

# Funding the Future

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*This is the [transcript](#) of the evidence Alex Cobham of the Tax Justice Network and I [gave to Parliament yesterday](#) on the Criminal Finances Bill:*

## Examination of Witnesses

Alex Cobham and Professor Richard Murphy gave evidence.

10.59 am

The Chair: We will now hear evidence from Tax Research UK and the Tax Justice Network. You have until 11.25 am prompt. Even if we are not concluded by then, I will adjourn the Committee because Members have to be over in the House for other business. Would you introduce yourselves and outline the work you do?

Professor Murphy: I am Richard Murphy, the director of Tax Research UK. I am a chartered accountant and also a professor of practice in international political economy at City University.

Alex Cobham: I am Alex Cobham, chief executive of the Tax Justice Network and a visiting fellow at King's College London.

Dr Huq

Q It is a pleasure to serve under your chairmanship, Sir Alan. It is good to have two academics in front of us; I am an academic trapped in an MP's body.

Part 3 of the Bill would introduce the new criminal offence of failure to prevent facilitation of tax evasion. How do you rate the risk posed to the Exchequer by illegal tax evasion? We have just heard the figure of £5 billion a year. Is that accurate? Is it a conservative estimate? What are your thoughts on tax evasion versus tax avoidance and other activities that contribute to the tax gap? What would you say is the true scale of offshore tax evasion?

Professor Murphy: I have probably prepared the only alternative estimate to HMRC's. My estimate is that tax evasion in the UK could be as high as £70 billion a year, in

contrast to the HMRC estimate of £5 billion. Let us put that in the context of a £1.8 trillion UK economy. My estimate of tax avoidance is around £25 billion a year, as opposed to the Revenue's, which again is around £5 billion. I believe its estimates are wrong. I think this Bill is focusing heavily on types of tax evasion that are a small part of the problem. The biggest part of the problem is the domestic economy; the biggest risk within the domestic economy is the fact that HMRC does not collect tax returns from 1 million UK domestic companies a year. The problem is with HMRC in this case.

Alex Cobham: We find Richard's analysis rather more compelling than HMRC's on the tax gap in general. Perhaps the difference is that we consider the international avoidance element to be particularly badly treated in the HMRC methodology. In some ways, if all your estimates are lower than they should be but in proportion, that is not a big deal, because it is not telling you to go the wrong way, but if your estimates of avoidance are significantly depressed compared with your evasion estimates, and you then put your policy emphasis according to those bad estimates, that does matter. I think we would be concerned that the tax gap is not a neutrally wrong estimate; it drives attention towards evasion rather than avoidance. We think evasion is important-certainly Richard's numbers show that-but we are concerned that it encourages HMRC to take avoidance less seriously, and that is a risk.

Dr Hugo  
Q Several stakeholders who responded to the HMRC consultation-these clever people who know how to get around the rules-argued that a new corporate offence was unnecessary. It sounds as if you take issue with that. Do you think there is enough in the Bill to provide the significant behavioural change that is really needed to drive this out?

Alex Cobham: I think the behavioural change question is really important. There are two elements of it: one is how directly it affects the behaviour of actors involved in the process, but the second is how it affects the wider behavioural change. Over the years, we have had any number of economic models of tax behaviour, all of which have suggested that, in country after country, if we were rational economic maximisers we would be much more abusive about tax than we actually are. The reason for that is that we do not respond just to the risk of being caught and the price of being caught. Paying tax is a social act, and by and large two things drive people's tax compliance. One is the extent to which tax revenues are redistributed and seen to be redistributed in a fair way-the more you think that, the more likely you are to contribute. The other is your perception of other people's compliance. If you think that the people at the top-the big companies and wealthy elites-are systematically not paying their fair share, the prospects of you complying as a normal citizen are much lower. Who wants to be the only mug if the big guys are not playing the game?

There is one thing that I think is really important for the Bill. On the technical side we can have concerns about how it is framed, and on the enforcement side we might have concerns whether the resources are actually there to make it happen, but what is

perhaps missing from that discussion is whether or not we have consistent reporting about the performance under this measure. If, year on year, we hear HMRC saying, "This is our estimate of the tax gap in this area. This is the amount of evasion we have stopped and the number of prosecutions, the revenue at risk in that area," then, "This is the number of those cases where we have also gone after the facilitator, and so this is the proportion where we are consistently tracking this all the way through," what you do, apart from giving HMRC a useful metric to demonstrate progress—if HMRC thinks this is the biggest part of the tax gap, then clearly it needs to be tracking this, showing the reduction over time—it also shows the public this is not just one more piece of tax law that may be more form than substance.

Particularly if you think about the Google tax law, for example, there is a growing sense of a lack of trust among the public that when tax laws are passed they are actually meaningful or meaningfully enforced. This is a great opportunity to go the other way, to make sure from the beginning that you will have that accountability and, to go back to your question, to have that in place in a way that is likely to drive behavioural change both of the immediate actors and facilitators but also of the wider public.

Professor Murphy: Can I make three brief points? The first one is that the law as drafted is going to be very difficult to prosecute. We have seen that from the Bribery Act 2010 on which it is based. The number of prosecutions is likely to be very low indeed. This is a strict liability offence—tax evasion triggers the potential liability. The defence provided that is provided is that there are systems in place. That means that the company—the corporate entity that permits the action—has a defence available to it. That defence will largely be available only to the biggest companies. They will have systems that can be easily documented. Most money laundering training systems now in place in large companies will provide an automatic defence to them: the defence is that they have the systems in place and that there was a bad apple who did the wrong act. Therefore, I think the chance of prosecutions against large companies under this Bill is remote in the extreme. <sup>I think at most this will reinforce the impression that smaller companies are subject to penalty and larger companies are not. First, the chance of prosecution is low because the amounts of money involved will not attract SFO attention—by and large the SFO goes for high-profile cases and there will not be many here that can be prosecuted. Secondly, the behavioural change resulting from this Bill will be very low indeed. There are vastly better ways to achieve behavioural change in this Bill.</sup>

Tristram Hunt (Stoke-on-Trent Central) (Lab)

Q One of the attempts to deliver that kind of behavioural change is among the new clauses I am submitting. Will they garner your support for asking the Secretary of State, for example, to make an annual report to Parliament about unexplained wealth orders, to make it a duty to prevent corruption, and to establish quite swiftly a publicly accessible register of beneficial ownership of UK properties? Do you think the good intentions of the Bill could do with a boost to make sure the foot is on the accelerator on some of this?

Professor Murphy: I would entirely agree with a number of points you make. In fact, I would support all those measures. I do not need to comment further; they would all help.

It is clear that transparency is of enormous benefit. The biggest problem with regard to transparency in this country is that 400,000 companies a year in the UK do not file an annual return with the Registrar Of Companies and do not file accounts as required by law. We have no idea what those companies do. They are struck off. It is assumed they have no tax liability, so it is just assumed they have not traded. That is a completely unreasonable assumption for the registrar to make. HMRC does not pursue these companies. I did some research in 2014 on the recovery of penalties imposed on these companies for non-compliance. More than 99% of the penalties imposed were not paid.

In other words, we have an enormous hole in our economy, so we cannot rely upon these systems of registrars and beneficial ownership. The proposed register of beneficial ownership in the UK is simply a voluntary honesty box arrangement, because there are only four extra people being tasked to monitor it. When 400,000 companies do not even file a return, which is where they would disclose their beneficial ownership data, the chance that we will have reliable information is incredibly low indeed. We have to get down to very basic levels to get this right.

I am not saying that the Bill is wrong, but in terms of direction of effort, parliamentary time and resources, there are many more important tasks that would bring about the behavioural changes that Alex has talked about that would encourage compliance.

**Roger Mullin**  
Q I have been concerned for some time about the Scottish limited partnerships and similar vehicles. To what extent do you think that there are particular types of business formations that are most susceptible to criminal activity and tax evasion?

Alex Cobham: This is one of the interesting features of the Bill. If the Government were a relevant body, I think the continuing provision of Scottish limited partnerships would make it very easy to prosecute the Government for facilitating evasion. The work of Richard Smith and David Leask, who I think will be giving evidence later, is very clear on this point. Something like one in four limited partnerships in the UK, but about two in three of Scottish limited partnerships, are structured in such a way that one of their partners is an anonymous company registered in a secrecy jurisdiction.

That is the perfect model for unaccountable business, unaccountable ownership of assets and income streams that may be criminal. The effective facilitation that the UK provides in that way is simply unacceptable. What is good about this Bill is a very clear recognition that that facilitation is unacceptable; what is missing is application to the Government themselves. I think the only consistent action would be to make impossible the use of anonymous partners for limited partnerships.

Professor Murphy: I agree with all that. I extend the concern to the limited liability

partnership. I have been a partner in limited liability partnerships and they potentially have a very useful commercial role—they are tax transparent in a way that is very important, which is why I used one. The truth is that they are also used extensively by offshore agents, again using anonymous companies, to create structures that look as though they are present in the UK and give them an air of credibility. In fact, they are entirely controlled offshore and can be used for abuse. Both need a significant review. I can see no legal or commercial justification at all for limited partnerships in terms of their current use. Limited liability partnership legislation needs explicit change to make sure that it cannot be abused.

Roger Mullin:

Q You mentioned a review, so I take it that you would support the new clause we have tabled calling on the Government to have a specific review of Scottish limited partnerships?

Professor Murphy: Yes.

Roger Mullin:

Q You have mentioned the issue of money laundering and have given us an estimate of the tax gap. Do you have any estimates of the extent of money laundering in the UK?

Professor Murphy: The money laundering estimates that are available—for example, peer-reviewed work undertaken for the World Bank—would suggest that the UK has a shadow economy of about 10% of GDP. Curiously, that is very consistent with the data reported by HMRC with regard to VAT abuse, where the figure consistently runs at around 10%. It is absolutely impossible that you can lose 10% of VAT and end up with an overall tax gap of 6.4%, by the way. You cannot lose 10% of the top line and yet end up collecting the tax elsewhere. There is no accounting mechanism for that income to reappear in the national profit and loss account to be taxed further down the system—I say that as a chartered accountant. Therefore, absolutely on a basic methodological and logical level, HMRC's estimates have to be wrong, but around 10% is likely. We are relatively low in that figure, by the way; as a contrast, in Germany the figure is 16%.

Alex Cobham: On the money laundering point, an informal or shadow economy of 10% is not out of line with a number of other high-income countries, but at least anecdotally, the number of times that UK vehicles crop up in foreign criminal cases seems disproportionately high. It is true that because the UK has been a leader to an extent in transparency it is easier to do some of this analysis involving UK companies, but that would also be a reason why they should not be used by people committing crimes and yet, they still seem to be. I think you would probably conclude that at the moment, although the evidence is not consistent, it is likely that the UK is disproportionately important in national money laundering. How disproportionately so is completely uncertain and, again, that makes the case for a review.

Professor Murphy: We do have a disproportionate number of companies per head in the UK compared with any other European country.

The Chair: Can I point out that four Members are still asking to get the floor and you have 10 minutes left?

Antoinette Sandbach

Q Professor Murphy, I want to come back to your evidence that the new offence of corporate liability will effectively target small or mid-range companies. In relation to the “bad apple” point you made, do you accept there is still reputational damage for a company if one of its employees is charged, and that that in itself may make big companies’ compliance far more rigorous?

Professor Murphy: That is obviously true. No company wants to appear on the front page of a newspaper and no company wants to be prosecuted. I have spent quite a lot of time in the last year or two talking to large firms of accountants-names you will be familiar with-and large companies about their response to the sea change in public attitude towards tax, and I am reasonably convinced that they have noticed that there is reputational risk to them, and that they are changing their behaviour as a result. To that extent, I feel that this legislation is a little too late, in the sense that they are trying to steer clear of some of these activities as fast as they can. Again, that is a reason why I think the impact will be on smaller businesses. The largest ones will have learnt how to get rid of the risk.

Antoinette Sandbach

Q If I can go back to the smaller business point, I do not know if you were here when I asked Simon York about the other end of the scale. Some tax evasion is not for the purposes of evading tax-the purpose is to evade other liabilities that follow on from declaring taxable income. That can be supported by small accountancy firms that may not apply regulations as rigorously as they should do. Do you think this offence will have a deterrent effect on the smaller and mid-range companies?

Professor Murphy: I think it will. The reason why is that it is a strict liability offence: the existence of evidence of tax evasion is sufficient to prove liability without motive being questioned. That could be important in certain cases. I can think of a very recent example-it has been in the press-where somebody has not paid tax quite deliberately, it seems, out of a company for which they were responsible. It would make it easier to prosecute in those cases. It will have a deterrent effect. I do not have a problem with strict liability offences for that reason. I know many in my profession do.

Nic Dakin

Q You both spoke earlier in giving evidence about the great opportunity to bring about behavioural change or improve compliance. Are there measures we ought to be looking at in this legislation that you would like to see us take the opportunity to put in?

Alex Cobham: I would say it is the reporting of it. If the Bill is seen as having made it on to the books without driving any serious change either in the way that HMRC operates and the extent to which it looks at enablers or in the ultimate prosecutions and revenue recovery, or if there is a perception of that even without that being the case, that is a missed opportunity in terms of how much impact it has. There needs to be a

requirement for consistent reporting of the numbers of prosecutions, and of the transition between prosecution of evasion cases and, for each of them, whether there is a related prosecution of the enabler or not. If the second number is a very small fraction of the first number consistently, there needs to be space to come back and review, but at least having that will drive attention.

Professor Murphy: I would make the non-provision of accounts and a corporation tax return a strict liability offence for tax evasion under the terms of the Bill. I would also require a provision that is very similar to one we are demanding internationally, which is that banks simply report each year to HMRC which companies they provide services to.

We will next year be in the absurd position that HMRC will get more information on a company owned by a British person in the Cayman Islands than they will on a company owned by a British person in Stockport, because there is automatic information exchange from the Cayman Islands and there is not within the UK. If banks were required to provide information to HMRC on which companies they provide services to and the simple value of sums deposited in a bank account each year, we would know which companies were trading and therefore which were due to file accounts and which were due to submit a corporation tax return. Failure to submit would be a strict liability offence. Nothing would scare the accountancy profession or small company directors more than that. Make them personally liable for the tax not paid at the same time and you have solved the problem of tax evasion virtually overnight. It is simple.

**The Chair** We have only five minutes left, so I will ask the three Members who want to speak to ask their questions first, and then you can reply. You will get a copy of the minutes, which will include any questions that you did not have time to answer.

**Victoria Atkins** Q Professor Murphy, there is good precedence in the world of health and safety, where companies are prosecuted for causing workplace fatalities and accidents or bringing about an environment in which they occur. Do you agree that that success in health and safety bodes well for sending out the message to corporate entities that tax evasion is not permissible and will be prosecuted where evidence of it exists?

**Richard Arkless** Q Professor Murphy, you have highlighted the difficulty with the Bill's proposals on tax evasion in relation to corporate economic crime. Your solution would be a position of strict liability. Do you see any case to extend the provisions on corporate economic crime beyond tax evasion, leaving aside the problem of strict liability and enforcing it? Is there a case, for example, to extend the provisions to catch people who rig the LIBOR market, or perhaps mortgage brokers who fraudulently completed application forms that caused the mess we are in? Do you think there is a case for extending corporate economic crime beyond facilitating tax evasion?

**Peter Dowd** Q Oh resources for agencies-enforcement or otherwise-in relation to prosecutions and

chasing up, do you believe that the authorities have sufficient resource to do their job, or are they just misdirecting the resources that they already have?

**The Chair** You have only two or three minutes to answer, so please be very brief. If you want to give fuller answers to Members, you can write to the Committee Clerk and we will make sure that all Members get a copy.

Professor Murphy: One brief answer—yes, it is effective. I think there are more effective mechanisms available but I am not disputing it has a behavioural consequence. I am afraid I am not expert enough to comment on the other areas. I simply am not an expert on mortgage fraud or LIBOR in that area. I am a tax specialist not a criminal finance specialist.

Does HMRC have enough resource? No, clearly, it does not. It needs to have a lot more resource and to be seen in local communities so that people realise that the threat is personal in that sense, but it is going in the wrong direction of travel at present. It is the risk of being caught that changes behaviour at the criminal end of activity, and transparency would expose that. That is why I think creating the smoking gun of information is the critical measure that needs to be taken to give HMRC a chance to identify those who are creating most risk.

Alex Cobham: We have a report out with the Public and Commercial Services Union, being launched across the road this afternoon, that says exactly that HMRC neither has enough resources and nor are they appropriately allocated to deal with the relative prioritisation that we think it should have.

**Mr Wallace** Q The ARIS scheme allows HMRC, the investigators and the prosecutors to keep 50% of the proceeds of any confiscation. If the Bill leads to further confiscation, would you say that therein lies some of the solution that you are going to highlight across the road? If they will be able to keep what they recover, will unexplained wealth orders, for example, or seizures improve their budgets?

Alex Cobham: That seems potentially helpful, but I think you would be wise to look at the bigger question of whether HMRC is appropriately resourced given the bang per buck that it actually gets in different areas, rather than having just that one measure in mind.

Professor Murphy: I would rather have no crime and no proceeds than fund collection through increased recovery.

**Mr Wallace** Q Unlike Corbyn economics, we live in the real world.

Professor Murphy: But it is the wrong direction of travel.

The Chair

I thank the witnesses for coming to answer Members' questions. If you wish to give fuller answers, please submit them to us in correspondence.