Analysis

Tax transparency round up

Speed read

Over the next two years, many taxpayers will find that they are spending more time and resources providing information to HMRC, some of which will be shared with overseas authorities under tax information exchange agreements; and, under country by country and tax strategy requirements, making available information about how they structure their tax affairs. Taxpayers will also face the risk of increased penalties for failing to comply with new measures designed to tackle tax evasion, such as the corporate offence of failing to prevent tax evasion. They will have to consider seriously how this will affect their communications with customers and investors.

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Over the next two years, taxpayers will find themselves facing a wide range of measures designed both to give tax authorities more information on a global basis and also to reassure the public that multinational companies and high net worth individuals are paying the right amount of tax. Taxpayers can be forgiven for struggling to keep track of the multiple requirements. This article provides a digest of key legislation and deadlines.

Tax information exchange (TIE) agreements

UK financial institutions (FIs) were required to report to HMRC under both FATCA and the International Tax Compliance (Crown Dependencies and Gibraltar) Regulations, SI 2014/520, by 31 May 2016; and thereafter annually on the same date under FATCA and the Common Reporting Standard (CRS) and/or the EU Directive on Administrative Cooperation in Tax Matters (DAC). Broadly, other than where a UK FI has no overseas account holders, all FIs can expect to be subject to reporting requirements from 2017, if not earlier.

FIs should consider the differences between FATCA and the CRS/DAC provisions; in particular, the interpretation of 'controlling persons'. Under FATCA, controlling persons of corporate entities are typically interpreted as shareholders owning more than 25% of the shares. However, the OECD Commentary states that where no shareholders own over 25% of the shares, the controlling person of the entity will be the natural person(s) who hold(s) the position of senior managing official. The OECD Commentary on the CRS should also be considered when implementing the DAC. (See the OECD *Standard for automatic exchange of financial account information in tax matters*, commentary on section VIII para 132.)

Consequently, individuals holding senior positions at companies may have to be reported, even where they have no shareholding in the entity which they manage. This may come as an unwelcome surprise. Under the CRS/DAC, the expectation is therefore that there will always be one or more controlling person(s) of a company; and the number of people brought into the reporting net will expand significantly.

Client notification regulations

In addition to information flowing *out of* the UK, HMRC has also produced draft client notification, whereby FIs and specified relevant persons (those who give financial or legal advice as part of their business) will have to write letters to clients (and former clients) in a form partly prescribed to explain that HMRC will be receiving information *from* overseas tax authorities about their offshore assets. The letters will have to enclose a document under HMRC branding. In essence, HMRC expects FIs and tax advisers to put pressure on taxpayers.

The draft regulations are intended to implement the client notification obligations contained in FA 2013 s 222(2)(ca), inserted by F(No. 2)A 2015 s 50. The provisions of s 222(2)(ca) impose obligations on certain financial institutions and on 'specified relevant persons' to give 'specified information' to 'clients or specified clients'.

HMRC therefore intends to use FIs and advisers to reinforce the message that TIEs are, in the main, reciprocal; and it clearly expects that a letter from an adviser or FI will effect a behavioural change on taxpayers. The obvious question is: what capacity do tax authorities have to interrogate the data they will receive?

Use of taxpayer data received by authorities

HMRC has a clear strategy for data from TIEs. It will process data using Connect software, supported by a team of specialist data analysts and HMRC inspectors. The software operates in two environments: the 'telescope'; and the 'microscope'. The 'telescope' interrogates data from multiple sources and identifies patterns or anomalies. Inspectors take these results under the 'microscope' to build pictures of taxpayers' affairs, identify risks and open enquiries.

Outside the UK, however, residents in certain jurisdictions may have greater concerns than mere tax enquiries. For example, some individuals hold assets overseas for privacy and security purposes, owing to the risks of kidnapping or extortion in their home country. It is important that these people understand what information will be reported and to whom, and how it may be used in their home jurisdiction. There is already an indication that individuals are changing tax residency as a result of such concerns.

HMRC's strategy for tackling offshore non-compliance

With the advances in TIEs and the ability to handle large volumes of data, HMRC's approach to individuals with offshore compliance issues has hardened. Beneficial disclosure facilities, such as the Liechtenstein disclosure facility, have closed; and although a new offshore disclosure facility is in the pipeline, it is not expected to include beneficial terms. HMRC has instead promised a tougher environment to encourage future compliance.

The introduction of the offshore asset 'move penalty' (contained FA 2015 s 121 and Sch 21) from 27 March 2015 means that individuals can already be subject to penalties of up to 300% of the tax loss in relation to their offshore assets. Finance Bill 2016 includes measures that go even further, including:

- a criminal offence for offshore tax evasion: HMRC will no longer need to prove intent to commit the offshore evasion (TMA 1970 ss 106B–106H);
- an asset based penalty: 10% of the value of the asset, in addition to existing penalties (FB 2016 s 153, Sch 22); and
- publishing details of deliberate tax defaulters: FA 2009 s 94 is amended, and existing safeguards will only apply to unprompted disclosures.

These measures will only apply where the loss of tax exceeds £25,000 in a tax year, but those who deal with high net worth individuals will know how complex their clients' tax affairs can be. The £25,000 threshold could easily be broken in one transaction, and the seriousness of the sanctions means they must be considered for any advice or services.

Finance Bill 2016 also introduces tougher measures not limited by the £25,000 threshold. The minimum level for some offshore penalties will increase by 10%. Taxpayers will also be required to give a full account of the evasion to achieve full penalty reductions, e.g. details of anyone who facilitated the evasion. We await the draft statutory instrument to give effect to the FB 2016 measures, but taxpayers should review their offshore arrangements and correct offshore compliance issues without delay.

Notwithstanding the enhanced penalty regime on taxpayers, HMRC is also seeking to tackle all aspects of what it sees as the chain of evasion by introducing new civil and criminal offences.

Civil penalties for enablers of offshore tax evasion

Finance Bill 2016 introduces penalties for persons who knowingly enable taxpayers to carry out 'offshore tax evasion or non-compliance'.

An enabler is defined as a person who 'encouraged, assisted or otherwise facilitated' the taxpayer. The enabler can suffer a penalty of up to 100% of the tax loss, where the taxpayer is convicted of an offence or charged a penalty in relation to an offshore matter. The penalty can be for a careless or deliberate taxpayer error, which could give rise to significant disparities between the taxpayer and enabler penalties.

Where the loss of tax exceeds £25,000 in a tax year, or an enabler suffers five or more penalties in five years, HMRC will be able to publish details of the enabler, its business and the penalty. This would be likely to cause significant reputational damage.

Enablers will be able to mitigate the impact by disclosing details of the evasion, but this will likely present challenges with regard to client confidentiality and conflicts of interest where both the enabler and taxpayer make disclosures.

Corporate offence of failure to prevent the criminal facilitation of tax evasion

The second consultation on this offence will close 10 July 2016, with the offence expected to come into force at some point in 2017. As drafted, the offence would apply to a 'relevant body', including corporates and partnerships, if a person associated with the relevant body commits a UK or foreign tax evasion facilitation offence. Associated persons include those providing services on behalf of the relevant body (employees, agents and subsidiaries). There is also a requirement to look past the contractual arrangements and to consider all the facts and circumstances when identifying associated persons.

A UK tax evasion facilitation offence occurs when an associated person facilitates the evasion of UK tax. The relevant body can be in the UK or abroad. A foreign tax evasion facilitation offence occurs when an associated person facilitates the evasion of tax in a foreign country.

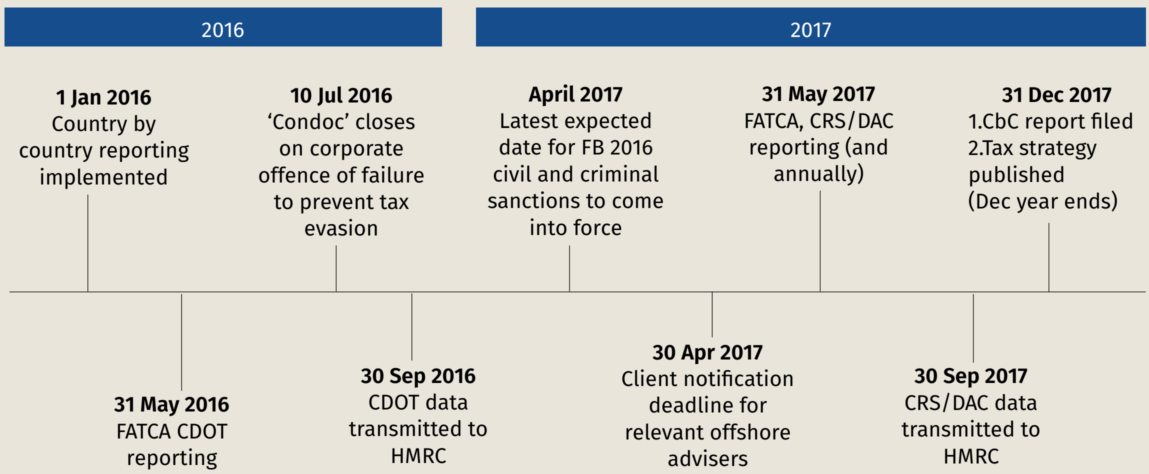
The defence against the offence will be to have reasonable procedures in place to prevent associated persons from criminally facilitating tax evasion. HMRC's draft guidance for developing procedures is based around six key principles, including that of proportionality as to what reasonable procedures are.

HMRC has been quick to point out that the guidance is neither prescriptive nor a 'one size fits all'. The onus is on the relevant body to prove that its procedures are reasonable. Ultimately, it will be up to the courts to decide, based on the facts and circumstances.

Other data sharing measures: making information public

In addition to the above measures, corporate taxpayers are also being required to make other data available either directly to HMRC or to which HMRC will have access.

Timeline of transparency measures



Again, the rationale is to enforce greater transparency and, in some cases, to make such details public.

Country by country reporting

Legislation was introduced in FA 2015 s 122 to enable the making of regulations to implement country by country (CbC) reporting. The Regulations obligate multinational enterprises with parent entities resident in the UK, and with consolidated group revenue of £586m or more in a 12 month accounting period, to make an annual CbC report to HMRC for the following period. The obligation to file applies to accounting periods starting on or after 1 January 2016 and reports must be filed no later than 12 months after the related period.

Pressure from EC to make CbC reporting public

Although the original expectation was that reports would not be made public, the European Commission issued a press release on 12 April 2016 proposing that large multinational companies should disclose publicly the income tax they pay within the EU, on a country by country basis. In addition, groups would be asked to disclose how much tax they pay on the business they conduct outside the EU.

Publication of UK tax strategy

Finance Bill 2016 will require large businesses to publish a UK tax strategy document on an annual basis. In March, HMRC published draft guidance (see www.bit.ly/1NWrpJX) and expanded on what it might expect to see within a tax strategy to meet the four requirements detailed in the legislation, namely:

- the approach of the UK group to risk management and governance in relation to UK tax;
- the attitude of the group to tax planning, insofar as it affects UK tax;
- the level of risk appetite for UK tax that the entity is prepared to accept; and
- the approach of the group towards its dealings with HMRC.

This draft guidance also considers multinational enterprises (MNEs). An MNE group is defined as a group which is subject to CbC reporting (or that would be if the head of the group were based in the UK). HMRC has indicated that UK subsidiaries of MNE groups will therefore be caught by the requirements of the tax strategy legislation, irrespective of the size of the UK group. The strategy must be published by the end of the accounting period starting on or after the date of royal assent of Finance Bill 2016.

Where does this leave us?

With new initiatives being driven by governments and the OECD, tax transparency is a rapidly developing area. Businesses must have the correct operational framework in place to deal with reporting, but these new measures mean they also need to review internal procedures and relationships with third parties. Individuals should be reviewing their offshore arrangements and correcting any compliance issues before tougher sanctions bite. ■

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