Katten

TAX ADVISORY

The UK Government and HMRC's Efforts to Clamp Down on Promoters of Tax Avoidance

June 3, 2021

Tax avoidance is the process of manipulating tax rules to reduce the amount of tax payable and obtaining a financial advantage that was never the intention of the legislation. A typical example of tax avoidance involves the use of contrived or artificial transactions that serve little purpose other than to reduce the amount of tax due. A person is a promoter if they make a firm approach to another person in relation to the relevant proposal about tax avoidance with a view to making the proposal available for implementation by such person, make the relevant proposal available for implementation by other persons, or is responsible for the design, organisation or management of the arrangements. Some promoters profit from promoting schemes while others evade HM Revenue and Customs (HMRC) altogether by closing down the promoter company, dissipating or moving its assets and subsequently setting up a new company to continue to promote avoidance.

The Government has commenced renewed efforts to stop promoters and enablers of tax avoidance. The Finance Bill 2021 contains provisions that give HMRC increased powers to seize assets of promoters of tax avoidance who profit by continually sidestepping anti-avoidance regime rules but the Government published in March of this year a Consultation Document, "Clamping Down on Promoters of Tax Avoidance", on proposed additional powers to further curb the activities of promoters.

Clamping Down on Promoters Who Dissipate or Hide Assets to Avoid Paying Penalties

The Government has already announced and consulted on the measures that have been included in the Finance Bill 2021. These measures will enable HMRC to take quicker action against promoters and enablers. The measures aim to strengthen anti-avoidance legislation and support HMRC compliance work by:

- amending the Disclosure of Tax Avoidance Schemes (DOTAS) rules to enable HMRC to obtain information and documents, as well as to identify taxpayers using suspicious schemes at an earlier stage;
- enabling HMRC to issue a stop notice requiring the promoter to stop promoting the scheme as soon as HMRC believes the proposed tax advantage cannot be achieved and a subsequent penalty for non-compliance with this stop notice; and
- strengthening information powers to enable HMRC to obtain information about the enablers of tax avoidance schemes when they are identified and ensuring early penalties are given.

The consultation sets out a proposed measure permitting HMRC to seek an order from a court or tribunal to ensure that a promoter's assets are ring-fenced, so preventing the promoter from dissipating the assets. This order can be obtained where HMRC can demonstrate that the assets need to be protected (e.g., if there is a risk that the assets will be dissipated during a penalty hearing). There are two options for ring-fencing the assets:

(1) an upfront security payment — which would require the promoter to pay to HMRC an amount ordered by the court in line with the value of the penalty that is about to be applied; or

(2) a freezing order — which would prevent the promoter from using or dealing with their assets.

Non-compliance with either of these ring-fencing options will result in a charge of contempt of court and is punishable by either a fine or up to two years in prison. The proposal protects HMRC's ability to recover penalties imposed on promoters under anti-avoidance legislation and ensures that promoters cannot dissipate their assets to avoid paying such penalties. The intention behind the measures is to clamp down on promoters and build on existing legislation to make it riskier and harder to promote schemes, as well as directly disrupting the promoter's business models.

Tackling Offshore Promoters and the UK Entities That Support Them

It is more complex for HMRC to tackle offshore promoters of tax avoidance as it can face difficulty in enforcing and collecting sums due from the promoter. It can also take HMRC longer to investigate offshore promoters. Purchasers of promoted schemes often do not realise that they are dealing with an offshore entity because there is a UK entity acting as an interface between the client and the promoter.

The Finance Bill 2021 strengthens the existing DOTAS and Promoters of Tax Avoidance Schemes (POTAS) legislation by allowing HMRC to impose certain obligations on UK entities involved in tax avoidance schemes on behalf of offshore promoters. Where these obligations are not met, the UK entities will be liable to a penalty, so the UK associate is penalised for assisting the offshore promoter's activities.

However, the Government proposes to go further than the existing anti-avoidance legislation and the amendments in the Finance Bill 2021. It plans to introduce an additional penalty where activities are undertaken within a structure that includes an offshore promoter. This additional liability penalises the UK entity for facilitating an offshore promoter's business activities in the UK. The penalty will be an amount up to the total fees earned by all those involved in the development and sale of that tax avoidance scheme, not just the fees earned by the UK entity. The additional penalty would be chargeable directly on a UK entity, where the UK entity has:

- undertaken activities to facilitate the use of a tax avoidance scheme;
- been subject to a penalty under anti-avoidance regimes for its own activities in relation to that tax avoidance scheme; and
- undertaken its activities in relation to that tax avoidance scheme within an offshore promoter structure.

The proposal aims to deter UK-based entities that are involved with an offshore promoter by increasing the financial risk to that UK entity. Furthermore, where more than one UK entity is involved in the promotion structure, the additional penalty would be chargeable on each UK entity. The Government also proposes that where HMRC discovers that the underlying promoter is based overseas, and a liability has been charged on the UK entity for facilitating offshore arrangements, HMRC can then seek a security or freezing order to protect the additional penalty chargeable on the UK entity where HMRC believe there is a risk of assets being dissipated or the business being dissolved.

Closing Down Companies That Promote Tax Avoidance Schemes and Tackling the Directors of Those Companies

Promoters often use contrived organisational structures and continually rearrange the entities to circumvent the legislation and market tax avoidance. Once tax avoidance schemes are sold, it is not unusual for the promoter company to be closed down or its activity significantly reduced, and new entities set up to continue the promoting activities. These behaviours delay and disrupt HMRC's investigations, as well as perpetuate the sale of tax avoidances schemes.

The Finance Act 2020 introduced provisions which make directors jointly and severally liable for the tax of a company in certain circumstances, namely (1) tax evasion; (2) tax avoidance; and (3) repeated insolvency and non-payment. These provisions apply equally to LLPs. Learn more about the changes brought in by the Finance Act in Katten's advisory, "New Tax Risks for Directors: Insolvent Companies and COVID-19 Fraud".

Currently, companies can be wound up by the court on the petition of one or more creditors, the Official Receiver, Secretary of State for Business, Energy and Industrial Strategy or by the directors or shareholders of a company. HMRC can only take action itself against promoter companies under existing insolvency legislation where there is an enforceable tax debt.

The Finance Bill 2021 goes further — under the proposals, HMRC could petition the court to wind up a company where:

- a significant breach demonstrates non-compliance with the anti-avoidance legislation; and
- HMRC have established the evidence to petition the courts that because of a series of non-compliant and deliberate actions by the company, it should be wound up on public interest grounds.

There are proposed threshold conditions for significant breaches that would need to be met for HMRC to initiate a winding up petition, for example, non-compliance with a POTAS monitoring notice. HMRC will also have to demonstrate that the company is operating against the public interest. Where companies are subject to other promoter measures proposed in this consultation, such as security payment or a freezing order, these would form part of HMRC's overall consideration to petition the court for the winding up of a promoter company.

In June 2020, the Corporate Insolvency and Governance Act 2020 (CIGA) was introduced. Under the provisions of CIGA, restrictions were brought in preventing the presentation of winding-up petitions. These restrictions are due to last until 30 June 2021. The Finance Bill 2021 comes into force when it receives Royal Assent (except for some narrow exceptions). The Government has not confirmed whether or not the restrictions introduced by CIGA will be extended again. As such, it remains to be seen whether or not public interest petitions as proposed by the Finance Act 2021 will be permitted to be presented or will fall under the restrictions under CIGA.

Supporting Taxpayers to Identify and Stay Clear or Exit Tax Avoidance

The Government also proposed new powers to enable HMRC to inform taxpayers of its enquiries into specific promoters and schemes, including publishing names and details, at an earlier stage, as well as clarifying and correcting claims by promoters about the chances of success of their schemes.

The measures discussed give HMRC the ability to intervene earlier to disrupt promoters' activities, ring-fence assets to protect HMRC's ability to collect penalties and apply strong sanctions for promoting or enabling tax avoidance. This will help to reduce the harm that promoters may cause to taxpayers and the wider economy. The Finance Bill 2021 has outlined the legislation for these additional powers. Although these measures aim to act as a deterrent to promoters and strengthen current anti-avoidance regimes, the Government recognises that these measures may not go far enough and wants to continue to supplement these rules.

The comment period for the consultation closed on 1 June 2021.

CONTACTS

For more information on Finance Act 2020 tax provisions, contact your Katten lawyer or any of the following:




Prav Reddy
+44 (0) 20 7770 5213
prav.reddy@katten.co.uk

Charlotte Sallabank
+44 (0) 20 7776 7630
charlotte.sallabank@katten.co.uk

Dominique Hodgson
+44 (0) 20 7770 5239
dominique.hodgson@katten.co.uk

Christy Wilson
+44 (0) 20 7770 5241
christy.wilson@katten.co.uk

Ciara McBrien, a trainee in the Financial Markets and Funds practice, contributed to this advisory.