Tackling offshore tax evasion: A new criminal offence
HM Revenue & Customs (HMRC) consultation document
Response from the Low Incomes Tax Reform Group (LITRG)

1 Executive summary

1.1 We appreciate the opportunity to respond to the consultation on the new strict liability criminal offence for tax evasion; but we strongly believe that a fundamental question is omitted from the consultation document, namely whether it is right to have such a new offence at all.

1.2 We do not support the introduction of this new offence. Although the latter part of this paper responding to the specific consultation questions gives views as to how it might be best implemented so as to protect low-income migrants to the UK, these comments should not be read as an endorsement of the principle and we totally oppose it.

1.3 Whilst we have no interest in protecting those who seek to evade taxes by using 'expensive offshore banks and complex financial structures', it must be recognised that there are also people coming to the UK to work with assets and bank accounts abroad in their home countries, of whom these proposals seem to take no account whatsoever.

1.4 Our concern is for low-income and unrepresented taxpayers, who may have no intention of evading tax but who mistakenly fail to declare offshore income or gains – for example because they think, quite reasonably but wrongly, that they are not liable to UK tax. The suggestion in the consultation document seems to be that anyone getting it wrong should be penalised as if they had deliberately set out to act in a criminal way. We cannot see how this can be right at all, especially when overseas tax matters can be so complicated.

1.5 At the moment, the extent to which low-income migrants would be excluded from the scope of the new offence is not at all clear. For example, whilst many migrants have limited or no means in their home country, there are some – particularly from certain EU countries – who may own property as their home or as part of a family.

1.6 We therefore explain in this response why it is crucial for them to have special consideration and, if the proposed offence is introduced, why there should be proper safeguards to protect them – such as a *de minimis* threshold and 'reasonable belief' defence – incorporated into statute.

CHARTERED INSTITUTE OF TAXATION
1st Floor, Artillery House, 11-19 Artillery Row,
London, SW1P 1RT
REGISTERED AS A CHARITY NO 1037771

Tel: +44 (0)20 7340 0550
Fax: +44 (0)20 7340 0559
E-mail: litrg@ciot.org.uk
www.litrg.org.uk

UK REPRESENTATIVE BODY ON THE
CONFEDERATION FISCALE EUROPEENNE

2 About Us

2.1 The Low Incomes Tax Reform Group (LITRG) is an initiative of the Chartered Institute of Taxation (CIOT) to give a voice to the unrepresented. Since 1998 LITRG has been working to improve the policy and processes of the tax, tax credits and associated welfare systems for the benefit of those on low incomes. Everything we do is aimed at improving the tax and benefits experience of low-income workers, pensioners, migrants, students, disabled people and carers.

2.2 LITRG works extensively with HM Revenue &Customs (HMRC) and other government departments, commenting on proposals and putting forward our own ideas for improving the system. Too often the tax and related welfare laws and administrative systems are not designed with the low-income user in mind and this often makes life difficult for those we try to help.

2.3 The CIOT is a charity and the leading professional body in the United Kingdom concerned solely with taxation. The CIOT's primary purpose is to promote education and study of the administration and practice of taxation. One of the key aims is to achieve a better, more efficient, tax system for all affected by it – taxpayers, advisers and the authorities.

2.4 Our response supplements that of our CIOT colleagues.

3 Introduction

3.1 It seems that prior to the launch of this consultation, a decision had already been made to bring in this new offence: *'The Government plans to introduce a new strict liability summary criminal offence of failing to declare taxable income and gains arising offshore and seeks views on the design of the new offence*'[1]. To pre-empt consultees who may wish to express firm views on whether such an offence should exist at all is quite wrong.

3.2 We firmly believe that the first questions to be posed are: whether or not it is right to introduce this measure; whether it is necessary; and what stakeholders' views might be as regards the Government's perceived inadequacy of HMRC's existing powers in terms of dealing with UK tax evasion on offshore income and gains.

3.3 External engagement at an early stage in the policy-making and decision-making processes can bring expertise and alternative perspectives, and identifying unintended effects and practical problems – saving time and effort later.

3.4 The risk of undermining stakeholders' roles in consultations (and it must be remembered that there was a similar lack of early engagement with the recent Direct Recovery of Debts (DRD) proposals) is that they may see little point in responding in the future, possibly even disengaging altogether. This can only result in the serious potential for bad laws and policy in the long term. We therefore urge that in the future stakeholders be given a proper opportunity to comment on the merits of policy proposals prior to fundamental decisions being taken.

[1] Para 1.1, page 5 of the consultation document.

4 General comments

4.1 We agree with the robust detection, deterrence and prosecution of tax evasion, however – except in certain limited situations where physical safety is at risk (for example certain motoring offences) – we think the state of mind of the perpetrator should always be a relevant consideration in establishing criminal liability.

4.2 The UK's current criminal tax offences are generally based on intention, knowledge, and recklessness – all words that indicate an awareness of a particular circumstance or an act's consequence or result[2]. This is a reflection of the fact that it is generally neither fair, nor useful, to subject people to criminal punishment for unintended actions or unforeseen consequences.

4.3 The Government's stated aim with this measure is to tackle taxpayers 'evading' UK tax. In the foreword to the consultation document, those 'hiding' their undeclared income offshore are warned off. Both of these words indicate some kind of appropriate awareness to merit a criminal prosecution. Yet a strict liability offence would not confine itself to such people – it would affect those that had been careless, or forgetful, or who had made a genuine mistake over what taxes they have to pay. Therefore there is a worrying divergence between the Government's stated aims and the reality of what is being proposed.

4.4 We are very concerned about the potential impact of the proposals on low-income and unrepresented taxpayers – particularly 'asset rich but cash poor' migrants into the UK from Eastern and Central European countries, who are likely to have benefited from land and property being passed to them or their families in the transition from a centralised to a market economy[3]. One example is migrants from Romania, with statistics showing that it has nearly 96 % home ownership[4]. Migrants to the UK could therefore have rental income or property disposals arising in their home countries while they are here, which means they could be caught within these proposals.

4.5 Realistically, migrants with rental income in their home countries will probably never visit an accountant or HMRC's website (or GOV.UK) to try and understand the rules, as intuitively one expects a tax liability to occur in the country in which the property is situated.

5 Specific comments on EU migrants

5.1 We see migrant workers from all over the EU. Whilst they vary in age, profession (but many are in low-income jobs such as building or agricultural labourers and cleaners), educational achievement and standard of English, all have in common that they do not understand the requirements of the UK tax system in respect of anything they have left behind in their homeland. This is not surprising, because HMRC does not tell them (not in a way that they can understand anyway).

5.2 What little guidance for migrants there might have been in the past has now dwindled. For example, introductory guides to the UK tax system translated into some of the more common migrant languages that used to be available to download, have been removed from HMRC's website without any replacement. But even so, those materials were not specifically disseminated to the migrant

---

[2] For example, Section 106A Offences of fraudulent evasion of income tax: The Taxes Management Act 1970 (TMA 1970) imposes criminal liability on a person who is 'knowingly concerned ' in the fraudulent evasion of income tax by him or another person.

[3] See for example: 'The changing role of housing assets in post-socialist Countries' http://www.birmingham.ac.uk/documents/college-social-sciences/social-policy/demhow/b8.pdf

[4] Source: Distribution of population by tenure status, type of household and income group, Eurostat (http://appsso.eurostat.ec.europa.eu/nui/show.do?dataset=ilc_lvho02&lang=en)

population so were probably not well used. Migrants really need HMRC to produce (or fund production of) targeted, clear and easy-to-understand information and to ensure it reaches them through various channels, such as voluntary sector organisations dealing with that part of the population, or large employers of migrant labour.

5.3 It must also be remembered that migrants are unlikely to have (or be able to afford to pay) anyone else to explain the situation to them or provide them with advice.

5.4 For those that do have an inkling that they might need to do something in the UK about their offshore income and who delve deep into the recesses of HMRC's website to try and understand for themselves what the situation is, there are many reasons why they may still get it wrong. After all, our residency, domicile, remittance and double taxation treaty rules are so complex and detailed that the unrepresented are virtually guaranteed to make mistakes.

5.5 It is important to say at this stage that they will probably have an even harder time working things out when the HMRC guidance is fully migrated to GOV.UK, as we find that there is so much dilution of the material that often important key messages are being lost in transit. It seems to us more important than ever that taxpayers clearly understand what is expected of them and what the implications are of their actions (or inactions) and we question whether they will be able to do this once the full HMRC content is transferred to GOV.UK.

5.6 It is worth examining the questions that an EU migrant would have to ask themselves to come to a decision about whether or not they need to declare their overseas rental income to the UK authorities:

- ***Am I tax resident in the UK?***
  If not, then the rental income is not taxable in the UK. But deciding one's residence for tax purposes is not always straightforward. For migrants visiting the UK, it is only really straightforward when you have spent more than 183 days in the UK in a particular tax year (and that is if you even understand the concept of what is a 'day' for the purposes of UK residence). For those spending fewer than 183 days, the statutory residency test (SRT)[5] has been in place since 6 April 2013 to help determine their position. However some of the concepts behind the questions in the SRT are extraordinarily complicated – meaning that without professional advice, they may be wrongly answered. Whilst HMRC offers Guidance Note RDR3[6] to the SRT, this is more than 100 pages long and many individuals would not be able to understand it due to language difficulties.

- ***Have I made a net profit for UK tax purposes which falls above the personal allowance?***
  Rental income may show a loss under their local law (because perhaps it permits depreciation, for example Poland[7]), but it shows a profit under UK rules (while the UK rules do not allow depreciation to be deducted, you may be able to deduct capital allowances for 'plant and machinery', or perhaps a wear and tear allowance for furnished property. But most migrants will be unaware of the means of calculating UK rental profits).

[5] The SRT consists of automatic tests for non-residence; automatic tests for residence; and UK ties and day counting, known as the Sufficient Ties test, for individuals who are neither automatically non-resident or resident. See: http://www.hmrc.gov.uk/international/residence.htm
[6] Guidance Note: Statutory Residence Test (SRT), RDR3 – HM Revenue & Customs (December 2013): http://www.hmrc.gov.uk/international/rdr3.pdf
[7] See EY guide: The Polish Real Estate Guide Edition 2014 (http://www.ey.com/Publication/vwLUAssets/EY_Real_Estate_Guide_Book_2014/$FILE/EY_Real_Estate_Guide_Book_2014.pdf)

- ***Does the remittance basis apply to me?***
  If there is a taxable profit, the migrant may consider the implications of their likely non-domiciliary status to avoid a UK tax charge, as this allows income or capital gains that you make outside the UK, and never remit to the UK, to be tax-free in the UK. Someone who is UK resident but not domiciled in one of the parts of the UK has the option to claim the remittance basis. There is a special exemption from the charge for non-domiciliary whose unremitted non-UK income and capital gains are less than £2,000 in a given tax year, which may be particularly useful to low-income migrants as they would not also lose their personal allowance.

- ***Can the double tax treaties help?***
  The double tax treaties overrule the general principles set out above, so migrants have the added complication of having to consult their terms. This is no easy task for the unrepresented! If the country where the property is situated levies a tax charge then a double tax agreement will usually give credit relief for foreign taxes paid. Depending on the tax rate in the foreign country, this could reduce or extinguish even, the UK tax liability.

  There is also a school of thought that if the migrant has remained tax resident in their home country as well as establishing residence in the UK, then then under the tie breaker tests (used in situations where there is dual residence by virtue of domestic legislation) the migrant will generally be treaty resident in their home country and treaty non-resident in the UK, meaning that the immovable property clause can be interpreted as awarding taxing rights to the home country only.

5.7 As we can see here, there are many reasons why a migrant might not declare their offshore rental income, even if they were able to fathom in the first place that they might have to. HMRC must therefore acknowledge that the rules around offshore income are not obvious or readily understood and that in such situations, criminal punishment is wholly unmerited and inappropriate.

5.8 HMRC may say that as there has been much publicity around tax evasion and the various disclosure facilities, there is a prompt for migrants to check their position and a suitable way to correct any irregularities. Therefore if taxpayers do not come forward then it is right that they face tough consequences.

5.9 However, migrants might have a very limited picture of what 'evasion' is – perhaps understanding (if at all) that it involves some contrived, artificial transaction – more often than not formed through what they hear about in the news. In comparison, their own positions will seem very simple to them, particularly if they are paying some tax in their home country, so they would not identify themselves as being the target of such publicity.

5.10 In summary, we do not think that the impact of the strict liability offence on low-income, unrepresented taxpayers has been sufficiently addressed in the consultation. Whilst we understand that offshore evasion is costly and complex to deal with and HMRC have ambitious targets to meet in terms of conviction rates[8], strict liability is a hugely serious matter and should not be justified on the basis of it being administratively convenient. Indeed, inappropriate use of this new power could pose a real risk to HMRC's reputation – all it would take is one 'miscarriage of justice' and confidence and trust in HMRC could be damaged irreparably.

[8] http://www.cps.gov.uk/news/articles/prosecuting_tax_evasion/

6 Consultation questions

6.1 The comments that we go on to make must be taken in the context of our reservations about the policy per se. If the proposals are to be taken forward, we strongly recommend the addition – in statute rather than guidance – of safeguards for low-income migrants to the UK, for whom there is not currently adequate proposed protection.

6.2 We have avoided answering the first set of questions on the basis that by inviting comments on the scope of the proposed offence they presume approval of the proposal itself on the part of those who answer. The remaining questions we have answered to the extent that they are germane to the argument we have put forward in the main body of this response.

7 Do you agree that a de minimis threshold is appropriate?

7.1 A *de minimis* is not only appropriate, it is **vital**. The Government and HMRC must ensure that, if introduced, the new criminal offence is only prosecuted where the failure to declare taxable offshore income and gains leads to a tax loss over a certain amount and that low-income individuals are protected.

8 Should the *de minimis* be set by reference to the potential lost revenue arising from the failure/inaccuracy, or some other measure? If so, should the potential lost revenue be calculated in the same way as it is for the purposes of determining civil penalties?

8.1 Yes – see the response to our question above. Potential lost revenue seems reasonable, however this should be after all available claims have been made – for example, after foreign tax credits or any potential double tax relief (DTR).

8.2 If the *de minimis* is to be set by reference to the potential lost revenue, we assume that any non-compliance will be initially pursued through civil means – until it is established whether a criminal investigation is appropriate or not. This is not clear from the consultation.

8.3 If introducing these proposals, Government and HMRC must be clear on how cases would be handled in practice. If a case is investigated and the potential lost revenue is less than the *de minimis*, we presume that a civil penalty appropriate to the circumstances may still be imposed. If a case is civilly investigated and the potential lost revenue is more than the *de minimis*, will this see a handover of the case to HMRC's specially trained and empowered Criminal Investigation team? Yet, by then, much of the operational investigation will have been done – presumably not to the criminal standards of proof required. We would appreciate clarity on this.

8.4 Also, on the assumption that not all non *de minimis* cases will be automatically criminally pursued (because that would create a bottleneck) we would like to understand what the selection criteria will look like. It is important for certainty and clarity that we are all clear on the situations in which a criminal sanction will be applied.

9 Should the threshold be incorporated in statute or guidance?

9.1 The threshold **must** be in statute, for certainty. Guidance is of very little use to the taxpayer if neither HMRC nor the courts are bound by it.

10 Are there any further options (for setting the threshold)?

10.1 No comment.

11 Which approach to setting the threshold do you favour?

11.1 We would suggest this is set as high as possible so as to protect as many EU migrants as possible. A sensible measure would be the financial threshold for entry into the Managing Serious Defaulters programme – £5,000 of potential lost revenue.

11.2 If the figures in Box 3 (on page 18 of the consultation document) which illustrate the typical scale of tax lost in offshore non-compliance cases are correct, then 28% of offshore cases in 2013/14 involved more than £5,000 of tax. On the basis that the consultation document says more than once that prosecutions are likely to be rare, it would be sensible to ensure that these involve only the most serious cases. Setting the *de minimis* at £5,000, would help achieve that.

11.3 We would mention in passing though, that we are somewhat surprised at the figures quoted in the consultation document for the median potential lost revenue (PLR) in all offshore penalty cases. These seem rather low to justify introducing this whole new regime of criminal sanctions, thus reinforcing our view that the proposals themselves are disproportionate.

12 The Government's view is that the threshold should apply for each tax year, rather than in respect of a cumulative amount of potential lost revenue, as a new offence would be committed for each tax period – e.g. each time an incorrect return is filed. Do you agree?

12.1 We think this should be assessed year on year, for maximum protection of those on lower incomes.

13 Do you agree with the principle that the available criminal sanction for offshore non-compliance should not be seen as more lenient than the available civil sanction?

13.1 It seems to us that a criminal record cannot be compared to a civil sanction – for most people a criminal record will always be worse due to the stigma that it carries and the fact it can cause immense damage to a person's reputation. For example, it may need to be declared for employment purposes, so can also result in practical consequences which could be far reaching.

14 Should an unlimited financial penalty be available to the courts in England and Wales?

14.1 We are not sure why the concept of 'unlimited' has been introduced in this question, as immediately preceding it, the consultation document states that the Government is minded to ensure a criminal penalty of a maximum of twice the potential lost revenue – bringing it more or less in line with those permissible under the civil code. We assume the Proceeds of Crime Act 2002 would also provide an additional means of recovery?

15 As part of this consultation, HMRC would be interested in views as to how the policy intention of a tax geared penalty could best be delivered in Scotland and Northern Ireland.

15.1 No comment.

16 Is the harm which could be caused by a failure to declare offshore income and gains sufficient that a custodial sentence could be justified in the most serious cases?

16.1 The authorities already have sufficient powers to prosecute those they discover have been failing to disclose offshore taxable income. Therefore this is a strange question on the basis that under current law, someone who has concealed offshore income *mens rea*, already can go to prison.

17 If a custodial element is appropriate, should the maximum sentence be six months?

17.1 We decline to answer this question on the basis that if a person did not mean to evade their taxes, they should not be going to prison at all.

18 Should it be a defence for (i) a person to demonstrate that they had taken reasonable care in conducting their tax affairs, or (ii) a person to demonstrate that they had sought and followed appropriate professional advice? What would be the impact on the likelihood of successful prosecutions if statutory defences are included?

18.1 We agree that a general defence of reasonable care must be provided – if a person would not receive a penalty under the civil code, they should absolutely not face criminal prosecution for a strict liability offence.

18.2 However, a migrant who had not considered their UK tax position at all in respect of their home country income would not be able to prove reasonable care, based on HMRC's view of it on page 24 that:

> 'In HMRC's view it is reasonable to expect a person who encounters a transaction or other event with which they are not familiar to take care to find out about the correct tax treatment or to seek appropriate advice.'

18.3 Therefore to protect low-income migrants, this protection needs to be strengthened. We recommend a 'reasonable belief' defence be provided to cover situations where people have

wrongly but genuinely believed that their income was not taxable in the UK – for example, because they had been taxed in the local jurisdiction, or that they were non-resident under the statutory residence test (SRT), or were taxable on the remittance basis.

19 Should any other statutory defences be introduced?

19.1 See answer to question above.

20 Are further safeguards appropriate? What should these be?

20.1 The best safeguard for innocent taxpayers who have no intent to evade tax would be retaining the requirement to prove all elements of an offence, including the intention of the person to do the act.

20.2 However, if the proposals are to be implemented, then there will need to be a very widespread publicity campaign before this offence comes into force. We therefore suggest that there is a long lead time.

20.3 To date, only the most serious cases of tax evasion have resulted in criminal charges[9] so needless to say, for maximum transparency, HMRC will need to review their criminal investigation policy and provide an updated criminal investigation policy statement.

20.4 We assume that there is no question of these provisions having retrospective effect, such that cases will only be considered under the new provisions for tax years on or after they are legislated.

20.5 HMRC say that the majority of cases will continue to be pursued through civil means (paragraph 5.11). As alluded to earlier, we would ask that HMRC provide some guidelines on the sorts of occasions when they would use the strict liability offence rather than civil action to minimise uncertainty about when the offence would apply.

21 Do you have any views, comments or evidence which may help inform our understanding of likely impacts?/Do you have any views, comments or evidence which may help inform our understanding of likely equalities impacts?

21.1 We are surprised at the lack of detail in the equality assessment and this only strengthens our view that HMRC have not thought these proposals through sufficiently. Through our above comments, we hope to have shown that it is not necessarily the case that ‘any affected equality groups are likely to be those over represented amongst those of above average wealth’; indeed, there could be impacts on low-income migrants who may be vulnerable for a number of reasons.

21.2 If these provisions are taken forward, further protection must be afforded to them by way of a sensible *de minimis* threshold and ‘reasonable belief’ defence that is written into statute and takes

[9] http://www.hmrc.gov.uk/prosecutions/crim-inv-policy.htm

full account of personal circumstances such as educational background, literacy, numeracy, English language skills and so forth.

LITRG

31/10/2014