The Requirement to Correct
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Finance Bill 2017 included provisions relating to the 'Requirement to Correct'. This provision was removed prior to the passing of the preliminary Bill but is expected to be re-tabled in the autumn.The 'Requirement to Correct' (RTC) and the subsequent 'Failure to Correct' (FTC) regimes apply to anyone with unpaid historic UK tax liabilities relating to overseas assets. This, therefore, potentially affects offshore trustees, UK resident and domiciled individuals and UK resident non-UK domiciled individuals. It applies equally to those who have deliberately evaded tax and those who have failed to pay the correct amount of tax through oversight or careless error. HMRC also see this as being applicable to complex situations where advice was taken but is no longer up to date.

This article focuses on the impact of the RTC and FTC on offshore trustees and in particular the areas where action may be required to mitigate the risk of falling foul of the FTC penalties.

The RTC offers a final chance, before 30 September 2018, to correct historic offshore tax evasion but also non-compliance. It includes all periods up to and including 5 April 2017. Income tax, capital gains tax and inheritance tax may be reported under the RTC.

The end date of 30 September 2018 (and the start of the FTC regime) corresponds with the date by which all countries committed to the Common Reporting Standard (CRS) will be exchanging data with HMRC. From this point any disclosure of undeclared liabilities will be considered to be prompted.

Where historic errors are not corrected in the RTC period (6 April 2017 to 30 September 2018) taxpayers will face much tougher new penalties for their 'Failure to Correct' (FTC). FTC penalties include;

- A standard penalty of between 100% and 200% of the tax that has not been corrected;

The above is much harsher than any of the current rules.

In addition HMRC will also be able to apply the heightened offshore penalties that came into force on 1 April 2017 being:

- A 10% asset-based penalty (relevant to 'the most serious cases' where tax underpaid in a tax year is greater than £25,000);
- An enhanced penalty of 50% of the standard penalty amount if HMRC could show that assets or funds had been moved to attempt to avoid RTC; and
- Naming and shaming of taxpayers 'in the most serious cases' (total loss of tax greater than £25,000). Including an extension of this to the 'controlling party' behind the trust i.e. the trustees (a serious reputational risk).

These new penalties are far more severe than any chargeable under present legislation.
The only defence for those who fail to correct liabilities in the RTC period is a 'reasonable excuse' for not meeting the obligation. The scope of 'reasonable excuse' will be based on existing provisions in law. The law sets out the circumstances in which taxpayers can and cannot rely on tax advice they have received. Per HMRC's consultation document, it is worth noting that:

- Reliance on sub-standard advice should not constitute a reasonable excuse
- Where a taxpayer does not understand the law and assumes their affairs are in order and does not take professional advice this does not constitute a reasonable excuse as in this case it would have been reasonable to take advice.
- If all the facts are provided to a professional adviser who is competent to give the advice, and the advice is fully implemented, the taxpayer should be able to rely on this to show that they have taken reasonable care to ensure that their UK tax position is correct.

The method of making corrections will depend on the circumstances. For example, this could be by submitting outstanding tax returns, by delivering information to HMRC as part of an enquiry or another method agreed with an officer of HMRC, or by using an existing method for disclosure (for example the Worldwide Disclosure Facility (WDF) which might be more appropriate for more serious cases).

Pitfalls and action for Trustees

In practice, we find that one of the most misunderstood and overlooked taxes for trustees is inheritance tax (IHT). Due to the nature of IHT, changes in circumstances can easily bring the trustees into the charge. Some common circumstances are outlined below:

- Additions made after a change of domicile of settlor
- Inadvertent multiple settlors
- Incorrect anniversary date assumptions
- Where an excluded property trust acquires relevant property
- Where UK situs trust assets are overlooked (ie, loans to beneficiaries, UK shares in portfolios)
- Where chattels are in the UK (yachts, planes, jewelry, art) at relevant dates.

Any of the triggers above (which are not exhaustive) could bring a trust into the charge to IHT.

In addition following changes in 2006 it is no longer only discretionary trusts which may be liable to IHT. And a trust will not necessarily escape the charge to IHT because the UK assets are worth less than the nil rate band.

Of course IHT is not the only tax which is misunderstood and trustees may be liable to income tax on UK source income but have not reported it (this is common with offshore pensions schemes).
To avoid the pecuniary and reputational risks associated with FTC trustees should ensure that their UK tax affairs are in order before 30 September 2018. Relying on flawed or misinformed tax advice will not be sufficient excuse to exonerate the trustees.

To mitigate risks of falling into the FTC trustees may wish to consider undertaking thorough tax reviews of their structures to identify any potential tax issues.

While it is possible that the whole book of business should be reviewed particular parcels of business may require priority, such as:

- where trustees have been appointed as new trustees of an existing structure
- where trustees have bought or been passed an existing book of business
- structures which are old and have not been reviewed from a tax perspective for some time
- structures which are being exited

Furthermore there is no jurisdictional restriction to the reach of FTC and business in jurisdictions with weaker links with the UK are, perhaps, potentially more exposed than where there is a working awareness of UK tax.

Summary

These measures are further evidence of HMRC's continued crackdown on offshore tax evasion and non-compliance. With penalties of up to 200% of the tax underpaid, plus a 10% asset based penalty and naming and shaming in the most serious cases, FTC signifies a step change in HMRC's attitude to dealing with those who fail to put historic non-compliance right.

The focus of FTC is not the behaviour that led to the original non-compliance, as with standard penalties, but instead the person's failure to take steps to correct that non-compliance. Those who have historic tax liabilities to disclose resulting from careless errors will be subject to the new FTC penalties in the same way as those who have deliberately evaded tax. The RTC regime provides an opportunity to correct that non-compliance, but we would not recommend that trustees wait to commence reviews. Those with any doubt concerning UK tax issues linked to offshore structures should review their affairs as soon as possible.

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