Comment
Views on topical issues

HMRC's use of criminally obtained evidence

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There remains considerable uncertainty in English law regarding HMRC's ability to use criminally obtained evidence when pursuing taxpayers in respect of their concealed offshore income.

Around four years ago, news broke that HMRC had paid £100,000 to Heinrich Kieber, a former data clerk, to acquire details of undisclosed offshore bank accounts held by UK taxpayers at a Liechtenstein bank.

Moreover, at about the same time HMRC came into possession of information from French revenue officials relating to approximately 7,000 UK taxpayers who held undisclosed bank accounts at a bank owned by HSBC in Geneva. The information had been stolen by Herve Falciani, a computer specialist employed by HSBC, who passed it to the French authorities, almost certainly for financial reward.

Whilst the acquisition of information by HMRC from informants is hardly new, the provenance of the material from Liechtenstein and Geneva raises novel issues, for in both cases the information had been stolen by an employee from his employer, disseminated in breach of the duty of confidence owed by an employee to his employer, and notwithstanding its status as stolen property the information was purchased by a State revenue authority for money.

The activity of these individuals has triggered interesting litigation in France and Germany, but not as yet in the UK. In December 2010, the Federal Constitutional Court of Germany held that information of a similar nature supplied by Mr Kieber to the German revenue authorities could be used to provide the initial moment of suspicion needed for the grant of a search warrant of a taxpayer's premises.

The Court rejected an argument that the information was inadmissible because it had been acquired in breach of international law conventions for the exchange of tax information and its use would violate provisions of domestic law.

A few months later, the Court of Appeal in Paris rejected a petition by a taxpayer to nullify proceedings for tax fraud which had been founded on the information which Mr Falciani had stolen from HSBC.

The Court determined that use of this information against the taxpayer was not unfair.

In an extraordinary turn of events which demonstrates the countries' anger and concern about the use of this information, Switzerland issued warrants three months ago for the arrest of three German civil servants, accusing them of industrial espionage for purchasing the bank details of German tax evaders. If the German bankers enter Switzerland, they will be arrested and put on trial.

Whilst HMRC has been using the Kieber/Falciani material to launch investigations into the affairs of a number of UK taxpayers, an opportunity to challenge the use of this material in civil or criminal proceedings has not yet arisen.

When it does, there are some good arguments to be advanced and HMRC should not be in any doubt that the taxpayer's lawyers will be ready and waiting.

Self-certification of 'approved' employee share schemes

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The government intends to legislate for self-certification of the three types of employee share scheme which currently require prior HMRC approval. Practitioners should accept this as a fait accompli and concentrate their energies on lobbying for effective protections for companies, their employees and their advisers.

On 27 June 2012 HMRC published a consultation document in response to the Office of Tax Simplification's report on tax-advantaged employee share schemes.

The most significant OTS recommendation, which the government has accepted, is that a company establishing an approved company share option plan, SAYE option plan or share incentive plan should no longer need to obtain prior HMRC approval.

The consultation period runs until 18 September 2012 and self-certification will come into effect no later than 2014.

Practitioners who have always enjoyed the protection of HMRC's rubber stamp will be understandably apprehensive about the responsibility which will now fall on their shoulders.

But resistance to this change will almost certainly be futile. HMRC can persuasively point to other jurisdictions – in particular, the USA and France – where the absence of pre-approval appears never to have been a problem.

And on the home front, EMI options seem not to have suffered from being the only tax-advantaged scheme which is not 'approved'.

So what safeguards should advisers prioritise?

Most crucially, the legislation must lend itself to doubt-free self-certification.

It is currently a condition of approval that a scheme must not contain features 'which are neither essential nor reasonably incidental' to the purpose of providing share incentives.

This vague formulation gives HMRC carte blanche to strike out any rule it dislikes.

The consultation document recognises that this open-ended prohibition is incompatible with self-certification but it asserts that:

'a requirement as to the purpose of a scheme is likely to remain necessary in order to ensure effective targeting of tax advantages'.

Practitioners need to explore the fears which are keeping HMRC awake at night and find creative ways of assuaging those fears without making self-certification a nightmare.

However successful this process, there will still be cases where an adviser is on the horns of a dilemma.

The best solution, which the consultation document anticipates, will be a speedy advance clearance procedure.

Practitioners should work with HMRC to ensure that such a system does not become bogged down by anxious applicants still hankering after the ancien regime.

HMRC's consultation document is available via www.lexisurl.com/jxg0G. The consultation closes on 18 September 2012. To submit responses or raise enquiries, email shareschemes@hmrc.gsi.gov.uk.

More on the proposed GAAR ...

Last week we published a feature on the proposed general anti-abuse rule (GAAR). Taxjournal.com now contains further commentary on the draft GAAR, with views from the following practitioners:

- **Michael Cant** (Nabarro): 'It is dispiriting to see that the draft GAAR ... has moved so far from where Aaronson had suggested we should begin.'
- **Adam Craggs** (RPC): '[The fact] that a clearance system is not included in the proposals is disappointing and may be due to a lack of resources at HMRC, rather than for any principled reason.'
- **Paul Davison** (Freshfields Bruckhaus Deringer): 'The draft GAAR is much more concisely drafted than the Aaronson illustrative GAAR. Nonetheless, we are a long way from ensuring "sufficient certainty" without undue cost.'
- **Pat Dugdale** (Olswang): 'Chapter 5 of the consultation document states that the GAAR should, as far as possible, operate within existing self-assessment regimes. It is unclear how this will operate in practice.'
- **Nigel Eastaway** (BDO): 'The key to whether the proposed GAAR would be effective hinges on the interpretation of the "double reasonableness" test.'
- **Ashley Greenbank** (Macfarlanes): 'The effect [of the 'double reasonableness' formula] will be an uncertain test which hands a wide degree of discretion to HMRC.'
- **Stephen Herring** (BDO): 'It would be very disappointing if the responses to the GAAR proposals were to focus exclusively upon the minutiae or to assert some sort of HM Treasury conspiracy involving thin ends of wedges and the like.'
- **Andrew Hubbard** (RSM Tenon): Why 'reasonableness is not an abstract proposition and context is everything.'
- **Peter Jackson** (Taylor Wessing): 'The proposed extension of the GAAR beyond the main direct taxes and NICs to other taxes (including a new annual charge for "enveloped" high value residential property) will do little to promote certainty as to how the GAAR will impact on taxpayers.'
- **Ray McCann** (Pinsent Masons): 'If HMRC drop an abuse stone in the pond, how far will the ripples extend?'
- **Pete Miller** (The Miller Partnership): Why it would be preferable to see the advisory panel's decisions being binding, 'with the role of the advisory panel being similar to that of the First-tier Tribunal when HMRC is considering counteraction under the transactions in securities rules'.
- **Simon Letherman** (Shearman & Sterling): 'The proposed DTA override potentially goes even further than DTA abuse cases ... To say the least, it is unclear that the OECD commentaries support a just and reasonable override absent DTA abuse'.
- **Eamon McNicholas** (Temple Tax Chambers): 'The "Yes Minister"' approach to tax and legislation still holds sway in Whitehall ... judging from recent events the expectation from experience is that prospects for a workable and reasonable GAAR are poor.'
- **Kassim Meghjee** (Mishcon de Reya): 'The impact of a GAAR on existing and intended legislation is likely to complicate rather than simplify the UK legislative landscape for the foreseeable future.'
- **Lakshmi Narain** (Baker Tilly): 'The inclusion of a general anti-avoidance principle in addition to the GAAR would, I submit, assist in providing a solid base for determining the "purpose" of both the relieving provisions and the anti-avoidance rules and facilitate the longer term objective of a simpler tax system.'
- **Mark Simpson** (Squire Sanders): 'A cynic might conclude that the intention is to keep the ambit of the GAAR unclear, to act as a deterrent to taxpayers.'
- **Stephen Woodhouse** (Deloitte): If the proposed GAAR was in place, would the litigation in *PA Holdings* have been unnecessary?
- **Stephen Hoyle** (DLA Piper): 'A better target would have been the distributors of high risk schemes rather than the users.'

The commentary is free to view via www.lexisurl.com/LQeM8.

Proposed changes to overseas workday relief

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When the new statutory residence test (SRT) is introduced, the government intends to abolish 'ordinary residence' for tax purposes. However, overseas workdays relief (OWR) will continue to exempt the unremitted foreign earnings of employees temporarily resident in the UK. But the qualifying conditions will restrict severely the number of employees able to benefit.

From 6 April 2013 OWR will only be available to individuals who claim to be taxed on the remittance basis if they are not domiciled in the UK, have not been resident at any time during the three tax years prior to the year of arrival and it is reasonable to assume that the employee will not be based in the UK beyond the end of the second full tax year after the year of arrival. The draft legislation specifically defines the meaning of 'based' in the UK.

At first glance the proposed test appears broadly similar to the current test for being 'resident but not ordinarily resident' (R/NOR) and thereby entitled to OWR under current legislation. However, closer examination reveals that this is not the case. Even ignoring the limitation to individuals regarded as not domiciled in the UK, the 'reasonable assumption' test will both limit the relief and throw up some anomalous results.

For example, it would be easy to assume that an individual who arrives in the UK on 1 July 2013 for a 30-month assignment would obtain the same tax treatment as an individual who arrived on 1 January 2014 for a 30-month assignment, but this is not the case.

Assuming all other conditions are met and there are no changes in circumstance, the employee arriving on 1 July 2013 will be able to claim OWR for the entire 30-month period they are in the UK, whereas the employee arriving on 1 January 2014 will not be able to claim relief for any of the relevant tax years. This is because, right from the outset, it is reasonable to assume that the second employee will continue to be based in the UK beyond the end of the second full tax year. He therefore stays beyond the 'three year cut-off point' (proposed new ITEPA 2003 s 26A), which starts from 6 April in the year of arrival.

If the rules remain as drafted many secondments are likely to reduce to two years as companies try to avoid the loss of OWR.

The draft legislation can be found in Chapter 6 of the document released by HM Treasury on 21 June 2012 (available via www.lexisurl.com/mX7IA).
See also the article on page 12.