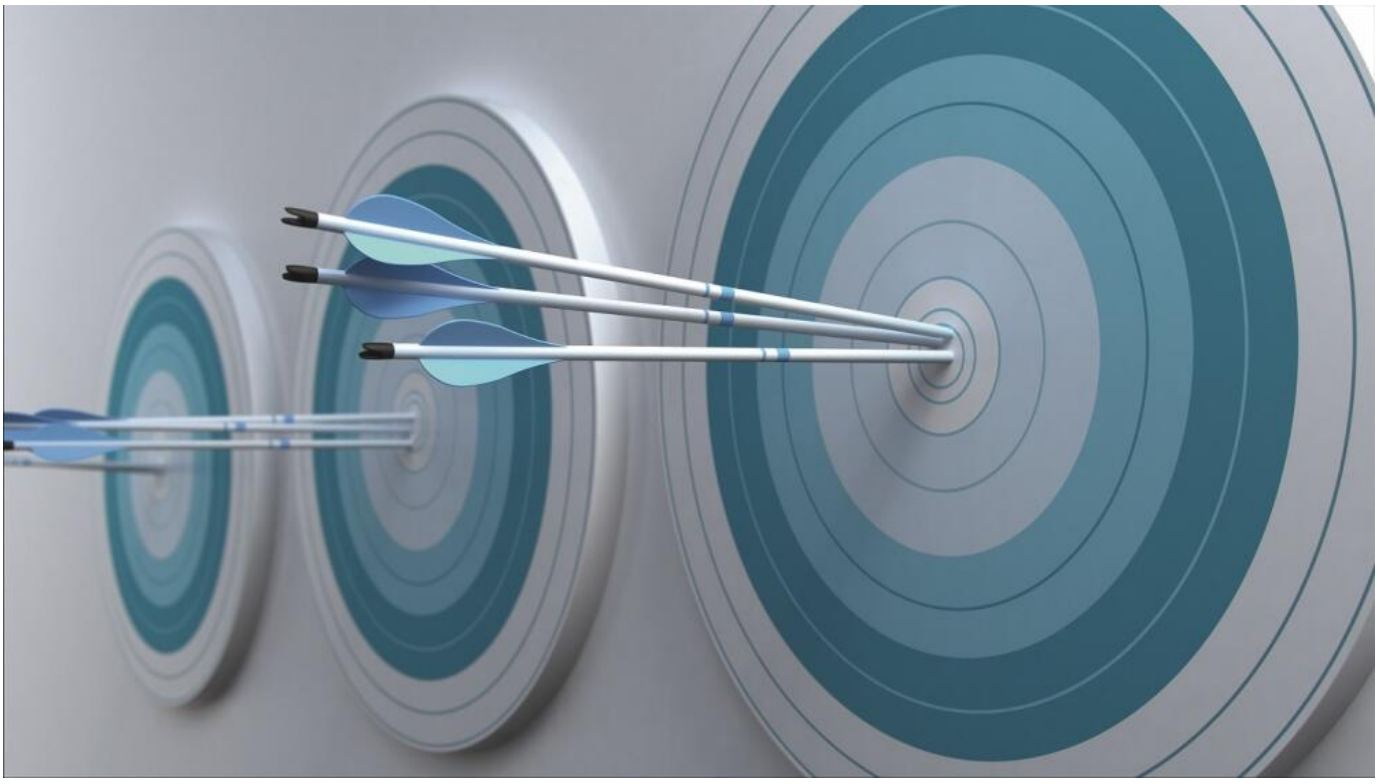
An easy target

Management of taxes



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Anton Lane looks at what advisers need to know regarding the tougher tests for reasonable excuse when offshore tax planning

Key Points

What is the issue?

The offshore criminal offence may see a significant increase in prosecutions, subject to whether a reasonable excuse is available.

What does it mean to me?

Advisers need to be aware of the scope of the offence as well as the increasing tougher tests for reasonable excuse.

What can I take away?

It is envisaged that HMRC will test ‘reasonable excuse’ more vigorously in relation to offshore planning as well as schematic planning.

A December 2015 report from the National Audit Office contained the following: ‘HMRC agreed a target to increase the number of prosecutions not involving organised crime by 1,000 a year by 2014-15 from a baseline of 165 in 2010’.

To help meet this target, and also as a deterrent to offshore tax planning, HMRC has introduced the Offshore Criminal Offence from a date to be set by Statutory Instrument. This article considers the defence of ‘reasonable excuse’ for failed or late return filings or payments and the threats to that defence which have potential to land the unknowing with fines and/or a prison sentence.

The reasonable excuse that many taxpayers will currently be confident of applying is where reliance has been placed on professional advice. I will discuss this too.

What is the offshore offence?

FA 2016 para 166 is headed ‘Offences relating to offshore income, assets and activities’. It amends TMA 1970 to introduce new criminal offences, which apply for the purposes of income tax and capital gains tax only, where a person has failed to declare offshore income or gains in accordance with TMA 1970 ss 7 and 8. The offence applies to any subsequent loss of tax over a threshold amount, which will be defined in the regulations annually.

Crucially, the offence does not prescribe the need to prove intent for failing to declare taxable offshore income and gains.

TMA 1970 ss 106B to 106D set out the new offences, which are broadly:

- Failing to give notice to being chargeable to income tax or CGT;
- Failing to deliver a return; and
- Making an inaccurate return.

The offences could therefore apply to potentially many situations including:

- Where it is not possible to rely on an offshore structure being within the commercial exemption disapplying the anti-avoidance legislation;
- Where a scheme with an offshore element has not been successful;
- If interpretation of associated operations for the transfer of asset abroad rules is incorrect, bearing in mind the more recent subtle changes to the legislation: HMRC hold the opinion that the changes reflect the position in the earlier legislation but our view is that the scope has changed significantly.

A lot of offshore structures sit within an area of law where the tax treatment is open to debate. At worst, this means that HMRC could seek to apply the offence where there is a failure relating to income or gains of offshore companies, trusts, foundations, protected cell companies, qualifying non-UK pension schemes, retirement benefit schemes, pension liberation arrangements, employee benefit schemes, employee remuneration trusts, contractor loan arrangements and remuneration trust structures.

In the absence of a reasonable excuse, the offence could apply to a considerable amount of offshore tax structuring. This appears to meet HMRC's policy because, as stated in the same NAO report I mentioned earlier: 'Criminal investigations and prosecutions are reserved for where the conduct involved is such that only prosecuting an offender is appropriate or where HMRC needs to send a strong deterrent message'.

Luckily, each offence is open to a reasonable excuse defence. Where there is no excuse a taxpayer may face an unlimited fine in England and Wales and/or a custodial sentence of up to six months for offences committed before section 281(5) of the Criminal Justice Act 2003 comes into force, and 51 weeks thereafter.

What is a reasonable excuse?

FA 2009 Sch 55 para 23(2)(b) and (c) states:

- 'Where P (the taxpayer) relies on any other person to do anything, that is not a reasonable excuse unless P (the taxpayer) took reasonable care to avoid the failure.'

- ‘Where P had a reasonable excuse for the failure but the excuse has ceased, P is to be treated as having continued to have the excuse if the failure is remedied without unreasonable delay after the excuse ceased.’

HMRC’s Compliance Handbook further defines reasonable excuse, saying it may be where the taxpayer was ‘acting on advice from a competent adviser which proves to be wrong despite the fact that the adviser was given a full set of accurate facts’.

Considering a client adviser relationship over several years and the legislation in conjunction with HMRC’s interpretation, my view is that a reasonable excuse will be available where:

- A client seeks a competent adviser to provide tax advice on a proposition, including whether a notice to chargeability needs to be made, a tax return delivered, and whether disclosures or entries need to be entered onto a return;
- All relevant facts are provided to a competent adviser;
- Based on those facts, complete tax advice is provided;
- The tax advice provided is considered independent and of a standard where it would be reasonable for the client to believe that advice is delivered in their best interest;
- The tax advice is specific on the actual tax treatment i.e. does not state that the treatment is open to differing interpretations; and
- An adviser is placed in a position by the client to be able to provide ongoing comprehensive and accurate advice based on all relevant facts.

Unfortunately, levels of advice and relationships are not always so perfect, for example:

- The adviser may have advised on an unfamiliar area;
- The client may not have taken prudent steps, having regard for their financial astuteness and tax knowledge, to ensure the adviser was competent in that area;
- The advice provided may lack detail and/or references to supporting legislation or case law and having regard for the client’s financial astuteness and tax knowledge, it is not reasonable that the advice was relied upon;
- The client may not have provided all relevant facts or may have not implemented advice as intended;

- Advice may have included several potential risks, which may be considered to be acceptance by the client that the transactions undertaken may not be necessarily treated as hoped;
- The advice may come from a provider of a structure (or scheme) and it may be reasonable for a client to consider that advice may be conflicted, not independent nor in their best interest; and
- The adviser is not regularly kept informed of what and how transactions are undertaken within the offshore structure, leaving them in a position that they are unable to provide continued and accurate advice.

Case law supports these views

In both *Schola UK Ltd* 2011 (TC001004) and *Life Property Management Limited (The Ironworks)* 2013 (TC02708) it was confirmed that when considering reasonable excuse (in that case in respect of an employer) it is regarding the actions of the taxpayer from the perspective of a prudent person exercising reasonable foresight and due diligence and having proper regard for responsibilities under the Tax Acts.

The case of *Anderson (deceased) v HMRC 2009* set out the same requirement to consider what a reasonable taxpayer exercising reasonable due diligence would have done. Meanwhile, *Hanson v HMRC 2012* confirms that reasonable excuse will be available where reliability is sought from a reputable adviser.

The older case of *Nunn v Gray 1997* illustrates the risk where reliance was placed on an old adviser because the taxpayer had failed to correct the omission of dividend income and a gain on the disposal of shares without unreasonable delay. The taxpayer was considered to have experience of tax having submitted returns for a number of tax years, so he should have been aware of the responsibility to include such income and gains.

With regard to those using tax schemes, the cases of *BP Litman & A Newall v Commissioners for HMRC* [2014] (TC03229) and *Herefordshire Property Company Ltd v Commissioners for HMRC* [2015] (TC04286) should be of interest. Both cases were in relation to capital redemption scheme planning although reasonable care was denied in the first but accepted in the second. In the Litman case, reliance was place on the promoter for tax advice as well as for entries to be included in their tax return. The advice provided was minimal. The taxpayers relied on the promoter to complete the documents for the scheme and implement it. The taxpayers did not

check the steps, in particular whether loans were entered into, ahead of submitting their returns. The taxpayers were negligent in signing their returns reflecting transactions which they had no evidence of being entered into. The outcome for Herefordshire Property Company was different because the director explained that the promoter's previous scheme had not failed and he had no reason to doubt their abilities, reputation or advice.

What is the risk of the offshore offence applying?

HMRC has added an extra 200 staff to work on criminal investigations and revising the conduct of investigations. HMRC has also agreed with the Crown Prosecution Service on how the two organisations work together to achieve the target. HMRC met and exceeded the prosecution target in 2014/15 (1,183 tax fraud prosecutions not involving organised crime). Additional funding has been made available for criminal investigations into serious and complex tax crime. The intended focus is on wealthy individuals and corporates, with the aim of increasing prosecutions in this area. HMRC aims to secure widespread publicity for prosecutions because it believes that this has a significant part to play in creating the deterrent effect.

If HMRC is looking for an easy target to bolster prosecutions the offshore criminal offence offers a fast track route to obtaining the desired numbers, in particular from users of avoidance schemes who relied on the promoter. The increased information passing to HMRC from offshore gives a great opportunity to execute the intended focus on wealthy individuals and corporates, although it may be a little while before this is achieved.