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FINANCE BILL 2017: AVOIDANCE MEASURES

This update looks at how the Finance Bill 2017 proposes to implement two of the anti-avoidance measures on which the government has recently consulted:

- penalties for "enablers" of defeated tax avoidance and changes to the penalties for taxpayers using defeated tax avoidance; and
- the requirement to correct past non-compliance.

ENABLERS AND USERS OF DEFEATED TAX AVOIDANCE

The Finance Bill introduces a new penalty for so-called enablers of tax avoidance arrangements which are defeated by HMRC and, as trailed in the consultation, the government has also changed how the penalty rules work for taxpayers using tax avoidance schemes so they are presumed to have acted carelessly in many cases if they do not obtain tailored, personal advice from an expert.

Abusive tax arrangements

The scope of these rules has been narrowed dramatically since the initial consultation, by limiting them to "abusive" tax arrangements. Tax arrangements are "abusive" if entering into them or carrying them out cannot be regarded as a reasonable course of action in all the circumstances – a test very much like the General Anti-Abuse Rule or "GAAR".

In deciding whether tax arrangements are indeed abusive, the draft legislation stipulates that the principles of the relevant tax provision and their policy objectives must be considered, as well as whether any contrived or abnormal steps are involved and whether the arrangements are intended to exploit any shortcomings in the provisions.

Anything according with established practice which HMRC has accepted in the past is cited as an example of an arrangement which may not be abusive for these purposes. There is also a provision to refer arrangements to the GAAR Advisory Panel for an opinion on whether the arrangements in question are indeed abusive.

All this means that the regime should only catch very aggressive planning. It will also only apply to arrangements entered into after the Finance Act 2017 is given Royal Assent next year, so will not, as many had feared, have retrospective effect.

Defeated

As expected, arrangements are "defeated" when they are:

- counteracted by the GAAR;
- subject to a follower notice;
- notifiable under the Disclosure of Tax Avoidance Schemes (DOTAS) or the VAT disclosure regimes; or
- counteracted by HMRC if the arrangements hinge on a targeted anti-avoidance rule in legislation, for example, a rule that refers to the purpose of a transaction having a tax avoidance motive or being pursued otherwise than for genuine commercial reasons. However, it should be remembered that the arrangements still have to be "abusive" to be within the scope of the enabler penalties.

The enabler

The draft legislation provides for five categories of enabler: a designer, a manager, a marketer, an enabling participant and a financial enabler.

- A "designer" is anyone who, in the course of business, was to any extent responsible for the design of the tax avoidance arrangements in question, if the advice they have given suggests that the arrangements could obtain a tax advantage and the adviser knew or could reasonably be expected to know that the advice would be used to design an "abusive" tax arrangement (unless of course the advice recommended against such a course of action).
- A "manager" is anyone who, in the course of business, is to any extent responsible for organising and managing the arrangements – a definition which does not give much away.
- A "marketer" is anyone who makes a tax avoidance proposal available to the taxpayer or communicates information to the taxpayer with a view to them entering into the arrangements, which includes an explanation of the tax advantage that might be expected to be obtained.
- An "enabling participant" is anyone apart from the taxpayer who enters into the arrangements without whose help the tax advantage could not be obtained, but only if that person knew or could reasonably be expected to know, that they were becoming involved in an abusive tax arrangement.

- A “financial enabler” is anyone who, in the course of business, provides a financial product to the taxpayer or an enabling participant, which includes a loan, share, derivative contract and various other kinds of financial product.

The scope of the term “enabler” is therefore extremely broad and may include IFAs, accountants, company formation agents, trustees, banks, auditors or lawyers.

The penalty

The amount of the penalty is the total value of all consideration received by the enabler for their role in the arrangements. Therefore, if these rules were successfully invoked against an advisor in relation to a one-off piece of advice to a single individual, he would stand to pay all the fees he earned (less VAT) to HMRC. In the case of schemes used by a number of taxpayers, HMRC cannot assess a penalty until it reasonably believes that more than 50 per cent of the arrangements concerned have been defeated.

HMRC will have the power to publish information about enablers who receive penalties, including their name and address, the nature of their business and the total amount of the penalty. The enabler in question will have the opportunity to make representations about whether the information should be published and HMRC will have no power to publish any information once a year has passed from the date of the penalty.

How do HMRC investigate?

HMRC’s information and inspection powers are extended to allow them to investigate potential enablers, including obtaining the information necessary to assess the fees which the enabler charged as this forms the basis of the penalty. If HMRC do not have all the information required to determine the penalty and have taken all reasonable steps to obtain it, they can assess the penalty on the basis of a reasonable estimate. An enabler then has 30 days from notification to pay the penalty.

For lawyer enablers, the draft legislation includes a framework for making declarations about the contents of legally privileged documents which are to be fleshed out by Treasury regulations in due course. This appears to be a way to oblige lawyers to disclose the contents of privileged documents, without disclosing the documents themselves, although exactly how this will work remains to be seen.

The taxpayer - penalties

The Bill also targets taxpayers using defeated avoidance schemes by changing the basis on which penalties are imposed. It is usually for HMRC to demonstrate that a taxpayer was careless or deliberate in submitting a tax return with errors. It can be difficult for HMRC to establish carelessness where a taxpayer has entered into a scheme under assurances from the provider that it would work. Therefore, with effect from 2017 / 2018, the burden of proof will, in most cases involving tax avoidance which fails (and not just “abusive” avoidance), be on the taxpayer to show, both to HMRC and on an appeal to the tribunal, that he did take due care in completing his tax return. The taxpayer will not be permitted to argue that he relied on any of the following categories of advice to show that he was not careless:

- advice from a person who facilitated the avoidance for a fee of any kind, participated in the avoidance arrangements, or from anyone with whom that person had an arrangement (unless the taxpayer took steps to establish this was not the case and reasonably believed it did not);
- advice given by a person without appropriate expertise (again unless the taxpayer took steps to establish that the advisor had appropriate expertise and reasonably believed he did);
- advice which did not take into account the taxpayer’s individual circumstances; or
- advice addressed to anyone apart from the taxpayer.

This effectively puts anyone entering into a scheme on notice that they will pay the higher level of penalties for careless behaviour if the scheme is found not to work (or indeed deliberate behaviour if relevant), and if the taxpayer tries to mitigate this by seeking independent advice, he may very well find that the advisor is wary of his possible exposure as an “enabler”.

What next?

The penalties for enablers are thankfully nowhere near as broad as many had feared and are now better targeted at abusive tax planning that most professionals would advise against in any case. It is also welcome that the provisions cannot apply retrospectively. It remains the case, for any enabler who does not correctly assess the risks of what they are enabling, that they will be left very exposed by these new rules as it is in the taxpayer’s gift to settle with HMRC without reference to the court, and to bring the enabler within the scope of these penalties. And that, of course, is exactly what the government intends.

THE REQUIREMENT TO CORRECT

The Finance Bill 2017 also contains provisions to implement the government's final push before disclosure under the Common Reporting Standard bear fruit to encourage people to come clean about past offshore non-compliance.

The carrot

Taxpayers will have a window of opportunity between 6 April 2017 and 30 April 2018 to make a report to HMRC. This covers UK non-compliance as well as offshore non-compliance if the proceeds of the UK non-compliance have been moved offshore.

The requirement will apply to the 2016 / 17 tax year and all earlier tax years. So long as HMRC would be in time to make an assessment on 6 April 2017, the requirement applies, and HMRC will have an extended window until 5 April 2021 to make assessments. This gives HMRC time to make assessments after the requirement to correct window closes at the end of September 2018, by which time it would also be receiving information under the Common Reporting Standard.

Non-compliance that would ordinarily fall out of time for assessment is therefore frozen in HMRC's sights: HMRC will be able to look back to the 2013 / 14 tax year for innocent mistakes (i.e. four years), to the 2011 / 12 tax year for carelessness (six years) and to the 1997 / 98 tax year for deliberate non-compliance, in each case in relation to income and capital gains tax. The requirement to correct also applies to inheritance tax, for which there is a 20 year time limit for innocent and careless conduct and no time limit for deliberate conduct. The requirement to correct will not, at this stage, apply to other taxes.

Taxpayers wishing to make a disclosure of offshore non-compliance should take advice on how best to do so, but the draft legislation allows for any missing return to be lodged, the new Worldwide Disclosure Facility service online (see our note "Last Chance to Come Clean" from September 2016) to be used or the matter simply to be raised with HMRC in the course of an enquiry or as an HMRC officer may otherwise agree.

The stick

For offshore non-compliance which is not corrected during the 6 April 2017 to 30 September 2018 window, the penalty payable is 200 per cent of the offshore potential lost revenue attributable to the non-compliance. An asset based penalty of up to 10 per cent of the value of the relevant asset will also apply where the tax involved was over £25,000 in any tax year.

The penalty can be reduced to 100 per cent of the offshore potential lost revenue if the person liable tells HMRC about the non-compliance, gives HMRC reasonable help, informs HMRC of any person who acted as an enabler of the non-compliance and allows HMRC access to such records as it might reasonably require to resolve the matter and identify enablers. Therefore, while the penalty for the taxpayer may be reduced, HMRC will be in a position to attempt to recover some of this from the taxpayer's advisor or other "enablers" under the first measures addressed by this note.

HMRC also have power to reduce or stay a penalty, or to agree to a compromise in relation to proceedings for a penalty,in special circumstances at HMRC's discretion, but it is worth noting that a taxpayer's ability to pay is specifically excluded from "special circumstances".

In a similar vein, a taxpayer is saved from a penalty if he had a reasonable excuse for failure to correct the non-compliance within the 6 April 2017 to 30 September 2018 window. As we anticipated, "reasonable excuse" is drawn narrowly, and excludes:

- the taxpayer having insufficient funds, unless this is attributable to events outside his control;
- a situation in which the taxpayer relied on someone else in any way, unless the taxpayer took reasonable care to avoid the failure to correct;
- a situation in which the taxpayer had, but no longer has, a reasonable excuse, unless he takes steps to correct the non-compliance without unreasonable delay after the excuse ceased; and
- reliance on advice if it was addressed to or given to someone other than the taxpayer, took no account of the taxpayer's individual circumstances or was given by somebody without the appropriate expertise (these criteria echo the circumstances in which a taxpayer is deemed to have been careless when filing a tax return on the basis of advice in relation to an avoidance scheme – see above).

As above, HMRC has the power to publish details of people assessed to penalties, if the taxpayer was aware during the 6 April 2017 to 30 September 2018 period that he had offshore non-compliance to correct but was given a penalty for failing to do so. Power to publish arises where there is one or more relevant penalties exceeding £25,000 each, or where the taxpayer has incurred five or more penalties (of any amount).

What next?

It is clear that taxpayers who know that they have offshore non-compliance should come forward as soon as possible and make use of the Worldwide Disclosure Facility. The coming wave of disclosure through the various transparency initiatives puts them even more firmly on the back foot.

Because of the very substantial penalties involved, taxpayers with complex affairs should also take the opportunity to review tax planning with offshore elements. Proper, tailored advice may be sufficient to give the taxpayer a reasonable excuse for not reporting an offshore non-compliance, which later comes to light in a much less favourable penalty regime.

CONTACT DETAILS

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This note is intended to provide general information about some recent and anticipated developments which may be of interest.
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