New corporate criminal offence: Failure to prevent tax evasion

From 30 September 2017 it is a criminal offence if a business fails to prevent its employees or any person associated with it from facilitating tax evasion. Businesses need to consider the implications of this new offence and what action they need to take to minimise their risk of exposure.

Background

The UK government first announced its intention to introduce a new corporate offence of failing to prevent tax evasion (FTP) in spring 2015. Since that time, the government has held two public consultations. The offence is being introduced as part of the Criminal Finances Act, which received Royal Assent on 27 April 2017. It took effect from 30 September 2017.

The offence

The legislation creates two new offences. The first offence applies to all businesses, wherever located, in respect of the facilitation of UK tax evasion. The second offence applies to businesses with a UK connection in respect of the facilitation of non-UK tax evasion.

The FTP offences apply to both companies and partnerships. They effectively make a business vicariously liable for the criminal acts of its employees and other persons “associated” with it, even if the senior management of the business was not involved or aware of what was going on.

There are two stages for the new corporate offences to apply:

1. Criminal tax evasion (and not tax avoidance) must have taken place; and
2. A person/entity who is associated with the business must have criminally facilitated the tax evasion whilst performing services for that business.

Associated persons are employees, agents and other persons who perform services for or on behalf of the business, such as contractors, suppliers, agents and intermediaries.

For either of the offences to apply, the employee or associated person must have criminally facilitated the tax evasion, in its capacity as an employee or associated person, providing services to the business. A business cannot be criminally liable for failing to prevent the facilitation of tax evasion if the facilitator was acting in a personal capacity.

If stages 1 and 2 above have occurred (there has been criminal tax evasion that has been criminally facilitated by a person associated with the business), the business will have committed the new FTP offences.

A defence of reasonable prevention procedures

A business will have a defence if it can prove that it had put in place reasonable prevention procedures to prevent the facilitation of tax evasion taking place (or that it was not reasonable in the circumstances to expect there to be procedures in place).

HMRC has published guidance on the offences, in which it explains that there are 6 guiding principles that underpin the defence of having reasonable prevention procedures:

- Risk Assessment;
- Proportionality of risk-based prevention procedures;
- Top level commitment;
- Due diligence;
- Communication (including training); and
- Monitoring and review.

A business will have to undertake a risk assessment to identify the risks of facilitation of tax evasion within the organisation and the potential gaps in the existing control environment. The risk assessment should be documented so that it can provide an audit trail to support any policy decisions regarding the implementation of new procedures to reduce the risk of exposure to FTP.

It is expected that following a risk assessment most businesses will have to introduce changes to ensure that they have robust procedures in place to prevent their employees, service providers, agents, suppliers and customers from engaging in or facilitating tax evasion.

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It will be important to secure top level commitment from a company’s board and/or senior executives about the risks of exposure to FTP and the need for the business to respond to the new offences with Anti-Facilitation of Tax Evasion (AFTE) procedures.

Businesses will also need to ensure that sufficient training on AFTE is provided to all staff.

Territoriality

As noted, there are two separate offences which apply where UK and non-UK tax respectively is evaded.

In relation to UK tax, the offence will apply to any company or partnership, wherever it is formed or operates.

Where non-UK tax is evaded a business will commit an offence if the facilitation involves a UK company or partnership, any company or partnership with a place of business in the UK (including a branch), or if any part of the facilitation takes place in the UK. In addition, the foreign tax evasion and facilitation must amount to an offence in the local jurisdiction and involve conduct which a UK court would consider to be dishonest.

Distinguishing avoidance and evasion

As noted, the offences only apply when there has been fraudulent tax evasion. Essentially, fraudulent evasion occurs where a person knows he has a tax liability and forms a dishonest intention not to declare it. It does not arise where a person makes a mistake or is careless. It also doesn’t apply where a person actively seeks to avoid tax, even if the planning in question does not work, provided that the person has an honest belief when filing his tax return.

Equally the facilitator must have a criminal intent – and thus be an ‘accomplice’. At its simplest, the facilitator knows that he is helping another person to carry out a fraud. Unwitting facilitation of tax evasion is not enough. Nor would knowing facilitation of tax avoidance be enough.

Action to be taken

The proposals could have serious implications for all businesses. Although businesses, such as banks, fiduciaries and professional service firms may on the face of it be exposed to a higher risk of the facilitation of tax evasion, the offences are expected to increase compliance requirements across all business sectors. Businesses are likely to have to conduct more due diligence in relation to their suppliers, contractors and employees and will probably have to look much more closely at where and the manner in which payments are made for goods and services, especially if offshore accounts are involved or payments are made in cash.

All businesses should be taking action now to ensure that they are aware of and have control over how their employees, agents or service providers are operating to reduce the risk of exposure to FTP offences.

Aside from the possibility of incurring a heavy fine, a successful prosecution under either of the new offences could give rise to serious reputational damage for an organisation and is not something that businesses can afford to overlook.

How can we help?

Pinsent Masons is a leading international law firm and is the only firm with tax and anti-bribery and corruption compliance teams that received Band 1 rankings in the Legal 500 rankings and Chambers for 2016. We also recently represented a client under the first prosecution brought under section 7 of the Bribery Act - the “failure to prevent” offence. This means that we are ideally positioned to help your business comply with AFTE.

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