Funding the Future

Why offshore tax abuse should be a strict liability off...

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There has been much debate in the tax profession about the government's proposal, included in a policy consultation published this week, that failure to declare offshore income and capital gains arising that should have been included in the UK tax return should be considered a strict liability offence in UK law, and therefore be a criminal act whatever the intention or otherwise of the person committing it.

It is important to note with regard to this that whilst at present it is possible for the government to prosecute anyone who fails to declare their income on their tax return their failure to do so is not a strict liability offence. In other words, the government has to prove that they had intention not to disclose the income with the aim of evading tax liability. Mere omission is not enough to secure a conviction and the person's intention does, therefore, matter, meaning that a defence of honest mistake can be made to a court with the possibility, therefore, of a person being found not guilty despite having undeclared offshore income.

It is also important to note that there are quite a number of strict liability offences in the UK. Examples include speeding in a car, driving without insurance, driving whilst disqualified, having a firearm without appropriate authority, and some tax offences including failing to provide information in some situations.

Strict liability offences are, though, an exception; it is generally presumed in criminal cases that there must be an intention to commit the crime - called the mens rea in legal parlance - but this is not necessary in the case of a strict liability offence. In the case of these offences merely undertaking the act is enough to make the act criminal. The issue that then appears to be engaging the tax profession, who are up in arms about this, is that someone who has made a genuine mistake with regard to the declaration of an offshore source of income or gain could now be subject to criminal prosecution as a result.

I find myself in a now familiar paradoxical position in commenting on this issue. The tax profession always likes to side with HMRC against me on matters relating to the tax gap, where they claim that the problem hardly exists, but mysteriously oppose my

support for HMRC when it comes to measures that might assist tax collection. The coincidence cannot go unnoticed: the fact that they lack any hint of objectivity on this issue has to be placed on the record now. They will not like me saying so, but I would suggest that my own comments are on this occasion considerably more objective: I have no vested interest apart from being a tax compliant citizen of the UK in this matter, and it is from that perspective that I will view it, albeit that I will bring the attributes of a chartered accountant with some knowledge of taxation to the discussion.

There are, I think, four main reasons why the government thinks that failure to disclose income and capital gains arising offshore on a UK tax return in which they should have been declared should be a strict liability offence. These are, that in the first instance, those who provide the opportunity for UK resident individuals to undertake activity offshore have a very strong incentive to make sure that the identity of those individuals is not known to the UK tax authority.

I am pleased to note that in saying this the UK government has effectively offered long overdue and welcome recognition to the redefinition of tax havens as secrecy jurisdictions, which I and the Tax Justice Network have promoted for a number of years. I define secrecy jurisdictions as places that intentionally create regulation for the primary benefit and use of those not resident in their geographical domain with that regulation being designed to undermine the legislation or regulation of another jurisdiction and with the secrecy jurisdictions also creating a deliberate, legally backed veil of secrecy that ensures that those from outside the jurisdiction making use of its regulation cannot be identified to be doing so. The new proposal recognises the significance of the second part of this definition and the threat that it poses and that taking advantage of this opportunity can, I think, in itself be the necessary evidence of intent that replaces the need to prove the existence of mens rea.

Secondly, I also warmly welcome the fact that the government has made very clear that many of those who facilitate this offshore tax evasion are themselves actually resident in the UK and use the cover of a secrecy jurisdiction to also disguise this fact. The government's implication is very clear: they do not believe that the chance of mistake is very high in the vast majority of cases, if it exists at all. I agree with them, subject to the point on de minimis limits, noted below.

Thirdly, and again at long last, the government has now finally recognised something **that I said most clearly in June 2009, when I pointed out (following a meeting at the Treasury) that the prospect of a UK government making any significant use of a Tax Information Exchange Agreement was remote in the extreme because it had to have the evidence of the existence of an offshore bank account held by a UK resident person before it could ask the secrecy jurisdiction to provide any information upon it. In other words, as I realised at the time, but they did not appear to, these agreements were utterly useless without a smoking gun, and such smoking guns did not exist. It has taken a**

long time for the government to reach this point of obvious recognition, but at least it has now done so, and as a result recognised that the inherent bias that this creates against HMRC when trying to investigate offshore abuse justifies an increase in liability for the abuser.

Finally, the government also recognises that some jurisdictions are still refusing to consider tax evasion as a predicate offence for anti-money-laundering prosecution purposes and that this is an impediment to information exchange which can be abused, which does again increase the difficulty in securing information on those evading tax, and so justifies increased penalty for those who try to exploit that situation for personal gain.

That then is the government's case, although, as I note below, I think it incomplete. Let's before considering what else needs to be said to support this new law, consider the objections. Leaving aside the rants of those with vested interest, let me offer this more reasoned comment from Pinsent Mason, a firm of leading tax lawyers:

Tax expert **James Bullock of Pinsent Masons said that although the approach set out in the consultation was more measured than the chancellor of the exchequer had implied in April, the proposals could still result in criminal prosecutions for those who simply did not understand tax law.**

"HMRC has more powers in its arsenal — and more funding — than ever before and the tax take through their investigations is at a record level," he said. "Considering the success that HMRC is having in cracking down on tax evasion there doesn't seem to be the public policy requirement for these extra powers."

"The detailed proposals are more moderate than many had feared, but the principle remains that individuals shouldn't lose their liberty and be sent to jail because they have been careless or forgetful or allowed themselves to be misled over what taxes they had to pay. They can already be hit by massive fines," he said.

Let me leave aside the claim on tax recoveries; they are simply made up figures and the amount of cash recovered is vastly less than HMRC claim and so are not worthy of being included in an argument on this issue and instead look at the rest of this comment, and the objection raised.

The first is that a person could be prosecuted for simply not understanding tax law.

The second is that this change is not required because HMRC already have the resources they need to investigate such cases. This is simply blatantly untrue, not just for the reasons that the government has laid out, already noted above, all of which are

true, but also because for any self-respecting law firm to make such representation when it is so obviously contrary to what is actually happening with regards to the level of resources available to HMRC reveals either a total lack of awareness on their part of what is happening with regard to the resource crisis within HMRC or a willingness to be disingenuous that is hardly conducive to their case.

Third, to claim that there is no public policy reason to continuing to crack down on tax evasion because some people have made voluntary disclosure to date is again, extraordinary: the issue is real, ongoing, and a matter of considerable cause of loss to the Exchequer and therefore has to be an issue a public policy.

And finally, the suggestion that carelessness will lead to prison sentences is a gross exaggeration. it is not even clear in the consultation that this is the logical consequence of the new proposal. Scaremongering is not an argument.

Three of these arguments are, on the basis of these comments, not worthy of further consideration: they are, to be candid, complete nonsense. If the profession can come up with nothing better than this during the course of the consultation process then I have little doubt that the proposal will sail through unhindered by their objections. The first does, however, merit slightly more attention.

There is nothing in the proposal made that does actually suggest that a person will necessarily be prosecuted as a consequence of not understanding tax law. Principally that is because suggestion is made that there should be a de minimis limit of lost tax revenue below which prosecution should not take place. This seems a wise, and necessary precaution, meaning that those who are not represented by professional tax advisers who might, as a consequence, have the reasonable defence of not being fully familiar with tax law, are likely to fall out of any risk of prosecution. Those that remain within the scope will either be committing quite significant offences, for which there is no excuse for non-declaration because either scale alone should mean that they should have taken the precaution of making enquiry as to their liability or that they were deliberately hiding their affairs from both their advisers and HMRC, in which case there is, again, absolutely no defence for non-declaration, but the need to prove this intent is avoided, so increasing the chance of successful prosecution against those who deliberately abuse the UK tax system. I would have concern without a de minimis limit: with it I do not.

There is also another fact to consider: speeding whilst driving a car is a strict liability offence but in practice discretion is used on occasion when prosecuting precisely because there are always some margins for error where doubt must play a part. I suspect that this would also be the case in the tax system so that, for example, if a person suffered real incapacity at the time of making the return I would very much doubt that HMRC would prosecute simply because even if, by default, the person would be found guilty of a crime there would, at most, be a token penalty imposed, and therefore no one would seek to bring the charge.

In that case I have yet to find any substance to any of the objections that have been raised by the tax profession to this proposal. But what I would say is that the government has also failed to set out its case appropriately. They have seriously undersold the public policy reason for making this a strict liability offence and I am disappointed in their having done so. This is because I think that their own understanding of the tax system and the way in which it operates is wrong and that their understanding of the reason for tax penalties is also, as a consequence, incorrect. The tax profession simply exploit this fact. These are arguments that I will be developing in much more depth in my new book, The Joy of Tax, but which I will summarise here.

As a matter of fact, and as I have long argued, I think that the vast majority of all taxation is paid voluntarily. HMRC seem to think so as well, having said in recent years that 90% of all taxes are paid in this way (a figure I only dispute because they very obviously, and significantly, understate the tax gap when making an estimate). The existence of the tax gap does not change this argument: it only proves that those who try to avoid or evade the obligation are acting outside the norms that have been created by society, where compliance is the expectation. The reason for laws compelling the payment of tax is not, then, to require anyone to pay, but because some do not conform to the norm that most willingly participate in with regard to payment and, as a matter of fact, it is always the case that criminal law (and all tax non-compliance can, ultimately, be considered criminal under existing arrangements: it is just means rea has to be proved) exists to impose sanctions on those who do not comply with society's norms rather than to enforce a norm upon society. In that case all non-payment of tax, whether as a result of avoidance or evasion, is considered by definition to be non-compliant behaviour, which is precisely why there is so much moral outrage on the issue.

Now it so happens that of all the various types of behaviour that are considered to be unacceptable by society when viewed from the position of the 'normal' compliant taxpayer that of tax evasion by use of a tax haven is often considered the most egregious, a fact that is compounded by the widespread understanding that the use of such places never removes the obligation to declare a tax liability in the case for a UK resident and domiciled person, and that such nondisclosure must, therefore, just about invariably represent a deliberate act on the part of the person undertaking it, coupled with the perception, which is soundly based, that those participating in this abuse do so because they know of the difficulties tax havens put in the path of their crime being discovered.

Put all this together and it is quite clear that there is a very strong public policy reason for the making such abuse the subject of a strict liability offence. Although I am the first to admit that there are many in this country who participate in tax evasion it remains a matter for public opprobrium, and in its more extreme form, as offshore tax evasion is, a matter where significant sanction is sought, and rarely applied. It is the very absence

of that sanction at this extreme of unacceptability that is then take as a suggestion by some that this issue is of limited importance, which conclusion they then use to justify their less egregious abuse and it is that that precise policy reason that this penalty is appropriate.

I am disappointed that the tax profession, which is supposedly so opposed to tax abuse, is so unwilling to recognise this, as I see it, fact.