



Tax Administration  
Research Centre

# CHEATING THE PUBLIC REVENUE

## THE MEANING OF 'TAX AVOIDANCE' AND 'TAX EVASION' IN LAW

# Tax Dogma

‘Tax Evasion is illegal but Tax Avoidance is (perfectly) legal.’

# 3 Legal Concepts

- **Cheating or fraud or dishonesty.**
- **Negligence or carelessness** or failure to take reasonable care.
- **Honesty** (compliance or non-compliance due to honest mistake).

# Negligence

‘The test is to consider what a reasonable taxpayer would have done.’

Judge Berner in *Anderson v HMRC* [2009] UKFTT 206 at para 22.

# Cheating the Public Revenue

‘Cheating can include any form of fraudulent or dishonest conduct to **prejudice** the Revenue’s right to the tax in question.’

Justice Hardy, *R v Less* (*The Times*, March 30, 1993).

# General Law

## Criminal Law

- Common law offence of cheating the public revenue
- Common law offence of conspiracy to defraud
- Fraud Act 2006

## Civil Law

- Common law civil fraud
- Judicial anti-avoidance principles (e.g. the Ramsay Principle)
- Schedule 24 of Finance Act 2007

# HMRC's Criminal Investigation Policy

'It's HMRC's policy to deal with fraud by use of the cost effective civil fraud investigation procedures under Code of Practice 9 wherever appropriate.

Criminal investigation will be reserved for cases where HMRC needs to send a strong deterrent message or where the conduct involved is such that only a criminal sanction is appropriate.'

# Legal Nonsense

‘peculiar concepts not defined in terms of empirical fact or ethics but used to answer empirical and ethical questions, and thus bar the way to intelligent investigation of social fact and social policy.’

Cohen, ‘The Nature of Legal Nonsense’ (1935) *Columbia Law Review*, 809, p.820.

# Misselling

‘the act of selling something that is not suitable for the person who buys it.’

*Cambridge English Dictionary*

# Legal Nonsense in Tax

- Tax Evasion\*
- Tax Avoidance, Tax Shelter
- Aggressive Tax Avoidance
- Tax Mitigation, Tax Planning, Tax Minimisation, Tax Optimisation
- Transfer Mispricing
- Base Erosion and Profit Shifting (BEPS)
- Abuse

# Tax Evasion & Tax Avoidance

## Tax Evasion

- T's income = £1.1M
- T declared £100K on SA tax return
- T concealed £1M from the Revenue
- Loss to the public revenue > £400K

## Tax Avoidance

- T's income = £1.1M
- T declared £100K on SA tax return
- T claimed tax scheme sold by tax advisers eliminated £1M
- IT loss to the public revenue > £400K

# My Definition of Tax Evasion

Cheating the public revenue by a **taxpayer** who deliberately (a) fails to make a return or (b) makes a false return of the relevant tax liability without using a tax scheme.

- *R v Mavji* [1987] 1 W.L.R. 1388.
- *R v Hudson* [1956] 2 Q.B. 252.

# My Definition of Tax Avoidance

Cheating the public revenue by **the professional advisers** that devise, market, implement and otherwise facilitate the use of **tax schemes** in which the taxpayer using a scheme may or may not be complicit.

- *R v Charlton, Cunningham, Kitchen and Wheeler* [1996] S.T.C. 1418.

# *R v Charlton, Cunningham, Kitchen and Wheeler*

‘These defendants were convicted on 14 counts of cheating the public revenue. Kitchen and Wheeler are qualified accountants. Charlton has practised for many years as an accountant, as a partner in a firm called Charltons, but was not professionally qualified. Cunningham is a barrister practising at the Revenue Bar.’

# Cheating by the Professional Enablers

‘The case for the prosecution was that Charlton had **devised** a dishonest, tax-avoidance scheme for the benefit of some of the firm’s clients and that the defendants were involved with the **implementation** of the schemes.’

# Base Erosion & Profit Shifting (BEPS) or Transfer Mispricing

‘The accounts presented to the Revenue by the UK companies were false in that by using Charlton’s scheme to transfer part of their profits to the Jersey companies they were not disclosing the full extent of the profits they had made. Each of the defendants was charged with cheating the Revenue by “falsely representing that the apparent purchases (by the UK company) from (the Jersey company) were bona fide commercial transactions”.’

# Taxpayer's Immunity in Tax Avoidance

‘if a taxpayer reasonably relies on a reputable accountant for advice in relation to the content of his tax return then he will not be liable to a penalty for negligence or fraud.’

Judge Cannan in *Hanson v HMRC* [2012] UKFTT 314 at para 21.

# Google

**‘Q195 Caroline Flint:** Does the fact that Google have paid £130 million, of which £18 million is interest, reflect that they did not pay enough tax?

**Jim Harra:** Yes, it clearly does.

**Q196 Caroline Flint:** If that is the case, why hasn't HMRC applied any penalties to Google for non-payment of tax?

**Jim Harra:** In order to attach a penalty, we have to demonstrate two things: first of all, that the return was wrong – and it clearly was in this case – and secondly, that insufficient care was taken in producing the self-assessment. The challenge in transfer pricing is that they can take a lot of expert advice and opinion, and can take a reasonable position in relation to a complex area of law. We can challenge that and they can accept that they need to change their position, but it is very difficult to establish that they have taken insufficient care.'

# Normal Stages of a Tax Scheme

1. Promoters devise a scheme.
2. QC (Queen's Counsel) '**blesses**' the scheme.
3. Promoters sell scheme to the Taxpayer (T).
4. **T uses scheme to avoid tax in tax return.**
5. Revenue disagrees and demands the tax.
6. T appeals to the Tax Tribunal.
7. Tribunal judges **the scheme** as a matter of statutory construction and/or under the *Ramsay* principle.

# Working Wheels Tax Scheme

- Promoted by NT Advisors (NTA) Ltd.
- Used by 450 wealthy individuals (including Chris Moyles) to avoid IT and CGT.
- Estimated tax avoided - £1.26 billion (40% of £3.15 billion).
- Estimated payments to NTA - £157 million (5% of £3.15 billion).
- Estimated further payments to NTA - £94.5 million (3% of £3.15 billion).

# How a Tax Scheme Works

‘A common starting point is to find a statutory relief or other provision in the tax code normally invoked to obtain a reduction in a taxpayer’s liability in the context of some commercial transaction.

A transaction bearing a marked resemblance to such a commercial transaction is then engineered and the relief or deduction is claimed.’

# Trade Loss Relief

A person may make a claim for trade loss relief against general income if the person (a) carries on a trade in a tax year, and (b) makes a loss in the trade in the tax year.

**Section 64 Income Tax Act 2007**

‘Trade’ includes any venture in the nature of trade.

**Section 989 Income Tax Act 2007**

**Section 261B Taxation of Chargeable Gains Act 1992**

# Flanagan

- 12/3/07 – received scheme documents.
- 5/4/07 – tax year 2007-08 ended.
- 15/01/08 – submitted tax return for 07-08:
  - total **income of £5,902,112**
  - traded in buying and selling used cars from 16/3/07 to 5/4/07 but **sold no car**
  - made a **loss of £5,000,284**

# Details of Alleged Loss

- Cost of cars - £100
- Turnover - £0
- Bank interest (loan of £7,500\*) - £184
- **Finance cost (loan of £7,500\*) -  
£5,000,000**

\* Total income of £5,902,112

(1) In calculating the profits of a trade, a deduction is allowed for incidental costs of obtaining finance.

(2) '*Incidental costs of obtaining finance*' means expenses (a) which are incurred on fees and other incidental matters, and (b) which are incurred wholly and exclusively for the purpose of obtaining the finance.

# Moyles & Stennett

## Allan Stennett

- Trade loss relief - £14,500,192
- Bank interest (£10,500 loan) - £192
- **Finance charge (£10,500 loan) - £14,500,000**

## Chris Moyles

- Trade loss relief - £1,000,159
- Bank interest (on £7,000 loan) - £159
- **Finance charge (on £7,000 loan) - £1,000,000**

# Civil Litigation v Criminal Prosecution

## *Moyles & Others*

‘It is not disputed that the purpose of the scheme was to **manufacture a tax loss much greater than any true economic loss** at little or no financial risk to the user’.

## *Charlton & Others*

‘Each of the defendants was charged with cheating the Revenue by “falsely representing that **the apparent purchases** (by the UK company) from (the Jersey company) **were bona fide commercial transactions**”.’

# Statutory Construction v Cheating

## ***Moyles & Others***

‘The issues in the appeals are, first, whether each of the appellants was carrying on a trade in used cars under s 64 of ITA and, second, whether in calculating the profits of that trade, there should be allowed a deduction under s 58 of ITTOIA for the incidental costs of obtaining finance.’

## ***Charlton & Others***

‘The case for the prosecution was that Charlton had devised a dishonest, tax-avoidance scheme for the benefit of some of the firm’s clients and that the defendants were involved with the implementation of the schemes.’

# Civil Fraud or *Ramsay* Principle

‘As a further alternative, HMRC contend that the scheme was an **abuse** in the sense developed in *W T Ramsay Ltd v Inland Revenue Commissioners* [1982] AC 300 (“Ramsay”).’

# HMRC's Definition of Tax Evasion

Tax evasion is an illegal activity, where registered individuals or businesses deliberately omit, conceal or misrepresent information in order to reduce their tax liabilities.

# HMRC's Definition of Tax Avoidance

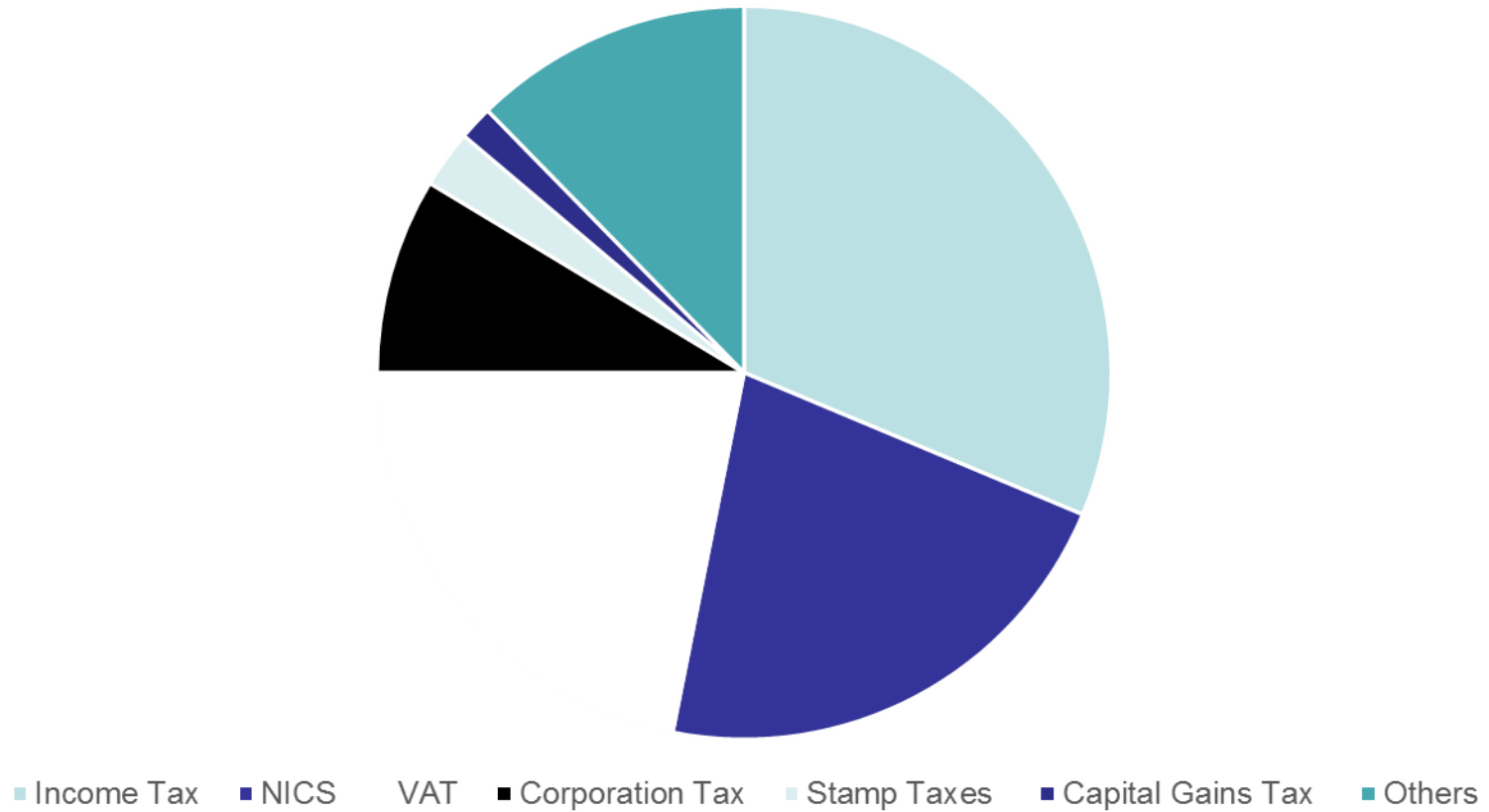
‘Avoidance is bending the rules of the tax system to gain a tax advantage that Parliament never intended. It often involves contrived, artificial transactions that serve little or no purpose other than to produce a tax advantage. It involves operating within the letter, but not the spirit, of the law.’

# HMRC's Definition of Tax Planning

‘Tax avoidance is not the same as tax planning. Tax planning involves using tax reliefs for the purpose for which they were intended. For example, claiming tax relief on capital investment, saving in a tax-exempt ISA or saving for retirement by making contributions to a pension scheme are all forms of tax planning.’

# Background

UK Total Tax Revenues (2018-19) – £627.9bn



# Breakdown of £627.9bn

- Income Tax – £194.0bn (30.89%)
- PAYE – £162.57 (83.8%); **SA – £31.43 (16.2%)**
- NICS – £135.0bn (21.50%)
- VAT – £135.6bn (21.59%)
- **Corporation Tax – £53.5bn (8.52%)**
- **Stamp Taxes – £15.7bn (2.5%)**
- **Capital Gains Tax – £9.3bn (1.48%)**
- **Diverted Profits Tax – £0**
- Others – £84.8 (13.5%)