somewhat idiosyncratically, concluded that ‘taxpayers and their advisers cannot ignore the detrimental effect that arrangements which are perceived as being aggressive can have on the courts’. Understandable as it is, this comment is surely wide of the mark. The response of H.M. Treasury to the Special Commissioners’ decision, and the Law Lords’ attitude on appeal, were each prudent responses. It was not even necessary for the judges or the Department to resort to casuistry,<sup>360</sup> or to adopt the kind of ‘conventional’ attitude to property rights

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<sup>355</sup> See Chapter 2 above, n. 110.

<sup>356</sup> Now superseded by a new FA 1989, s. 43, as inserted by ITEPA 2003, Sched. 6, para. 157.

<sup>357</sup> See *Macdonald (H.M. Inspector of Taxes) v. Dextra Accessories Ltd and Others* [2005] UKHL 47; [2005] STC 1111.

<sup>358</sup> [2005] STC 1111, para. 21.

<sup>359</sup> See Levy, *Tax Journal*, 25 July 2005, 9-11.

<sup>360</sup> See Loughlin, n. 39 above, p. 152. On casuistry, see H. Patrick Glenn, *Legal Traditions of the World*, 2<sup>nd</sup> edn (Oxford: Oxford University Press, 2004), pp. 352-353n; on ‘casuistry’ in tax law, see, e.g., *Inland Revenue Commissioners v. Scottish and Newcastle Breweries Ltd* [1982] 1 WLR

discussed above. The Paymaster General, the Rt Hon. Dawn Primarolo, MP, using familiar imagery,<sup>361</sup> spoke of Schedule 24, FA 2003, as a ‘measure [which] levels the playing field between employers who remunerate employees direct and those who do so through third parties’. What the judges were doing in *Macdonald v. Dextra Accessories* was to underline the prudence of the approach taken by HMG. Even the Opposition took this view, in its tabled amendments concentrating on points of detail only. ‘Let it be placed on the record’, said Stephen O’Brien, MP,<sup>362</sup> somewhat portentously, ‘that there is no attempt to undermine the major thrust of the Government’s policy on anti-avoidance’.<sup>363</sup>

If the two sets of provisions discussed so far illustrate ‘thick’ and ‘thin’ approaches to fairness, the major remodelling of the transfer pricing rules in 2004 may mark out a middle ground.<sup>364</sup> The idea of these provisions is to prevent profits or losses from being allocated to different parts of domestic or international groups (i.e. MNCs), in such a way as to enable group members to take advantage of differences in tax rates.<sup>365</sup> Since the measures relate solely to corporate groups, they can raise fairness issues not necessarily highlighted by the two measures discussed above. The two sets of measures already discussed relate to fairness as between taxpayers and groups of taxpayers. The transfer pricing rules have this function, to be sure, but they also address the question of fairness between states.<sup>366</sup> The amendments

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322, 325 (Lord Wilberforce); *Lingfield Park (1991) Ltd v. Shove* [2004] EWCA Civ 391, para. 4, unreported (Mummery L.J.).

<sup>361</sup> See Ruth Kelly, n. 348 above.

<sup>362</sup> Eddisbury, Conservative.

<sup>363</sup> See Hansard HC Standing Committee B, 12 June 2003, col. 542.

<sup>364</sup> See Chapter 1 above, n. 32.

<sup>365</sup> See Tiley, n. 29 above, p. 892.

<sup>366</sup> See Plender, *Financial Times*, 21 July 2004, 1; Plender, *Financial Times*, 21 July 2004, 15; Plender and Simons, *Financial Times*, 22 July 2004, 15; Brian J. Arnold and Michael J. McIntyre, *International Tax Primer*, 2<sup>nd</sup> edn (The Hague: Kluwer, 2002), ch. 4; Reuven S. Avi-Yonah, *International Tax as International Law: An Analysis of the International Tax Regime* (Cambridge: Cambridge University Press, 2007), ch. 6; Picciotto, n. 157 above, ch. 8; Angharad Miller and Lynne Oats, *Principles of International Taxation* (Haywards Heath: Tottel Publishing, 2006), ch. 14.

made by FA 2004<sup>367</sup> to Schedule 28AA, ICTA 1988, combine the corporation tax thin capitalisation regime with the provisions on transfer pricing,<sup>368</sup> and apply the expanded rules both to transactions across borders and to ones within the UK.<sup>369</sup> Subject to exceptions for ‘dormant companies’<sup>370</sup> and ‘small and medium sized enterprises’,<sup>371</sup> goods transferred, and services provided (including loans made), between group companies are therefore treated as being in return for an ‘arm’s length’ price.<sup>372</sup> Although, in extending the rules to transactions between UK-resident companies, HMG was seeking to make the rules conformable to Community law,<sup>373</sup> one of their main justifications was again that of fairness. This type of fairness is generally referred to as ‘inter-nation equity’,<sup>374</sup> but it is perhaps better thought of as being a still further implication of the benefit principle. It will be recalled that the second fundamental principle of corporation tax is that non-resident companies are taxed only on the profits of a ‘permanent establishment’ in the UK.<sup>375</sup> The non-resident is taxed in the UK, so it was once judicially stated, because of the protection that its UK possessions receive under UK law.<sup>376</sup> When FA 2004 was at Committee stage, the Paymaster General made a similar point in maintaining that: ‘[t]he rules are vital to ensure that business, especially multinationals, are taxed fairly in respect of their activities in the United Kingdom’.<sup>377</sup> Not only that, in fact, but ‘[t]ransfer pricing regulations and rules are about insuring and

<sup>367</sup> See FA 2004, ss. 30-37 and Sched. 5.

<sup>368</sup> See ICTA 1988, Sched. 28AA, paras 1A-1B, 6, 7 and 14 (1) (as expanded by FA 2004, ss. 34-36).

<sup>369</sup> See ICTA 1988, Sched. 28AA, para. 5.

<sup>370</sup> See ICTA 1988, Sched. 28AA, para. 5A (added by FA 2004, s. 31(3)).

<sup>371</sup> See ICTA 1988, Sched. 28AA, para.5B (added by FA 2004, s. 31(4)).

<sup>372</sup> See ICTA 1988, Sched. 28AA, para. 1(1).

<sup>373</sup> See Chapter 1 above, n. 44 (Case C-524/04, *Test Claimants in the Thin Cap Group Litigation v. Commissioners of Inland Revenue* [2007] 2 CMLR 31, para. AG84 (Advocate General Geelhoed).)

<sup>374</sup> See Arnold and McIntyre, n. 366 above, p. 4; also Picciotto, n. 157 above, pp. 65-68, 82-83; Roy Rohatgi, *Basic International Taxation*, 2<sup>nd</sup> edn, vol. 1 (Richmond: Richmond Law and Tax, 2005), p. 23.

<sup>375</sup> See Chapter 1 above, nn. 4-5.

<sup>376</sup> See *Whitney v. C.I.R.* [1926] AC 37, 54 (Lord Wrenbury).

protecting the corporate tax base of this country’.<sup>378</sup> This kind of fairness is not so much about the innovative shaping, but the protecting, of the public interest, ‘the national interest’,<sup>379</sup> which means protecting the UK tax base. ‘As a Minister, [said the Paymaster General] I am not prepared to allow the Exchequer risk that goes with ... [allowing MNCs] ‘to reduce taxable profits in the UK’.<sup>380</sup> This is, of course, an impeccably correct statement of HMG’s duties in the matter. The conception of fairness being played out in this part of the code is thus, possibly, not so much a reflection of an ideology of the public interest, as an illustration of the duties of HMG in protecting the tax base.<sup>381</sup> The distinction may be a slender one, but the problem raises issues common to the Community law issues discussed in Chapter 3. Prudential advancement of the public interest, in cases involving cross-border transactions, requires particular vigilance against the depredations of non-residents.<sup>382</sup>

With the transfer pricing and thin capitalisation rules seeking to forestall the erosion of the corporation tax base, by preventing the allocation of income profits among group companies, we turn finally to attempts to manipulate capital profits. This possibility arises because chargeable gains for an accounting period consist of chargeable gains minus allowable losses.<sup>383</sup> It is met by the four ‘targeted anti-avoidance rules’<sup>384</sup> (TAARs) brought

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<sup>377</sup> See Hansard HC Standing Committee A, 11 May 2004, col. 111 (Rt Hon. Dawn Primarolo, MP).

<sup>378</sup> See Hansard HC Standing Committee A, 11 May 2004, col. 112.

<sup>379</sup> See Chapter 3 above, p. 183.

<sup>380</sup> See Hansard HC Standing Committee A, 11 May 2004, col. 120.

<sup>381</sup> On this basis, Murphy’s criticisms may be misconceived: see *BBC File on Four*, 2007. ‘Companies “looting” a continent’. Radio, BBC Radio 4. 29 July. (Transcript available from [www.bbc.co.uk](http://www.bbc.co.uk).) See Chapter 2 above, n. 346.

<sup>382</sup> The virulence of the controversy over the income tax treatment of non-remitted income of resident but non-domiciled individuals may reflect something of this: see, e.g., Anon, *Financial Times*, 8 February 2008, 12 (editorial); Willman, *Financial Times*, 9-10 February 2008, 2.

<sup>383</sup> See TCGA 1992, s. 2(2)(a).

<sup>384</sup> See David F. Williams, ‘Avoidance through the creation and use of capital losses by companies’ [2006] BTR 23-33, 23-24.

in by FA 2006,<sup>385</sup> then further strengthened in FA 2007,<sup>386</sup> which are intended to block the inappropriate ‘creation and use of corporate capital losses’.<sup>387</sup> The spur to each of these measures was HMG’s analysis of information gathered under the disclosure regime introduced in 2004.<sup>388</sup> The first TAAR<sup>389</sup> dramatically excludes from the scope of the term ‘allowable loss’ a loss that accrues to a company pursuant to<sup>390</sup> arrangements whose purpose, or main purpose, ‘is to secure a tax advantage’.<sup>391</sup> The idea with this TAAR, as the Paymaster General explained in Standing Committee in May 2006, was to block ‘tax relief for capital losses where their existence or amount has been contrived, that is, where the losses that arise do not reflect commercial reality’.<sup>392</sup>

The second and third TAARs<sup>393</sup> seek to shore up what Bramwell calls ‘structural weaknesses’<sup>394</sup> in TCGA 1992, Sched. 7A, some of which had been evident to HMG since at least 1998.<sup>395</sup> The second TAAR appears in TCGA 1992, s. 184A, and restricts the buying of losses, while the third TAAR (which appears in section 184B, TCGA 1992) curbs the buying of *gains*. It is the latter that illustrates the piquant sophistication of tax avoidance schemes in this area. Bramwell illustrates the point by showing how, absent the second TAAR, a company that owned an asset with an unrealised loss might be advised to buy a company that owned an asset with an unrealised gain, the former transferring the ‘loss asset’ to the latter,

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<sup>385</sup> FA 2006 was debated as F(No. 2)B 2005, but the clause numbers of the Bill usefully correspond to the section numbers of FA 2006.

<sup>386</sup> See FA 2007, s. 32. See Chapter 1 above, n. 36.

<sup>387</sup> See Chapter 1 above, n. 36.

<sup>388</sup> See Chapter 1 above, nn. 29 and 35.

<sup>389</sup> FA 2007, s. 27 extended the first TAAR to all chargeable persons, FA 2006, s. 69 having applied only to companies.

<sup>390</sup> TCGA 1992, s. 16A (inserted by FA 2007, s. 27, which repealed FA 2006, s. 69 (see FA 2007, s. 27(6))).

<sup>391</sup> TCGA 1992, s. 16A(1)(b).

<sup>392</sup> See Hansard HC Standing Committee A, 23 May 2006, col. 313 (Rt Hon. Dawn Primarolo, MP).

<sup>393</sup> See FA 2006, s. 70.

<sup>394</sup> See Bramwell, n. 225 above, para. D9.1.1.

which would then sell both assets and set the loss against the gain for corporation tax purposes.<sup>396</sup> What the second and third TAARs state is that using losses is blocked in any case where a company is purchased mainly, or indeed wholly, ‘to secure a tax advantage’.<sup>397</sup> That they have been successful in this was attested to by the Economic Secretary to the Treasury in the debates on FB 2007.<sup>398</sup> The second and third TAARs are mirror images of each other, but the fourth, which appears in TCGA 1992, ss. 184G-I,<sup>399</sup> is quite distinct, and aims actually to shape further legislative development.

The fourth TAAR, innovative as it was, was another response to information that HMRC had received under the disclosure regime. Briefly, if ‘the main purpose’<sup>400</sup> of ‘arrangements’ into which a company enters, is to transform an income profit into a chargeable gain, so that the gain can be reduced by available losses, the use of the losses to reduce the gain is denied.<sup>401</sup> The novelty consists partly in the fact that HMRC may issue a notice informing the company of the block on the deduction,<sup>402</sup> and partly in the fact that, as already suggested, ‘[u]nlike the other measures being introduced as part of this package[,] this rule primarily provides protection against *future schemes*’.<sup>403</sup> The main safeguard for taxpayers is that HMRC may ‘issue the notice [only] when it [reasonably believes] ... that the conditions of the clause [are] ... met; ... [and] companies need not be concerned by the provisions [of

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<sup>395</sup> i.e. when what was TCGA 1992, Sched. 7AA was introduced (Sched. 7AA repealed by FA 2006, s. 70(2), which inserted TCGA 1992, s. 184F(4)).

<sup>396</sup> See Bramwell, n. 225 above, para. D9.1.4.

<sup>397</sup> See TCGA 1992, ss. 184A(1)(c) and 184B(1)(c) (see Bramwell, n. 225 above, para. D9.1.1); also Hansard HC Standing Committee A, 23 May 2006, col. 332 (Rt Hon. Dawn Primarolo, MP).

<sup>398</sup> See Hansard HC Public Bill Committee, 17 May 2007, cols 215, 222, 223 (Ed Balls, MP).

<sup>399</sup> As inserted by FA 2006, s. 71.

<sup>400</sup> See TCGA 1992, s. 184G(5) (added by FA 2006, s. 71(1)).

<sup>401</sup> See TCGA 1992, s. 184G(7) (added by FA 2006, s. 71(1)).

<sup>402</sup> See TCGA 1992, s. 184G(6) (added by FA 2006, s. 71(1)).

<sup>403</sup> See H.M. Revenue and Customs, *HMRC Guidance: Avoidance through the creation and use of capital losses by companies*, 27 July 2006 (available from [www.hmrc.gov.uk](http://www.hmrc.gov.uk) (accessed 28 July 2006)), para. 72; also H.M. Revenue and Customs, *HMRC Guidance: Capital Gains Tax -*



the TAAR] unless they receive a notice'.<sup>404</sup> An explanation is offered by the technical guidance:

'HMRC is aware that a large amount of unused capital losses is potentially available to companies, and this fact, combined with experience to date, suggest [*sic*] that there is likely to be increased activity in this area. This poses a significant risk not only to corporation tax on future capital gains, but also to corporation tax on companies' income profits.'<sup>405</sup>

In line with the approach taken in this study, these safeguards may be seen as a prudent recognition of the need for HMG to augment its constituent power. Given the objective of encouraging fairness, there is a certain prudence in the four TAARs, since they are certainly consistent, not only as between themselves, but also with other anti-avoidance measures. As David F. Williams points out, they each use 'a tax avoidance motive test', just like paragraph 13 discussed above, and like other anti-avoidance measures in FA 2002.<sup>406</sup> They are examples of 'evidence-based' policy making; they are not 'stabs in the dark'. All four TAARs, as the Paymaster General pointed out in Standing Committee, 'result from information specifically provided under the disclosure regime and are specifically targeted to deal with that'.<sup>407</sup> They reflect, in other words, the prudence of the process analysed in Chapter 3, and a democratically sanctioned configuration of values. Given the ideology of fairness discussed above, and given the public interest, it is difficult to argue with them.<sup>408</sup> Ministers are right to be sceptical of the kind of criticism levelled in Standing Committee

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*Avoidance through the creation and use of capital losses, 19 July 2007* (available from [www.hmrc.gov.uk](http://www.hmrc.gov.uk) (accessed 17 February 2008)).

<sup>404</sup> See Hansard HC Standing Committee A, 23 May 2006, col. 334 (Rt Hon. Dawn Primarolo, MP).

<sup>405</sup> See H.M. Revenue and Customs, HMRC Guidance: *Avoidance through the creation and use of capital losses by companies, 27 July 2006* (available from [www.hmrc.gov.uk](http://www.hmrc.gov.uk) (accessed 28 July 2006)).

<sup>406</sup> See FA 2002, Sched. 26, paras 23 and 24; also FA 2002, Sched. 29, para. 111.

<sup>407</sup> See Hansard HC Standing Committee A, 23 May 2006, col. 313.

debates. It is necessary, too, to be sceptical about allegations of uncertainty. The provisions are certainly intricate, but it is revealing that Bramwell is able to state the legal position on each of the four TAARs with great clarity.<sup>409</sup>

‘Between the idea/ And the reality ...’, so Eliot wrote, ‘Falls the Shadow’.<sup>410</sup> Whether he was thinking of Hegel in writing these words, or about Hegel’s immanent critique, we would prefer not to say, but it might be an image for what has been attempted here. Comparing the ideal of fairness in corporation tax, as it appears from the policy documents, with the intricate and evolving reality, is complex, yet it yields significant insights. The first of these has come from confronting the ‘brokenness’ of fairness as a concept. Disagreements about its application to specific situations prevail, both on the Left, and between Left and Right. Although there has been a certain consensus about the need for anti-avoidance measures in each of the areas examined, simmering below the surface has been a disagreement about whether HMG’s approach to avoidance has been a fair one. The Opposition attack on the measures imported to the code since 1997 has tended to be situated on the intersection of fairness and certainty.<sup>411</sup> Most of their criticism has been concerned with the ‘unfairness’ of companies not knowing for sure whether or not they fall within the scope of the new anti-avoidance provisions, or by invoking a form of procedural unfairness. As is evident, the code contains ambitious direct or indirect attempts to help bring about a fairer distribution of benefits and burdens in society, so HMG and Opposition are often, perhaps inevitably, talking past each other when fairness (anti-avoidance) issues are raised.

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<sup>408</sup> See Hansard HC Standing Committee A, 23 May 2006, col. 315 (Paul Goodman, MP (Wycombe, Conservative)).

<sup>409</sup> See Bramwell, n. 225 above, section D9.1; hence, possibly, the success that HMG has claimed for these provisions: see Hansard HC Public Bill Committee, 17 May 2007, col. 223 (Ed Balls, MP, Economic Secretary to the Treasury).

<sup>410</sup> See n. 38 above.

<sup>411</sup> See above in this chapter.

One consequence of this, as a National Audit Office (NAO) report of 2007<sup>412</sup> has indicated, is that both sides (not to mention academics)<sup>413</sup> have missed the impact of corporation tax reform for more traditional notions of ‘vertical equity’<sup>414</sup> and ‘horizontal equity’.<sup>415</sup> Reporting on the NAO’s findings, in August 2007, the *Financial Times* calculated that, given the availability of certain types of relief to only some areas of the corporate sector, the oil and gas industries, banks and insurance companies had had to assume a disproportionate share of the overall corporation tax burden.<sup>416</sup> Seven per cent. of the 700 companies within the jurisdiction of HMRC’s Large Business Service, so the *Financial Times* reported, ‘paid 67 per cent of the tax [i.e. due from the 700] while about 220 paid none and another 210 each paid less than £10m’.<sup>417</sup> Could it be that, since the unfairness has not been felt by the governing party’s wider constituency, prudence enables its significance to be downplayed?<sup>418</sup>

Secondly, a comparison of the ideal, as set out in the policy documents, and the reality, reveals a fundamentally different perspective as between HMG and the Opposition, not only as to the role of the corporation tax code, but also as to the nature of corporation tax law itself. Moreover, to the extent that the attitude of the professional members of policy networks involved in this policy area reflects the Opposition view, their arguments, far from being merely technical, have a political significance. The nub of the issue is the fact that, as contended throughout this study, corporation tax reform represents, on a comprehensive scale, a harnessing of public law, not just to map out the limits of the permissible, but to

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<sup>412</sup> See National Audit Office, *HM Revenue & Customs: Management of large business Corporation Tax* (House of Commons Papers, Session 2006-2007, 614) (London: The Stationery Office, 2007).

<sup>413</sup> See Houlder, *Financial Times*, 28 August 2007, 1 (‘It is certainly surprising’ (Michael Devereux, Oxford University Centre for Business Taxation)).

<sup>414</sup> See Murphy and Nagel, n. 22 above, pp. 13-16.

<sup>415</sup> *Ibid.*, pp. 37-39.

<sup>416</sup> See Houlder, n. 413 above; also Houlder, *Financial Times*, 25 February 2008, 4.

<sup>417</sup> See Houlder, *Financial Times*, 28 August 2007, 1.

mould the relations between corporate sector and the state, to promote a specific ideological view of the public interest.<sup>419</sup> Except to the extent that it is part of the system of rule, this development is the actualisation of the functionalist tenets of public law study.<sup>420</sup> It follows that criticism of HMG's approach needs to be carefully weighed. Much of the criticism follows from an inability to interpret the reality,<sup>421</sup> an unwillingness to forsake normative intellectual positions. Thus, when the CIOT, or the CBI, criticises tax legislation for its 'complexity', their argument is valid as far as it goes. What is important, however, is to recognise it for what it is. It represents a political position as to the role of law in the state that is fundamentally different from that taken up by HMG.<sup>422</sup> Criticism of complexity is not neutral, nor is it merely technical.<sup>423</sup>

It is thus that, with great respect to Philip Baker, QC,<sup>424</sup> who argues otherwise, there is indeed a 'principle of equality' in UK tax law, or at least a 'principle of fairness'. It is, however, not a legal principle, much less a 'rule of law value', but an 'essentially contested concept'. It is fairness as conceived of in the highly specific terms discussed above, a principle of the political jurisprudence that is the corporation tax code. It is 'high' on anti-avoidance and, as the recent NAO report has shown, 'low' on 'traditional' ideas of 'vertical equity' and 'horizontal equity'. The NAO report demonstrates the consequences for companies. Those for individuals are more strident, shocking even,<sup>425</sup> and illustrate the fact

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<sup>418</sup> See Anon, *Private Eye*, No. 1204, 22 February-6 March 2008, 28.

<sup>419</sup> See Hansard HC Public Bill Committee, 17 May 2007, col. 222 (Ed Balls, MP, Economic Secretary to the Treasury).

<sup>420</sup> See Loughlin, n. 14 above, chs 6 and 10.

<sup>421</sup> See Hansard HC Public Bill Committee, 17 May 2007, col. 224 (Mark Hoban, MP (Fareham, Conservative)).

<sup>422</sup> See, e.g., Tax Law Review Committee, n. 134 above, para. 8.2.

<sup>423</sup> See Hansard HC Public Bill Committee, 17 May 2007, cols 215-216 (Ed Balls, MP, Economic Secretary to the Treasury); also Houlder, *Financial Times*, 15 August 2007, 3.

<sup>424</sup> See Chapter 1 above, n. 113.

<sup>425</sup> See Institute for Fiscal Studies (2004) and (2007), n. 317 above; Giles, *Ibid*; Robert Peston, *Who Runs Britain?* (London: Hodder and Stoughton, 2008), pp. 3, 7-8.

that despite the anti-avoidance provisions, prudence declares so often, not for fairness, but for efficiency. What is most important, and too often elided, is the idea that the situation is one manifestation of an ideology validated, for the moment at least, by the judgment of the electorate.

## CONCLUDING COMMENTS

If readers have been willing to assent to the arguments developed in this study, what will have emerged is a somewhat novel, and, it is hoped, a realistic interpretation of the theory and values that have been at work in corporation tax reform, over the past 15 years or so. Some may, to be sure, find the picture presented a rather disturbing one. Most, it is hoped, will see in it a persuasive depiction of a hitherto somewhat under-theorised reality.

We may, therefore, feel some trepidation in spelling out, and reflecting on, the study's core conclusions. Given the complex, and layered, nature of the discussion, these are set out in detail in the final chapter. We can conveniently anticipate some of theme here, however. What the corporation tax code represents is a pattern of values that, though not perhaps ideally laid out, reflect a consensus around the imperative of economic growth, around the importance of fairness, and, in the code's shifting nature and constant change, a series of more or less prudential responses to the contingencies of an uncertain world. All criticisms of the code, and all proposals for further reform, have to take account of this, much underestimated, proposition.

If such a view of the UK's current system of corporation tax is correct, it has a number of rather startling - and unfashionable - implications, some of which might perhaps be expressed as follows. First, that the public law nature of the corporation tax code strongly

suggests the practical impossibility of a more ‘durable’, or less complex, reality. What the Economic Secretary to the Treasury said, at the Committee Stage of FB 2007, is revealing:

‘The hon. Gentleman might want to reflect a little more on the reality of tax policy making before he gives us another of his lectures on complexity ... [T]he global corporate tax system has become very complex. Many skilled and ingenious people are coming up with complex ways to avoid tax, and the Government must counter the resulting complexity.’<sup>426</sup>

If this is the case, then many of the simplification arguments are, as we might say, ‘so much chaff’; there is no qualitative or quantitative difference between corporation tax legislation and any other area of economic or social regulation. Secondly, arguments about corporation tax are not merely ‘political’; they are also ideological. If the former assertion springs from the political nature of the values immanent to the code, the latter arises from the ideological nature of the idea of the public interest itself. Prioritisations of efficiency and fairness, however delicate, might, in truth, amount to nothing less than a manifestation of the role of the state in the moulding of the public interest, of the level of the tax burden to be laid, in the first instance at least, on the corporate sector. Anti-avoidance measures with therefore provoke controversy, not just because of their tendency to increase the complexity and volume of the legislation, but also because of disagreements about the role of the state in shaping the public interest. The corporate sector has traditionally been keen on the idea of efficiency in the public interest, less so on the role of fairness. Given the political consensus, it is difficult to see a way out of complexity – certainly not by the conferring of a wide judicial discretion, and possibly not by introducing a general anti-avoidance rule either.

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<sup>426</sup> See Hansard HC Public Bill Committee, 17 May 2007, col. 216 (Ed Balls, MP). This was a response to an interjection from Brooks Newmark, MP (Braintree, Conservative).

Thirdly, given the ideological nature of the prioritisation of efficiency and fairness, sustaining the corporation tax code is, above all, an enterprise of Machiavellian prudence. If politics is really about governing, then, in the UK's representative democracy, it is about management too. The world is too uncertain, London's financial markets at once too fragile, and too valuable to the present ideological consensus, for matters to be otherwise.

## Chapter 5

### CONCLUSIONS

The purpose of this study has been to offer an interpretation of the main themes in Britain's reform of its corporation tax law. Since this is an interpretative project, the objective has not, in the main, been to proffer solutions, but to identify issues and the prospects for a constructive discussion in the future. The conclusion of the study, in essence, is that many of the criticisms of commentators in this area are at worst historically naïve, and at best expressions of rival ideological positions.

The implication of the arguments presented in this study is not that the difficulties of reforming corporation tax are inevitable or insurmountable. Rather, it is that the challenges of reform, whilst undeniable, can be understood only by an approach that emphasises the need for prudent management, and for a consistent and coherent view of the public interest. These imperatives must shape the kind of criticisms made of the corporation tax code, if future discussion is to be meaningful.

#### ‘THEORY’ AND ‘VALUES’

The principal inspiration for the study has been the idea that traditional discussions of corporate tax reform have failed to capture important theoretical issues. The absence of a theoretical dimension is worrying, since corporation tax is gradually being separated out from income tax, and its reform has long been developing a momentum of its own. Seven



main themes have been discernible in UK corporate tax reform since the early 1990s: ‘the accounting theme’;<sup>1</sup> ‘the anti-avoidance theme’;<sup>2</sup> ‘the compliance and enforcement theme’;<sup>3</sup> ‘the European and international theme’;<sup>4</sup> ‘the consultation theme’;<sup>5</sup> ‘the technical theme’;<sup>6</sup> and ‘the Departmental theme’.<sup>7</sup> The research for this study began as an examination of the interaction of the accounting theme with the last three themes, with only subsidiary reference to anti-avoidance and to European and international influences. However, as the research progressed and legislative changes gathered momentum, it became easier to justify the inclusion of the anti-avoidance and the European and international themes than their exclusion. And since one common thread in the increased prominence of these themes, especially since 2004, has been the protection of the corporation tax base, it seemed only appropriate to include a compliance and enforcement theme. The seven themes, due no doubt to the volume and complexity of the statutory material, are largely untheorised. Such theory as exists on corporation tax treats it as an enterprise of classical political economy. But tax is, first and foremost, public law, and the purpose of this study has been to interpret the themes in accordance with an innovative public law vision.

Corporation tax reform has become a political arena. It is political in the sense that it discloses a constant possibility of conflict (what Martin Loughlin calls the ‘first order of the political’).<sup>8</sup> The possibility is usually manifested by corporate sector threats to leave the jurisdiction. Conflict is usually averted through the practice of politics, the ‘handling’ or

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<sup>1</sup> See Chapter 1 above, nn. 13-26.

<sup>2</sup> *Ibid.*, nn. 27-36.

<sup>3</sup> *Ibid.*, n. 37.

<sup>4</sup> *Ibid.*, nn. 38-45.

<sup>5</sup> *Ibid.*, nn. 46-65.

<sup>6</sup> *Ibid.*, nn. 66-71.

<sup>7</sup> *Ibid.*, nn. 72-83.

<sup>8</sup> See Martin Loughlin, ‘Constitutional Law: the Third Order of the Political’, in *Public Law in a Multi-Layered Constitution*, ed. by Nicholas Bamforth and Peter Leyland (Oxford: Hart Publishing, 2003), pp. 27-51, 31.

‘managing’ of that potential conflict, sometimes in a slightly ‘guileful’ manner. This latter is what Loughlin refers to as the ‘second order of the political’.<sup>9</sup> Thus, as public law, corporation tax legislation is symbolised, not by ‘some slim constitutive document’,<sup>10</sup> but by the practitioner’s loose-leaf encyclopaedias referred to throughout this study.<sup>11</sup> A view of the British constitution that regarded it as configuration of values, albeit one subject to constant re-adjustment, might help us to offer insights into why what is contained within these tomes actually works. The ‘rule of law values’ of the Sheffield school<sup>12</sup> will not do for this purpose, but ‘political values’, shaped by theory, as envisaged in Loughlin’s account, might.

What Loughlin supplies is the key to a ‘functionalist’ and ‘interpretative’ approach to public law. Functionalism, as distinct from normativism, focuses ‘upon law’s regulatory and facilitative functions’, is ‘oriented to aims and objectives[,] and adopts an instrumentalist social policy approach’.<sup>13</sup> An interpretative approach enables us to avoid the positivist mistake of attempting to keep ‘fact’ and ‘value’ separate from each other. It also enables a measure of historical sensitivity; the testing of solutions adopted for their non-contradiction, their consistency and their coherence; and an understanding of the role of law relative to the business of government generally.

In the light of all this, Loughlin says, public law can be recognised as ‘the third order of the political’.<sup>14</sup> It is about governance, or government, and it should be ‘even-handed’ and free from manipulation by wielders of power. The more successful public law is in

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<sup>9</sup> *Ibid.*

<sup>10</sup> See Martin Loughlin, *Public Law and Political Theory* (Oxford: Clarendon Press, 1992), p. 241.

<sup>11</sup> *Ibid.* See *Taxation of Companies and Company Reconstructions*, ed. by Richard Bramwell, Alun James, Mike Hardwick and John Lindsay, 8<sup>th</sup> edn (London: Sweet and Maxwell, 2002); also Julian Ghosh and Ian Johnson, *Taxation of Loan Relationships and Derivatives* (London: Butterworths LexisNexis, 1999).

<sup>12</sup> See Ian Harden and Norman Lewis, *The Noble Lie: The British constitution and the rule of law* (London: Hutchinson, 1986).

<sup>13</sup> See Loughlin, n. 10 above, p. 60.

<sup>14</sup> See Loughlin, n. 8 above, pp. 40-42.

promoting consistent, coherent and non-contradictory solutions, which reconcile often disparate political values, towards a clear end, the greater legitimacy those solutions will have. Thus, corporation tax reforms must reflect both political values and the relative importance of those values in the particular field. Since there is still very little constitutional law on UK taxation, anyone seeking to understand the significance of the various themes in corporation tax reform must embark on a much more broadly-based inquiry than tax law scholarship has hitherto provided. The present study has applied the ‘functionalist’ and ‘interpretative’ technique referred to above. A key element in the argument has been to conceive of corporation tax as similar to any other type of economic regulation. Corporation tax is concerned, not only with raising revenue in a way that is both fair and efficient, but also with promoting growth in the UK economy. In the particular context of taxation, the approach is assisted by Murphy and Nagel’s inquiry into the legitimacy of taxation generally,<sup>15</sup> a strategy which involves accepting the ‘conventional’, rather than any supposedly ‘absolute’, status of property rights which, on Murphy and Nagel’s view, are ‘created’, not ‘disturbed’, by a system of taxation.<sup>16</sup>

The discussion in Chapters 2 to 4 unfolded in three distinct, but interrelated, stages. The common strand in the analysis was our preoccupation with uncovering the ‘aims’ and ‘objectives’ of corporation tax law as part of a tax system designed to facilitate the aims of economic policy more generally. Documents from four specimen Budgets enable us to infer that the reform of corporation tax has the objective of producing a tax that raises certain levels of revenue, to be sure, but that is also designed to promote economic growth, as well as greater fairness in society.

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<sup>15</sup> See Liam Murphy and Thomas Nagel, *The Myth of Ownership* (Oxford: Oxford University Press, 2000).

<sup>16</sup> See Chapter 1 above, nn. 361-367.

In line with this approach, Chapter 2 began a three-stage examination of corporation tax reform, considering the strengths and weaknesses of the institutional framework within which it has been taking place.

#### ACTORS 'IN CONCERT'

The discussion in Chapter 2 emphasised the fact that the relevant institutions of H.M. Government (HMG) and the corporate sector operate in close geographical proximity. Four strands were recurrent in this discussion. First, the idea that the state (i.e. the UK), although a fictitious person, is fundamentally different from other fictitious persons, such as corporations, since it exists 'precisely for the purpose of creating law'.<sup>17</sup> Secondly, that, especially in the light of taxation's exclusion from the UK's 'transfer of jurisdiction and competence' to the institutions of the EU, the UK remains a sovereign state.<sup>18</sup> Thirdly, that sovereignty is, in Loughlin's word, 'relational'.<sup>19</sup> HMG's competence in corporation tax policy depends on its capacity, and that depends on the quality of the relationship between the state and the corporate sector. Finally, that the quality of this relationship relies in turn on the ways in which objectives, structures and values augment or detract from the creation of trust and confidence in this particular area of public policy.

Governance, the idea that informs the relationship between state and corporate sector, may either strengthen or detract from the sovereign authority of the state in corporation tax reform. The very notion of governance presupposes practices that present specific challenges

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<sup>17</sup> See Martin Loughlin, *The Idea of Public Law* (Oxford: Oxford University Press, 2003), p. 60.

<sup>18</sup> *Ibid.*, p. 94.

<sup>19</sup> *Ibid.*, pp. 83-86.

to the effectiveness of representative institutions: a perceived lack of legitimacy;<sup>20</sup> possible blame-shifting by those ‘in a position to interpret and lead public debate’, if policies misfire;<sup>21</sup> the unintended and undesirable consequences of policies of reform;<sup>22</sup> accountability problems created by ‘policy networks’;<sup>23</sup> and, finally the consequences of failure,<sup>24</sup> the most striking example in this area being the legendary ‘complexity’ of corporation tax law. The extent to which each of these five issues – either alone or in combination - augment, or detract from, HMG’s sovereignty in tax matters depends, first, on the extent to which the objectives and values of state and corporate sector institutions complement or oppose each other; and, secondly, on the effectiveness of representative institutions in addressing significant divergences between them.

Chapter 2 viewed the matching or opposition of the objectives and values of state and corporate sector in terms of five propositions: firstly, widespread agreement that the state and its sovereignty is being transformed by the effects of economic globalisation; secondly, that this transformation can be viewed as enabling for the nation state, a point which involves making a distinction between power as domination and ‘power as action in concert’;<sup>25</sup> thirdly, that the interests of the state and the corporate sector (especially multinational corporations) may be found in some measure to coincide; fourthly, that, if the foregoing points seem worrying, there is considerable empirical evidence to suggest that a level of social responsibility by the corporate sector, far from being a cynical ‘add on’ in their financial statements, is perhaps essential to their economic prosperity; and, finally, that

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<sup>20</sup> See Gerry Stoker, ‘Governance as theory: five propositions’ (1998) 50 *International Social Science Journal*, 17-28, 20.

<sup>21</sup> *Ibid.*, p. 22.

<sup>22</sup> *Ibid.*, pp. 22-23.

<sup>23</sup> *Ibid.*, p. 23.

<sup>24</sup> *Ibid.*, p. 24.

<sup>25</sup> See Angus Stewart, *Theories of Power and Domination: The Politics of Empowerment in Late Modernity* (London: Sage, 2001), p. 6.

governments can draw on experience - there have been many predictions of capital flight from the UK but, thus far at least, little realisation of it.

Although it might be reassuring to find some identity of interest between state and non-state institutions, it would be even more pleasing to think that the state's institutions could deal effectively with significant divergences. The capacity of the UK's political institutions in this respect centres on H.M. Treasury and HMRC, as well as on the effectiveness of Parliament in following their activities. However, effectiveness means different things to different institutions. For Parliament, effectiveness resides in its scrutinising powers, in its ability to hold HMG to account for the latter's corporation tax measures. For H.M. Treasury and HMRC, however, effectiveness means an ability to confront unexpected combinations of economic events in such a way as to maintain appropriate levels of corporation tax revenue. The discussion in Chapter 2 accepted Tomkins' interpretation of the 'separation of powers' in the British constitution as being a separation, not of the executive, the legislature and the judiciary, but of the Crown, on the one hand, and Parliament, on the other.<sup>26</sup> The enterprise of the British constitution is to ensure the accountability of the Crown to Parliament.<sup>27</sup> Viewed in this light, the effectiveness of Parliament in building up trust and confidence in corporation tax reform lies in its ability, via the House of Commons Treasury Select Committee, to create a convincing and authoritative narrative of the strengths and weaknesses of corporation tax reform measures. This is what, in this particular context, the concept of 'accountability' entails. It is the construction of the record that provides the basis on which, in due course, the electorate will confirm or dismiss the governing party. Although this system of scrutiny has strengths, it also has weaknesses. The effectiveness of H.M. Treasury and HMRC in building up trust and confidence in HMG's corporation tax reform

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<sup>26</sup> Adam Tomkins, *Public Law* (Oxford: Oxford University Press, 2003), p. 44.

measures resides in the prudential qualities of Treasury ministers and civil servants. Parliament looks over its shoulder; HMG faces an unknown future. This is prudence, not as an Aristotelian virtue, but as an essential, pragmatic, tool in the art and science of government, of governing through governance. Part of that art is to ensure that the UK's sovereignty in corporation tax matters is enhanced, rather than depleted, by its membership of the EU.

The opposition in the British constitution of Crown and Parliament, and their combined strength when, as the Crown in Parliament, they act together, gave rise to the final two segments of the analysis in Chapter 2: the nature of the contributions to corporation tax reform of the policy networks referred to above, and of the judiciary. Policy networks, it will be recalled, cover both 'policy communities', and 'issue networks'.<sup>28</sup> Policy communities are characterised by their close integration in the policy making process; issue networks by their exclusion from the policy making process. It is thus that the reason for policy communities presenting accountability problems becomes obvious. If corporation tax reforms fail, and we want to know why, we may not be in a position to find out from those members of policy communities, the civil servants, most closely involved with HMG itself.

Two key points about the role and values of the judges in corporation tax reform were made in Chapter 2. One of them related to their constitutional position. This was that they are positioned much more closely to the Crown than to Parliament.<sup>29</sup> Indeed, the role of senior judges has strong similarities to that of senior politicians.<sup>30</sup> Whilst, in former times, this may have led judges to approach the interpretation of tax legislation in a manner calculated to

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<sup>27</sup> *Ibid.*, p. 46.

<sup>28</sup> See David Marsh and R.A.W. Rhodes, 'Policy Communities and Issue Networks: Beyond Typology', in *Policy Networks in British Government*, ed. by David Marsh and R.A.W. Rhodes (Oxford: Clarendon Press, 1992), pp. 249-268.

<sup>29</sup> See Tomkins, n. 26 above, p. 53.

<sup>30</sup> *Ibid.*

reinforce a particular political position, in our own time it seems to have forced them to a careful reappraisal of their constitutional position in relation to taxation matters. Recent decisions of the House of Lords have disclosed a particular form of prudence, in which the public interest seems to be considered best served by leaving the formulation of tax law rules to the legislature, in conjunction with the experts.

#### PRUDENCE IN THE REFORM PROCESS

How, then, do the stages in which corporation tax reform takes place augment or detract from the state's capacity in this particular policy area? The answer, in a word, is 'prudence', and Chapter 3 sought to show what prudence has required in relation to the four substantive themes of the study: accounting; anti-avoidance; compliance and enforcement; and the impact of European and international developments. The study contends that current arguments over the state of corporate tax legislation strongly underline the need for prudential management of corporation tax reform. The significance of this point is inextricably bound up in our acceptance of the idea that, in tax as elsewhere, prudence is the indispensable skill of the legislator. This in turn relies on the functionalist style of corporation tax law scholarship, one that recognises the public law nature of corporation tax, and which embraces the idea of public law as a practice of politics.

The prudence of the former Chancellor, the Rt Hon. Gordon Brown, MP, has of course been legendary. What Gordon Brown knows, however, as a student of Adam Smith, and what we have been in a position to infer, by reading Smith in his eighteenth century context, is that prudence has a highly specific, though elusive, significance in relation to the art and



science of government. Smith wrote ‘of the value of prudence in a legislator’, so Donald Winch has written, ‘in terms that Machiavelli himself might have approved of’.<sup>31</sup>

‘We talk of the prudence of the great general, of the great statesman, of the great legislator. Prudence is, in all these cases, combined with many greater and more splendid virtues, with valour, with extensive and strong benevolence, with a sacred regard to the rules of justice, and all these supported by a proper degree of self-command. This superior prudence, when carried to the highest degree of perfection, necessarily supposes the art, the talent, and the habit or disposition of acting with the most perfect propriety in every possible circumstance and situation ... It is the best head joined to the best heart. It is the most perfect wisdom combined with the most perfect virtue.’<sup>32</sup>

The commonplace idea of prudence in a financial, in one might say an ‘Aristotelian’, sense, has certainly been part of Gordon Brown’s political vocabulary. The use of prudence in this financial sense does not, however, preclude its use in a legislative, or Machiavellian, sense. This is because the legislative sense of prudence rests on a view of Smith’s greatest work, not simply as a classic of economic liberalism, but as part of a political theory, of the art and science of government.

In order to illustrate the role of prudence in augmenting the state’s capacity in corporation tax reform, it was necessary to isolate, first, three aspects of the ‘political’ dimension to the policy area. What is prudential depends, to some extent at least, on what the political aspect of corporation tax reform is taken to be; on what politics is thought to consist of, considered in relation to the adjacent notions of ‘policy’ and ‘reform’; and, finally, on the relationship between politics and political economy. Chapter 3 offered the following main reflections on each of these factors: that, as mentioned above, the political status of corporation tax reform derives from its constant conflictual (whether within the UK or within the EU as a whole),

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<sup>31</sup> See Donald Winch, *Adam Smith’s Politics: An Essay in Historiographic Revision* (Cambridge: Cambridge University Press, 1978), p. 159.

and also because it has a strongly deliberative dimension; that, managing this potential and harnessing deliberation, in line with a particular policy, is the business of the politics of corporation tax reform; and that ‘reform’ may be a misnomer, unless it is understood as the creation of a new tax, or at least as a tax with newly-defined political objectives. An understanding of these points is important because it shows that effective policy making depends in part on the skills with which the policy is kept ‘on track’, and in part on communicating the nature and objectives of reform to those affected by it. This last point is crucial to the relationship between politics and political economy. Following Carl Schmitt,<sup>33</sup> the study holds that the economics of designing taxes is sustained by the political; it does not run alongside it. It is a matter of ideology, as indeed is the concept of the public interest itself. This, again, is in line with Smith’s view of political economy as that ‘branch of the science of a statesman or legislator’ which relates to providing, not simply ‘a plentiful revenue or subsistence for the people’, by ensuring that they can ‘provide such a revenue or subsistence for themselves’, but also supplying ‘the state or commonwealth with a revenue sufficient for the publick services’.<sup>34</sup>

Though under-discussed in the literature, it is plain from both the public pronouncements of the former Chancellor, and from the reform measures themselves, examined in Chapters 3 and 4, that the direction of reform has been informed by a particular ideology of the public interest. This ideology has been conceived of slightly differently from ‘the common good’,

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<sup>32</sup> See Adam Smith (1723-1790), *The Theory of Moral Sentiments*, ed. by D.D. Raphael and A.L. MacFie (Oxford: Clarendon Press, 1976), p. 216; see Simon Lee, *Best for Britain? The Politics and Legacy of Gordon Brown* (Oxford: Oneworld, 2007), pp. 45-47.

<sup>33</sup> See Carl Schmitt, *The Concept of the Political*, trans. by George Schwab (Chicago: University of Chicago Press, 1996), p. 88 (note by Leo Strauss).

<sup>34</sup> See Adam Smith (1723-1790), *An Inquiry into the Nature and Causes of the Wealth of Nations*, ed. by R.H. Campbell and A.S. Skinner (textual editor W.B. Todd), 2 vols (Oxford: Clarendon Press, 1976), I, p. 428. But note changes in usage: see Charles S. Maier, ‘Introduction: Political economy and history’, in *In search of stability: Explorations in historical political economy*, ed.

since, within a ‘welfare economics’ framework, it has drawn attention to HMRC’s duty to make prudent decisions to combine efficiency with fairness in economic policy; to put the interests of the UK first; and to put the tax system to work in the service of the vision of strong economic growth tempered by social justice. Interestingly, lawyers (although not other commentators) have either ignored this ideological dimension, or refused to recognise that it is a legitimate objective of corporation tax reform, as the practice of a particular type of public law designed ‘to meet the objectives of the government of the day’.<sup>35</sup>

The necessity for HMG to make prudent decisions in the public interest is nowhere more apparent than in relation to the initiation of reform proposals. This stems from the need for HMG to maintain its sovereignty. Wide ministerial discretion in policy initiation, combined with the secrecy properly involved in choosing between alternatives, means that initiatives will be closely examined by those outside HMG itself. Corporation tax reform proposals usually pass this test. The fact that legislative proposals are well advanced when they are presented for argumentative scrutiny in the Commons is entirely compatible with a representative democracy. This is why we need to be aware of the true role, historically speaking, of Parliament, in developing corporation tax reform measures. It comes at the end of a multifaceted stage in the process, one that requires the close interaction of public servants with ministers (in clarifying policy objectives), as well as with the public (in terms of public consultation on measures). Chapter 3 contended that this process of consultation, research and drafting was all that was required, constitutionally speaking, before proposals were put before the representative assembly. The arguments mounted by Christopher

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by Charles S. Maier (Cambridge: Cambridge University Press, 1987), pp. 1-16, esp. 2-6; also Chapter 1 above, n. 94.

<sup>35</sup> See Chapter 3 above, n. 127.

Wales,<sup>36</sup> and by the Institute for Fiscal Studies,<sup>37</sup> about ‘effective [parliamentary] scrutiny’ fail to recognise the true role of Parliament in a representative democracy. Finance Bill debates do much better than either commentator is willing to recognise in fulfilling the requirement that legislative proposals be subject to ‘argumentative scrutiny’.<sup>38</sup>

If the true role of Parliament in a representative democracy is to subject legislative provisions to ‘argumentative scrutiny’, and this is a facet of the ‘Gothic prudence’ adverted to by James Harrington,<sup>39</sup> prudence is required also from those involved in presenting the resulting legislation to the electorate. Wales is right to criticise O’Donnell for omitting this stage from his picture of the legislative process since, especially when the most contentious measures are ‘handed down’ (usually in relation to the anti-avoidance theme), much skill is required in explaining and justifying them to those affected. The prudence involved in judging the appropriate level of engagement, in explaining and justifying measures to the electorate, has a continuation in the delivery of the measures themselves. This, too, involves prudential calculation, the careful weighing of ends and means.<sup>40</sup> It also has its counterpart in the role of the judiciary. This was discussed much earlier in the study.<sup>41</sup> The judges’ role, in ‘delivering’ corporation tax reforms, is much noted but little understood. Judges are much better at making prudential decisions in the public interest, when it comes to tax cases, than is often realised.

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<sup>36</sup> See Christopher Wales, ‘The Implications of the O’Donnell Review for the making of Tax Policy in the UK’ [2004] BTR 543-565.

<sup>37</sup> See Tax Law Review Committee, *Making Tax Law: Report of a Working Party on the Institutional Processes for the Parliamentary Scrutiny of Tax Proposals and for the Enactment of Tax Legislation chaired by Sir Alan Budd* (London: Institute for Fiscal Studies, 2003).

<sup>38</sup> See Bernard Manin, *The Principles of Representative Government* (Cambridge: Cambridge University Press, 1997), p. 191; also Chapter 3 above, n. 290.

<sup>39</sup> See Manin, n. 38 above, quoting James Harrington’s ‘The Prerogative of Popular Government’, in *The Political Works of James Harrington*, ed. by J.G.A. Pocock (Cambridge: Cambridge University Press, 1977), pp. 389-499, 477.

<sup>40</sup> See Chapter 3 above, n. 347.

<sup>41</sup> See Chapter 2 above, pp. 137-146.

## CORPORATION TAX AS 'POLITICAL JURISPRUDENCE'

The discussion of the reform process suggests that, at any one time, the boundaries of the corporation tax base are a very good barometer of the UK's sovereignty in taxing corporate income. Redolent as it is of questions of sovereignty, the code should be regarded as political jurisprudence, the strength of which is drawn (paradoxically) from the constraints under which it has been created. It is a case, not of 'Prometheus unbound' but rather, of Odysseus tied to the mast.<sup>42</sup> The fact that it ranks as political jurisprudence means that it is entirely appropriate for the corporation tax code to be designed to further the ideological objectives of 'the government of the day'. It also means that the code transcends morality; indeed, it helps to create the conditions under which morality is possible.<sup>43</sup> Finally, it is clear both from the code itself, and from the approach of the judges to interpreting its provisions, that the dominant theory of the corporation tax code is 'reason of state', and the chief technique of the code is a juristic prudence.

This juristic prudence has implications for arguments about the 'complexity' and 'instability' of the corporation tax code. Neither of these is relevant to the concept of the rule of law as it inheres to political jurisprudence. Montesquieu's rule of law, 'freedom from fear'<sup>44</sup> (as taken up by E.P. Thompson)<sup>45</sup> refers only to 'the rule of institutions'. As stated

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<sup>42</sup> See Stephen Holmes, *Passions and Constraint: On the Theory of Liberal Democracy* (Chicago: University of Chicago Press, 1995), pp. 109-110, 178-201 (see Loughlin, n. 17 above, pp. 113 and 137).

<sup>43</sup> See Thomas Hobbes (1588-1679), *Leviathan, or The Matter, Forme, & Power of a Commonwealth Ecclesiasticall and Civill*, ed. by C.B. Macpherson (London: Penguin, 1985), p. 186.

<sup>44</sup> See Charles de Secondat, baron de Montesquieu, *The Spirit of the Laws*, trans. and ed. by Anne M. Cohler, Basia Carolyn Miller and Harold Samuel Stone (Cambridge: Cambridge University Press, 1989), pp. 156-166.

<sup>45</sup> See E.P. Thompson, *Whigs and Hunters: The Origin of the Black Act* (London: Penguin, 1990), pp. 258-269.

above, the corporation tax code, ‘complex’ and unstable’ though it may be, is undeniably the product of such a rule. This does not necessarily endow ‘instability’ and ‘complexity’ with the cloak of virtue, however. Levels and degrees of either quality are subject to prudential rule. Prudential rule may require a degree of complexity in certain circumstances (e.g. to ensure fairness), but not in others. Likewise, prudence may require stability in some circumstances, but not in others. Prudence means different things at different times, if trust and confidence in HMG is to be maintained, and even augmented. So we come to the crux of the matter. Given that the corporation tax code, as public law, is a form of political jurisprudence, and that the prudential technique demands, not simplicity and stability in the name of ‘the rule of law’, but the prudential management of complexity and of change, we consider the actualisation of the prudential technique in the code itself.

The snapshot offered in the latter stages of Chapter 4 should be imagined as a glimpse of the state of affairs on any day when the processes analysed in Chapter 3 are in motion. The dominant rationale at work, as carefully explained by Scottish Enlightenment thinkers including Adam Smith, is that of effectiveness, the realisation, if only from day to day, of the prince’s conception of the public interest. Although Smith died well over a century before the UK became a democratic state, he did live in an era of modern representative institutions, so it is not too great a leap, instead of thinking of some perception of ‘the common good’ in the mind of an eighteenth century monarch, to think of the ideology of a governing party in possession of a significant Parliamentary majority. Effectiveness, as Winch and others have shown, is linked in Smith’s writing with a certain Machiavellian prudence,<sup>46</sup> which, in corporate tax policy at least, places considerable powers of initiative in the hands of the

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<sup>46</sup> See Winch, n. 31 above, *passim*; Loughlin, n. 10 above, ch. 1; Loughlin, n. 17 above, ch. 8; Roy Porter, *Enlightenment: Britain and the Creation of the Modern World* (London: Penguin, 2000), pp. 188-189.

UK's representative institutions. Prudence in the advancement of the public interest is what, it is proposed, gives HMG sovereignty in corporation tax matters. This is so, as long as the prudential conduct of policy continues, whatever restrictions (relatively few, in fact) have been placed on its competence by Community law, including the European Court of Justice's (the ECJ's) interpretation of the impact on corporate taxation of 'the fundamental freedoms' of the European Treaty.

So, if we have to elaborate on what prudence might mean in the conduct of corporation tax reform might mean, what can we say? Everything, it is suggested, turns on the ability of HMG to enlist the reform of corporate taxation in the maintaining of a state of affairs that bears some plausible relationship to its ideology. Ideologies are sometimes depicted as having a certain purity, something that in the minds of some would exclude the economy-driven New Labour enterprise.<sup>47</sup> The view taken here is that the vision of combining economic growth with social justice is indeed an ideology. Its status, its perceived flaws, are not part of the inquiry. Keeping the vision credible, maintaining trust and confidence, needs 'quick footwork',<sup>48</sup> we might say prudence, at every turn, in a complex and uncertain world. The electorate is always ready to enforce a government's duty to make the people richer.

Seen in this light, the values of efficiency realised, if only in part, in the corporation tax code, assume their proper proportions. Making the code more efficient, as Chapter 4 has shown, has meant shaping the code to reflect ever more closely the imperatives of post-neoclassical endogenous growth theory. Whether in its closer alignment of taxable profits with commercial profits, in its enhancement of relief for borrowing costs, in its maintenance of generous relief for exchange differences, or in the provision of wide relief for intangibles,

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<sup>47</sup> But not in the mind of Adam Smith: see Porter, n. 46 above, pp. 394-396.

<sup>48</sup> See the comment of the former Conservative Chancellor, Ken Clarke, about Alistair Darling's response to the Northern Rock crisis ('He was too slow; a bit wooden ...': see Parker, Thal Larsen, Giles and Saigol, *Financial Times*, 19 September 2007, 3).

the corporation tax code might, without exaggeration, be viewed as a vast economic instrument in the service of growth. Achieving fairness, by contrast, has meant recognising and confronting what is a highly contentious idea, to some extent re-imagining tax law as creating only 'conventional' rights, and prudentially managing the relationship of fairness with efficiency. Neither efficiency nor fairness prevails; no conclusive relationship exists between them. Only effectiveness matters, because things change. The effective balancing of efficiency and fairness depends on what is prudential at any given moment, since augmenting trust and confidence is all-important.

It would, of course, be rash to predict how all this might end. The incremental process of reform is ongoing. It might be wrecked on the rocks of unforeseen economic contingencies. Rather less likely, it might be destroyed by a reaction to the economic inequalities to which it seems to have contributed. What is clear is that only prudent management, in the public interest, can further the corporation tax reform project.



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