Client Update

How Not to Become a Criminal, or, Preventing the Facilitation of Tax Evasion

Even if you have not watched *Jaws*, you are likely to recognise the ominous theme tune that warns viewers that danger approaches. Swimmers off Amity Island did not see, or chose not to see, the killer shark coming, even after there had been pretty blatant warning signs. We hope that the United Kingdom's new criminal offences of failing to prevent the facilitation of UK or foreign tax evasion (the "Offences") will not go similarly unheeded.

The Offences merit immediate attention from sponsors; they have global reach and the potential to catch the unwary, which may hurt given the associated unlimited financial penalties. The new offence criminalises any "relevant body" (a company or a partnership, UK or otherwise) that fails to prevent an "associated person" from facilitating tax evasion on behalf of a third party. It is expected that the new Offences will be brought into force after the summer.

There are three core elements necessary for one of the Offences to apply:

Offence Requirements	Fund Context
A taxpayer criminally evades tax anywhere in the world. In a UK context this means either: (a) cheating the public revenue; or (b) being knowingly involved in, or taking steps with a view to, the fraudulent evasion of tax.	Potential tax evaders: • investors; • portfolio companies; and • carry/management fee recipients.
An **"associated person" of a relevant body criminally facilitates** such tax evasion. An "associated person" is defined very widely, and includes both natural persons (e.g., employees, agents or contractors), and legal persons performing services for, or on behalf of,	Potential associated persons: • partners/employees of the manager and adviser(s); • the manager;

the relevant body. Facilitation is a very broad concept including aiding, abetting, counselling or procuring tax evasion, as well as being knowingly concerned in, or taking steps with a view to, the fraudulent evasion of a tax by another person.	• any adviser(s); • lawyers; • accountants; • fund administrators; • placement agents; and • management consultants.
The **relevant body failed to prevent** its associated person from committing the criminal facilitation act.	Potential relevant bodies: • fund vehicle; • manager; or • adviser.

As stated above, the Offences are global in scope, and cover the facilitation of UK tax evasion and tax evasion anywhere else in the world.

UK TAX EVASION FACILITATION OFFENCE

The key for this Offence is the existence of UK tax evasion. It does not matter where the relevant body or the associated person is based. It is not even necessary for any material conduct to have taken place in the United Kingdom.

NON-UK TAX EVASION FACILITATION OFFENCE

A relevant body may be caught by these rules in respect of non-UK tax evasion if:

- there is some UK nexus (a relevant body undertakes business in the United Kingdom, or its associated person performs a facilitation activity in the United Kingdom); and
- both the foreign tax evasion and the facilitation is criminal in the relevant jurisdiction and would be criminal in the United Kingdom if such tax evasion and/or evasion were to take place in the United Kingdom.

EXAMPLES

Heat-of-the-Moment Negotiation

- A deal team member negotiating an investment is asked by the company's management team to pay their consideration into a [Swiss/Cayman/Panamanian] bank account so that they are not taxable in their local jurisdiction.

- Third-party tax evader: depending on local law, potentially the company's management team.
- Relevant body: fund, manager, adviser (if relevant).
- Associated person: the deal team member.

Portfolio Company Dealings

- The fund has an appointed director on the board of a portfolio company. The portfolio company decides to pay its staff in cash to enable its staff to reduce their tax bill.
  - Third-party tax evader: depending on local law, potentially the portfolio company staff.
  - Relevant body: fund, manager, adviser (if relevant).
  - Associated person: the appointed director.

Demanding Investor

- An important investor contacts a member of the fund administration team asking them to amend the investor's distribution notice to record a capital distribution, not an income distribution.
  - Third-party tax evader: depending on local law, potentially the investor.
  - Relevant body: fund, manager.
  - Associated person: the fund administrator.

THE DEFENCE

If the tax evasion and its facilitation by the associated person are established, the relevant body is strictly liable, subject to a defence of having had in place **reasonable prevention procedures**. These procedures need to be planned, if not implemented, when the Offences come into force.

Sponsors, UK and overseas, should anticipate that these rules will add to their compliance burden. In particular, HMRC has made it clear that it is not enough to simply add compliance with these rules to existing KYC/AML procedures as an additional box to tick. The starting point is therefore to undertake a risk assessment—HMRC has indicated that it regards a third-party risk assessment as more valuable. The risk assessment should inform the nature of preventative measures that should be taken. These measures are likely to include top-level commitment and due diligence on associated persons, as well as adding in new representations to engagement letters, staff training, compliance monitoring, and disciplinary action for noncompliance.

The warning siren has sounded; it is now for sponsors to vacate the water. The government wants behavioural change; we stand ready to assist sponsors in developing their compliance strategies for the new rules.

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Please do not hesitate to contact us with any questions.

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