Facilitation of tax evasion: A new corporate offence

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HM Revenue & Customs (**HMRC**) has recently published a number of Consultation Papers, including a proposal to introduce a new corporate criminal offence of *failing to prevent the facilitation of tax evasion*.

This strict liability offence will seek to extend criminality to corporations where they fail reasonably to prevent their representatives (for example, employees) from facilitating criminal tax evasion during the course of a business (the **Proposed Offence**). It aims to make it easier for corporations to be found liable for the acts of their representatives, removing some of the previous hurdles that have historically made such liability difficult to prove (for example, showing the requisite level of intent).

Crucially, and as explained below, it seeks to have extra-territorial effect along the same lines as the Bribery Act 2010, meaning that it is potentially of great importance to offshore financial services businesses.

HMRC has received responses on the Consultation Papers from industry, and, in December, provided its own reply together with a draft of the legislation. The areas of interest arising out of this reply are as follows, and each is covered in more detail below:

- what reasonable procedures will corporations be expected to have in place to guard against the Proposed Offence?
- what constitutes a *"corporation"* under the Proposed Offence?
- whose behaviour will a corporation be liable for?
- is a prior criminal conviction of the UK tax payer and/or an employee or other representative of the corporation a necessary pre-requisite to a conviction of the corporation?
- what is the geographical scope of the Proposed Offence?

- does the Proposed Offence have retrospective effect and is there a *de minimis* threshold?

Reasonable procedures? It is a defence to the Proposed Offence for the corporation to show that *"reasonable procedures"* were in place to prevent the facilitation of tax evasion. However, it is unclear whether this will in practice necessitate the implementation of additional procedures for checking the activities of employees/representatives beyond what is already required.

For example, organisations will already have in place procedures for awareness and reporting of suspicious activities. It is unclear whether this will be sufficient.

Formal guidance will be provided by HMRC as to what constitutes *"reasonable procedures"*. This is a requirement under the new draft legislation. The next stage of the consultation process will include consideration of the content of such formal guidance.

What is a "corporation"? The UK Government has confirmed that *"corporation"* should be read *"as including all legal persons"*. This includes companies and partnerships *"regardless of whether they operate commercially or for other reasons (such as charity)"*.

This is a wide definition. However, the UK Government has confirmed that *"the procedures that are considered reasonable will be proportionate to the risk faced by the corporation"*. Thus, what comprises *"reasonable procedures"* may differ between, for example, commercial entities and charitable ones.

Whose behaviour is caught? The UK Government has stated that corporations *"should be liable for all those who provide services on their behalf"*. This includes all those over whom the corporation has some control, for example employees, and the situation where *"someone not ordinarily employed by the entity"* provides *"services to its customers on its behalf"*.

It is unclear whether it could apply to a trust company for: (i) the actions of directors of companies that are subsidiary to a trust of which it is trustee; or (ii) the actions of third parties, for example, investment advisers, to whom the trust company's responsibilities (in relation to that particular trust) are delegated.

Consideration of the reasonableness of procedures will take into account the level of control that an entity is able to exert over those acting on its behalf. For example, if Corporation A provides services on behalf of Corporation B to the clients of Corporation B, reasonable procedures might include an assessment of Corporation A itself. However, Corporation B has limited control over the actual employees of Corporation A, and therefore may not be expected to be able to monitor them.

Only acts carried out by an employee in that capacity will be caught by the new offence. Acts undertaken by an employee in their personal/private capacity will not be covered, unless it can be shown that the culture of the corporation was generally encouraging of tax evasion.

Prior conviction of UK tax payer and employee/representative? The UK Government has confirmed that prior *"non-compliance by the* [UK] *tax payer should meet the standards of criminal conduct"* before the Proposed Offence can take hold as against the corporation. In other words, there should be a predicate offence by the UK tax payer under either:

- existing laws, for example the common law offence of cheating the public revenue or section 106A of the Taxes Management Act 1970 (fraudulent evasion of income tax); or
- the new offence of *"offshore tax evasion"* to be introduced as part of the Finance Act 2016. This will create a strict liability criminal offence for UK tax payers relating to tax payable on overseas income and gains not reportable under common reporting standards (although this will have a *de minimis* threshold of £25,000 tax evaded and apply only to income and gains from the tax year in which the legislation is introduced i.e. it will not have retrospective effect).

However, there does not necessarily have to be an actual formal conviction of the UK tax payer. There may be circumstances where the basis of the evasion is sufficient to warrant proceeding without such a conviction (e.g. where there has clearly been evasion, but a decision has been taken that it is not in the public interest to prosecute the UK tax payer). In such a case, the prosecution of the Proposed Offence would, as a pre-requisite, *"have to prove to the criminal standard during the prosecution of the corporate that the predicate offence had been committed* [by the UK tax payer]".

Likewise, a formal conviction of the employee or other representative of the corporation for aiding, abetting, counselling, procuring, encouraging, assisting in or be knowingly involved in the offence by the UK tax payer is not strictly necessary. If, for example, the representative is a whistle-blower, or there is some other public interest reason that precludes prosecution, then the Proposed Offence can still bite. However, again, the UK Government has confirmed that it will be *"necessary to prove (beyond reasonable doubt) that the representative had criminally facilitated the tax payer's tax crime"* before the corporation can be convicted.

Thus, if either or both of the UK tax payer or the employee/representative has not been formally prosecuted and convicted, the prosecution will need to demonstrate that such a conviction would have been forthcoming had such steps been taken.

This appears to be burdensome on the prosecution, involving a number of potential prior hurdles to be overcome. It also potentially impacts on the UK tax payer or employee/representative, reaching conclusions on the criminality of their actions but without a proper trial. It may discourage both UK tax payers and employees/representatives from making voluntary disclosures if there is the possibility that the potential benefits in doing so (for example, a decision not to prosecute them for a criminal offence) may be rendered nugatory in a later prosecution of the corporation by publicly inferring criminality on their part.

Liability of the corporation is strict, in the sense that the prosecution does not need to prove *intent* to facilitate offshore tax evasion. The UK Government does, however, acknowledge that *"it is not reasonable to expect corporations to be able to uncover all criminal acts conducted by its representatives, especially where the representative has taken steps to hide their criminal conduct from the corporation"*. This will, however, go to the reasonableness of the procedures operated by the corporation i.e. was the behaviour so obscured that it was incapable of detection by reasonable procedures.

Geographical scope of the Proposed Offence? The Proposed Offence will operate against corporations who are:

- incorporated or formed under any part of UK law; or
- are incorporated anywhere else (or is of a similar character to a UK entity, e.g. a foreign partnership), and carries on all or part of its business in the UK.

Thus, if the business of the corporation touches the UK then it will be caught. It is immaterial for these purposes whether the Proposed Offence takes place in the UK or elsewhere. It is the nexus with the UK that is all-important and provides jurisdiction.

The Proposed Offence covers the facilitation of a UK tax loss by both UK and non-UK corporations (where the latter's business touches the UK). However, it also covers the facilitation of a tax loss overseas by a representative of a UK corporation. The UK Government has confirmed that *"…the preference will always be for the jurisdiction suffering the tax loss to take the criminal or civil response it feels most appropriate"*. However, if: (i) that overseas jurisdiction is prevented from taking action; (ii) the entity involved is a UK corporation; and (iii) there is public interest in doing so, the UK should be empowered to take action itself.

Does the Proposed Offence have retrospective effect and is there a *de minimis* threshold? The Proposed Offence will not have retrospective effect if the predicate offence by the UK tax payer is the new offshore tax evasion offence (because, as indicated above, this does not have retrospective effect itself). Likewise, where it is based on this new offence, it will indirectly have a *de minimis* threshold of £25,000.

However, where it is based on existing tax evasion offences under UK law it is unclear whether it will have retrospective effect. Further, there is no indication of a general *de minimis* threshold in this regard.

Comment

Whilst this reply by the UK Government is helpful in further understanding the nature of the Proposed Offence, the next stage of the consultation process is arguably even more crucial. It will be this phase that shapes what *"reasonable procedures"* a corporation will be expected to have in

place as a defence against the Proposed Offence. Whether this increases the regulatory burden on offshore regulated providers of financial services business remains to be see.

In addition to the criminal offence, a new civil offence of *"enabling offshore tax evasion"* is proposed as part of the Finance Act 2016. This will arise where:

- a person (this could be an individual or corporation) has knowingly enabled a UK tax payer to carry out a tax evasion offence (for which they have been prosecuted) or where the UK tax payer has been found liable to UK tax penalties; and
- the conduct in question has involved *"offshore activity"* (which is widely defined).

Enabling might include the provision of trust or corporate services.

The potential civil penalty on someone who has enabled the tax evasion is 100 per cent of the potential lost revenue (although this may be mitigated if there has been, for example, voluntary disclosure).

The UK Government *"recognises the difficulties in applying civil sanctions to those enablers who operate overseas"* and indicates that it *"will continue to work with international partners to find solutions to this problem"*. Whether this involves the further development in Jersey and elsewhere of mutual assistance in foreign tax matters remains to be seen. If, however, the enabler operates in the UK then this is unlikely to present an issue, and it may operate in tandem with, or as an alternative to, the Proposed Offence.

The civil offence also provides for the public *"naming and shaming"* of those who have been found liable. In the event that an overseas-based regulated enabler is held to be liable *in absentia*, and is named and shamed, it may cause reputational damage or, worse, prompt its own regulator to take enforcement action.

The risks to offshore regulated businesses associated with the new proposed civil offence are, therefore, far from negligible. Those providing trust and corporate services should be certain that settlors and beneficial owners are not using their services to evade tax.

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