HM Revenue
& Customs

Tackling tax evasion: Government guidance for the corporate offence of failure to prevent the criminal facilitation of tax evasion.

Draft Government Guidance
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1. Introduction

1.1 Aim of the legislation

The Government believes that relevant bodies should be criminally liable where they fail to prevent those who act for, or on their behalf from criminally facilitating tax evasion.

The new offences will be committed where a relevant body fails to prevent an associated person *criminally* facilitating the evasion of a tax, and this will be the case whether the tax evaded is owed in the UK or in a foreign country.

Previously, attributing criminal liability to a relevant body required prosecutors to show that the senior members of the relevant body were involved in and aware of the illegal activity, typically those at the Board of Directors level. This had a number of consequences:

- It can be difficult to hold a large multinational organisation to account. In large multinational organisations decision making is often decentralised and decisions are often taken at a level lower than that of the Board of Directors, with the effect that the relevant body can be shielded from criminal liability. This also created an un-level playing field in comparison to smaller businesses where the Board of Directors will be more actively involved in the day-to-day activities of a business

- The common law method of criminal attribution may have acted as an incentive for the most senior members of an organisation to turn a blind eye to the criminal acts of its representatives in order to shield the relevant body from criminal liability

- The common law may also have acted as a disincentive to internal reporting of suspected illegal tax activity to the most senior members, who would be required to act upon such reporting since otherwise the corporate entity might be criminally liable.

The cumulative effect was an environment that could do more to foster corporate monitoring and self-reporting of criminal activity related to facilitating tax evasion. This meant that bodies that refrained from implementing good corporate governance and strong reporting procedures were harder to prosecute, and in some cases lacked a strong incentive to invest in preventative procedures.

It was those bodies that deliberately turned a blind eye to wrongdoing and preserved their ignorance of criminality within their organisation that the earlier criminal law most advantaged. Those most disadvantaged by the law were compliant businesses who invested in robust governance procedures and refused to become involved in the provision of illicit services.

The new corporate offence therefore aims to overcome the difficulties in attributing criminal liability to relevant bodies for the criminal acts of employees, agents or those that provide services for or on their behalf.

The new offence, however, does not radically alter what is criminal, it simply focuses on who is held to account for acts contrary to the current criminal law. It does this by focussing on the failure to prevent the crimes of those who act for or on behalf of a corporation, rather than trying to attribute criminal acts to that corporation.

The legislation aims to tackle crimes committed by those who act for or on behalf of a relevant body. The legislation does not hold relevant bodies to account for the crimes of their customers, nor does it require them to prevent their customers from committing tax evasion. Nor is the legislation designed to capture the misuse of legitimate products and services that are provided to customers in good faith, where the individual advisor and relevant body did not know that its products were intended to be used for tax evasion purposes.

The Government recognises that any regime that is risk-based and proportionate cannot also be a zero failure regime. If a relevant body can demonstrate that it has put in place a system of reasonable prevention procedures that identifies and mitigates its tax evasion facilitation risks, then prosecution is unlikely as it will be able to raise a defence.

1.2 Purpose of guidance

This guidance explains the policy behind the new offences and is intended to help relevant bodies understand the types of processes and procedures that can be put in place to prevent associated persons from criminally facilitating tax evasion. It will inform the conduct of a risk assessment and the creation of procedures proportionate to that risk.

The guidance is designed to be of general application and is formulated around the following six guiding principles:

- **Risk assessment**
- **Proportionality of risk-based prevention procedures**
- **Top level commitment**
- **Due diligence**
- **Communication (including training)**
- **Monitoring and review**

The Government guidance aims to:

- Provide guidance to relevant bodies on how they might conduct an assessment of the risk of their representatives criminally facilitating tax evasion
- Help relevant bodies adopt a more effective, risk-based and outcomes-focused approach to mitigating the risk of associated persons criminally facilitating tax evasion
- Assist consideration of whether the reasonable procedures defence is available
- Enhance the understanding of Government expectations and help relevant bodies to assess the adequacy of their existing systems and controls, and remedy deficiencies
- Assist trade bodies in the formulation of more detailed sector-specific procedures.

The guidance and examples are intended to be illustrative and cannot cover every form of risk of associated persons criminally facilitating tax evasion that a relevant body may face. The examples present ways, but not the only ways, in which relevant bodies might comply with the requirement of reasonable “prevention procedures”. Similarly, there are many examples of poor practices that have not been expressly covered.

The guidance is not prescriptive or a one-size-fits-all document. It is not a checklist of things that all relevant bodies must do to reduce their risk of liability under the corporate criminal offences, and should not be used as such.

The guidance should be considered and applied in a risk-based and proportionate way. This includes taking into account the size, nature and complexity of a relevant body when deciding whether a certain example of good or poor practice is appropriate to its business. The guidance therefore needs to be used to inform the creation of bespoke prevention procedures designed to address a relevant body’s particular circumstances and the risks arising from them.

Departures from suggested procedures within the guidance will not mean that an organisation does not have reasonable procedures, as different prevention procedures may also be just as reasonable. In addition, a small organisation and a large multi-national organisation may implement the principles in very different ways: what is reasonable for a small business in a low risk sector may be entirely unreasonable for a large business in a high risk sector.

Nor is this guidance intended to provide a safe-harbour: compliance with the guidance will not render a relevant body immune from prosecution. Even strict compliance with this guidance will not necessarily amount to having reasonable procedures where the relevant body faces particular risks arising from the unique facts of its own business that remain unaddressed.

The onus will remain on the relevant organisation, where it seeks to rely on the defence, to prove that it had reasonable prevention procedures in place (or that it was unreasonable to expect it to have such procedures). Ultimately only the courts can determine whether a relevant body has *reasonable prevention procedures* in place to prevent the facilitation of tax evasion in the context of a particular case, taking into account the facts and circumstances of that case.

This guidance is not the only source of guidance on preventing associated persons from criminally facilitating tax evasion. Relevant bodies are reminded that other bodies produce guidance that may also be relevant and useful, for example trade associations and representative bodies.

This Government guidance will also inform trade bodies and sector representatives in the development of more precisely tailored sector-specific guidance for their members which can be put forward for endorsement by the Government.

1.3 Overview of the offence and illustrative examples

There are three stages that apply to both the domestic and foreign tax evasion facilitation offences. There are additional requirements for the foreign offence set out below (including the ‘dual criminality’ requirement):

Stage one: the criminal tax evasion by a taxpayer (either an individual or a legal entity) under existing law

Stage two: the criminal facilitation of the tax evasion by an “associated person” of the relevant body who is acting in that capacity

Stage three: the relevant body failed to prevent its representative from committing the criminal facilitation act

Defence: where the relevant body has put in place ‘reasonable prevention procedures’ to prevent its associated persons from committing tax evasion facilitation offences (stage two), or where it is unreasonable to expect such procedures, it shall have a defence.

“*Relevant body*”

Only a “relevant body” can commit the new offences. This means that only incorporated bodies (typically companies) and partnerships can commit the new offences. The new offences cannot be committed by natural (as opposed to legal) persons. Companies and partnerships, not men and women can commit the new offences.

"*Associated Person*"

A relevant body can only commit the new offences if a person associated with it criminally facilitates a tax evasion offence (deliberate and dishonest action).

A person is "associated" with a relevant body if that person is an employee, agent or other person who performs services for or on behalf of the relevant body. The offence is committed where the facilitation offences are committed by someone acting in the capacity of an associated person. The associated person can be an individual or an incorporated body.

The question as to whether a person is performing services for or on behalf of an organisation is to be determined by reference to all the relevant circumstances and not merely by reference to the nature of the relationship between that person and the organisation. The contractual status or label of a person performing services for or on behalf of the organisation does not matter, so, for example, employees, agents and sub-contractors can be associated persons.

The concept of a person who 'performs services for or on behalf of' the organisation is intended to be broad in scope, to embrace the whole range of persons who might be capable of facilitating tax evasion whilst acting on behalf of the relevant body.

For more detail and case studies explaining the terms (and other commonly used terminology please see **Section 3**).

- **UK Tax Evasion Facilitation Offence**

Where there is a UK tax evasion facilitation offence it does not matter whether the relevant body is UK-based or established under the law of another country, or whether the associated person who performs the criminal act of facilitation is in the UK or overseas. In such cases the new offence will have been committed and can be tried by the courts of the United Kingdom.

Stage one: the **criminal tax evasion** by a **taxpayer** (either an individual or a legal entity) under existing law

For the corporate offence to be committed there must first be a criminal offence at the taxpayer level (stage one). Non-compliance, falling short of fraud, at the taxpayer level will not result in the corporate offence being committed. This offence only relates to the failure to prevent the facilitation of fraud.

Any fraudulent activity that intends to divert funds from the public revenue constitutes the common law offence of cheating the public revenue. There are also a range of statutory offences of “fraudulently evading” various taxes (for example fraudulently evading VAT, contrary to section 72 of the Value Added Tax Act 1994; or fraudulently evading income tax, contrary to section 106A of the Taxes Management Act 1970).

These provisions make it an offence to dishonestly “take steps with a view to” or “be knowingly concerned in” the evasion of the tax. For these offences to be committed it is not necessary that any tax actually be successfully evaded.

A conviction at the taxpayer level is not a pre-requisite for bringing a prosecution against a relevant body under the legislation. For example, a taxpayer may voluntarily come forward and make a full and honest disclosure to HMRC of their actions and it may not be in the interests of justice to criminally prosecute that individual. Where there is no criminal conviction of the taxpayer (stage 1) the prosecution would still have to prove during the prosecution of the relevant body, to the criminal standard of beyond all reasonable doubt, that the taxpayer level offence had been committed.

Stage two: the **criminal facilitation** of the tax evasion by an **“associated person”** of the relevant body

It is already a crime to deliberately and dishonestly facilitate the commission of revenue fraud by another person. It is already a crime for a person to be knowingly concerned in, or take steps with a view to, another person fraudulently evading tax that they owe. It is also a crime to aid and abet another person in committing a revenue fraud.

Therefore if a professional such as a banker, accountant or lawyer, deliberately and dishonestly facilitates the commission of revenue fraud by a client, then that banker, accountant or lawyer also commits a crime. The fact that the crime is committed during the course of their work is no defence.

For the corporate offence to be committed there must be criminal facilitation of the taxpayer evasion by an associated person (stage two). The associated person must deliberately and dishonestly take action to facilitate the taxpayer-level evasion. If the associated person is only proved to have accidentally, ignorantly or even negligently facilitated tax the evasion offence then the new offence is not committed by the relevant body.

Stage three: the relevant body **failed to prevent** its representative from committing the criminal facilitation act

As the offence is a strict liability offence, if stages one and two offences are committed then the relevant body will have committed the new corporate offence unless it can show it has put in place reasonable preventative procedures.

Defence: where the relevant body has put in place reasonable prevention procedures to prevent the criminal facilitation of tax evasion by an associated person (or where it is unreasonable to expect such procedures) the relevant body shall have a defence. This guidance provides suggestions of the types of processes and procedures that can be put in place to prevent associated persons from criminally facilitating tax evasion.

Below are some illustrative examples of the different types of procedures which would be relevant for companies of varying sizes, complexity, industry focus and risk profile. For all the examples below it should be noted that the precise scale and nature of the tax evasion taking place would influence any decision to prosecute:

1) Low/Medium risk

- A mid-size car parts maker ("UKCO") operating in the UK and Europe, entered into a sub-contracting arrangement with an UK distributor. The senior managers of the UK distributor created a false invoicing scheme with the assistance of a purchaser, allowing the purchaser to evade UK taxes due on its purchase of the car parts in the UK

- UKCO itself undertook a tax evasion focused risk assessment, identifying only low and medium level risks to the organisation, subsequently implementing a number of prevention policies and procedures to mitigate the identified risks. UKCO had a clear policy against tax evasion, including terms and conditions within contracts with all third parties

- UKCO also carried out a due diligence assessment of its sub-contracting partner, but not for the entire supply chain. Nothing abnormal was detected during the due diligence test and consequently, UKCO had no reason to believe that the staff of the distributor were involved in a fraudulent tax scheme

In these circumstances, UKCO had undertaken a tax evasion facilitation risk assessment, had procedures and processes in place, as well as conducting a due diligence assessment of its sub-contracting partner. It is therefore unlikely that this company would have committed the offence as it has a valid defence of having reasonable procedures in place and articulating and evidencing what it had done, even if it did not conduct due diligence for the entire onward supply chain.

Whilst UKCO could have done more, it would not have been reasonable or proportionate to do so, the steps that it did take were proportionate to the risks it identified and faced.

2) Higher risk

- As part of a large transaction an employee of a UK-based multinational bank knowingly referred a corporate client to an offshore accounting firm with the express intention of assisting the corporate client to set up a structure allowing the client to evade foreign income tax

- The bank, which had rigorous prevention procedures for money laundering and bribery procedures, undertook only a light-touch tax evasion risk assessment, nominally including the word 'tax' into existing procedures and processes, but not effectively implementing or enforcing them or reviewing tax fraud risks

- The bank undertook no tax evasion focussed due diligence assessment of the accounting firm to which the client was referred.

In these circumstances, although the bank could attempt to mount a defence of having reasonable procedures in place on paper for tackling the facilitation of tax evasion, in reality it had relied on unaltered money laundering and bribery procedures. Despite being in a high risk sector, it had also failed to undertake a thorough risk assessment, or follow Government or sector-focused guidance on the types of processes and procedures needed to mitigate risks. It is therefore likely that the bank would be found to have committed the new offence and would be unable to put forward a successful reasonable procedures defence.

- **Foreign Tax Evasion Facilitation Offence**

The fraudulent evasion of tax is wrong. It would also be wrong for a UK-based relevant body to escape liability for acts which, if they were in relation to UK tax would be criminal, just because the country suffering the tax loss is unable to bring an action against that relevant body within that jurisdiction's legal system.

The foreign offence operates in a broadly similar way to the domestic offence, first with a requirement for <u>criminal evasion</u> by a taxpayer (stage one), then the <u>criminal facilitation</u> of tax evasion by an associated person (stage two) and if stages one and two offences are committed then the relevant body is <u>criminally liable</u> (stage three) unless it can show it has put in place reasonable preventative procedures: where the relevant body has put in place reasonable prevention procedures it will have a defence, in the same way as for the domestic offence.

The foreign offence, however, is slightly narrower in scope, in that only certain relevant bodies with a UK nexus can commit the foreign revenue offence. The prosecution in the UK would also still need to show to the criminal standard that the offences at taxpayer and associated person level had been committed and that there was "dual criminality".

UK Nexus

The foreign tax offence can only be committed by a relevant body:

- incorporated under UK law, for example a limited company incorporated under UK law;
- carrying on a business or other undertaking from a permanent establishment within the UK, for example a company incorporated under the law of France but operating from an office in Manchester; or
- whose associated person is located within the UK at the time of the criminal act that facilitates the evasion of the overseas tax, for example a company incorporated under German law whose employee helps another person to commit a foreign tax evasion offence whilst in London.

These bodies, described above, are considered to be sufficiently connected to the UK and therefore should be subject to the new offence in relation to overseas tax. Further guidance and examples of different scenarios are in Section 3.

“Dual Criminality”

The legislation also requires that there is ‘dual criminality’ in order to prosecute a foreign tax evasion facilitation offence. There are two stages of dual criminality:

- Firstly, the overseas jurisdiction must have an equivalent tax evasion offence at the taxpayer level and it must be the case that the actions carried out by the taxpayer would constitute a crime if they took place in the UK (an offence of being knowingly concerned in or taking steps with a view to the fraudulent evasion of the tax).

  Therefore, the corporate offence cannot be committed where the acts of the associated person would not be criminal if committed in the UK, regardless of what the foreign criminal law may be.

- Secondly, the overseas jurisdiction must have an equivalent offence covering the associated person’s criminal act of facilitation, and it must be the case that the actions of the associated person would constitute a crime had they took place in the UK.

  Even where the foreign criminal law renders inadvertent or negligent facilitation of tax evasion criminal, the corporate offence will not be committed because the requirement for dual criminality will not be met - UK law renders only deliberate and dishonest acts of facilitation criminal.

Therefore, any conduct that contravenes the criminal law of another country relating to tax evasion may give rise to the foreign tax evasion offence where:

- **Stage A** - under UK law the actions of taxpayer (tax evasion) and associated person (facilitation) would be an offence

AND

- **Stage B** - the overseas jurisdiction has equivalent offences at both the taxpayer and facilitator level

Therefore the foreign tax offence cannot be committed by act that would be lawful in relation to a UK tax. Due to the dual criminality requirement, it is only necessary to have an understanding of the foreign criminal law when doing something that would be illegal if done in the UK. If the actions of the associated person would be lawful in the UK then the “dual-criminality” requirement will not be fulfilled and the new foreign tax offence will not be committed regardless of what the foreign law may be.

The legislation also requires that before proceedings for the foreign offence are issued in England, Wales or Northern Ireland the personal consent of the Director of Public Prosecutions or the Director of the Serious Fraud Office must be gained[1]. Such consent would only be forthcoming where, having weighed up all factors, the prosecution was in the public interest.

It is highly unlikely that a prosecution would be taken forward where a foreign tax was in some way incompatible with the UK’s legal values, such as respect for human rights. It would also be very unlikely to be in the public interest to bring a prosecution where a foreign tax was discriminatory and applied on the basis of race, religion or gender.

Whilst the preference will normally be for the jurisdiction suffering the tax loss to take the appropriate criminal or civil response, if this is not possible (for example due to lack of resources, corruption, or any other reason) the UK Government believes that it should be open to the UK to hold the relevant body to account, should it be in the public interest to do so.

1.4 Initial Implementation Period

The prevention procedures that are considered *reasonable* will change as time passes. What is reasonable on the day that the new offences come into force will not be the same as what is reasonable when the offence has been in effect for a number of years. The Government accepts that some procedures (such as training programmes and new IT systems) will take time to roll out, especially for large multi-national organisations. HMRC will therefore take into consideration the prevention

[1] In relation to Scotland, the decision to prosecute is always taken by the Crown Office and Procurator Fiscal Service and so personal consent is not required in the legislation on the corporate offence. As a public body the Crown Office and Procurator Fiscal Service are bound by the Human Rights Act.

procedures that were in place and planned at the time that the facilitation of tax evasion was committed.

At the same time the Government expects there to be rapid implementation, focusing on the major risks and priorities, with a clear timeframe and implementation plan on entry into force. In addition, HMRC expects reasonable procedures to be kept under regular review and to evolve as a relevant body discovers more about the risks that it faces and lessons are learnt.

1.5 Investigations, Penalties and Sanctions

The UK tax offence will be investigated by HMRC, with prosecutions brought by the Crown Prosecution Service (CPS), whilst the foreign tax offence will be investigated by the Serious Fraud Office (SFO) or National Crime Agency (NCA) and prosecutions will be brought by either the SFO or CPS.

The penalties for this offence will include:

- unlimited financial penalties
- ancillary orders such as confiscation orders or serious crime prevention orders

The mere fact of criminal conviction will also have consequences for a relevant body: it may require disclosure to professional regulators both in the UK and overseas and prevent the body being awarded public contracts.

In order to encourage relevant bodies to disclose wrongdoing, timely self-reporting will be viewed as an indicator that a relevant body has reasonable procedures in place.

A Deferred Prosecution Agreement (DPA) is an agreement reached between a prosecutor and an organisation which could be prosecuted, under the supervision of a judge. As DPAs can be used for fraud, bribery and other economic crimes, they can also be used for this offence.

The agreement allows a prosecution to be suspended for a defined period provided the organisation meets certain specified conditions. The key features of DPAs are:

- They enable a corporate body to make full reparation for criminal behaviour without the collateral damage of a conviction (for example sanctions or reputational damage that could put the company out of business and destroy the jobs and investments of innocent people)
- They are concluded under the supervision of a judge, who must be convinced that the DPA is ‘in the interests of justice’ and that the terms are ‘fair, reasonable and proportionate’
- They avoid lengthy and costly trials
- They are transparent, public events.

DPAs were introduced in February 2014, under the provisions of Schedule 17 of the Crime and Courts Act 2013[2]. The decision as to when a DPA should be offered is for the Crown Prosecution Service or the Serious Fraud Office. A DPA Code of Practice for Prosecutors[3] was published jointly by the SFO and CPS in February 2014.

[2] Available at: www.legislation.gov.uk/ukpga/2013/22/schedule/17/enacted
[3] Available at: www.cps.gov.uk/publications/directors_guidance/dpa_cop.pdf

2. The 6 Guiding Principles

The Government considers that prevention procedures put in place by relevant bodies to prevent tax evasion from being committed on their behalf should be informed by the following six principles.

- **Risk assessment**
- **Proportionality of risk-based prevention procedures**
- **Top level commitment**
- **Due diligence**
- **Communication (including training)**
- **Monitoring and review**

Commentary and guidance on what procedures the application of the principles may produce are set out below.

These principles are not prescriptive, they are intended to be flexible and outcome focussed, allowing for the huge variety of circumstances that relevant bodies find themselves in. As set out in more detail below, procedures to prevent facilitation of tax evasion should be proportionate to risk.

Principle 1 - Risk assessment

The relevant body assesses the nature and extent of its exposure to the risk of those who act for or on its behalf engaging in activity during the course of business to criminally facilitate tax evasion. c

Commentary

Those relevant bodies most affected by the new offence, for example those in the financial services, legal and accounting sectors, may already undertake a range of risk assessments relating to their business activities. The purpose of this principle is to promote the inclusion of tax evasion risk within the relevant body's wider financial crime risk assessment.

Relevant bodies may wish to consider The Financial Conduct Authority's (FCA) guide for firms on preventing Financial Crime[4] , the Law Society's Anti Money Laundering Guidance, particularly Chapter 2 which considers a risk based approach[5], as well as the Joint Money Steering Group (JMLSG) guidance[6].

Relevant bodies that operate in a regulated sector should also consider any guidance published by their regulator. This would include guidance issued by HMRC as part of its Anti-Money Laundering Supervision[7] to Money Services Businesses[8] and Estate Agency Businesses[9].

Ultimately, relevant bodies need to "sit at the desk" of their employees, agents and those who provide services for them or on their behalf and ask whether they have a motive, the opportunity and the means to criminally facilitate tax evasion offences, and if so how this risk might be managed.

Procedures

Risk assessment procedures that allow a relevant body to accurately identify and prioritise the risks it faces will, whatever its size, activities, customers or markets, usually reflect a few common themes. These are:

- Oversight of the risk assessment by senior management
- Appropriate allocation of resources to the detection and monitoring of risk – this will reflect the size and nature of the relevant body
- Identification of the internal and external information sources that will enable the risk to be assessed and reviewed, as well as any gaps in the information available to the relevant body and how these gaps might be filled

[4] https://www.handbook.fca.org.uk/handbook/document/FC1_FCA_20150427.pdf
[5] http://www.lawsociety.org.uk/support-services/advice/practice-notes/aml/risk-based-approach/.
[6] http://www.jmlsg.org.uk/industry-guidance/article/jmlsg-guidance-current
[7] https://www.gov.uk/topic/business-tax/money-laundering-regulations
[8] https://www.gov.uk/government/publications/anti-money-laundering-guidance-for-money-service-businesses
[9] https://www.gov.uk/guidance/registration-guide-for-estate-agency-businesses

- Due diligence enquiries (see Principle 4)
- Accurate and appropriate documentation of the risk assessment and a clear articulation of tax evasion facilitation risks where this is considered as part of the relevant body's wider risk assessment
- Risk assessments are periodically reviewed and updated in line of changing circumstances
- Organisations should have in place procedures to identify emerging risks and feed these into the organisation's risking
- Internal challenge to risk assessments.

The nature of the risks of facilitating tax evasion faced by a relevant body will evolve as the relevant body's business and customer base evolves. For example, a relevant body may consider that its risk has increased, and thus requires enhanced procedures, where it begins to provide services in jurisdictions not reporting taxpayer information under the Common Reporting Standard[10] or offers a new product which carries a known risk of being misused by those seeking to evade tax.

<u>Commonly encountered risks</u>

An assessment of external and internal risks is intended to help inform how these risks can be mitigated by the relevant body's procedures and the level of due diligence a relevant body may deem it reasonable to apply in relation to a given situation.

Stakeholders may wish to consider the commonly encountered risks based on the Bribery Act guidance[11], which are considered from a tax fraud perspective. <u>Country risk</u>: this is evidenced by perceived high levels of secrecy or use as a tax shelter. Such countries are also unlikely to subscribe to the Common Reporting Standard and be given a low tax transparency score by the OECD. (Tax transparency ratings and lists of high risk tax jurisdiction published by organisations like the OECD[12] may also be relevant for tax purposes). <u>Sectoral risk</u>: some sectors pose a higher risk of facilitating tax evasion than others, such as financial services, tax advisory and legal sectors. <u>Transaction risk</u>: certain types of transaction give rise to higher risks, for example, complex tax planning structures involving high levels of secrecy, overly complex supply chains, or transactions involving politically exposed persons.

[10] Under the standard, jurisdictions obtain financial information from their financial institutions and automatically exchange that information with other jurisdictions on an annual basis. For more information please see: https://www.oecd.org/ctp/exchange-of-tax-information/automatic-exchange-financial-account-information-common-reporting-standard.pdf
[11] www.gov.uk/government/publications/bribery-act-2010-guidance
[12] http://www.oecd.org/tax/transparency/

Business opportunity risk: such risks might arise in high value projects or with projects involving many parties, jurisdictions or intermediaries.

Business partnership risk: certain relationships may involve higher risk, for example, the use of intermediaries in transactions, where those intermediaries are based in jurisdictions operating lower levels of transparency and disclosure. Entering into a business partnership with organisations that have either has no fraud prevention procedures, or has known deficiencies in their fraud procedures may involve higher risk. .

In addition, the following risks may also be considered for tax fraud:

Product risk: certain products and services may have a higher risk of misuse by either clients of associated persons.

Customer risk: the identification that a business unit has particular risks related to customers or products is highly likely to indicate that there is a greater risk of the criminal facilitation of tax evasion by an associated person.

In addition, stakeholders may also want to consider the JMLSG guidance on high and low risk factors, although these will need to be considered specifically from a tax fraud perspective:

JMLSG Guidance – high risk factors (4.34-4.36)

Customer risk factors

- The business relationship is conducted in unusual circumstances
- Non-resident customers
- Legal persons or arrangements that are personal asset holding vehicles
- Companies that have nominee shareholders or shares in bearer form
- Business that are cash intensive
- The ownership structure of the company appears unusual or excessively complex

Country or geographic risk factors

- Countries identified by credible sources as not having adequate Anti-Money Laundering and Counter-Terrorism Financing (AML/CTF) approaches
- Countries subject to sanctions, embargoes, or similar measures issued by, for example, the UN
- Countries identified by credible sources as providing support for terrorist activities, or that have designated terrorist organisations operating within their country

Product, service, transaction or delivery channel risk factors

- Private banking
- Anonymous transactions (which may include cash)
- Non face-to-face business relationships or transactions
- Payment received from unknown or un-associated third parties

Firms should examine, as far as reasonably possible, the background and purpose of all complex, unusual large transactions, and all unusual patterns of transactions which have no apparent economic or lawful purpose.

JMLSG Guidance – low risk factors (4.37-4.41)
Customer risk factors

- Other regulated firms and other bodies, where they are subject to requirements to combat money laundering and terrorist financing consistent with the Financial Action Task Force (FATF)[13] Recommendations, have effectively implemented these requirements, and are effectively supervised or monitored to ensure compliance with those requirements
- Public companies listed on a stock exchange and subject to disclosure requirements which impose requirements to ensure adequate transparency of beneficial ownership
- Public administrations or enterprises

Country or geographic risk factors

- Countries identified by credible sources as having effective AML/CTF systems
- Countries identified by credible sources as having a low level of corruption or criminal activity

Product, service, transaction or delivery channel risk factors

- Life assurance policies where the premium is low
- Insurance policies for pension schemes if there is no early surrender option and the policy cannot be used as collateral
- A pension, superannuation or similar scheme that provides retirement benefits to employees, where contributions are made by way of deduction from wages, and the scheme rules do not permit the assignment of a member's interest under the scheme
- Financial products or services that provide appropriately defined and limited services to certain types of customers, so as to increase access for financial inclusion purposes

[13] http://www.fatf-gafi.org/

A risk assessment should also consider the extent to which internal structures or procedures may themselves add to the level of risk. Commonly encountered internal factors may include:

- Deficiencies in employee training, skills and knowledge
- A bonus culture that rewards excessive risk taking
- Lack of clarity on the organisation's policies on, and procedures for, the provision of high risk services and products
- Deficiencies in the organisation's submission of Suspicious Activity Reports (SARs)
- Lack of clear financial controls or whistle-blowing procedures
- Lack of clear messaging from top-level management on refusing to engage in tax fraud.

Principle 2 - Proportionality of risk-based prevention procedures

Reasonable procedures will be proportionate to the risk a relevant body faces of persons associated with it committing tax evasion facilitation offences. This will depend on the nature, scale and complexity of the relevant body's activities. We recognise that the reasonableness of prevention procedures should take account of the level of control and supervision the organisation is able to exercise over a particular person acting on its behalf, and the proximity of the person to the relevant body. The new offences do not require relevant bodies to undertake excessively burdensome procedures in order to eradicate all risk, but they do demand more than mere lip-service to preventing the criminal facilitation of tax evasion.

<u>Commentary</u>

The term reasonable 'prevention procedures' within this guidance is used to mean both:

- formal policies adopted by a relevant body to prevent criminal facilitation of tax evasion by those acting on its behalf, and
- practical steps taken to implement these policies, enforcement of compliance with the policies, and the monitoring of the policies' effectiveness.

To be "reasonable", prevention procedures should be proportionate to the risks that the organisation faces. An initial assessment of the risks that a relevant body's associated persons may commit tax evasion facilitation offences is therefore a necessary first step.

The prevention procedures should outline the relevant body's position on involvement in the criminal facilitation of tax evasion, including the provision of services which pose a high risk of being misused to commit a tax crime. The relevant body should also have a plan of how it will implement and review measures to ensure that persons associated with it are not criminally facilitating tax evasion.

Burdensome procedures designed to perfectly address every conceivable risk, no matter how remote, are **<u>not</u>** required. Procedures need only be reasonable given the risks posed in the circumstances.

A number of factors (see table below) will be relevant when assessing the risk posed to a relevant body by the services it provides and the manner in which it provides them, including the size of the relevant body, the nature and complexity of its business and the jurisdictions in which it operates.

When considering the proportionality of reasonable prevention procedures, some suggested risk factors to consider may include the following: • **Opportunity – could someone facilitate tax evasion?**   - Do any associated persons have the opportunity to facilitate client tax evasion?

- Is their work subject to monitoring or scrutiny, for example a second pair of eyes?
- How likely is detection of any facilitation?

- **Motive – why could it happen?**
  - Does the reward and recognition system and corporate culture (including sanctions and penalties) incentivise or dissuade potential criminal facilitation of tax evasion, or whistle-blowing when tax evasion is uncovered?
  - What are the consequences of wrong-doing?

- **Means – how could it be done?**
  - What means of criminally facilitating tax fraud do your associated persons have?
  - Are there particular products, services or systems that could be open to abuse and used to criminally facilitate tax evasion?
  - Do those in high risk roles receive regular fraud training and how vigorously is compliance with training evaluated or monitored?

Some organisations may face significant risks, and will need more extensive procedures than their counterparts facing limited risks, for example those providing private wealth management services. However, in general small organisations are unlikely to need procedures that are as extensive as those of a large multi-national organisation.

A very small lower risk business, for example, may be able to rely on oral briefings to communicate its policies while a large business may need to rely on more extensive written communications. Larger organisations may also exercise less day-to-day oversight over those providing services on its behalf, and may therefore need to put in place alternative oversight arrangements.

Procedures to prevent the criminal facilitation of tax evasion by a person associated with the relevant body may be independent, standalone procedures; but so long as they properly address the risk of facilitating tax evasion they may form part of a wider package of procedures, for example internal Anti-Money Laundering, Bribery Act or fraud prevention procedures.

What is considered a proportionate timescale for implementing, reviewing and amending procedures to prevent criminal facilitation of tax evasion will depend on the nature, scale and complexity of the relevant body’s activities and the resources available to the relevant body. It is expected that a relevant body’s procedures will not be static, but will evolve and develop in line with the relevant body’s activities and identified risks.

Procedures

The precise prevention procedures that will be reasonable will differ for each organisation, but they are likely to include common elements. For example:

- A clearly articulated risk assessment on which the procedures are based
- A top level commitment to preventing the involvement of those acting on the relevant body's behalf in the criminal facilitation of tax evasion
- An articulation of the approach to mitigating risks of involvement in the criminal facilitation of tax evasion, such as those arising from the nature of its services and areas of operation
- An overview of the strategy and timeframe to implement prevention policies. It is expected that what is reasonable will evolve over time. For example, IT systems which form part of a relevant body's due diligence procedures may take time to develop and subsequently review and amend
- Monitoring and enforcing compliance with procedures
- Reviewing procedures for effectiveness and refining them
- A clear pathway for reporting wrongdoing by persons associated with the relevant body
- Protection for whistle-blowers (with no retribution)
- A commitment to compliance over profit or bonuses.

The procedures put in place to implement a relevant body's preventative policies should be designed to mitigate identified risks as well as address the risk of criminal conduct on the part of those providing services on behalf of the relevant body.

An organisation does not have to publish policies on an external website, but may wish to summarise key principles within corporate materials. The following list is intended as guidance for the topics that preventative procedures may embrace depending on the nature of the particular risks faced:

- The involvement of the relevant body's top level management
- The procedures and methods used to assess the risk to the relevant body posed by its activities
- Due diligence conducted in relation to persons associated with the relevant body
- The contractual terms and conditions of persons associated with the relevant body
- Disciplinary and enforcement action taken against those persons breaching the relevant body's policies
- How the relevant body will communicate its policies to all persons associated with it

- Policies around reporting criminal actions by persons associated with the relevant body
- The process and timeline by which the organisation plans to implement its preventative procedures and training in their application
- The monitoring, review and evaluation of the relevant body’s preventative policy and procedures
- Disclosure of client information in line with existing legal requirements, for example reporting under the Common Reporting Standard and the Proceeds of Crime Act.

No Procedures

It is also worth noting that in some limited circumstances it may be unreasonable to expect a relevant body to have prevention procedures in place. For example, where a relevant body has fully assessed all the risks and they are considered to be extremely low and the costs of implementing any prevention procedures are disproportionate or cost-prohibitive in relation to the negligible risks faced. However, it will rarely be reasonable to have not even conducted a risk assessment.

It should be noted that a relevant body should keep the risks under review and be able to articulate the outcome of the risk assessment and the active decision not to implement any procedures, should they be challenged at a later stage.

Principles 3 - Top level commitment

The top-level management of a relevant body should be committed to preventing persons associated with it from engaging in criminal facilitation of tax evasion. They should foster a culture within the relevant body in which activity intended to facilitate tax evasion is never acceptable.

<u>Commentary</u>

Those at the most senior levels of the organisation are best placed to foster a culture where actions intended to facilitate tax evasion are considered unacceptable. This principle is intended to encourage the involvement of senior management in the creation and implementation of preventative procedures. It is also intended to encourage senior management involvement in the decision making process in relation to the assessment of risk, where this is appropriate.

<u>Procedures</u>

The level and nature of the involvement of senior management of a relevant body will vary depending on the size and structure of the relevant body, but is likely to include:

- communication and endorsement of the relevant body's stance on preventing the criminal facilitation of tax evasion, and
- involvement in the development and review of preventative procedures.

<u>Communication and endorsement of the relevant body's position on preventing the facilitation of tax evasion</u>

The manner and form in which a relevant body chooses to communicate, both internally and externally, its position on ensuring that persons associated with it do not criminally facilitate the evasion of taxes may vary depending on a number of factors including the size of the relevant body, the nature and complexity of its business and the jurisdictions within which it operates.

Communication may vary depending on the target audience, for example communications aimed at the relevant body's clients may be different from those aimed at employees of the relevant body or those to whom it sub-contracts work.

Effective formal statements to demonstrate the commitment by senior managers within the relevant body may include:

- A commitment to zero tolerance towards the criminal facilitation of tax evasion
- The consequences for persons associated with the relevant body for breaching the relevant body's policy on the facilitation of tax evasion
- A commitment not to recommend the services of others who do not have reasonable prevention procedures in place
- Articulation of the benefits of rejecting the provision of services to enable tax evasion (reputational, customer and business partner confidence)

- Articulation of the relevant body’s main preventative procedures
- Key individuals and/or departments involved in the development and implementation of the organisation’s prevention procedures
- Reference to any membership of collective action against the facilitation of tax evasion, for example, through initiatives undertaken by representative bodies.

<u>Involvement in developing preventative measures</u>

The level and nature of involvement in the creation and implementation of preventative measures will be bespoke to the relevant body involved. It is expected that the level of involvement will be proportionate to the relevant body’s size, management structure and business activities.

In smaller relevant bodies, it may be proportionate for the most senior management to be personally involved in the design and implementation of preventative measures. In a large multinational organisation, personal involvement in the design and implementation of preventative measures may not be proportionate, and senior management may instead take responsibility for preventative measures by providing oversight of work delegated to a committee and the publication with positive endorsement for the preventative measures thereby created.

Regardless of the scale of involvement of senior management, it is likely to reflect the following elements:

- Members of the senior management of the relevant body having designated responsibility for prevention measures
- Endorsement of the relevant body’s prevention policy and associated publications
- Leadership and designated responsibility for awareness raising of the relevant body’s prevention policies
- Engagement with relevant associated persons and external bodies to help articulate the organisation’s policies
- Designated responsibility for certifying the assessment of risk
- Designated responsibility at senior level for disciplinary procedures relating to the breach of the relevant body’s policies
- Senior management’s commitment to whistleblowing processes and rejecting profit by way of facilitating tax evasion.

Principle 4 - Due diligence

The organisation applies due diligence procedures, taking an appropriate and risk based approach, in respect of persons who perform or will perform services on behalf of the organisation, in order to mitigate identified risks.

Commentary

Those organisations in the sectors facing the greatest risks (those providing bespoke financial or tax-related services to clients, for example) are likely already to undertake a wide variety of due diligence procedures, both mandatory and due diligence undertaken in response to risks associated with specific transactions, customers or jurisdictions.

It is envisaged that due diligence procedures for this offence will be capable of identifying the risk of criminal facilitation of tax evasion by associated persons. However, it should be noted that merely applying old procedures tailored to a different type of risk (or clients-focused procedures) will not necessarily be an adequate response to tackle the risk of tax evasion facilitation.

Those with exposure to the greatest risk may choose to clearly articulate their due diligence procedures specifically in relation to the corporate offence. In addition, a single relevant body might have differing procedures for different parts of its business reflecting the varying levels of risk across all of its activities.

A relevant body may, upon conducting a risk assessment, decide that services provided to a certain group of its clients pose a higher risk of being misused to perpetrate a tax fraud. As a result they may apply increased scrutiny over those providing services to those clients, or over those who provide those services, to address the specific risks of tax evasion facilitation identified.

Procedures

The due diligence procedures put in place should be proportionate to the identified risk. For example, it may be that the risk identified in given situations is so remote as to justify there being no procedures in place. Alternatively, an organisation may assess the risks as being substantial in relation to a particular associated person, or service, and so apply considerably greater scrutiny in that circumstance.

Organisations may choose to conduct their due diligence internally, or externally, for example by internal audit teams or external consultants.

We recognise that the reasonableness of prevention procedures should take account of the level of control and supervision the organisation is able to exercise over a particular person acting on its behalf and the relevant body's proximity to that person.

It is expected that the effectiveness of the organisation's procedures will be reviewed and where necessary the procedures will be amended.

Principle 5 - Communication (including training)
The organisation seeks to ensure that its prevention policies and procedures are communicated, embedded and understood throughout the organisation, through internal and external communication, including training. This is proportionate to the risk to which the organisation assesses that it is exposed.

<u>Commentary</u>

A clear articulation of an organisation's policy against engaging in activities to help clients commit tax fraud deters those providing services on behalf of the relevant body from engaging in such activities. Communication should be from all levels within an organisation, i.e. it is not enough for the senior management say that staff should not commit fraud, if middle management then actively ignore this and encourage junior members to circumvent the relevant body's prevention procedures.

It is important that the relevant body ensures awareness and understanding of its policies amongst those who provide services for or on its behalf. The organisation may feel that it is necessary to require its representatives to undertake fraud or potentially tax evasion-specific training, depending on the risks it is exposed to. This would be to ensure that they have the skills needed to identify when they and those around them might be at risk of engaging in an illegal act and what whistle-blowing procedures should be followed if this occurs.

<u>Procedures</u>

The nature of internal and external communication may vary depending on the nature of the risk being addressed, the size, business and operation of the organisation in question.

Internal communications should make clear the relevant body's zero tolerance policy for the facilitation of tax evasion by its representatives and the consequences for anyone found to be complicit in illegal activity. Such communication may focus on high risk areas of operation for the relevant bodies and what is expected of representatives who find themselves being asked to provide a service which they believe will be used to facilitate a tax fraud.

An important aspect of internal communication is an established and confidential means for representatives of the relevant body to raise concerns about the provision of services to facilitate tax fraud. It should be clear to those providing services on behalf of the relevant body whom they should contact within if they have questions or concerns about the services they are providing. Relevant bodies may wish these communications to form part of their existing communications, for example on money laundering prevention, or to be a standalone communication.

External communication of a relevant body's policy on the provision of services to facilitate tax evasion can act as a strong deterrent to those who would seek to use the relevant body's services to further illegal activity. Relevant bodies may consider it proportionate and appropriate to convey these messages to partner organisations, particularly those to whom it is making referral, or from whom clients are referred.

Training

The training should be proportionate to the risk faced. Some relevant bodies may wish to incorporate training into their existing financial crime prevention training, other organisations may wish to introduce bespoke training to address specific tax fraud facilitation risks.

Consideration should be given to the specific training needs of those in the highest risk posts, and to training required to ensure that the relevant body's representatives understand the process for referring any concerns. The effectiveness of training should be monitored and evaluated.

Relevant bodies may choose either to train third party associated persons, or encourage them to ensure their own arrangements are in place.

Suggested Training Requirements:

It is not envisaged that all associated persons will require a detailed understanding of tax rules in any one country, but instead training should equip them to understand the scope of this offence and the associated risks, without needing to understand the underlying tax law.

Suggested content for tax evasion and general fraud training could include the following:

- the organisation's policies and procedures, which include provisions of the Act and any other sector regulatory rules and principles
- an explanation of when and how to seek advice and report any concerns or suspicions of tax evasion or wider financial crime, including whistleblowing procedures
- an explanation of the term 'tax evasion' and associated fraud
- an explanation of an employee's duty under the law
- the penalties, relating to the person and corporate entity, for committing an offence under the act
- the social and economic effects of failing to prevent tax evasion.

Principle 6 - Monitoring and review

The organisation monitors and reviews its prevention procedures and makes improvements where necessary.

<u>Commentary</u>

The nature of the risks faced by an organisation will change and evolve over time. This may be as a natural result of external developments, the failure to prevent an incidence of facilitation of tax evasion by an associated person, or as a result of changes in the organisation's activities. The organisation will therefore need to change its procedures in response to the changes in the risks that it faces.

<u>Procedures</u>

There are a range of approaches which a relevant body may wish to take when reviewing its monitoring mechanisms. A relevant body may wish to have its review conducted by an external party, or may choose to conduct its review internally.

Organisations can review their procedures in a number of ways, for example:

- By seeking internal feedback from staff members and looking to other financial crime prevention procedures
- Through formalised periodic review with documented findings
- Through working with other organisations, such as representative bodies or other organisations facing similar risks.

This is not an exhaustive list and it is expected that organisations will choose the approach most suited to their needs. Relevant bodies may change their review process in light of developments, for example a relevant body may need to take a more formalised and detailed approach to reviewing its procedures, following criminal activity by persons associated with it.

3. Common Terminology and Additional Case Studies

3.1 Relevant Body

Only a “relevant body” can commit the new offences. This means that only incorporated bodies (typically companies) and partnerships can commit the new offences. The new offences cannot be committed by natural (as opposed to legal) persons. The new offence can be committed by companies and partnerships, not men and women.

The UK tax offence can be committed by any relevant body regardless of whether it is established under UK law or the law of a foreign jurisdiction. This reflects the fact that under the current law any person can be guilty of a UK tax evasion offence contrary to UK law, regardless of their location, if they assist somebody to evade UK tax with the requisite guilty state of mind.

The fact that an offence is committed against the UK is sufficient to give the criminal courts of the UK jurisdiction over the offence. Thus companies incorporated under the law of France or partnerships formed under German law would be capable of committing the offence in section 2 in relation to taxes owed to the UK.

However, the foreign tax offence can only be committed:

- by a relevant body incorporated under UK law, for example a limited company incorporated under UK law;
- by a relevant body carrying on a business or other undertaking from within the UK, for example a company incorporated under the law of France but operating from an office in Manchester; or
- 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, for example a company incorporated under German law whose employee helps another person to commit a foreign tax evasion offence whilst in London.

These bodies, described above, are considered to be sufficiently connected to the UK and therefore should be subject to the new foreign tax offence.

3.2 Associated Person

The associated person must commit the tax evasion facilitation offence in the capacity of an associated person. Where an employee criminally facilitates his or her partner’s tax evasion in the course of their private life and as a ‘frolic of their own’, they commit a tax evasion facilitation offence but <u>NOT</u> in the capacity of person associated with their employer. Therefore in this situation the employer does not commit the new offence.

A third-party (e.g. an introducer or agent) may have relationships with multiple organisations and perform tasks for several relevant bodies, or in a personal capacity, at one time. Such a person might be associated with various different relevant bodies as he does various tasks. It should therefore be noted that the new offence is only committed where a tax evasion facilitation offence is committed by a person acting in the capacity of a person associated to the relevant body, that is undertaken ‘for or on behalf of’ the relevant body. Any activity of the associated person beyond that relationship, for example for other relevant bodies or carried out in their private capacity would not lead to liability for the relevant body.

This broad scope means that contractors could be ‘associated’ persons to the extent that they are performing services for or on behalf of a commercial organisation. The decision will always necessitate looking past the contractual form and considering all the relevant factors including contractual proximity, control, and benefit.

The Government recognises that the relevant body will be able to operate greater levels of control and supervision over some categories of representatives (for example those directly employed) than over others (for example those ordinarily employed by another entity but providing services on a temporary basis). We recognise that the reasonableness of procedures should take account of the level of control, proximity and supervision the organisation is able to exercise over a particular person acting on its behalf.

Where a supply chain involves several entities or a project is to be performed by a prime contractor with a series of subcontractors (and even sub-sub-contractors), an organisation is likely only to exercise control over its relationship with its contractual counterparty. Indeed, the organisation may only know the identity of its contractual counterparty.

The principal way in which commercial organisations may decide to approach tax fraud risks which arise as a result of a supply chain is by employing the types of anti-tax evasion facilitation procedures referred to elsewhere in this guidance (e.g. risk-based due diligence or the use of contract terms and conditions) in the relationship with their contractual counterparty, and by requesting that counterparty to adopt a similar approach with the next party in the chain.

3.3 Branches and Subsidiaries

The law does not view branches as separate legal entities (in the way that subsidiaries are): all the branches of a relevant body comprise a single legal entity. This means that any relevant body with a number of branches, including one in the UK, would be subject to these offences. For the UK branch to say “But a different branch did this” is akin to a person’s left arm protesting that an assault was committed by the right arm.

Subsidiaries are not automatically presumed to be associated persons of UK relevant bodies, and an examination of the relevant circumstances will be needed to determine whether they are an associated person or not, in the same way as is required for entirely unrelated legal entities or sister companies that that share a parent company. Moreover it is the relevant body, not the UK branch that would commit the offence.

Examples

Branches and the overseas fraud offence
Gladstone Bank is a bank incorporated and headquartered in Switzerland. The bank has branches in a number of jurisdictions, including the UK and Germany. Whilst the bank has several branches across the world, the branches are not separate legal entities (they are branches not subsidiaries): the bank is a single legal entity, a company incorporated under Swiss law. All the bank's branches comprise a single legal person.

UK Branch

The UK Branch consists of a small number of employees whose functions are restricted to:

- attracting and on-boarding clients for Gladstone Bank;
- providing minor administrative services; and
- acting as a first point of contact for UK based customers.

The UK branch attracts and on-boards a number of clients for Gladstone Bank resident in London, including Freya who has UK tax liabilities and Larry who has German tax liabilities. The employees of the UK branch attract the clients in good faith believing that Gladstone Bank is providing routine financial services to its clients. Once the clients have been attracted all financial services are provided by either the bank's headquarters in Switzerland or employees in the German Branch.

German Branch
Employees of the German Branch, deliberately and dishonestly help Larry to evade his German tax liabilities. The employees:

- ➢ advise Larry on structures that allow him to hide his assets and income from the German tax authorities;
- ➢ provide false certification to hide the true owners of accounts; and
- ➢ deliberately fail to comply with the applicable Anti Money Laundering Regulations.

Swiss Head Office
Employees of the Swiss headquarters deliberately and dishonestly help Freya to evade her UK tax liabilities. The employees:

- ➢ advise Freya on structures to help her hide overseas income from the UK tax authorities;
- ➢ deliberately set up a bank account in Switzerland knowing it is going to be used to hide the overseas income from the UK tax authorities

A. Liability for the UK fraud offence

Stage 1: Taxpayers
Freya has deliberately and dishonestly failed to declare her taxable income and assets to HMRC with the intention of not paying the tax that she legally owes. She has committed the offence of being knowingly concerned in the fraudulent evasion of income tax contrary to section 106A of the Taxes Management Act 1970.

Stage 2: Associated persons of Gladstone Bank and criminal facilitation
Employees of Gladstone's Swiss Head Office have deliberately and dishonestly provided services to Freya to help her to hide her taxable income and assets in order to help her evade her UK tax liability. They are also guilty of being knowingly concerned in the fraudulent evasion of income tax, an offence contrary to section 106A of the Taxes Management Act 1970.

The associated person was providing services (advice to clients) for or on behalf of the bank when they committed the tax evasion facilitation offence.

Stage 3: Liability for Gladstone Bank for failing to prevent the criminal facilitation of tax evasion
Gladstone Bank is not guilty of the section 106A Taxes Management offence. It is not possible to attribute the requisite guilty mind to the bank itself in respect of the criminal act committed, because none of the people considered to be the bank's directing mind and will (typically the Board of Directors) were involved in the offence. However, the bank is liable for having failed to prevent its associated persons operating in its Swiss Head Office from criminally facilitating Freya's UK tax liability (the new UK tax offence) unless it is able to establish the reasonable prevention procedures defence.

Gladstone Bank cannot mount a reasonable prevention procedures defence, its procedures were not reasonable because it had only implemented procedures for a small number of UK-based staff. It is no defence to claim that it should not be expected to put in place prevention procedures designed to prevent its associated persons from being complicit in fraud resulting in a tax loss outside of Switzerland.

B. Liability for the Overseas Fraud Offence

Stage 1: taxpayers
Larry has deliberately and dishonestly failed to declare his taxable income and assets to the German revenue authorities with the intention of not paying the tax that he legally owes. There is 'dual criminality' as there are equivalent offences at the taxpayer level in the UK and Germany.

Stage 2: Associated persons of Gladstone Bank and criminal facilitation
Employees of Gladstone's German branch have deliberately and dishonestly provided services to Larry to help him hide his taxable income and assets in order to help him evade his German tax liability.

The associated person was providing services (advice to clients) for or on behalf of the bank. There is ‘dual criminality’ at the facilitator level as there equivalent offences in both the UK and Germany.

Stage 3: As Gladstone Bank has a UK branch and the bank is a single legal entity it is within scope of the new foreign tax evasion facilitation offence. Gladstone Bank has also failed to prevent its associated person, i.e. employees of its German Branch, from criminally facilitating the evasion of German tax by Larry.

Gladstone Bank is unable to put forward a defence of having put in place reasonable procedures to prevent the criminal facilitation of tax evasion because its procedures were not reasonable as it decided to only introduce prevention procedures for staff dealing with UK taxpayers. Claiming that it does not believe that it should have to exercise due diligence over employees of its branches in other countries provides no defence to this.

Further examples of branch structures that would be in scope of the overseas offence as there is sufficient UK nexus:

- Any bank incorporated under UK law with overseas branches

- Any bank incorporated under the law of another country that conducts part of its business from the UK, for example a French bank with a London branch

- Any bank incorporated under the law of another country that conducts none of its business from the UK but where its associated person does the facilitating criminal act from within the UK, for example any bank incorporated under the law of another country that sends someone to the UK to perform a criminal act.

3.4 Joint Ventures

Joint ventures sometimes operate through a separate legal entity, but at other times through contractual arrangements. In the case of a joint venture operating through a separate legal entity, where a tax fraud has been facilitated by the entity this may lead to liability for a participant in the joint venture if the entity is performing services on behalf of that participant.

However, the existence of a joint venture entity will not of itself mean that it is automatically ‘associated’ with any of the participants. The facilitation of tax evasion by an employee or associated person of the joint venture entity will therefore not always trigger liability for participants in the joint venture simply by virtue of them being connected through their investment in or ownership of the joint venture. The question will always be whether the entity is acting for or on behalf of the participant.

The degree of control that a participant has over the arrangement (for example where the joint venture is conducted through a contractual arrangement) is likely to be one of the ‘relevant circumstances’ that would be taken into account in deciding whether a person who facilitated tax evasion in the conduct of the joint venture business was ‘performing services for or on behalf of’ a participant in that arrangement.

The question is always whether the person performing the facilitating act is providing a service for or on behalf of the relevant body. A corporate entity set up to deliver a joint venture may perform services for or on behalf of the participants in that venture, and when it does, it will be an associated person

3.5 Referrals

Where a relevant body makes an introduction in good faith, and believes the external service provider is unlikely to be involved in facilitating tax evasion, and also steps away from the transaction entirely, the company which makes the referral is unlikely to fall within scope of the new offence. This is because in this instance the company to which the referral is made does not provide services for or on behalf of the referrer, it a ‘vanilla’ referral, not a case of sub-contracting.

However, this would not be the case where the introducing party is aware that either the motive of the client involved is to evade tax or that the external provider to whom a client has been introduced is likely to be involved in facilitating tax evasion. This dishonest referral would itself constitute a deliberate action to facilitate tax evasion at the taxpayer level.

<u>Examples</u>

1) Straight-forward Referral Out

A UK Bank ‘B’ gets occasional client requests for services in South Africa, where it has neither a branch, nor a subsidiary. It has a relationship with a firm ‘F’ in that country to which it refers business. This arrangement is a ‘pure’ or ‘vanilla’ referral. Once the referral has been made, the client becomes a client of F, and bank B takes no further part in any provision of services in the country in question (although its own separate relationship with the client continues to exist independently). Firm F criminally facilitates the client’s tax evasion. It is not a relationship in which services are provided by F for or on behalf of bank B.

Question: Would firm F be an associated person of bank B?

Answer: No. Firm F is not an associated person, as it was not providing services on behalf of bank B; once the client was introduced, bank B stepped back.

2) Inward Referral

A UK bank uses a consultancy firm in India that introduces clients to the bank. The consultancy firm was previously exclusive to the UK bank but now also introduces

Indian clients to the UK bank's sister bank in India. The consultancy firm is not used by the UK bank to provide any tax advice to clients of either bank.

The consultancy firm later offers additional services (beyond the contracted services with the banks) and criminally facilitates tax evasion for clients of both the UK and Indian-based banks, including by falsifying documentation. Neither bank was aware of the additional services and illegal activity.

Question: Would the activity of the consultancy firm attract liability for the bank?

Answer: No. The Indian consultancy firm was offering tax services outside of its relationship with the bank. Although the consultancy firm was providing some services on behalf of the bank (introducing clients) the criminal facilitation of tax evasion was outside the contracted service provision and was therefore not provided for or on behalf of the bank.

3) Holistic Service Provision / Sub-contracting

A UK financial services firm instructs a foreign tax adviser on behalf of a client to give advice on tax and estate planning proposals in a foreign jurisdiction. The UK firm controls the ongoing relationship with the client and the advice sought, passing the advice on to the client. The UK firm takes responsibility for the foreign lawyer's fees and includes those fees as a disbursement in the annual bill to their client.

Question: Would the advice of the foreign tax advisor attract liability for the UK firm?

Answer: Yes. The foreign tax advisor is providing a service for or on behalf of the UK firm; it is doing work that the UK firm sub-contracted to the foreign tax advisor having entered into a contract with its client. The foreign tax advisor is therefore an 'associated person' under these circumstances.

3.6) Foreign Tax Evasion Facilitation Offence

- **Dual Criminality**

Below is an example of the dual criminality test to illustrate the types of situation that are in scope of the new offence.

<u>Dual criminality example</u>

Gladstone Bank is a bank incorporated and headquartered in Switzerland. The bank has branches in a number of jurisdictions, including the UK and Germany. Whilst the bank has several branches across the world, the branches are not separate legal entities (they are branches not subsidiaries): the bank is a single legal entity, a company incorporated under Swiss law. All the bank's branches comprise a single legal person.

The German taxpayer, Larry, has committed an offence contrary to section 370 of the German Fiscal Code. He is assisted by an employee of Gladstone Bank who is also based in a branch in Germany.

> <u>Section 370 German Fiscal Code</u>
> Any person who:
> - Furnishes the revenue authorities or other authorities with incorrect or incomplete particulars concerning matters of substantial significance for taxation.
> - Fails to inform the revenue authorities of facts of substantial significance for taxation when obliged to do so

There is therefore dual criminality at the taxpayer level as there is an equivalent offence in 106A of the Taxes Management Act 1970 (fraudulent evasion of income tax).

The facilitating acts of the staff of the bank would be an offence if done in the UK and Germany also has the equivalent offence, criminal facilitation of tax evasion, by virtue of sections 26-27 of the German Fiscal Code.

> <u>Section 26 Abetting</u>
> Any person who intentionally induces another to intentionally commit an unlawful act (abettor) shall be liable to be sentenced as if he were a principal.
>
> <u>Section 27 Aiding</u>
> (1) Any person who intentionally assists another in the intentional commission of an unlawful act shall be convicted and sentenced as an aider.

There is therefore dual criminality at the taxpayer (stage 1) and associated person (stage 2) levels.

Stage 3: Liability for Gladstone Bank for failing to prevent the criminal facilitation of tax evasion

Gladstone bank is within scope of the foreign tax evasion offence as it has an establishment in the UK. The fact that the company is incorporated under Swiss law, and that the facilitating acts of its associated person took place outside the UK, does not take it outside the scope of the new offence. It is a legal person with a business presence in the UK and bound by the new foreign tax offence.

Gladstone Bank will be guilty of the foreign tax evasion offence unless it can establish the defence of having reasonable prevention procedures.

3.7 Further illustrative case studies

Example 1) Acting as a broker/conduit – arranging access to others in the "supply" chain and providing introductions.

Sarah was introduced to Malus GmbH, a Swiss adviser, to create a tax efficient structure for potential future investment into UK property. Malus was an approved intermediary of a UK high street bank (with the referral made in good faith after they carried out appropriate due diligence on Malus), and Sarah planned to put her post-tax employment earnings into this structure.

Sarah had a relative, Maisie, who was neither resident nor domiciled in the UK. Malus advised Sarah that she should set up a Swiss trust using Maisie as the settlor. This was done, although Maisie was never asked to sign anything and was not aware that a trust was being set up with her named as the settlor. Sarah was advised that she retained beneficial ownership of all the assets despite the trust arrangement.

The trust had bank accounts with Lunar Bank in Monaco. Sarah admitted her actions following initial contact with Malus were deliberate.

<u>Under the new offences</u>: There is no evidence that the UK high-street bank knew that Malus would help Sarah to evade UK tax, and the 'vanilla' referral to Malus was made in good faith. Under these circumstances Malus was not acting as an 'associated person' of the UK high-street bank, so the UK High Street Bank is not liable under the new offences.

Malus's staff, however, provided structuring advice which Sarah knew was not legal, as well as professional trustee services to Sarah's trust which they knew was not properly constituted and would be used by Sarah to hide her assets and evade the appropriate level of tax. The staff of Malus are persons associated with it. If Malus had not taken reasonable steps to prevent their staff from facilitating Sarah's tax evasion in the course of their work then Malus would be guilty of the new offence. Its compliance with any applicable published guidance, its contractual terms for its staff, the training it provides, and any steps taken to monitor and ensure compliance would all be relevant to the assessment of whether it had taken reasonable steps.

Lunar Bank's staff have performed acts that facilitated Sarah's tax evasion. However, they did so without being aware of any tax evasion. They may have been negligent and failed to comply with their anti-money laundering obligations, but they lack the requisite guilty state of mind to commit an offence relating to facilitating Sarah's tax evasion. Therefore, there is no tax evasion facilitation offence that Lunar Bank has failed to prevent.

Example 2) Providing planning and advice on the jurisdictions, investments and structures which will enable the taxpayer to hide their money.

John ran a UK business. John opened a Channel Islands bank account in which he could hide untaxed business income from HMRC.

John took his untaxed funds on a regular basis to a business contact, Michael, who travels regularly to the Channel Islands. Michael would take the money in a suitcase to the Channel Islands and deposit it in John's bank account.

In 2004, following unsolicited advice from the Channel Island bank, John transferred the bank accounts to a nominee Foundation in Panama to avoid reporting under the EU Savings Directive and retain secrecy over his funds. The Foundation was operated by Channel Island professionals.

<u>Under the new offences:</u> Michael was knowingly helping John to physically move funds offshore for tax evasion purposes. Michael was happy to do this because it fostered continued good business relations with John. Michael is guilty of a tax evasion facilitation offence by virtue of facilitating John's actions but, as he is an individual and not an associated person of a relevant body, no question of his committing the new offence arises.

The Channel Island bank's staff initially opened the account for John knowing that he wanted his activities to remain hidden from HMRC. Many years later the Channel Island bank staff actively advised John on how he could continue to hide his money. This conduct amounts to the criminal facilitation of tax evasion. The Channel Island bank would be guilty of the new offence unless it had taken reasonable steps to prevent its staff facilitating John's tax evasion. Its compliance with any applicable published guidance, its contractual terms for its staff, the training it provides, and any steps taken to monitor and ensure compliance would all be relevant to the assessment of whether it had taken reasonable steps.

The Channel Island bank professionals helped John to maintain a structure which facilitated his evasion activities. These professionals were asked by the bank to assist others in John's position and knew they were assisting people evading UK tax. This conduct amounts to the criminal facilitation of tax evasion. The bank therefore failed to prevent this conduct occurring and would be guilty of the new offence if it could not show that it had taken reasonable steps to prevent its associated persons from facilitating John's tax evasion.

Example 3) Delivery of infrastructure – e.g. setting up companies, trusts and other vehicles which are used to hide beneficial ownership; opening bank accounts; providing legal services and documentation which underpin the structures used in the evasion such as notary services and powers of attorney.

Manjit was the owner and Director of a UK-based interior design business. He generated false invoices and drew cheques with fictitious payee details logged in the company records, in order to divert proceeds offshore and reduce taxable profits in the UK. These cheques were in fact made payable to an extensive network of offshore discretionary trusts and corporate vehicles in Gibraltar, Belize, Seychelles, and the British Virgin Islands ("BVI").

In particular, the trustees invested the funds in a portfolio of bank accounts and investment properties held in the name of "off the shelf" corporate vehicles in the Seychelles and BVI. The properties, acquired with the proceeds of tax evasion, were then rented out commercially with UK taxes paid on the rental income under the non-resident landlord scheme ("NRLS") to give the appearance of a genuine offshore ownership arrangement. The NRLS arrangement had been accepted by HMRC, being the only contemporaneous information that was available at the time.

Following an HMRC investigation, Manjit accepted that these transactions were fraudulent. Manjit admitted he deliberately committed offshore tax evasion.

<u>Under the new offences:</u> The trustees claimed that they believed everything they were doing was "above board" - but they also stated that "the affairs of their clients were none of their business". HMRC's view was that the trustees turned a blind eye to the true beneficial ownership of the structure in order to retain Manjit's business. If the trustees in truth had knowledge of, but decided to ignore, Manjit's tax evasion, their conduct would amount to the criminal facilitation of Manjit's tax evasion and any trust company or partnership for which they worked would be guilty of the new offence if it had not taken reasonable steps to prevent the facilitation of Manjit's tax evasion. Their employer's compliance with any applicable published guidance, its contractual terms for its staff, the training it provides, and any steps taken to monitor and ensure compliance would all be relevant to the assessment of whether it had taken reasonable steps.

Of course, if the trustees were truly unaware of the tax evasion (whether out of negligence or otherwise) their assistance would not amount to a tax evasion facilitation offence (as these cannot be committed negligently) and the new offence would not be in point.

Example 4) Maintenance of infrastructure e.g. providing professional trustee or company director services including nominee services; providing virtual offices, IT structures, legal services and documentation which obscures the true nature of the arrangements such as audit certificates.

Paula was domiciled in Australia, but had been resident in the UK since the 1970s. In 2017, Paula wanted to regularise her affairs and disclosed to HMRC that she had been hiding substantial UK taxable income for a prolonged period. She had been using companies in Bermuda and the Bahamas to shelter both business and private assets and to facilitate the movement of funds through a variety of jurisdictions.

The network of companies had been set up by Paula’s lawyer, a partner in a Guernsey-based legal partnership, in total secrecy, meaning that Paula had never paid UK taxes for more than 30 years of UK residence.

<u>Under the new offences:</u> The lawyer actively assisted Paula in evading UK taxes, knowing that the structures would enable her to evade UK tax. Any company or partnership for which the lawyer was an associated person would be guilty of the new offence if it had not taken reasonable steps to prevent him facilitating Paula’s tax evasion. Its compliance with any applicable published guidance, its contractual terms for its staff, the training it provides, and any steps taken to monitor and ensure compliance would all be relevant to the assessment of whether it had taken reasonable steps.

Example 5) Financial assistance – helping the evader to move their money out of the UK, and/or keep it hidden by providing ongoing banking services and platforms; providing client accounts and escrow services; moving money through financial instruments, currency conversions etc.

Christoph was a wealthy non-domiciled individual who was a long-term UK resident. His job entitled him to significant bonus payments, related to duties performed wholly in the UK, on which he did not want to suffer UK tax. His UK accountant put him in touch with an adviser in Israel. The Israeli adviser set up a number of bank accounts in Singapore in the names of BVI-registered companies, under the control of a discretionary trust. Christoph arranged for his bonus payments to be lodged in the accounts operated in Singapore. As well as evading income tax on his employment income over a number of years, Christoph's settlements also attracted significant Inheritance Tax liabilities.

Under the new offences: The UK accountant understood what Christoph was trying to achieve, and for many years acted as a conduit through which Christoph contacted the Israeli adviser. This amounts to a tax evasion facilitation offence. The company or partnership that the accountant worked for would be guilty of the new offence if it had not taken reasonable steps to prevent him or her facilitating the tax evasion. Its compliance with any applicable published guidance, its contractual terms for its staff, the training it provides, and any steps taken to monitor and ensure compliance would all be relevant to the assessment of whether it had taken reasonable steps.

The Israeli adviser also understood Christoph's aims, and knew that secrecy was key to achieving those aims. He provided advice, and also set up and maintained the structure. This conduct facilitated Christoph's tax evasion. The company or partnership that the adviser worked for would be guilty of the new offence if it had not taken reasonable steps to prevent the adviser facilitating the tax evasion. Its compliance with any applicable published guidance, its contractual terms for its staff, the training it provides, and any steps taken to monitor and ensure compliance would all be relevant to the assessment of whether it had taken reasonable steps.

The Singapore bank's staff were unaware that the structure was being used to evade UK tax. As such they would not have the requisite state of mind to be guilty of facilitating Christoph's tax evasion. Therefore the Singapore bank could not be guilty of failing to prevent its staff from facilitating tax evasion.

4. Suggested reasonable prevention procedures for lower risk SMEs

An SME should first undertake a risk assessment of the products and services it offers, as well as internal systems and client data that might be used to facilitate tax evasion, including by ‘sitting at the desk’ of employees and other associated persons, considering the motive, means and opportunity for facilitating tax evasion.

Consider some of the hallmarks of fraud or fraud ‘red flags’ when undertaking the risk assessment, for example:

- Are there staff who refuse to take leave and do not allow anyone else to review their files, or are overtly defensive over client relationships?
- Do existing processes ensure that for higher risk activity at least a sample of files are routinely reviewed by a second pair of eyes?

Then consider tailoring existing processes and procedures accordingly to prevent and detect potential tax evasion facilitation – this could include:

- Having a commitment to preventing the involvement of those acting on the relevant body’s behalf in the criminal facilitation of tax evasion, which might be demonstrated by issuing a prominent message from the board of directors (or the leadership team) against all forms of tax evasion
- An overview of its strategy and timeframe to implement its preventative policies.
- Having terms in contracts (with employees and contractors) requiring them not to engage in facilitating tax evasion and to report and concerns immediately
- Providing regular training for staff on financial crime detection and prevention
- Having clear reporting procedures for whistle-blowing of suspected facilitation
- Ensure their pay and bonus policy/structure encourages reporting and discourages pursuing profit to the point of condoning tax evasion
- Monitoring and enforcing compliance with prevention procedures
- Having regular reviews of the effectiveness of prevention procedures and refining them where necessary

5. Next Steps

Stakeholders should be aware that this guidance remains draft guidance and may change to reflect changes to the legislation during the Parliamentary scrutiny process. Where requested, HMRC will continue to work with industry bodies to support them in drafting their own sector specific guidance for the offence.

Any organisation interested in discussing drafting tailored guidance for their sector should contact: consult.nosafehavens@hmrc.gsi.gov.uk