STEP BRIEFING NOTE: Requirement to Correct

The 'Requirement to Correct' (RTC) is contained within schedule 18 of the *Finance (No 2) Bill 2017*.

Its obligation is to compel taxpayers with outstanding offshore tax non-compliance as at 5 April 2017 to correct the position on or before 30 September 2018, ahead of the widespread adoption of the Common Reporting Standard (CRS).

RTC applies to income tax, capital gains tax and inheritance tax and if adhered to ahead of the 30 September deadline then the taxpayer will pay the tax, interest and penalties under the current rules. Taxpayers who fail to meet this requirement will face a ‘Failure to Correct’ (FTC) penalty, which will be a single, simplified and tougher set of sanctions for offshore tax evasion applying to all relevant years that have not been corrected. The ‘asset moves penalty’ (Schedule 21 FA15) and the ‘asset based penalty’ (Schedule 22 FA16) will also both apply to any FTC.

In the meantime, taxpayers can correct their tax position in advance of an FTC penalty applying.

What is considered as non-compliance?

The tax non-compliance must contain:

- an offshore matter or offshore transfer;
- income tax, capital gains tax or inheritance tax;
- non-compliance committed on or before 5 April 2017; and
- HMRC must be able to make an assessment to recover the tax on 6 April 2017 or the day after Royal Assent is granted.

How to make a correction

A tax correction can be made in various different ways:

- notify HMRC of the tax irregularity and give HMRC the information that they require;
- deliver the outstanding return;
- provide HMRC with the information so that they can calculate the tax liability;
- use HMRC’s Digital Disclosure Service;
- provide the information to HMRC during the course of the inquiry; or
- use a method that has been agreed with an HMRC officer.

Sanctions

The proposed penalties are applied on a scale determined by: the ‘behaviour category’ (either careless, deliberate, or deliberate with concealment); and the ‘territory category’ (the jurisdiction where the assets are held). Individuals judged to have been merely careless, and who make an unprompted disclosure, could escape with no penalties. HMRC acknowledge that offshore matters can be complex and an innocent error that is corrected quickly will probably not be
penalised, whereas a careless error could attract a penalty of up to 30 per cent of the undisclosed tax.

Those who have committed deliberate evasion with concealment, could pay the standard FTC penalty of 200 per cent of the tax, which can be reduced to a minimum of 100 per cent upon consideration of the quality of the disclosure, the level of disclosure and the seriousness of the offence. However, HMRC may apply any of the following sanctions on a case-by-case basis.

- A tax geared penalty of between 100 per cent and 200 per cent of the tax not corrected – penalties will be reduced within this range to reflect the taxpayer’s cooperation with HMRC, including whether they came forward unprompted to tell HMRC of their failure.
- An asset-based penalty of up to 10 per cent of the value of the relevant asset would apply in the most serious cases, involving over GBP25,000 in any tax year.
- The ability to name those who have failed to correct in the most serious cases, and where over GBP25,000 tax per investigation is involved.
- To adopt the enhanced penalty for asset moves of 50 per cent of the amount of the standard penalty, which would apply if HMRC could show that assets or funds had been moved to attempt to avoid the requirement to correct.

**Time limits for assessments**

Time limits have been extended so that HMRC can assess tax up until 5 April 2021 where there has been a FTC:

1. FTC despite reasonable care being taken – all years 2013/14 onwards
2. FTC is careless – all years 2011/12 onwards
3. FTC is deliberate – all years 1997/98 onwards

Therefore on 5 April 2021, the number of assessed previous years will be seven, nine and 23 respectively.

**Reasonable excuse defence**

Taxpayers should double check that their tax affairs are in order, although there is a reasonable defence contained within Paragraph 23 (1) of the Bill, which states:

‘Liability to a penalty under paragraph 1 does not arise in relation to a particular failure to correct any relevant offshore tax non-compliance within the RTC period if the person concerned satisfies HMRC or the relevant tribunal (as the case may be) that there is a reasonable excuse for the failure.’

If you are unsure or are unable to obtain a second opinion on advice that you have previously taken, then HMRC are encouraging you to come forward to discuss the technicalities with their specialist team. In these circumstances your penalty could be reduced and you may not face prosecution.

In circumstances where HMRC has previously agreed the correct course of action, via discussion or a ruling, and there has been no material change to the facts or legislation, then it is extremely unlikely that an arrangement will be deemed to be an avoidance arrangement for the purpose of the RTC.

It is important to note that you will **not** be able to rely on the automatic defence of having taken professional advice because the advice may be disqualified for various reasons under Paragraph 23 (3):

‘Advice is disqualified … if:’
(a) the advice was given to taxpayer by an interested person;
(b) the advice was given to taxpayer as a result of arrangements made between an interested person and the person who gave the advice;
(c) the person who gave the advice did not have appropriate expertise for giving the advice;
(d) the advice failed to take account of all taxpayer’s individual circumstances (so far as relevant to the matters to which the advice relates); or
(e) the advice was addressed to, or was given to, a person other than taxpayer.’

An ‘interested person’ is someone who participated in the avoidance arrangements or any transaction forming part of them or who for any consideration (money or not) facilitated the taxpayer into entering the avoidance arrangements.

HMRC has confirmed that any UK tax or legal body, such as STEP, would fall into the ‘appropriate expertise’ category. An interested person can include a body of persons both corporate or unincorporated, including an individual, an organisation such as a limited company, form of accountants, or a limited liability partnership.

**Avoidance arrangements**

Avoidance arrangements are defined in Paragraph 23 (6) and (7):

‘(6) … “avoidance arrangements” means arrangements as respects which, in all the circumstances, it would be reasonable to conclude that their main purpose, or one of their main purposes, is the obtaining of a tax advantage.

(7) But arrangements are not avoidance arrangements for the purposes of this paragraph if …

(a) they are arrangements which accord with established practice, and

(b) HMRC had, at the time the arrangements were entered into, indicated its acceptance of that practice.’

HMRC has confirmed that advice given by an advisor after the avoidance arrangements have taken place cannot be related to the facilitation of the initial avoidance arrangements and will not be disqualified on the grounds of it being from an interested person or as a result of arrangements made between an interested person and the person who gave the advice. As long as the advisor did not participate in the relevant avoidance arrangements then they should not be implicated in the initial arrangement.

It is also perfectly acceptable for an advisor to be employed to give a second opinion on a potential avoidance arrangement, if the client is uncertain for RTC purposes.

HMRC will apply Paragraph 23 on a case-by-case basis and anticipates that the majority of cases in which they will disqualify advice will be scenarios whereby the person who gave the advice did not have the appropriate expertise, or whereby advice failed to take into account all of the taxpayer’s individual and relevant circumstances.

**Guidance**

HMRC is hoping to be able to produce some more prescriptive guidance in 2018.