Draft legislation setting out a new, strict liability, corporate offence of failing to prevent tax evasion has been included in the Criminal Finances Bill 2016 – 2017 (the “Bill”) currently making its way through the House of Lords (the Bill is expected to come into effect within the next few months).

We have set out below a summary of the main elements of the proposed offence. However, the key take-away here is that the Government has moved on from simply targeting those individuals and entities who may be evading taxes and is now also targeting firms (e.g. banks, asset managers, lawyers and accountants) where someone acting for the firm assists a third party to evade tax.

The impact of these rules is not limited to tax advisers or those who promote “tax schemes” – the Government is aiming to dissuade firms from:

- advising or implementing, in any capacity, questionable schemes or transactions
- taking a “see no evil, hear no evil” approach to what others (including counterparties) involved in a transaction are doing when working on the transaction.

**The new criminal offence**

The new offence can be committed by any “relevant body” (that is, a company, partnership, or other similar entity) wherever incorporated or formed. Extra-territoriality is central to this legislation and is considered further below.

Very broadly, for the new offence to be activated, there needs to be:

- tax evasion by a taxpayer (already a criminal offence); and
- facilitation of that tax evasion (again, already a criminal offence) by an “associated person” of a relevant body; and
- failure by the relevant body to prevent the “associated person” from the facilitation.
It is the third bullet above, that is the “new” offence.

The offence is one of strict liability; the mens rea requirement (commonly necessary for a criminal offence to have been committed) has been removed. As such, the fact that senior management were unaware of the facilitation will no longer be a defence for the firm. The only defence available to a relevant body is for it to demonstrate that it either had in place “reasonable prevention procedures”, or that it was not reasonable in all the circumstances to expect it to have any prevention procedures in place.

**Failure to prevent the facilitation of tax evasion**

The Bill separates the offence into two baskets – domestic and foreign:

- failure to prevent facilitation of a UK tax evasion offence; and
- failure to prevent facilitation of a foreign (i.e., non-UK) tax evasion offence.

**Domestic tax evasion (and extra-territorial application of the rules)**

Subject to the availability of the defence mentioned above, a relevant body (that is, any entity – UK or non-UK) will be guilty of an offence if a person associated with that relevant body (see further below) commits a “UK tax evasion facilitation offence” when acting in their capacity as associate.

A “UK tax evasion facilitation offence” means an offence under UK law consisting of any of:

- being knowingly concerned in, or in taking steps with a view to, the fraudulent evasion of UK tax by another person (provided that such other person has actually committed a “UK tax evasion offence” facilitated by that conduct);
- aiding, abetting, counselling or procuring the commission of a “UK tax evasion offence”; or
- being involved art and part in the commission of an offence consisting of being knowingly concerned in, or in taking steps with a view to, the fraudulent evasion of a UK tax.

A “UK tax evasion offence” means either an offence of cheating the public revenue (that is, deliberate and dishonest conduct with an intention of defrauding the Revenue), or being knowingly concerned in, or in taking steps with a view to, the fraudulent evasion of (notably, this includes the non-payment of tax at the time it should have been paid) a UK tax.

**Foreign tax evasion**

Again, subject to the availability of the defence mentioned above, a relevant body will be guilty of an offence if a person associated with that relevant body commits a “foreign tax evasion facilitation offence” when acting in their capacity as associate. For a relevant body not formed under UK law to commit an offence, however, either:

- it must carry on business or part of a business in the UK (although that business or part thereof does not have to be the part in which the facilitation of tax evasion took place); or
- conduct by the relevant body or its associated person constituting part of the “foreign tax evasion facilitation offence” must have taken place in the UK.

A “foreign tax evasion offence” is conduct which is an offence under the law of a foreign country, and:

- relates to a breach of a duty relating to a tax imposed under the law of that country; and
- would be regarded by the UK courts as amounting to being knowingly concerned in, or in taking steps with a view to, the fraudulent evasion of that tax.

Consequently, a “foreign tax evasion facilitation offence” is conduct which is an offence under the law of a foreign country, and:

- relates to the commission by another person of a foreign tax evasion offence under that law; and
- would, if the foreign tax evasion offence were a UK tax evasion offence (see above), amount
to a UK tax evasion facilitation offence (see above).

In other words, in order for a failure to prevent the facilitation of foreign tax evasion offence to have occurred, a dual criminality test must be met; not only must there be an actual tax evasion offence in the foreign country, there must also be conduct which would, if it took place in the UK, constitute a facilitation offence.

**Who is an associated person**

A person is a (relevant) associated person of a relevant body if they are:

- an employee of the relevant body acting in that capacity;
- an agent of the relevant body acting in that capacity; or
- any other person who performs services for or on behalf of the relevant body who is acting in that capacity.

The explanatory notes published alongside the Criminal Finances Bill explicitly note that whether or not there is an association is:

"a question of function rather than form ... What determines whether a person is associated is whether they act for or on behalf of the relevant body"

Therefore, once enacted, the legislation will capture not only employees, agents, contractors, sub-contractors and consultants, but also branches, subsidiaries and anyone who does something on behalf of a relevant body, or does something for the relevant body that the relevant body needed it to do. However, draft guidance published following the draft legislation acknowledges that where an associated person carries out a tax evasion facilitation offence as a “frolic of their own”, he or she will not be acting in the capacity of a person associated with a relevant body.

**Extra territoriality**

As will be evident from the above, the “failure to prevent” offence has significant extra-territorial application.

In relation to a failure to prevent the facilitation of UK tax evasion, the offence can be committed by any relevant body, wherever formed or created, regardless of where any (i) evasion facilitation acts by an associated person or (ii) any prevention omissions by that body, took place.

A failure to prevent the facilitation of foreign tax evasion offence will apply only to organisations which:

- are formed or incorporated under the law of any part of the UK;
- are carrying on business or part of a business or an undertaking in the UK – for example, through a UK branch or UK representative office (although, as noted above, it need not be the UK business or part thereof where the facilitation of tax evasion takes place – the connection to the UK of the business itself is enough to bring the rules into play); or
- have an associated person act in the UK, where that conduct constitutes (part of) the facilitation of tax evasion offence (e.g., where an associated person in the UK is involved in the chain of communication leading to the offence).

**The (only!) defence: reasonable prevention procedures**

There will be a defence to the offence of failing to prevent facilitation of UK/foreign tax evasion if it can be shown that:

the relevant body had in place

“such prevention procedures as it was reasonable in all the circumstances to expect [it] to have in place”

or
“it was not reasonable in all the circumstances to expect [it] to have any prevention procedures in place.”

Prevention procedures are (unsurprisingly!) procedures designed to prevent persons acting in the capacity of a person associated with the relevant body from committing UK/foreign tax evasion facilitation offences (as applicable).

Clearly, in large organisations and any organisation involved in complex transactions, it will be challenging, as a practical matter, to avoid any associated person ever being involved in the facilitation of UK or foreign tax evasion. As such, the establishment of reasonable prevention procedures will be of paramount importance.

The draft guidance published following the Bill provides useful commentary on what will be seen as constituting reasonable prevention procedures, and states that such procedures:

“will be proportionate to the risk a relevant body faces of persons associated with it committing tax evasion facilitation offences [and] will depend on the nature, scale and complexity of the relevant body’s activities.”

The guidance is explicit that the new offences “do not require relevant bodies to undertake excessively burdensome procedures in order to eradicate all risk, but they do demand more than mere lip-service to preventing the criminal facilitation of tax evasion.” However, whilst the draft guidance does acknowledge that the procedures that would be considered reasonable will differ across organisations, it highlights certain common elements that should be taken into account, and outlines key principles to guide the development of reasonable procedures. These can be usefully summarised as ensuring that:

- Top-level management of an organisation is committed (and communicates that commitment) to preventing associated persons from engaging in the facilitation of tax evasion. This can be achieved by management “foster[ing] a culture within the relevant body in which activity to facilitate tax evasion is never acceptable” through the creation and implementation of preventative measures.

- The relevant body assesses the nature and extent of its exposure to the risk of those who act for it engaging in activity to facilitate tax evasion during the course of business. This risk assessment should be documented, kept under review and updated as needed.

- The organisation applies due diligence procedures, taking an appropriate and risk-based approach, in respect of persons who perform or will perform services on its behalf in order to mitigate identified risks (including, for example, increased scrutiny in respect of those providing services to clients who have been identified as utilising services or undertaking activities which pose a higher risk of being misused to perpetuate tax evasion).

- The organisation’s prevention policies and procedures are communicated, embedded and understood throughout the organisation, through internal and external communication, including training.

- The organisation monitors and reviews its prevention procedures and makes improvements where necessary.

It is worth noting that there is a requirement built into the Bill that guidance must be published on the procedures which can be put in place to prevent associated persons from committing tax evasion facilitation offences and that the guidance should be enshrined in a statutory instrument. It is expected that the current draft guidance will eventually (with or without amendment) be published to meet this requirement.
Impact

The draft guidance specifically notes that what is considered “reasonable” in terms of prevention procedures will change as time passes, and that whilst the Government appreciates that some procedures take time to roll-out, it also expects “rapid implementation, focusing on the major risks and priorities, with a clear timeframe and implementation plan on entry into force.”

As the only defence to a “failure to prevent” offence is having in place reasonable prevention procedures, it is important for all potentially affected organisations to review how and the extent to which this proposed legislation will impact them and take steps (which, for some organisations may involve making significant adjustments to their existing compliance procedures) to identify associated persons and risk exposure channels, conduct a thorough risk assessment to implement a risk mitigation strategy and, where relevant, review contractual terms for all persons and entities who may be considered associated persons.