SEPTEMBER 2016

mourant

UPDATE

Developments in UK tax law: the GAAR, new offences and sanctions affecting offshore practitioners

Update prepared by Christopher Edwards (Partner, Guernsey)

The UK's attitude to tax planning has hardened significantly as of late. Case law which might previously have protected individuals or entities taking advantage of rather more exotic tax planning has been superseded by statute. New civil sanctions and criminal offences are also proposed in relation to enabling offshore tax evasion and failure to prevent the facilitation of tax evasion. Offshore businesses should have robust procedures in place to mitigate their risk and, if in doubt, seek independent advice.

Developments in UK tax law: the GAAR, new offences and sanctions affecting offshore practitioners

The UK's attitude to tax planning has hardened significantly as of late. Case law which might previously have protected individuals or entities taking advantage of rather more exotic tax planning has been superseded by statute. New civil sanctions and criminal offences are also proposed in relation to enabling offshore tax evasion and failure to prevent the facilitation of tax evasion. Offshore businesses should have robust procedures in place to mitigate their risk and, if in doubt, seek independent advice.

The General Anti-Abuse Rule (GAAR)

Until 2013, the generally accepted position regarding tax avoidance in the UK was that the individual was free to take any steps permitted by law to reduce his tax bill. This was memorably summarised in the judgment of Lord Clyde in *Ayrshire Pullman v CIR* (1929) 14TC754:

> 'No man in this country is under the smallest obligation, moral or other, so as to arrange his legal relations to his business or to his property as to enable the Inland Revenue to put the largest possible shovel into his stores.'

HMRC was aided by over 300 targeted anti-avoidance rules which applied to particular situations and taxes. There was also a significant body of case law regarding what was and was not deemed acceptable by the Courts, and rules requiring disclosure of tax avoidance schemes.

However, the Finance Act 2013 (which came into force on 17 July 2013) introduced the GAAR. The GAAR applied to any tax arrangement which achieves a favourable tax result that Parliament did not anticipate when it introduced the relevant rule, and which goes beyond what could reasonably be regarded as reasonable. It was not intended to capture reasonable choices by taxpayers which may have different tax outcomes, or the use of incentives and reliefs as they were intended by Parliament. Instead, it was intended to prevent contrived arrangements to take advantage of tax reliefs without incurring an equivalent economic risk (ie 'abusive' tax arrangements).

The GAAR set a high bar for whether an arrangement is considered abusive. This is known as the 'double-reasonableness' test, and is whether entering into a tax arrangement 'cannot reasonably be regarded as a reasonable course of action in relation to the relevant tax provisions, having regard to all the circumstances'. The 'circumstances' include the policy behind the tax provisions, whether the arrangements involved 'contrived or abnormal steps', and whether they were 'intended to exploit any shortcomings' in the tax provisions. In particular, if the only (or dominant) purpose for any contrived or abnormal steps is to

minimise tax, and in particular to exploit shortcomings in tax laws, it is likely that they may be found to be abusive.

HMRC has provided extensive guidance as to what would and would not be considered abusive, and this guidance, together with a number of non-legislative materials in the public domain (such as Hansard records) may be taken into account by Courts in deciding whether an arrangement falls foul of the GAAR. However, the Finance Act 2013 did not provide for a pre-transaction clearance system, so taxpayers and advisors must take the guidance into account when deciding whether to effect a transaction.

If HMRC considers that an arrangement falls foul of the GAAR, it will issue a written notice allowing the taxpayer to make representations. Following that, an independent advisory panel will produce an opinion as to whether the arrangement was a reasonable course of action in the circumstances. HMRC must then take that opinion into account when applying the 'double reasonableness' test. If HMRC considers that the arrangement fails the test, it will issue a written counteraction notice. While the GAAR does not include specific penalties, it provides for 'counteraction' of the arrangement in a way that is just and reasonable, and pre-existing penalties for failing to take reasonable care in completing a tax return, or deliberately completing an inaccurate tax return, may apply.

Proposed new offences

The Finance Bill 2015-16 to 2016-17 (formerly known as the Finance Bill 2016) is not yet in force, but is expected to introduce measures to counteract offshore tax evasion. In particular, it will introduce civil penalties for 'enabling' offshore tax evasion, and the new criminal offence of failing to prevent the criminal facilitation of tax evasion.

The proposed civil sanctions (the higher of 100 per cent of the potential lost revenue, or £3,000, subject to reductions for cooperation with HMRC) will apply to people enabling another person to carry out offshore tax evasion, in the knowledge that their actions would enable or were likely to enable offshore tax evasion. The other condition of the sanction is that the evader has received a final conviction or penalty for the tax evasion offence. Being in breach of the GAAR would not in itself constitute a tax evasion offence.

The proposed criminal offence applies to a body corporate or partnership which has failed to prevent an 'associated person' (ie an individual or company acting as its agent) from facilitating any UK offence of tax evasion. The act of the associated person is already a criminal offence (ie deliberately aiding and abetting a person or entity to commit a UK offence of tax evasion). However, the proposed new offence appears to have as its primary target companies providing tax planning or advice which may previously have sought to avoid liability for the actions of employees, agents or subsidiaries. In particular, large corporations might previously have claimed that the board had no knowledge of the criminal activities of employees or agents.

A similar offence is also proposed in relation to the failure to prevent an associated person from facilitating a foreign tax evasion offence (where facilitating such a tax evasion offence in respect of UK tax would also constitute a UK tax evasion facilitation offence). It is a defence to both the UK and foreign offences to show that it had in place such preventative measures as it was reasonable in the circumstances to have in place. This defence is similar to the safe harbour defence under the Bribery Act.

Such reasonable procedures will vary according to the size and complexity of a business, and the risk of its associated persons facilitating tax evasion. However, typical measures proposed include a prominent and public commitment against tax evasion, contractual terms requiring that employees and agents do not engage in tax evasion facilitation, due diligence in relation to associated persons, regular staff training, and clear reporting procedures for whistle-blowers. Such procedures should be supported by a robust system of monitoring and enforcing compliance, and regularly-updated risk assessment in relation to the company or partnership's services being used to facilitate tax evasion.

Application to offshore businesses

Companies based offshore are not outside the reach of the proposed offences. In particular, the offence of failing to prevent the facilitation of UK tax evasion applies to any partnership or body corporate, whether or not it has a UK connection. The analogous offence in relation to foreign tax evasion is an offence under the proposed UK law if the partnership or body corporate is incorporated or formed under UK law, or carrying on a business or undertaking, or part thereof, from an establishment in the UK, or where any act or omission in committing the foreign tax evasion facilitation offence takes place in the UK.

Companies or partnerships at risk of finding themselves liable for the proposed offences should therefore implement procedures and, if unsure, insist on taking independent advice. They should also take steps to ensure that arrangements they put in place for their clients do not fall foul of the GAAR. Industry and HMRC guidance may provide helpful assistance, but if in any doubt, legal advice should be sought. It is also important to note that legal advice will be privileged from disclosure in any court proceedings which result from the arrangements put in place.

Contacts

Christopher Edwards
Partner, Mourant Ozannes
Guernsey
+44 1481 739 322
christopher.edwards@mourant.com

This update is only intended to give a summary and general overview of the subject matter. It is not intended to be comprehensive and does not constitute, and should not be taken to be, legal advice. If you would like legal advice or further information on any issue raised by this update, please get in touch with one of your usual contacts. © 2018 MOURANT OZANNES ALL RIGHTS RESERVED