INTERNATIONAL TAX INVESTIGATIONS IN THE U.K.

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INTRODUCTION

If you are reading this in December 2024, we in the U.K. have recently just had the first new Labour Government and Chancellor Rachel Reeves' first budget, our minds turn to the less enviable issues of the impact on tax.

It is no secret that the U.K. has a significant debt burden. A large part of that arose from the various support initiatives provided during COVID-19, but some are linked back to the financial crisis of 2008. Whatever the reason, the current public sector net debt, excluding public sector banks, as set out in the Budget speech was estimated to be equivalent to 98.5% of G.D.P. (£2.7665 trillion, per the Office for National Statistics) at the end of September, although the G.D.P. percentage figure is expected to be revised as it relies on G.D.P. estimates.

Ahead of coming into power, the Labour Party set out a number of measures they would introduce to pay for its agenda. One of those was the ending of the U.K. non-dom regime. This was confirmed in the Budget, and we are starting to see the first draft of legislation for the replacement four-year Foreign Income Gains ("F.I.G.") regime and the proposals to revise U.K. Inheritance tax from focusing on domicile to a residence-based test.

In brief, from April 2025, an individual who has been U.K. tax resident for ten or more of the previous 20 years will be a "long-term resident" and as such exposed to U.K. Inheritance Tax on worldwide assets for a number of years after U.K. residency terminates! Individuals in this category who have been U.K. resident for between ten and 13 years and then become non-U.K. tax resident will remain within the I.H.T. net for three years following their departure (the "tail"). Those who have been U.K. resident for 20 years will have an I.H.T. tail of ten years. A sliding scale will apply for those who were U.K. resident for between 13 and 20 years, with each year of U.K. residence beyond 13 adding one extra year to their I.H.T. tail. There are some transactional limitations for individuals who were not domiciled in the U.K. on October 30, 2024, and who are non-U.K. resident in tax year 2025/26.

Also, of particular interest to the writer, given the many asset managers he acts for, the Budget increased the rate of capital gains tax to 32% on carried interest from April 2025, alongside the wider proposals on C.G.T. to raise the rate to 18% and 24% from the current 10% and 20%, respectively, from October 30, 2024. A Consultation will also take place to bring carried interest gains into the Income Tax arena,(which currently has a maximum rate of 45%, possibly to sit alongside the Disguised Investment Management Fee ("D.I.M.F.") regime which was introduced in 2015.

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Another measure which the Labour Party pointed to in its pre-election manifesto was the countering of tax evasion and avoidance. It stated that the government would invest £855m over five years on the U.K. tax authority, H.M.R.C., to raise £2.7 billion per annum from this investment. They went further than this in the Budget by setting out various proposals to close the tax gap that will recoup £2.7 billion each year for the five years of the current Parliament period.

Considering the Government's statements on tax avoidance and fraud, this article focuses on the U.K. approach to tax fraud, through H.M.R.C.

H.M.R.C. APPROACH OF TAX FRAUD/EVASION

One of the first things to appreciate in terms of the U.K. and H.M.R.C. in serious tax matters is their use of words like fraud, tax evasion, and deliberate behavior interchangeably. In essence, they are looking at acts where tax has been lost to the exchequer, as a result of dishonest intent. But the interchanging of some of these words can have significant tax consequences, particularly in the case of deliberate behavior.

It's worth considering the H.M.R.C. criminal investigation policy. H.M.R.C. refers to this policy in terms of fraud. The U.K. Adopts a policy of selective prosecution. This in practice means that when H.M.R.C. discovers situations where fraud is prevalent, whilst they always consider the possibility of commencing a criminal investigation, more often than not they choose to pursue a civil settlement, to include tax, interest, and penalties.

The H.M.R.C. Criminal Investigation policy sets out examples of the types of areas where H.M.R.C. will more likely commence a criminal investigation rather than a civil investigation. While not exhaustive the list is set out as follows:

- Where organized criminal gangs attack the tax system or systematic frauds where losses represent a serious threat to the tax base, including conspiracy
- Where an individual holds a position of trust or responsibility
- Where materially false statements are made, or materially false documents are provided in the course of a civil investigation
- Where, pursuing an avoidance scheme, reliance is placed on a false or altered document or such reliance or material facts are misrepresented to enhance the credibility of a scheme
- Where deliberate concealment, deception, conspiracy or corruption is suspected
- Where there is use of false or forged documents
- Where there is importation or exportation breaching prohibitions and restrictions
- Where money laundering exists with particular focus on advisors, accountants, solicitors and others acting in a professional capacity who provide the means to put tainted money out of reach of law enforcement

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- Where the perpetrator has committed previous offences or there is a repeated course of unlawful conduct or previous civil action
- Where theft, misuse, or unlawful destruction of H.M.R.C. documents occurs;
- Where there is evidence of assault on, threats to, or the impersonation of H.M.R.C. officials
- Where there is a link to suspected wider criminality, whether domestic or international, involving offences not under the administration of H.M.R.C.

A central part of representing a client in any serious tax investigation or voluntary disclosure is to determine if tax fraud or deliberate behavior is prevalent. It is therefore very important to fully understand the concept of tax fraud. The badges of tax fraud are not always easy to identify, and over the years, the writer has come across many situations where a tax matter has some features of tax fraud and yet the advisers saw the facts differently, often reflecting the complexity of taxation law. Given the use of interchangeable terms between fraud, evasion, and deliberate behavior, it is worth also understanding how it all links together.

WHAT IS FRAUD?

As well as understanding H.M.R.C.'s policy on criminal prosecution, when considering cases of suspected serious fraud, some understanding of what constitutes fraud is clearly helpful. There is an abundance of common law (both tax and non-tax related) on this subject.

H.M.R.C.'s enquiry manual (EM5106) publishes the following extract from Halsbury's Laws of England (LexisNexis), in relation to "misrepresentation and fraud."

> **Section 757 What Constitutes Fraud?**
>
> Not only is a misrepresentation fraudulent if it was known or believed by the representor to be false when made, but mere non-belief in the truth is also indicative of fraud. Thus, whenever a person makes a false statement which he does not actually and honestly believe to be true, for purposes of civil liability, that statement is as fraudulent as if he had stated that which he did not know to be true, or knew or believed to be false.* Proof of absence of actual and honest belief is all that is necessary to satisfy the requirements of the law, whether the representation has been made recklessly or deliberately; indifference or recklessness on the part of the representor as to the truth or falsity of the representation affords merely an instance of absence of such a belief. A representor will not, however, be fraudulent if he believed the statement to be true in the sense in which he understood it, provided that was a meaning which might reasonably be attached to it, even though the court later holds that the statement objectively bears another meaning, which the representor did not believe.

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[* See Derry v Peek 14 App Cas 337, p 374, per Lord Herschell: fraud is proved when it is shown that a false representation has been made (1) knowingly, or (2) without belief in its truth, or (3) recklessly, careless whether it be true or false; the third case being but an instance of the second.]

Section 759 Irrelevancy of Representor's Motive

It follows from the meaning of fraudulent misrepresentation that, given absence of actual and honest belief by the representor in the truth of the misrepresentation, his motive in making the misrepresentation is wholly irrelevant. It may be that he intended to injure the representee without benefiting himself, or to benefit himself without injuring the representee; it may be that he did not intend to do either, but solely to benefit a third person, or even the representee himself, or otherwise to do right. Lastly, he may have acted with no intelligible or rational notice whatsoever and told a lie from mere caprice, mischievousness or stupidity. In all these cases, provided that there was an absence of actual and honest belief in the truth of his assertion, the misrepresentation is accounted fraudulent and no proof of any wicked or other intention (other than an intention to induce) on the part of the representor is required by the law; or if it is necessary to establish an intention to deceive or injure, that intention is immediately and irrebuttably presumed in law from the mere act of making the misrepresentation without such belief.

Section 760 Representation Subsequently Discovered by Representor to be False

Where a representation is a continuing one and where, between the time when it was made and the time when the representee altered his position on the faith of it, either (1) the representor discovers that his original statement which, when he made it, he honestly believed to be true, was false, or (2) supervening events render, to the knowledge of the representor, his statement no longer true, a duty to disclose the changed situation to the representee may arise. In such cases the mere fact that the statement may have been innocently made, though false, or true when made, will not, it seems, prevent the representee from establishing fraud where he can show that the representor dishonestly failed to discharge the duty of disclosing the change in the situation.'

The above demonstrates that, particularly in terms of civil liability, the term "fraud" is widely drawn. For example, it extends to the deliberate submission of understated accounts and incorrect tax returns.

The U.K. also introduced the Fraud Act in 2006. The Fraud Act 2006 defines fraud in three categories:

- Fraud by false representation
- Fraud by failing to disclose information
- Fraud by abuse of position

The Act states in all three categories that there must be an act of dishonesty.

The tests for dishonesty for many years were linked to two tests as set out in *R v Ghosh* [1982] EWCA Crim 2b.

The *Ghosh* test provided a two-limb test, which required juries to consider the following:

- Whether the conduct complained of was dishonest by the lay objective standards of ordinary reasonable and honest people (the "objective test") and
- If yes, whether the defendant must have realized that ordinary honest people would so regard his behaviour (the "subjective test")

More recently Ghosh has been surpassed by a number of judgements, including the Court of Appeal in *Booth and another v R* [2020] EWCA Crim.

In *Booth*, the central issue was the status of the Supreme Court decision in the civil case of *Ivey v Genting Casinos (U.K.) (trading as Cockfords Club)* [2017] U.K.SC 67 regarding the test for dishonesty in criminal cases. The Court of Appeal held that it was bound to a new two-stage test:

- What was the defendant's actual state of knowledge or belief as to the facts? (subjective)
- Was the defendant's conduct dishonest by the standards of ordinary, decent people? (objective)

"A key part of the changes was to introduce new terms such as 'deliberate' and 'deliberate behavior.'"

WHAT ABOUT DELIBERATE BEHAVIOR?

In 2007, H.M.R.C. undertook a significant review of its investigatory and administrative tax powers. This resulted in huge changes to its powers to raise assessments, seek information and charge penalties, among many other things.

A key part of the changes was to introduce new terms such as "deliberate" and "deliberate behavior." This replaced the previous use of terms "fraud" and "fraudulent behavior." As someone who participated in the professional consultations at the time, it was clear that while these were new terms they were to be regarded as a cut across from the old rules. But over the years there has been case law and various interpretations, not always confirming the cut across intended.

There is some legislative assistance in (TMA 1970, s. 118(7)). It confirms that, within the meaning of "deliberate," is the following:

> In this Act references to a loss of tax or a situation brought about deliberately by a person include a loss of tax or a situation that arises as a result of a deliberate inaccuracy in a document given to H[is] Majesty's Revenue and Customs by or on behalf of that person.

But this clearly doesn't provide clarity on the meaning.

A number of cases have all looked at the common law meaning of the term "deliberate." Included are *Auxilium Project Management v H.M.R.C.* [2016] U.K.F.T.T. 249, *Cliff v H.M.R.C.* [2019] U.K.F.T.T. 564, *Leach v H.M.R.C.* [2019] U.K.F.T.T. 352 (TC), and *Tooth v H.M.R.C.* [2021].

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In *Auxilium*, the F.T.T. stated as follows:

> "* * * a deliberate inaccuracy occurs when a taxpayer knowingly provides H.M.R.C. with a document that contains an error with the intention that H.M.R.C. should rely upon it as an accurate document. This is a subjective test. The question is not whether a reasonable taxpayer might have made the same error or even whether this taxpayer failed to take all reasonable steps to ensure that the return was accurate. It is a question of the knowledge and intention of the particular taxpayer at the time.

In *Tooth*, the Supreme Court stated as follows:

> * * * for there to be a deliberate inaccuracy in a document * * * there will have to be demonstrated an intention to mislead the Revenue * * *."

Current case law therefore states there must be an intention to mislead H.M.R.C. for the submission of an incorrect document to be treated as arising from deliberate behavior or inaccuracy and the administrative matters that turn on that intent, such as extended assessing time limits and increased civil penalties.

THE U.K. CIVIL APPROACH TO TAX FRAUD

C.O.P. 9

If H.M.R.C. discover tax fraud or fraud is prevalent when an individual is considering making a voluntary disclosure it is important to be aware of the main tool available to handle cases of tax fraud within a civil investigation. This is H.M.R.C. Code of Practice 9 ("C.O.P. 9").

> Under COP 9, the recipient is given the opportunity to make a complete, accurate, open and honest disclosure of all their deliberate behaviour bringing about a loss of tax or duty (and all other irregularities in their tax affairs, including basic mistakes). In return HMRC effectively provide an undertaking not to commence a criminal investigation for the matters disclosed. COP 9 has had various iterations over its many years of existence, including at one point the requirement of a formal interview under criminal caution under the UK Police and Criminal Evidence Act (PACE) rules. However, that was dispensed with some time ago and we saw the latest iteration of COP 9 being introduced in July 2023.

C.O.P. 9 in Practice

At the beginning of a C.O.P. 9 investigation the recipient is asked to sign a contract known as the Contractual Disclosure Facility ("C.D.F."). The C.D.F. contract effectively sets an understanding of what is required under C.O.P. 9 and that the recipient will abide by those terms. A rejection of the contract (or failing to reply) will risk H.M.R.C. commencing a criminal investigation.

Where the C.D.F. is accepted, an important next step is to submit an outline disclosure within 60 days. This should set out the basic issues around any fraudulent acts such as "what happened," "when did it occur," "how much was involved," and "what entities or what people are involved." Most importantly the outline disclosure is a statement confirming a loss of tax to H.M.R.C. from deliberate behavior. The burden of proof for deliberate behavior is on H.M.R.C., and so the up-front confirmation by the C.O.P. 9 recipient extent overcomes the point to some.

In some straight forward cases, the outline disclosure might amount to the whole disclosure. However, in larger more complex cases, it will often be necessary to work towards preparing and submitting a more detailed disclosure report further down the line. As long as H.M.R.C. accept the outline disclosure, the case can continue. The submission of the outline disclosure can be a stressful time for clients as H.M.R.C. have been known to reject outline disclosures, and this could again result in a criminal investigation. It is therefore essential to spend sufficient time and effort to ensure the Outline disclosure is not rejected.

An important aspect of C.O.P. 9 will be holding an opening meeting with H.M.R.C. where they can satisfy themselves that the recipient understands what is required, and his or her commitment to the process. It is also an opportunity for the H.M.R.C. investigator to ask questions about the outline disclosure and other questions about the recipient's tax affairs and circumstances more broadly. Opening meetings can last several hours and be incredibly detailed, and so it is essential to spend significant time in preparing for such meetings.

At the point that the final disclosure is submitted to H.M.R.C., it must be a complete and accurate disclosure. Disclosures will often involve the submission of various H.M.R.C. certificates, including signed certificates confirming details of bank and credit card accounts held and a statement of personal assets and liabilities held at specific points in time. It goes without saying these certificates must also be comprehensive and accurate. Errors in such certificates can result in the protection of C.O.P. 9 being lost and the commencement of a criminal investigation taking place, at the time of submission, or often many years down the line where errors are discovered.

H.M.R.C. will also expect a signed Certificate of Full Disclosure, where the C.O.P. 9 recipient makes a formal statement that they have made a complete and full disclosure. Again, if at some later point H.M.R.C. become aware that the disclosure was not full and accurate this certificate again could form part of a criminal investigation.

Once the investigation phase has completed and lost tax identified and agreed upon, discussions progress to penalties. H.M.R.C. charges interest on late paid tax (9% from April 2025). This is set in legislation, and there are very limited opportunities to mount successful arguments that interest should not apply.

The calculation of penalties and the number of back years H.M.R.C. can assess is now a complex affair in the U.K. It is important to recognize that where tax fraud is in point because of deliberate behavior – the current legislative language for civil penalties linked to tax fraud – H.M.R.C. are able to assess tax back 20 years. In certain cases of Inheritance Tax there is no time limit.

The U.K. made significant changes to the civil tax penalty regime in 2007. Prior to 2007, penalties were fairly straight forward. H.M.R.C. could charge penalties of up

to 100% of lost tax in cases of negligence or fraudulent behavior. These penalties could then be mitigated up to 100% based on factors such as disclosure, cooperation, size, and gravity. The change in 2007 brought in minimum penalties and also different rates for different categories of offence, such as carelessness, deliberate behavior, and deliberate behavior with concealment.

H.M.R.C. also applies different penalty rates depending whether the tax offences were voluntarily disclosed, or were identified by H.M.R.C. after having opened an enquiry. Deliberate penalties range between 20% and 70% and penalties for deliberate with concealment range between 30% and 100%. The penalty range can be mitigated to take into account disclosure, cooperation, and providing access to the relevant documents or issues. Careless behavior results in penalties of between 0% and 30%, and also the possibility of penalties being suspended.

"If the above isn't complicated enough, the U.K. brought in numerous different penalty provisions where the underlying lost tax is linked to offshore matters."

If the above isn't complicated enough, the U.K. brought in numerous different penalty provisions where the underlying lost tax is linked to offshore matters. In 2011 these provisions brought in the concept of an offshore multiplier linked to the category of the jurisdiction in which the tax offence occurred. The categories are linked to the commitments of those jurisdictions to international exchange of information agreements. For example, jurisdictions fully signed up to the O.E.C.D. Common Reporting Standard ("C.R.S."), or F.A.T.C.A. in the case of the U.S., the penalty limits stayed the same as for U.K. domestic offences. However, where countries involved lack exchange of information agreements, the penalties are double the domestic penalties, so the maximum penalty becomes 200%. In 2016, H.M.R.C. brought in penalties of 10% of the value of assets linked to the offshore noncompliance. Many other penalties and rules and categories exist, but are beyond the scope of this article.

Having agreed on tax, interest and penalties, the investigation will be concluded with a legal written contract.

Burden of Proof

In cases of fraud or deliberate behaviour the burden of proof rests with H.M.R.C.

Anti Money Laundering

One area that is highly relevant when looking at tax fraud and deliberate behavior is that of ancillary A.M.L. issues. Tax evasion is an indictable crime in the U.K. and as such falls squarely within the U.K. Anti Money Laundering Regulations and the Proceeds of Crime Act 2002, including the requirement for making Suspicious Activity Reports and in many cases seeking Consent Orders from the National Crime Agency. Consideration should always be given to A.M.L. obligations when any tax adviser discovers or seeks to act for clients with such issues.

CROSS BORDER TAX INVESTIGATIONS

For several decades the U.K. and H.M.R.C. has focused heavily on tax risk arising from cross border activities. That can include simple cases of U.K. residents holding bank accounts offshore, but it also extend to complex international tax structuring.

Companies as Targets

As part of H.M.R.C.'s strategy to counter cross border tax avoidance and fraud, H.M.R.C. has introduced various initiatives, beginning with the offshore disclosure campaigns starting in 2007, proceeding to the Requirement to Correct offshore noncompliance in 2017, and the introduction of various new penalty regimes as mentioned above. H.M.R.C. has also focused its criminal investigation capability and significant civil investigation resources on the tax gap associated with offshore matters.

Like many other countries, the U.K. has significant tax provisions designed to protect its tax base. Following the O.E.C.D. Model Tax Convention, it has Transfer Pricing, Permanent Establishment, Controlled Foreign Company and Anti-Hybrid rules, and most of the other model articles. The U.K. signed the Base Erosion Profit Shifting (B.E.P.S.) Multilateral Instrument. The U.K. has over 100 tax treaties. it has introduced its own Digital Services Tax, and in 2015, the Diverted Profits Tax ("D.P.T.") to counter structures set to avoid taxation of permanent establishments or to meet Transfer Pricing requirements.

H.M.R.C. regularly investigates overseas companies where it believes they resident in the U.K. because they believe Management and Control takes place in the U.K. This test is broadly similar to that of effective management and control as set out in the O.E.C.D. Model Convention articles.

The U.K. also introduced additional corporate criminal offenses in the 2017 Criminal Finances Act. They apply where a U.K. company – or in some cases and overseas company doing business in the U.K. – fails to prevent the facilitation of tax evasion in the U.K. or overseas.

Private Clients as Targets

Significant provisions are also available to counter offshore avoidance and fraud linked to private clients. This includes penalties for tax advisers. H.M.R.C. carefully monitors those U.K. resident non-domicile clients claiming the remittance basis.

In recent times we have seen criminal investigations and many serious civil fraud investigations in this area. Under the current rules that will change in April 2025, non-doms who have been resident in the U.K. for more than seven out of the previous nine years must pay a remittance basis charge ("R.B.C.") in order to continue to limit their taxation to U.K. situs income. Under the current regime, they are taxed only on foreign income and gains ("F.I.G.") that are remitted to the U.K. Currently that charge is £30,000. After 12 years out of the previous 14 of residence, the R.B.C. increases to £60,000.

We have seen many investigations where the R.B.C. has not been paid, yet the non-dom files a tax return without paying tax on offshore F.I.G.. If the nonpayment of the R.B.C. is deliberate, the basic elements for H.M.R.C. to conduct a criminal investigation exist. Also, where taxable remittances are made to the U.K. or complex structures are created to mask taxable remittances to the U.K., H.M.R.C. could mount a criminal investigation under the rules discussed above.

Often in these cases, tax advisers are involved. There are significant risks for advisers, as well as the non-dom client. In addition to the risk of a criminal investigation, H.M.R.C. has many new civil powers to charge significant civil penalties on

intermediaries linked to serious offshore noncompliance. In 2009 H.M.R.C. were also given powers by the U.K. Government to publicly name taxpayers or agents associated with serious tax noncompliance.

It is important to understand that the U.K. has powers to impute the income of offshore structures to U.K. residents by way of the Transfer of Assets Abroad ("T.O.A.A.") rules and also to tax U.K. resident participators on capital gains made by offshore companies. Both of these provisions can tax the U.K. resident, even where no benefit, income, or distribution has been received from the structure.

The T.O.A.A. rules can charge tax to a U.K. resident on income arising in an offshore structure where (i) there has been a relevant transfer of assets, and as a result, (ii) income arises to an overseas person. Note that the transferred assets need not have been in the U.K. prior to the transfer. Note also that the transferee can be an individual, trust, or company. The charge applies where the U.K. resident can benefit, so this is not restricted to amounts actually paid out currently. The rules can also tax beneficiaries but in those cases a benefit must be realized.

The T.O.A.A. rules will not apply where the offshore structure has been set up for commercial purpose or where tax avoidance was not a motive. For the exemptions to apply, they must be claimed in tax returns. In part, because of the complexity of these rules, they are hugely misunderstood, and so incorrect claims are common. Also, many situations are simply not reported to H.M.R.C.

However, where matters have been deliberately ignored or false claims made serious tax investigations can result, including criminal investigations. The T.O.A.A. rules have been viewed at times as providing an infringement to the rights of E.U. citizens Cases include *Commissioners for His Majesty's Revenue and Customs (respondent) v Fisher and another (Appellants)* [2023]U.K.SC 44. As a result, the rules were changed to try and make them more E.U. compliant. Nonetheless, with the U.K. leaving the E.U. and the sunset of E.U. retained law on December 31, 2023, U.K. citizens no longer can benefit from such protections. Whether E.U. citizens resident in the U.K. can continue to rely on the infringement arguments is beyond the scope of this article.

Non-doms claiming the remittance basis often have been sheltered from these rules. With the ending of the remittance basis in April 2025, former non-doms will face significant liabilities unless they qualify for the new four-year F.I.G. protections. Given the Government's Budget commitments to increase the number of investigations undertaken, this group will most definitely see more investigations.

The U.K. also has provisions to tax U.K. resident participators on gains in nonresident companies where they hold on their own or with associates 25% of the shareholdings of the nonresident company. Again, there are more recent exemptions linked to motive and again non-doms claiming the remittance basis may have been historically shielded, but just as for T.O.A.A., the rules are often overlooked leading to significant tax noncompliance, some undertaken deliberately.

Fund Managers

London and the U.K., as a major world financial center has resulted in H.M.R.C. opening investigations into asset managers, hedge funds, and private equity businesses for offshore noncompliance and fraud. The U.K. also introduced significant tax provisions specifically to tax disguised management fees and treat them as U.K.

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source to limit treaty protections. This has included criminal investigations linked to fraudulent transfer pricing positions taken. Again, it is important to appreciate that if transfer pricing adjustments are made without real foundation, and those adjustments were made deliberately, the elements of tax fraud would be present.

Often fund structures will be located in low or zero taxation jurisdictions, in part to reduce tax leakage for investors. Asset managers can share in the profits of the funds by way of tax structuring often using a mixture of opaque and transparent tax structures, mostly in the form of partnerships. Where asset managers are U.K. resident, they should always undertake a detailed review of the whole structure in case there are exposures to T.O.A.A.

The U.K. also introduced Profit Fragmentation rules in 2019. These rules apply where the following fact pattern exists:

- There has been a transfer of value from the U.K. trader to an offshore entity – this could take the form of a diversion of income to the offshore entity or payment of expenses to the offshore entity.
- The effect of the arrangement is that a significantly lower level of tax is paid on the profits than would be the case if they were correctly taxed in the U.K. in accordance with the current law.
- The proprietor of the business, whether a sole trader or partner in an unincorporated business, or as director or shareholder of a company, is able to enjoy the profits that have been diverted.
- The U.K. person must have arranged for the profits to be diverted to the offshore entity.
- The diversion or payments mentioned in the first bullet above are not commensurate with the work undertaken by the offshore entity.

Where these conditions are present, the arrangement can be counteracted by bringing the profits back into U.K. tax by attributing the correct amount of profits to the U.K. taxable source.

EXCHANGE OF INFORMATION

A significant part of H.M.R.C.'s armory when it comes to countering tax fraud and avoidance both domestically and internationally is the huge amounts of data it receives. When introducing the self-assessment system in 1997, the U.K. invested heavily in technology and continues to do so. Currently, H.M.R.C. is seeking to hugely digitize the tax system.

H.M.R.C. plays a significant role within the O.E.C.D. and was an early adopter of the O.E.C.D. Common Reporting System in 2016. As an early member of the E.U., the U.K. fully participated in the exchange of information mechanisms via the E.U. Directive of Administrative Cooperation ("D.A.C."). Since Brexit, the U.K. has continued to participate hugely in international exchange mechanisms by way of its membership in the O.E.C.D., through the Mutual Assistance in Taxation Convention ("M.A.C."), through its many treaties, and through multilateral and bilateral exchange of information agreements.

The U.K. is also a significant contributor to the O.E.C.D. Tax Inspectors Without Borders initiative. Tax payers should be cautious as the O.E.C.D. plans to use its Tax Inspectors Without Borders initiative to assist new O.E.C.D. members investigating Pillar II rules.

We see many information notices issued to tax residents in the U.K. by H.M.R.C., as a result of requests made by tax authorities overseas. Advisers should also review these requests carefully to ensure they meet their own countries domestic information powers but also that they meet the U.K.'s own domestic rules. The U.K. has many of its own safeguards and limitations on information notices and any request from an overseas authority must comply with the U.K.'s own rules.

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