

**Tackling tax evasion: legislation and guidance for a corporate offence of failure to prevent the criminal facilitation of tax evasion
Response by the Chartered Institute of Taxation**

1 Introduction

- 1.1 The Chartered Institute of Taxation (CIOT), in its response¹ to the first consultation last year by HM Revenue and Customs (HMRC) on the introduction of a new corporate criminal offence, highlighted that the proposals represent a very significant change with extremely wide ranging implications.
- 1.2 The CIOT has an interest in the proposals as our members will be directly affected by them, but we also have a wider interest, in accordance with our charitable objectives; the CIOT aims to work for a better, more efficient tax system for those affected by it, and one of our objectives for the tax system is a fair balance between the powers of tax collectors and the rights of taxpayers. The introduction of this new criminal offence affects this balance. Whilst amongst our objectives as stated in our Royal Charter is the “prevention of crime” and we are thus supportive of measures which promote this, we take the view that this offence must be applied in a proportionate manner and to appropriate cases only, if it is to be effective in the prevention of crime.
- 1.3 Our main concerns are, that the new offence must be subject to appropriate defences being available, that clear and unambiguous guidance is provided by the Government so that corporations understand exactly what measures they must put in place to comply, and that the measure is not used where it simply “adds to punishment”. We believe it is important that the use of criminal penalties in the tax system remains rare and is always seen as being of an utmost serious nature; we would not like criminal penalties becoming seen as an almost “routine” administrative measure as sometimes seems the case in other countries.
- 1.4 Our response to this second consultation concentrates on these aspects.

¹ A New Corporate Criminal offence – CIOT comments

https://www.tax.org.uk/system/files_force/file_uploads/151009%20A%20new%20corporate%20criminal%20offence%20-%20CIOT%20comments.pdf?download=1

2 Executive summary

- 2.1 We acknowledge that it is still HMRC's intention to keep to their original implementation timetable so that the legislation will be introduced to Parliament in the autumn with Royal Assent expected by early 2017. However, in our view, given the uncertainty that the EU Referendum decision is causing (and will continue to cause for some time) to business, HMRC ought seriously to consider delaying implementation of this measure.
- 2.2 We are concerned that this measure will promote further uncertainty (given that it is a matter of criminal law and not something on which a company can rely on HMRC guidance).
- 2.3 It is another provision for which a company will have to put in place compliance procedures, and there is thus an additional administrative burden, which needs to be justified by the effectiveness of the measure in protecting the public revenue.
- 2.4 We have specific concerns about the wording of the revised draft legislation and whether it completely achieves what it sets out to achieve. Our observations are set out in detail below.
- 2.5 It will be crucial for corporations affected to understand how they can rely on the defence of 'reasonable prevention procedures' so they can put in place an appropriate strategy to ensure compliance with their new obligations.
- 2.6 It would be helpful if corporations can build on current policies and procedures already in place under other legislative requirements to show that they have a defence to this offence. If not, the compliance costs could be significant. Even where current policies are acceptable, there will still be costs involved in training staff and in certification and reporting processes. There is therefore clearly a need to ensure that the measures can be implemented in a way which mitigates additional costs as far as possible.
- 2.7 Hence, we would urge HMRC to take time to understand how the provisions could be implemented with the minimum disruption. This will be particularly the case for businesses outside the current regulated sectors.
- 2.8 Guidance will be essential to help corporations identify how they can demonstrate that they have followed satisfactory due diligence procedures and have a reasonable care defence in the event that one of their associates is discovered to have criminally facilitated tax evasion. We welcome HMRC's willingness to discuss, develop and endorse sector specific guidance. However, it must be recognised that guidance is not legally binding even if it has been 'approved' by the government.
- 2.9 The importance of the guidance would be enhanced if the legislation explicitly states that the courts should 'have regard' to it. This would provide a valuable extra, although we recognise, not an absolute, safeguard for corporations who have relied on the guidance (whether HMRC's guidance or their own 'HMRC approved' sector specific guidance) when implementing their procedures.
- 2.10 Guidance also has an important role in helping to define the practical implementation steps that will actually achieve the stated policy objective of encouraging an environment that improves the corporate monitoring and self-reporting of criminal

activity, as well as discouraging and impeding criminal behaviour by corporations and their associates.

- 3 QA1. Do you believe that the draft legislation, when read with the draft guidance, adequately articulates the offence and defence?** The Government would welcome alternative or additional wording for inclusion in the guidance that stakeholders believe adds clarity to the offence and defence.
- 3.1 It is not very clear on the correlation between what is outlined in Stages 1-3 in paragraph 2.1 and the draft legislation. Stages 1 and 2 read together suggest that the taxpayer will not be the same person as the corporation and this makes sense if this legislation is predominantly aimed at corporations who advise taxpayers (eg accountants, lawyers, banks etc). However, in some circumstances, the taxpayer and the corporation may be the same. For example, the 'rogue' employee of a corporation who may deliberately defraud HMRC by falsifying invoices and submitting incorrect VAT returns, and this is done at the behest of one of the directors. We understand from discussions with HMRC that it would not be possible for a person to 'facilitate' their own act of evasion, but it would be helpful if this was made absolutely clear. Can HMRC therefore clarify how the new offence might be applied in such circumstances if indeed it would be?
- 3.2 We also believe that some clarification is required over the point that the criminal tax evasion offences which have to be committed at Stages One and Two require a criminal intent. Amended draft clause 2(4) refers to UK tax evasion and tax evasion facilitation offences which require 'mens rea' and we note that on page 29, HMRC do reference this as part of the guidance – referring to the 'requisite guilty state of mind'. However, if, in principle, the corporate criminal offence applies only where criminal tax evasion offences that require 'mens rea' have been committed, then this ought to be set out in the legislation itself, otherwise there is the risk of 'mission creep' in the future.
- 3.3 Draft section 2(3) second line "the body" should be replaced with "B".
- 4 QB1. Do consultees consider that this clause (clause 1(4)), when read with its associated guidance, will enable them to identify when a person acts for or on behalf of a corporation?** The Government welcomes suggested case studies from stakeholders for inclusion in the guidance to illustrate when a person can be said to be associated with a corporation for the purposes of the offence.
- 4.1 The consultation document explains that the offence will be committed where a person acting for or on behalf of the corporation criminally facilitates tax evasion. The draft legislation defines this relationship in terms of the person being 'associated' with the corporation (clause 2(1) and clause 1(4)).
- 4.2 The key is who will be regarded as a representative of the corporation when deciding if a criminal facilitation offence has taken place to meet the Stage 2 requirement outlined at paragraph 2.1. Simple referrals in good faith by a corporation to another adviser should not meet the 'Stage 2' requirement. We think that this aspect of the legislation will present some difficulties for corporations in practice.

- 4.3 We think that the wording of draft clause 1(4) is awkward and too widely drawn. We do think there needs to be some element of contractual, control or related party relationship between the person (A) and the relevant body (B), even if this is not a written relationship (e.g. if an oral contract is admitted or can be inferred). We believe this will be sufficient to drive the behavioural change desired amongst the vast majority of affected corporate bodies, without giving rise to undue uncertainty.
- 4.4 As a result of the current definition of associated person being so wide, it is conceivable that the offence will catch situations where there is no realistic possibility of the corporation exercising any measure of control over a person performing services for the corporation, especially when that person is located overseas. This will present significant challenges in developing and monitoring suitable risk assessment processes.
- 4.5 Draft clause 1(4)(a) indicates that 'A' is a 'person' who might be an employee, agent or subsidiary of B. Paragraphs 2.4 to 2.7 could imply that an 'associated person' must be an individual, i.e. an employee, agent or contractor, either of B itself or of a subsidiary company, although the draft guidance (p29-30) states that an associated person can be "an individual or an incorporated body" which would be consistent with the wider legal meaning of person. Please can HMRC clarify what is meant here? And if there are specific contexts in the legislation in which only natural persons are intended, could this be clarified? It would also be helpful to know how HMRC envisage a person other than a natural person can facilitate evasion, and whether that is possible without the intervention of a natural person.
- 4.6 Regarding guidance, in our view there needs to be a spectrum of examples that cover:
- (i) situations that the new legislation is definitely intended to catch;
 - (ii) situations which are not the primary target but where the legislation could potentially bite depending on the facts and might be deployed if HMRC felt they should use it; and
 - (iii) situations which fall clearly outside the legislation and HMRC would not invoke it because they do not believe they should or can.

In addition, the examples should attempt to flesh out what would be reasonable in a particular sector.

- 4.7 The policy objectives of the new legislation appear to include creating a way of dealing not only with deliberate acts but also where controlling minds turn a blind eye. It would be helpful if the examples in the guidance could draw out the sorts of omissions which would be regarded as falling within the offence. We understand from discussions with HMRC that the facilitation element of the offence would only apply where, for example, there was an obligation to do something (such as submitting a Suspicious Activity Report to the National Crime Agency) which was not carried out, rather than by a more general failure to act.
- 4.8 We think it would be particularly helpful if there was an acknowledgement in guidance or elsewhere that in situations where civil penalties can already provide a very effective "punishment" for companies that take insufficient steps to prevent tax evasion, and where a criminal prosecution would simply result in an additional fine, that the new criminal offence should only be pursued if the matter is very serious and will have a significant "exemplary" impact. We think there is a danger of the offence being applied in cases well removed from facilitation of offshore tax evasion, and a

plethora of such cases could lead to the “downgrading” of the significance of a criminal prosecution.

- 4.9 How this interacts with the Contract Disclosure Facility, which requires the taxpayer to admit fraud, will also require some careful consideration and clear guidance from HMRC.
- 4.10 In the appendix to this document, we provide some scenarios which we think provide a useful basis for discussing the scope of the new offence.

5 QB2. Do you believe the draft clauses, when read with the associated guidance, clearly exclude instances where the corporation’s representative is acting in a private capacity, rather than providing services for or on behalf of the corporation? The Government welcomes suggested language or case studies for inclusion in the guidance.

- 5.1 Yes, but we do think, as noted above, there must be some element of formal relationship involved for the legislation to have effect.

6 QC1. Do you have any comments on the draft clause above, when read with the associated guidance?

- 6.1 Draft clause 1(2) should include the words “trading or non-trading” if HMRC want it to reflect what is said in paragraph 2.9.

7 QD1. Do you believe that the legislation, when read with the associated guidance, makes it sufficiently clear in respect of what criminal acts a corporation can be liable for failing to prevent its representatives from criminally facilitating? The Government welcomes suggested language or case studies for inclusion in the guidance.

- 7.1 We wonder whether draft clause 2(4)(a) should read “UK Exchequer” rather than “public revenue” to make it clear it is focussed on UK tax evasion.
- 7.2 The example given on page 15 (paragraph 2.16) could be interpreted differently according to who had the idea of falsifying the invoices and submitting incorrect VAT returns. So, for example, the employee of the customer could have given the employee of the accountancy and invoicing services company false invoices and false information with which to compile the VAT return on behalf of the customer, in which case the ‘fault’ lies with the customer and not with the accountancy company. However, it would be different if the employee of the accountancy company persuaded the employee of the customer to do this, or took the information from the customer and falsified it, in which case the fault lies with the accountancy company. The legislation and guidance both need to differentiate between the two scenarios. Only the second scenario should bring the corporate criminal offence into play.
- 7.3 In revised Clause 2(5) on page 16, we are not sure whether the words “the commission of” are necessary.

8 QE1. Do you agree that the domestic tax fraud and overseas tax fraud elements of the corporate offence are better presented as two separate offences?

8.1 Yes.

8.2 At paragraph 2.20 on page 17, the second bullet envisages making a non-UK company liable for failing to prevent criminal facilitation of tax evasion in the UK, but makes it clear that the offence does not apply to foreign tax evasion by a non-UK based corporation. There must be an UK element.

8.3 On page 29, the draft guidance indicates that the foreign tax evasion facilitation offence can be committed by a relevant body whose associated person is located within the UK at the time of the act that facilitates the evasion of the overseas tax. We think that this is what is meant to be reflected in revised draft clause 3(2)(b)(ii), although it does not specify that the person has to be located in the UK only that the act or omission takes place in the UK. Nonetheless, this is still a much broader interpretation of the foreign tax evasion facilitation offence than is articulated on page 17.

8.4 What we think this means is that an offence could be committed if two employees of a non-UK company, (where the non-UK company has no business in the UK whatsoever and therefore no UK tax liability) meet at Heathrow airport and concoct a scheme to evade, say, Australian tax. We do not think this is what can be intended. We suggest that the remedy is that between 3(2)(b)(i) and 3(2)(b)(ii) the “or” should instead be “and”.

9 QE2. The Government welcomes stakeholder views on the new clauses, whether they sufficiently articulate the requirement for dual criminality at both the taxpayer and facilitator level, when read alongside the associated guidance. And whether they sufficiently articulate the requirement for dual criminality at both the taxpayer and facilitator level. The Government welcomes suggested language or case studies for inclusion in the guidance.

9.1 At paragraph 2.20 on page 17, the third bullet point envisages making a UK based corporation liable for failing to prevent the criminal facilitation of an overseas tax loss. However, the definition of ‘foreign tax evasion facilitation offence’ in revised clause 3(5) does not spell out that it applies only to a UK based corporation. Should this be made clearer?

9.2 Given the insertion of “and” between 3(6)(a) and 3(6)(b) we would hope that HMRC would not act in either of the following scenarios, that is (1) where something is an offence under foreign law but is not an offence under UK law, and (2) where something is not an offence under foreign law but could be an offence under UK law. Please can HMRC confirm this?

10 QF1. Do you believe the amended draft legislation brings within scope only those corporations with a sufficient presence in the UK, or those corporations

whose representatives are committing the relevant criminal act(s) from within the UK? The Government welcomes suggested language or case studies for inclusion in the guidance.

- 10.1 With regard to revised clause 3(2), we make similar comments to those in paragraph 8.4 above. We think the remedy should be to change the “or” to “and” between (2)(b)(i) and (2)(b)(ii)

11 Acknowledgement of submission

- 11.1 We would be grateful if you could acknowledge safe receipt of this submission, and ensure that the Chartered Institute of Taxation is included in the List of Respondents when any outcome of the consultation is published.

12 The Chartered Institute of Taxation

- 12.1 The Chartered Institute of Taxation (CIOT) is the leading professional body in the United Kingdom concerned solely with taxation. The CIOT is an educational charity, promoting education and study of the administration and practice of taxation. One of our key aims is to work for a better, more efficient, tax system for all affected by it – taxpayers, their advisers and the authorities. The CIOT’s work covers all aspects of taxation, including direct and indirect taxes and duties. Through our Low Incomes Tax Reform Group (LITRG), the CIOT has a particular focus on improving the tax system, including tax credits and benefits, for the unrepresented taxpayer.

The CIOT draws on our members’ experience in private practice, commerce and industry, government and academia to improve tax administration and propose and explain how tax policy objectives can most effectively be achieved. We also link to, and draw on, similar leading professional tax bodies in other countries. The CIOT’s comments and recommendations on tax issues are made in line with our charitable objectives: we are politically neutral in our work.

The CIOT’s 17,500 members have the practising title of ‘Chartered Tax Adviser’ and the designatory letters ‘CTA’, to represent the leading tax qualification.

The Chartered Institute of Taxation
15 July 2016

Appendix

It would be helpful if HMRC could explain in what circumstances, if any, an offence may arise in the following examples and include them, or variations on this theme, in their guidance, and whether HMRC would take the view it would be appropriate to prosecute that offence.

These examples are of situations where criminal offences by a taxpayer and facilitator may have been committed, and where the corporation may not have put reasonable procedures in place to prevent the offences occurring, but generally in these examples there are already significant civil remedies that HMRC can use to penalise the offending parties. Guidance should show the interaction between existing civil remedies and those that will apply further to the new criminal offence, particularly with regard to smaller organisations and cases.

The guidance should provide a clear steer as to when HMRC might apply the new corporate criminal offence in circumstances when existing civil penalties are available to them. Our preferred route would be for civil penalties to be used in the majority of cases with the use of criminal prosecutions reserved for only the most serious of cases. As noted in our submission, we do not wish to see the serious nature of a criminal prosecution “downgraded” by a series of prosecutions that simply add an extra fine and have little “exemplary” impact.

We are providing these examples to show situations which could arise, well away from the facilitation of offshore evasion by financial advisers and others, where companies small and large could face the risk of a prosecution, and HMRC would have to take a decision as to whether to refer the matter for prosecution. We also have concerns that if when the offence should be invoked is not clearly understood and controlled within HMRC, some HMRC officers could threaten taxpayers with a prosecution in a case where either a prosecution would be unlikely to proceed, or where a prosecution would not have a sufficient exemplary justification and civil penalties would already provide significant and appropriate “punishment”. We would be happy to meet with you to discuss these examples in more detail if that would help. It is likely also that we will have further examples to send to you in the coming weeks.

Example One (A): A corporation engages an employment agency to obtain temporary staff, and that agency engages the workers so that section 44 ITEPA 2003 (the agency worker rules) applies. It is clear that there is ‘supervision, direction and control’ (SDC), such that PAYE should be accounted for by the agency, but the corporation provides a fraudulent document to the agency denying SDC, so that no PAYE is paid. In particular, the agency suggests to staff at the corporation that they issue a fraudulent document to avoid a secondary NIC’s liability. The corporation does not provide any guidance to its staff on identifying whether there is an SDC, nor does it review the accuracy of the document provided by the agency. It appears that the corporation has acted recklessly and not done enough to prevent tax evasion. In such circumstances we assume HMRC would pursue the corporation for PAYE under the transfer of debt provisions and for a civil penalty for failure to take reasonable care, etc. But would the new corporate criminal offence also be applied?

Example One (B): A public sector body obtains workers through an agency. The worker is engaged through their own ‘personal service company’ (PSC). New rules are due to come into effect in April 2017 such that for the public sector there is an obligation to deduct tax at source under the intermediaries’ legislation (IR35). Staff at the public sector body, misled by the agency in order to avoid a secondary NIC liability, wrongly declare that the IR35

employment status test is not satisfied so that the agency can evade paying the secondary NIC. The public sector body does not carry out any checks that the agency's advice is correct. As the public sector body appears to have acted either carelessly or recklessly and appears not to have done anything to prevent tax evasion arising would the new corporate criminal offence apply to the public sector body in such a situation?

Example Two (A): Employees of a multinational corporation, which is UK based with branches across the globe, frequently move around between the UK and overseas locations in carrying out their work duties. The corporation is aware that these employees will be taxable in the UK and that PAYE may apply but its employees responsible for payroll tax compliance say "it's all too difficult and costly – how can we track everybody all the time? Nobody does this." It later transpires that the business travellers do not submit UK tax returns because "nobody does this" and so no UK tax is ultimately paid. Is the corporation facilitating tax evasion by the business travellers? In particular, if it advised employees to submit tax returns did the corporation do enough to prevent tax evasion by its employees?

Example Two (B): Assume that, in the above example, the corporation had no obligation to account for PAYE but its business travellers to the UK nevertheless had a responsibility to pay UK income tax on earnings. Where the corporation's staff's advice is that if the employees do not file a tax return HMRC will never know, is this criminal facilitation under the proposed new rules?

Example Three: ABC Limited is a company publishing children's books. It has a turnover of around £500,000 per annum. It has started making these books available for download. Parents across the EU have started downloading the books for their children, but the amounts are modest. The directors of ABC Limited ask their accountants, Numbers Limited, to advise on the VAT consequences. Numbers Limited advise that ABC Limited should either register for VAT in each of the Member States in which books are downloaded, or otherwise register under the Mini One Stop Shop (MOSS).

The directors of ABC Limited asked their in-house accountant to implement this advice and register under MOSS. However, because this seemed like a lot of hassle, and because the sales across the EU are relatively modest, the accountant ignored the advice and simply decided to charge UK VAT on all downloads – why should HMRC care as they actually get more tax than is strictly due? No VAT is paid in other EU Member States.

Would the new offence be applied as ABC Limited failed to prevent the evasion of VAT in other EU Member States by not seeing through the advice provided by Numbers Limited?

Example Four: A contractor turns a blind eye to deduction at source under the Construction Industry Scheme (CIS) rules and as a consequence a sub-contractor is paid gross when they should have been paid net. The sub-contractor does not report the income to HMRC eg by failing to file a tax return and so deliberately evades the associated tax.

Does the action of the staff at the contractor responsible for operating the CIS rules constitute a failure to do enough to prevent tax evasion by the sub-contractor so that an offence is committed under the new rules? We would assume that the new offence could apply unless the contractor has taken reasonable steps to prevent the evasion. That being so, would incompetence, negligence or recklessness by the staff in carrying out their duties be taken into account when considering the corporation's defence?

Example Five: Regulation 72 of the PAYE regulations allows recovery of tax from an employee where it has not been deducted by the employer where, inter alia, "*the employee*

has received...payments knowing that the employer has wilfully failed to deduct the amount of tax which should have been deducted from those payments". Consider the position when the employee subsequently deliberately fails to submit a tax return including the payments received from the employer and so pays no tax on them and where he subsequently leaves the UK. Does the new offence apply in this sort of scenario? Does it depend on the reason why the employer failed to deduct tax under PAYE? Does it make any difference that up until a direction is made by HMRC the PAYE is purely an employer liability with the employee being able to claim a notional credit under PAYE regulation 185(5)?

Example Six: A multinational corporation engages third party individuals (authors) to provide written articles and other works for which they are paid a royalty. The default position is that all royalties paid from the UK are net of withholding tax, unless the third party can provide appropriate evidence that a lower rate is applicable to them via a double tax treaty. One of the authors requests that the royalty payments made to him are paid into a Bermudian bank account. If the payroll team make the payment into the Bermudian bank account and it later transpires that the individual author was evading *UK* taxation would the new corporate criminal offence apply to this situation? We would assume that the offence could only apply if the payroll team knew it was colluding in tax evasion, and that the corporation would have a defence if it had trained its staff appropriately to be fully compliant and alert to situations when an author may be trying to evade tax.

If the royalties are paid from a UK multinational corporation to the authors and one of the authors requests that the royalty payments made to him are paid into a Bermudian bank account, and it later transpires that the individual author was evading *foreign* taxation would the new corporate criminal offence apply to this situation? Again, we assume the offence could apply if collusion had taken place, and the corporation would need to demonstrate a reasonable procedures defence.

If the corporation had a questionnaire for all third party authors which included a question such as *'please confirm that you have declared this income for income tax purposes in the relevant jurisdictions which apply to you'* would this be considered a reasonable procedure?