



# *Failure to Prevent Tax Evasion (The Criminal Finances Act 2017)*

## **AT A GLANCE**

The Act introduces 2 new offences: domestic and overseas.

Both require criminal conduct on the part of the taxpayer.

Both require criminal conduct on the part of an 'associated person'.

The offence is largely based on the Bribery Act 2010, the defence of having reasonable procedures to prevent the facilitation of tax evasion is available.

HMRC:

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.

### **This guidance is:**

A summary of the relevant legislation

Illustrative.

Designed to address FAQs

### **This guidance is not:**

Prescriptive

A checklist

Designed to be one-size-fits-all

Above all the approach taken by firms should be risk based and proportionate. Practitioners should note that the failure to prevent tax evasion offence only applies to bodies corporate (including LLPs) or partnerships, and these entities will need to have reasonable procedures in place to prevent it (see appendix). Although the new offence does not apply to sole practitioners, they still need to be alert to the risks of aiding and abetting criminal tax evasion, as this itself remains an offence.

## Introduction to the new offences

Failure to prevent facilitation of UK tax evasion requires:	Failure to prevent facilitation of overseas tax evasion requires:
STAGE 1: Criminal evasion by a taxpayer AND	STAGE 1: Criminal evasion by overseas taxpayer that would amount to a criminal offence in the UK and the relevant jurisdiction AND
STAGE 2: Criminal facilitation by an associated person of the body corporate or partnership AND	STAGE 2: Criminal facilitation, in the overseas jurisdiction, by an associated person of the body corporate or partnership, where this act would also constitute a criminal offence in the UK and the relevant overseas jurisdiction AND
STAGE 3: A failure of the body corporate or partnership to implement reasonable procedures to prevent the facilitation in STAGE 2.	STAGE 3: A failure of the body corporate or partnership to implement reasonable procedures to prevent the facilitation in STAGE 2.

All 3 of these stages need to be present for the new offences to bite. Note, however, that the criminal actions in Stages 1 and 2 do not require the persons concerned to be actually convicted of criminal evasion or facilitation.

### Definitions

Associated person: anyone who provides services for or on behalf of the body corporate or partnership eg. contractors, agents or employees.

Criminal facilitation: knowingly aiding, abetting, counselling or procuring.

Tax evasion: the illegal non-payment or underpayment of taxes, usually resulting from the making of a false declaration or no declaration at all of taxes due to the relevant tax authorities. For example, deliberately (or recklessly) treating expenditure as tax deductible when it is not, structuring advice known to be for the purposes of tax evasion, and concealing the true nature of income or expenses.

### Scenarios: UK offence

1. *Machin LLP is dealing with the UK tax affairs of a UK individual. The client is fraudulently understating revenue to reduce the UK tax liability. An employee of Machin LLP is knowingly submitting the tax returns of the individual on this basis.*

Since both the client and the associated person (in this case the employee) are acting with criminal intent then Machin LLP will have to demonstrate that they had reasonable procedures (see appendix) in place to prevent this from happening.

- 2. A UK employee of Grundy LLP fraudulently understates the UK tax liability of a client company and diverts repayments to their own bank account. The client is unaware that this is taking place.*

All three elements of the offence are not present since the taxpayer (ie the client company) is not acting with criminal intent. Grundy LLP will still need to consider its Anti-Money Laundering responsibilities. Firms may find it useful to refer to the Professional Conduct in Relation to Taxation (PCRT) guidance in addressing irregularities with HMRC.

- 3. The Waylon Partnership has a client with a complicated capital allowances claim for which the client has independently sought advice from another service provider. Waylon includes the claim in the tax return submitted to HMRC. The claim is rejected.*

There is no evidence of criminality here, in which case the elements of the corporate offence have not been met. Even where it is shown that the client and the other service provider were acting fraudulently it would have to be shown that Waylon knowingly facilitated this fraud in submitting the tax return. Accidentally, negligently or ignorantly facilitating evasion does not constitute an offence under this legislation.

#### **Scenarios: Overseas offence**

- 4. Karlo Ltd has a client operating in a number of overseas jurisdictions including Erewhon, the law of which includes tax offences similar to those in the UK. However, not having expertise in the Erewhon tax code, they refer this aspect of the global compliance work to an agent in that jurisdiction. It later emerges that client employees in the local branch have been colluding with the agent to understate tax liabilities.*

The taxpayer is engaged in criminal evasion, as is the agent. However it is not clear if the agent is an associated person of Karlo Ltd. If this is a subcontracting relationship where Karlo Ltd retain control over the engagement then Karlo Ltd will have to demonstrate that they had reasonable procedures (see appendix) in place to prevent this. Alternatively making a good faith referral or introduction where there is no suspicion of criminality is not an offence under this legislation.

- 5. Drake LLP provides tax services to Oracle Group. Some questions have arisen recently around transfer pricing, with some suggestions that the pricing of intellectual property is being used to distort asset flows. This has resulted in notable mitigation of the tax liability in a particular overseas territory.*

It will need to be established whether the subsidiary has been involved in criminal breach of tax legislation in the overseas territory. Tax mitigation or tax avoidance does not equate to criminal tax evasion. Legal advice may be necessary, especially in the overseas territory, but if the work is properly performed without intent to knowingly assist in tax evasion it is unlikely that the corporate offence will be relevant.

Firms may find it useful to refer to the Professional Conduct in Relation to Taxation (PCRT) guidance in determining what is acceptable when offering tax advice.

- 6. Talia LLP is involved in some mergers and acquisitions work which will result in some assets being transferred to a territory regarded internationally as a tax haven.*

The presence of a tax haven in the proposals does not automatically mean that tax evasion is being committed. Clearly the transaction will need to be assessed for compliance with the tax legislation of the relevant jurisdictions. Even where the transfer is being carried out for the purposes of tax avoidance the offence will not be relevant if this falls short of criminality. However members must comply with PCRT which includes the requirement to 'not create, encourage or promote tax planning arrangements or structures that i) set out to achieve results that are contrary to the clear intention of Parliament in enacting relevant legislation and/or ii) are highly artificial or highly contrived and seek to exploit shortcomings within the relevant legislation'.

Transactions with a genuine commercial purpose generally don't fall within the above,

- 7. Elliot Ltd has a business relationship with a third party contractor (Quinzel) to provide services on their behalf. Quinzel subcontracts part of this work to Isley. Isley is an overseas resident who deliberately omits her fees for this work from her tax return, a practice of which Quinzel is fully aware and is facilitating by paying an offshore company set up in Isley's name, rather than Isley herself.*

Isley is criminally evading tax in her home country. Furthermore Quinzel (an associated person of Elliot Ltd) is knowingly facilitating this evasion. Elliot Ltd will therefore need to demonstrate reasonable prevention procedures (see appendix).

- 8. Damian was employed by Todd LLP as a tax advisor. During his employment he provided services to a client with the intent of facilitating tax fraud on their behalf. Damian has since left his employment but Todd LLP has maintained the business relationship in good faith, without anyone else within the firm having knowledge or suspicion of the client's fraud.*

If an 'associated person' (most likely another employee) of Todd LLP becomes aware of the clients tax fraud and knowingly perpetuates the fraud then they are committing a facilitation offence. Furthermore if they fail to fulfil a statutory obligation such as submitting a Suspicious Activity Report to the National Crime Agency then they may also be liable for the facilitation offence. In either case Todd LLP will have to demonstrate that it had reasonable procedures (see appendix) in place to prevent this from happening.

## APPENDIX: REASONABLE PREVENTION PROCEDURES

The following suggestions are from the [HMRC guidance](#) directed at small and medium entities, supplemented with some specific suggestions for ICAEW members.

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.

A firm 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 '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.
- Having terms in contracts (with employees and contractors) requiring them not to engage in facilitating tax evasion and to report any concerns immediately.
- Providing regular training for staff on preventing the facilitation of tax evasion, which may form part of wider financial crime detection and prevention training. ICAEW members are also required to adhere to the [Professional Conduct in Relation to Taxation guidance](#) (PCRT) which can be included in training programmes. Regular training on the [ICAEW Code of Ethics](#) is also advised.

- Having clear reporting procedures for whistle-blowing of suspected facilitation of tax evasion offences. Firms should already have procedures for reporting suspicious activity to the Money Laundering Reporting Officer (MLRO) which could be adapted for this purpose. ICAEW members should also note that they are required to adhere to the **Duty to Report Misconduct** regulations.
- Carrying out second partner reviews on tax advice given.
- Ensuring their pay and bonus policy/structure encourages reporting and discourages pursuing revenue to the point of condoning tax evasion.
- Having regular reviews of the effectiveness of prevention procedures and refining them where necessary.
- Monitoring and enforcing compliance with prevention procedures.
- Documenting and retaining a record of the above.

Further guidance:

<https://www.gov.uk/government/consultations/tackling-tax-evasion-a-new-corporate-offence-of-failure-to-prevent-the-criminal-facilitation-of-tax-evasion>

[https://www.bdo.co.uk/getmedia/f79fa981-cdce-4fa9-9df9-d857b5709245/Corporate\\_Criminal\\_Offences\\_document\\_June\\_2017.pdf.aspx](https://www.bdo.co.uk/getmedia/f79fa981-cdce-4fa9-9df9-d857b5709245/Corporate_Criminal_Offences_document_June_2017.pdf.aspx)