



## ICAEW REPRESENTATION

### TAXREP 16/10

### TACKLING OFFSHORE TAX EVASION

***Comments submitted on 5 March 2010 by the Tax Faculty of the Institute of Chartered Accountants in England & Wales to HM Revenue & Customs in response to the consultation document 'Modernising Powers, Deterrents and Safeguards: Tackling Offshore Tax Evasion' issued on 9 December 2009.***

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# TACKLING OFFSHORE TAX EVASION

## INTRODUCTION

1. In this document we present the comments of the Tax Faculty of the Institute of Chartered Accountants in England and Wales (ICAEW) on the consultation document *Modernising Powers, Deterrents and Safeguards: Tackling Offshore Tax Evasion* (the Condoc) issued by HM Revenue & Customs (HMRC) on 9 December 2009.
2. We are pleased to have the opportunity to respond to this consultation. We would be happy to discuss any aspect of our comments and to take part in all further consultations on this area.
3. We had a preliminary meeting with HMRC on 16 February 2010, in which we were able to put forward our key comments and concerns and discuss aspects of the condoc.
4. Information about the Tax Faculty and the ICAEW is given below. We have also set out, in Appendix 1, the Tax Faculty's ten tenets for a better tax system, by which we benchmark proposals to change the tax system.

## WHO WE ARE

5. The Institute operates under a Royal Charter, working in the public interest. Its regulation of its members, in particular its responsibilities in respect of auditors, is overseen by the Financial Reporting Council. As a world leading professional accountancy body, the Institute provides leadership and practical support to over 132,000 members in more than 160 countries, working with governments, regulators and industry in order to ensure the highest standards are maintained. The Institute is a founding member of the Global Accounting Alliance with over 775,000 members worldwide.
6. Our members provide financial knowledge and guidance based on the highest technical and ethical standards. They are trained to challenge people and organisations to think and act differently, to provide clarity and rigour, and so help create and sustain prosperity. The Institute ensures these skills are constantly developed, recognised and valued.
7. The Tax Faculty is the focus for tax within the Institute. It is responsible for technical tax submissions on behalf of the Institute as a whole and it also provides various tax services including the monthly newsletter *TAXline* to more than 11,000 members of the Institute who pay an additional subscription, and a free weekly newswire.

## KEY POINTS SUMMARY

8. Our key comments on this consultation are as follows:
  - The ICAEW agrees that HMRC needs to tackle tax evasion (whether offshore or otherwise) and that it needs effective tools to do the job.
  - However, we do not support the proposals in this consultation. We do not think HMRC has got the balance right between the rights of the compliant majority and the need to tackle the small minority of tax evaders.
  - The proposals for new powers, particularly the notification of offshore accounts, will place an unnecessary burden on the compliant majority while not necessarily catching the evaders.
  - We are not convinced by HMRC's arguments that offshore non-compliance or evasion deserves tougher sanctions than the equivalent 'onshore' behaviour. We strongly oppose the idea of treating all non-compliance with an offshore element as though it were

deliberate. We do not think there should be a new level of penalty specifically for offshore evasion because we do not agree that offshore evasion is intrinsically more heinous than any other sort of tax evasion.

- We are not clear about how the start date for the new penalties will be applied, but we are concerned that there may be an element of retrospection.
- We suggest that there should be a de minimis where the offshore component is a relatively insignificant part of the whole settlement.
- We are concerned about the impact of the bank account notification requirements on people who have small offshore accounts for entirely innocent reasons. The burden on such people will depend on what Tax Information Exchange Agreements (TIEAs) the UK happens to have in place with their country of origin.
- We suggest that HMRC needs to address the reasons why the information which it can get from other tax authorities is limited.
- A major concern is how people will know about the notification requirement in the first place. HMRC will need to do a great deal of effective publicity.
- We also think that the notification procedure seems too complicated and the 60-day period is too short. We also have questions about how the penalty rules will be applied.
- We note that remittance basis users will be excluded from the notification requirement, but it is hard to see how the 60-day limit for notifying accounts would interact with the time limit for claiming the remittance basis.

## **GENERAL PRINCIPLES AND APPROACH (Chapters 1 and 2)**

9. The ICAEW agrees, of course, that HMRC needs to tackle tax evasion (whether offshore or otherwise) and that it needs effective tools to do the job.
10. However, we do not support the proposals in this consultation and are concerned about its approach. The proposals for new powers, particularly the notification of offshore accounts, will place an unnecessary burden on the compliant majority.
11. HMRC argues that offshore evasion is different from what one might call onshore evasion, in ways which justify HMRC having greater powers and tougher penalties to tackle it. The arguments in support of this appear to be as follows, with our comments on them:
12. First, para 1.13 notes that HMRC finds it more difficult to check the tax position of someone with assets overseas. This may be true, but it does not follow that offshore evasion deserves tougher penalties, as though it were somehow more heinous than onshore evasion.
13. Second, HMRC considers that everyone should now know about UK tax obligations on overseas income/gains (paras 1.16, 3.1). But we would doubt that most people have heard of the ODF, NDO or LDF. There was no publicity campaign for the ODF; the NDO and LDF have not attracted a huge amount of media coverage outside the professional press. We also doubt if the average person would equate media coverage of bankers, non-doms and tax havens with their own tax affairs. Further, even if people know they may be taxed in the UK on offshore income, they may struggle to understand how this complex area of the tax system applies to them.

14. Third, HMRC has concluded from the ODF and NDO that there ‘has been significant evasion of tax by investors in offshore locations’ (para 2.5) and that ‘there is a serious problem with UK taxpayers hiding assets and income overseas’ – the implication is that there is plenty more offshore evasion to be uncovered. But an equally valid conclusion from the response to these two initiatives might be that between them they have already flushed out most offshore tax evasion. Indeed the reportedly low uptake of the NDO might be said to support such a conclusion.
15. With regard to the design principles, we have no problem with the framework for the Powers Review set out in para 2.2.
16. We agree that powers must be proportionate and that there is a ‘balance between the rights of the honest citizen and the tax evader’ (para 2.6). However, we do not think that these proposals have got the balance right.
17. As para 1.1 notes, it is not just a minority of people but a **small** minority which carries on offshore evasion, yet to tackle these people HMRC is proposing a bank account notification requirement for everyone. The new requirement will bring with it a compliance burden and the risk of a penalty, even though it may be difficult for many to understand what they are required to do or even know about it. We comment below on the details of the proposals in Chapter 4.
18. We are not convinced by HMRC’s arguments that offshore non-compliance deserves tougher sanctions than non-compliance without an offshore element. Indeed the condoc is inconsistent in its use of the terms ‘evasion’ and ‘non-compliance’, and appears to equate the two. We have no problem with HMRC taking a tough approach to tax fraud, but ‘non-compliance’ covers a wide range of behaviour including mistakes and carelessness. We strongly oppose the idea of treating all non-compliance with an offshore element as though it were deliberate.

### **PENALTY FRAMEWORK FOR OFFSHORE NON-COMPLIANCE (Chapter 3)**

19. HMRC proposes to apply penalties to all offshore non-compliance as though it were deliberate; in other words, non-compliance through not taking reasonable care would be regarded as equivalent to tax evasion. This is unreasonable and we strongly disagree with it.
20. We do not think there should be a new level of penalty specifically for offshore evasion because we do not agree that offshore evasion is intrinsically more heinous than any other sort of tax evasion.
21. The proposal appears to be based on the arguments about difficulty of obtaining information, widespread public awareness, etc as discussed above under ‘General principles and approach’ and we have explained why we are not convinced by these arguments.
22. We find the Chapter 3 proposals hard to follow because the chapter appears to confuse evasion with non-compliance, and to equate the two (eg para 3.2 refers to increased penalties for offshore non-compliance but para 3.13 refers to the same proposals as being for offshore evasion).
23. We are also confused by the reference in various places to ‘reasonable excuse provision’. If the new penalties are to be based on the Sch 24, FA 2007 penalty regime, they will presumably take into account whether someone has taken reasonable care, not whether they have a reasonable excuse. The assessment of reasonable care should be considered in the context of the Individual taxpayer, whereas ‘reasonable excuse’ could be a much narrower safeguard.
24. One reason why people may not disclose overseas income or gains correctly is that they may not understand the rules or even know about them. This is potentially a very complex area of

the UK tax system. The interpretation of 'taking reasonable care' in this context should take into account whether the particular taxpayer could reasonably have been expected to know about and understand the rules.

25. Further, some people may not have taken reasonable care (eg not taking advice about how the tax rules work) but this will not amount to deliberate mis-statement. We do not see why someone who has accidentally or carelessly not complied with UK tax law should be liable to a higher penalty on the assumption their action was deliberate.
26. There should still be an onus on HMRC to show that behaviour was deliberate.
27. In particular, with regard to the ODF and NDO, we do not think it is enough for HMRC to assume that a person ought to have known about these opportunities and therefore if they have not come forward, any non-compliance is deliberate. HMRC should have to demonstrate that the person did know, eg provide evidence that they received a letter from HMRC or their bank.
28. We are also not clear about how the start date for the new penalties will be applied. We note from para 3.5 that legislation for the higher scale of penalties for offshore non-compliance is intended to apply from April 2011. For periods prior to that it appears that HMRC intends to achieve the same effect by treating offshore non-compliance as deliberate (from 2009 to 2011) or of the utmost gravity (for pre-April 2009 periods). This appears to us unfair and to include an element of retrospection.
29. Para 3.11 says that the 'more robust' penalty would only apply to the offshore component of non-compliance. We suggest that there should be a de minimis where the offshore component is a relatively insignificant part of the whole settlement.
30. We agree that any new penalty should apply to all taxes; but as we have said, we do not agree that there should be a new penalty.

#### **NOTIFICATION REQUIREMENT FOR OVERSEAS BANK ACCOUNTS (Chapter 4)**

31. The condoc notes that there are many wholly legitimate reasons for operating an overseas bank account (para 4.6). It also notes that the people who use offshore accounts for tax evasion are a small minority. But despite that, HMRC proposes to introduce a notification requirement for everyone, including the compliant majority. We do not support this proposal.
32. The Charter contains the right that HMRC will do all it can to keep taxpayers' costs as low as possible. We think that the bank account notification requirement is unreasonable in this context.
33. We are concerned about the impact on people who have small offshore accounts for entirely innocent reasons, unconnected with tax, in particular low-income people who originate from outside the UK. The burden on such people will depend on what Tax Information Exchange Agreements (TIEAs) the UK happens to have in place with their country of origin.
34. Para 4.8 says that where access to information is limited and there is evidence of significant tax loss, HMRC needs to reconsider the powers available to it. However, we think HMRC should turn its attention to considering **why** the information which it can get from other tax authorities is limited. If it is because HMRC (perhaps because of limited resources) has not got round to negotiating a TIEA with a particular country, it does not seem reasonable to single out for an extra burden people who happen to come from that country. The position may be different where a country has refused to discuss a TIEA.

35. For example, there are a lot of people in the UK who have come here from, say, the West Indies and send money home to their families. We suspect that such people may well transfer funds from their UK bank account to a local bank account. The UK has a TIEA with Antigua and Barbuda and also with St. Lucia, but not with Dominica, which lies between the two. It does not seem to us reasonable that, say, a waitress who comes from Dominica and sends money home out of her taxed earnings should have a burdensome reporting requirement imposed on her while her colleague who happens to come from one of the neighbouring islands may escape that burden.
36. A major concern is how people will know about the notification requirement in the first place, especially those who are not in self assessment or not in regular contact with HMRC. We agree that it would be burdensome to bring taxpayers into SA simply to comply with a notification requirement (para 4.24). However, as yet HMRC has not made clear what alternative method it would use to make taxpayers aware of the requirement. HMRC will have to do more than just publicise these rules on its website – it will need to find ways of reaching everyone who might open an offshore account.
37. The notification procedure seems too complicated. First, a person must be aware of it, then know in which category the account-holding jurisdiction falls, and finally (if it falls in Group C) monitor the accounts to see when the £25,000 de minimis applies.
38. Para 4.14 says HMRC intends to apply the notification requirement just to individuals. It seems to us that the requirement could be easily side-stepped by setting up accounts via some other entity.
39. There is no de minimis for the notification requirement, apart from the £25,000 which applies overall to all Group C accounts. In our view there should be a de minimis in all situations.
40. In this connection, we note that in para 4.13, the US system is given as an international precedent. In fact the US has a realistic de minimis exemption so we would question whether a system that omits such a de minimis can properly be categorised as similar to it (para 4.22). The US form FBAR does not actually require details of ‘all foreign accounts opened or used during the fiscal year’ (as the box at para 4.13 states). The de minimis is \$10,000, equivalent at present to around £6,000. A de minimis of at least this level would very likely remove the notification burden from many bona fide commercial accounts.
41. Para 4.26 proposes a 60-day period for notification, after which the penalty becomes due. We do not think this is long enough unless HMRC’s publicity is good enough for people to know about their obligations straight away.
42. Para 4.31 indicates that HMRC would ask for details of the source of funds in the account. First, we consider this is an unnecessary intrusion and that HMRC’s information powers should be limited to tax matters not financial affairs generally.
43. Second, defining the source of funds may be difficult. By way of illustration, a person might open an account while overseas on holiday using cash they happen to have in their pocket at the time. This could be money brought from England, and taken out of a UK bank account. The funds in the UK account could have come from a variety of sources. What information would HMRC want and how could it make this clear on the form?
44. With regard to penalties, unless HMRC’s communications are good enough to make sure that people will know about the notification requirement, it seems to us unfair to impose a penalty for failing to comply with it. Would this be covered by the proposed reasonable excuse provision? Failing to know about your obligations is not generally regarded by HMRC as a reasonable excuse.

45. Para 4.36 indicates that there will be tax-geared penalties. What will these be based on? If a notifiable account is opened on 6 April 2010 there may be no tax lost until 31 January 2012, but notification under the 60-day rule will be due long before then. What if no tax is in fact lost, because it is all paid by the due date, so the only misdemeanour is administrative in nature?
46. Para 4.36 also proposes daily penalties. It is hard to see how this would work – what would trigger such penalties? The situation is not like an SA return, where HMRC issues the form, so knows when it is late.
47. Paras 4.41–4.44 discuss the remittance basis of taxation. We note that remittance basis users would be exempt from the notification requirement. But a person will be brought into the notification regime if they decide not to opt for the remittance basis – in which case, we presume that he or she would immediately have to notify HMRC of all relevant accounts. As well as being an onerous requirement, it is hard to see how the 60-day limit for notifying accounts would interact with the time limit for claiming the remittance basis.

## **INFORMATION ON OTHER OFFSHORE FINANCIAL STRUCTURES (Chapter 5)**

48. Para 5.7 – we do not see the logic of aligning information requirements. IHT is based primarily on domicile, and CGT and income tax primarily on residence, so the two are dealing with different populations.
49. Para 5.8 – we think that HMRC should first of all do more to publicise and explain the existing requirements. We suspect that these are not well known, even by tax advisers.
50. Para 5.9 – with regard to the exclusion of barristers from the reporting obligations for offshore trusts, we had thought this was because of legal professional privilege. We agree it appears anomalous but we doubt whether this consultation is the appropriate place to discuss the wider issue of LPP.
51. Para 5.10 - on the basis that HMRC says at para 5.8 that the legislation is generally effective, there is little point in amending it to try to catch a minority of non-compliant people. We would also have thought that the number of people who set up overseas trusts without professional advice is tiny and that s 218, IHTA 1994, which imposes a notification requirement on the advisor, ought to be sufficient.
52. Para 5.11 – we think that because of the territoriality principle there is no legal basis for HMRC to impose information requirements on non-residents.
53. Para 5.14 – we think such a requirement would be onerous for settlors, since they may not be familiar with these rules or realise when they have transferred value to a non-resident trust or a company. For example, our understanding is that if a UK-resident settlor pays the trustees' fees and the payment is treated as a debt due by the trust to the settlor, HMRC considers that he or she has transferred value into the trust equal to the interest that he could have charged had he lent the money to the trust on a commercial basis. We doubt if many settlors would know this. Accordingly a notification requirement would achieve nothing without a great deal of extra publicity.

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## APPENDIX 1

### THE TAX FACULTY'S TEN TENETS FOR A BETTER TAX SYSTEM

The tax system should be:

1. **Statutory:** tax legislation should be enacted by statute and subject to proper democratic scrutiny by Parliament.
2. **Certain:** in virtually all circumstances the application of the tax rules should be certain. It should not normally be necessary for anyone to resort to the courts in order to resolve how the rules operate in relation to his or her tax affairs.
3. **Simple:** the tax rules should aim to be simple, understandable and clear in their objectives.
4. **Easy to collect and to calculate:** a person's tax liability should be easy to calculate and straightforward and cheap to collect.
5. **Properly targeted:** when anti-avoidance legislation is passed, due regard should be had to maintaining the simplicity and certainty of the tax system by targeting it to close specific loopholes.
6. **Constant:** Changes to the underlying rules should be kept to a minimum. There should be a justifiable economic and/or social basis for any change to the tax rules and this justification should be made public and the underlying policy made clear.
7. **Subject to proper consultation:** other than in exceptional circumstances, the Government should allow adequate time for both the drafting of tax legislation and full consultation on it.
8. **Regularly reviewed:** the tax rules should be subject to a regular public review to determine their continuing relevance and whether their original justification has been realised. If a tax rule is no longer relevant, then it should be repealed.
9. **Fair and reasonable:** the revenue authorities have a duty to exercise their powers reasonably. There should be a right of appeal to an independent tribunal against all their decisions.
10. **Competitive:** tax rules and rates should be framed so as to encourage investment, capital and trade in and with the UK.

These are explained in more detail in our discussion document published in October 1999 as TAXGUIDE 4/99 (see <http://www.icaew.com/index.cfm?route=128518>).