

Modernising Powers, Deterrents and Safeguards: Tackling Offshore Tax Evasion

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The Society of Trust and Estate Practitioners (STEP) is the worldwide professional body for practitioners in the fields of trusts and estates, executorship and related issues. STEP members help families secure their financial future and protect the interests of vulnerable relatives. With almost 6,000 members in the UK (and over 15,000 members around the world), STEP promotes the highest professional standards through education and training leading to widely respected professional qualifications. Many of our UK members are actively involved in preparing HMRC returns for their clients as part of their trust and estate practices.

STEP welcomes the opportunity to respond to HMRC's Consultation Document 'Modernising Powers, Deterrents and Safeguards: Tackling Offshore Tax Evasion'. STEP condemns tax evasion as a criminal act. In this context we have worked positively with the EU over the past year or so in helping to develop workable proposed reforms to the Savings Tax Directive in areas such as the reporting of interest payments to trusts. We look forward to working in a similarly positive fashion with HMRC on developing the proposals which are the subject of the current consultation.

We are concerned that the Consultation Document does not seem to differentiate between "historic" offshore tax evasion and the potential for offshore evasion in future. Although, we understand that the Offshore Disclosure Facility and the New Disclosure Opportunity may not have generated the yields expected by HMRC, we would expect that, to a large extent, the historic dimension of the use of overseas jurisdictions in tax evasion should be adequately dealt with by the Liechtenstein Disclosure Facility. As far as the future is concerned, as a result of the introduction of all crimes anti-money laundering legislation by most reputable offshore jurisdictions and the entry into force of new tax information exchange agreements/double tax treaties by these jurisdictions, we would expect offshore evasion to be less of an issue in future.

We do not think that the enhanced penalty regime and the bank notification regime are, in these circumstances, a proportionate response, but if the proposals are to be introduced they should not apply to any jurisdiction which has both all crimes anti-money laundering legislation and a tax information exchange agreement with the UK (or double tax treaty with equivalent provisions).

STEP members, including those working outside the UK, are committed to assisting their clients to pay the correct amount of tax wherever their assets are located.

We give below our responses to the specific questions in the Consultation Document. We should note that some of our responses mirror those we gave on similar points to the recent HMRC consultation on reforms to DOTAS.

Chapter 2

1. Are these the right design principles for this work? In applying these principles, are there other matters that should be taken into account?

We welcome the explicit recognition in the design principles that powers and statutory obligations should be easily understood, straightforward and proportionate. Among the safeguards for taxpayers we would like to see equally explicit recognition that compliance costs should be as low as possible, tax mechanisms should not interfere with legitimate business and savings activity and also that taxpayers have the right to arrange their affairs in a tax efficient manner within the law.

2. Have we identified the correct principles? Do you think these principles will be effective and influence behaviour?

We think it is appropriate that the level of disclosure required from an offshore investor is commensurate with the difficulties faced by HMRC in obtaining tax related information from the jurisdiction invested in.

Chapter 3

1. Is this a reasonable approach to defining offshore non-compliance, or are there other categories of behaviour that should be included in the definition?

STEP does not agree that offshore non-compliance should *per se* be seen as deliberate. This would be particularly harsh given the practical problems highlighted in our comments in relation to Chapter 4. Non-compliance may well arise accidentally and unintentionally.

The graded system of penalties in FA 2007 Sch 24 is in our view a good one. We fail to see why use of an offshore jurisdiction should attract a higher penalty than onshore evasion. Why is the use of an offshore jurisdiction any more “deliberate” than say, hiding money under a mattress in the UK or not declaring profits from illegal UK activities such as drug dealing? All these should attract the same level of penalty in accordance with Sch 24. To introduce different rules in relation to offshore evasion may constitute a breach of EU law.

Defining offshore non-compliance as the holding or transfer of assets outside the UK on which tax due is not declared or paid is a reasonable approach that captures the relevant categories of behaviour. However, we are concerned about the width of the statement in paragraph 3.10 of the Consultation Document that “the transfer of UK income and gains offshore without the intention of paying the tax due would also fall into the definition of offshore non-compliance and, would attract the new penalty provision”. Whilst we would agree that the transfer of UK income and gains offshore should not be used to avoid paying any UK tax due in relation to the period whilst they were in the UK or on any income and gains generated whilst they are held offshore, we do not agree that the individual’s intention at the date of the transfer should determine whether a penalty arises or not. Whatever the position at the date of transfer, the individual may still decide to declare all his income and gains in a full self assessment tax return filed by the due date and pay the tax due.

2. Do respondents agree that the new penalty should apply to all taxes?

Yes. We also agree that there is a need to maintain public awareness about the consequences of non-compliance.

Chapter 4

1. Should accounts held in a non-individual capacity (e.g. as a nominee, trustee, treasurer etc) fall within the scope of what is proposed?

We agree with HMRC’s assessment that the primary risk of tax evasion through the abuse of overseas bank accounts arises from individuals. As Chapter 5 notes, there are already reporting requirements in place in many circumstances for financial structures such as non-resident trusts. In that context we believe placing additional reporting requirements on, trustees, etc would be disproportionately burdensome. However, we would agree that where a UK taxpayer has a bank account held on his behalf by a nominee or bare trustee, the taxpayer should fall within scope of the proposals.

2. If not, how should the tax risk associated by these accounts be addressed?

We believe that the tax risk associated with these accounts is adequately addressed by the current reporting arrangements.

3. How should joint accounts be treated?

We believe that joint accounts highlight some of the practical difficulties taxpayers could face under the current proposals. For example, one joint account holder may be a UK taxpayer who in practice has little to do with the day to day running of the account which is instead effectively managed by the other joint account holder who is not liable for UK tax. While

accounting for UK tax due at the end of the year may be relatively straightforward in such circumstances, imposing a new requirement to report when the account in question (which may be one of several) takes the UK taxpayer above an aggregate balance of £25,000 may well result in significant additional compliance costs.

4. Are there further safeguards that should be considered?

While we applaud the desire to minimise compliance costs by requiring only one-off notification of a new overseas account or notification when the aggregate of overseas accounts exceed a set limit rather than requiring annual filing, we believe the requirement to report within 60 days when the aggregate of overseas accounts moves above the set limit could result in a significant amount of unintentional non-compliance due to the practical difficulties this will entail both due to exchange rate movements and the fact that banks report to account holders at different times. It may be preferable to simply require the reporting of all new overseas accounts in the designated jurisdictions at the end of the relevant tax year.

5. Are these the right criteria for classifying jurisdictions?

These appear to be plausible criteria for classifying jurisdictions although it is not clear which countries would fall within Group C as the criteria for Groups A and B seem to leave no scope for others. However, the listed criteria for classifying jurisdictions makes no mention of how jurisdictions which have robust all-crimes anti-money laundering legislation in place would be treated and this should be taken into consideration in classifying jurisdictions.

We feel that the list of jurisdictions should be set out in a statutory instrument as amended from time to time. It will nevertheless be important to make the public aware of the up to date list of which jurisdictions are in which group alongside the dates of any changes. To reduce unintentional non-compliance it will also be important to have regular publicity campaigns aimed at savers who may have bank accounts in the relevant jurisdictions requiring disclosure.

6. Are there other criteria that could be introduced to help target the requirement on where there is the greatest tax risk?

No.

7. Should other types of account fall within the scope of the notification requirement?

To minimise market distortions, there may be a case for examining whether “investments” with insurance companies, financial institutions, hedge funds, etc. as well as bank accounts should be brought within the proposals.

8. Is 60 days a reasonable period within which to expect an account holder to make a notification?

Taxpayers may find the requirement to report within 60 days very difficult to comply with where they need to aggregate a variety of accounts (some of which may be held jointly with others) in different currencies with different banks. Banks with no direct connection to the UK are unlikely to change their current reporting systems to enable customers to meet these distinctive UK reporting requirements. Even banks with substantial UK operations may find it difficult to amend their IT systems and processes in order to be able to accommodate this proposal and the associated costs of doing so may be quite significant.

9. Is this notification process the right response to the problem HMRC has identified?

Subject to the concerns we express at the beginning of this response, while in principle a notification process is a valid response to the problems identified, as we highlight in our other responses we foresee substantial practical problems with the notification process currently envisaged. We are also very concerned about the potential for inconsistency and multiple reporting requirements given the overlap between the proposals in this Consultation Document and the proposals on extending DOTAS to “offshoring schemes”.

10. Are there any unintentional or unduly onerous circumstances in which a notification could be triggered?

We have already noted the potential impact of sharp exchange rate fluctuations and the circumstances in which, for example, a UK taxpayer with a joint account overseas is not in practice the main day to day user of that account. We would also note that quite often overseas banks accounts will be used to deposit large sums temporarily before, for example, purchasing an overseas property. Notifications in these circumstances may prove both burdensome and of little practical benefit.

11. Are there further safeguards that should be considered?

It may be both less onerous for taxpayers and administratively convenient for HMRC if reporting was only required if the aggregate value of accounts went above a set minimum such as £25,000 for a period of time such as three or six months. This would avoid many of the problems associated with currency fluctuations or large one-off cash transfers connected with issues such as property transactions while posing little or no additional threat to the revenue base.

12. Is this proposed penalty model a proportionate response to the problem HMRC has identified?

As we have noted, in the scheme currently outlined it is easy to envisage taxpayers inadvertently moving above the declarable limits for Group C jurisdictions for relatively short periods. The proposed penalty regime does not look proportionate in such circumstances.

13. Would any further safeguards would be appropriate for remittance basis users when implementing this policy?

It is appropriate that remittance basis taxpayers should not be required to notify their overseas accounts under the current proposals. The issue of what requirements should apply to those who arrive in or leave the UK during the tax year will need to be addressed and this will depend on how the current uncertainties surrounding the acquisition and loss of residence status are resolved.

Chapter 5

1. Is there scope for aligning the information requirements on offshore assets for IHT, CGT and income tax?

We suggest that the reporting requirements in relation to settlements should be consolidated so that the delivery of one account (by a UK domiciled and resident settlor or if appropriate his adviser) could satisfy the requirements for both IHT and CGT as there is currently duplication of reporting. We welcome the confirmation at paragraph 5.16 that there will be no new reporting requirements in relation to remittance basis taxpayers.

2. Is there a case for extending existing information requirements on non-resident trusts?

We do not agree that there is “a clear potential for non-resident trusts to be used as vehicles for tax evasion” (paragraph 5.2). As the Consultation Document makes clear, there are significant reporting requirements already placed upon non-resident trusts, including the need to report details of assets transferred into a non-resident trust, the settlors and trustees. Those wishing to hide overseas assets are therefore far more likely to use other investment vehicles, as we noted in response to Question 7, Chapter 4.

There would also be significant practical difficulties in extending existing information requirements to non-resident trusts. For example, paragraph 5.7 refers to the possibility of the draft Savings Tax Directive requiring paying agents to indentify trust beneficiaries. Paying agents typically do not have this information. Furthermore identifying the relevant beneficiaries of a trust can be extremely complex since, the long term nature of trusts means that trust instruments are typically drafted very widely. Some or all of the stated “beneficiaries” may, or

may not, ultimately receive any funds. This raises the danger of substantially increasing compliance costs and increasing substantially the number of reports where no tax liability will arise which can only raise HMRC's administrative costs.

In relation to trusts which have been set up with full disclosure in another jurisdiction, eg the US, there may have been no UK connection for many years before a beneficiary moves to the UK. Such beneficiaries may or may not receive benefits whilst in the UK and to extend UK reporting requirements to such trusts would be unwarranted and unnecessary. The present system of putting the onus on the beneficiary to disclose distributions and benefits received from the trust which are taxable in the UK seems a fairer one.

Requiring non-UK resident trustees to provide information may also run contrary to duties of confidentiality imposed on them by their respective domestic jurisdictions. The problems posed by such requirements would be compounded if there were a mix of UK and non-UK beneficiaries.

3. Are there any further safeguards which should be considered?

There may be a case for introducing penalties for settlors who fail to meet their reporting obligations.

4. How practicable would a requirement be for UK resident settlors to notify HMRC of transfer values into non-resident trusts or subsidiary companies of such trusts?

Paragraph 5.14 of the Consultation Document raises the possibility of introducing a new requirement on UK resident settlors to notify HMRC "every time they transfer value into a non-resident trust". Would the current rules not be sufficient if there were adequate penalties for non-compliance?

5. Is there a case for removing the current exclusion of barristers from the information requirement which applies to professional advisers?

A barrister will typically have been involved in the creation of a non-resident trust only after engagement by other professional advisers acting for the settlor. The current exclusion of barristers from the reporting requirements thus has little impact in practice on the reporting of on non-resident trusts since the professional advisers working alongside the barrister will have an obligation to report.

Submitted by STEP UK Technical Committee on 9 March 2010