News round-up

Zahra Kanani sets out recent developments in anti-money laundering, enforcement and BPR

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From 1 April 2011, equitable liability was replaced by a new statutory, special relief. Special relief is a form of overpayment relief that can only apply to amounts charged in HMRC determinations for income tax self-assessment or corporation tax self-assessment where no other statutory remedy is available

The purpose of this article is to look briefly at the government's proposals in relation to the UK's anti-money laundering regime following the Budget 2011, the new 'special relief' for oppressed taxpayers and the availability of business property relief for group structures.

Anti-money laundering and the Budget

The Budget 2011 saw the launch of the government's 'Plan for Growth', which was described by the Chancellor, George Osborne, as 'an urgent call for action' to put the UK on a path to sustainable, long-term economic growth. In the 'Professional and Business Services' section, the government set out its proposal to consult on the Money Laundering Regulations 2007 (the Regulations).

In 2009/10 the Treasury conducted a thorough review of the Regulations. The Regulations implemented the third EU Money Laundering Directive and the Treasury committed to a review once the Regulations had been in place for two years. The review was published on 7 June 2011 and focused on whether the Regulations were effective and proportionate in practice, identifying where they were working well and where there may be room for improvement, together with a series of consultative proposals to amend the regulations.

In particular, the government consulted on its proposal to abolish over two dozen regulatory criminal offences for businesses that fail to have the appropriate systems and controls in place to combat money laundering. This would allow businesses to implement a fully risk-based approach, where businesses make their own assessment of the risks they face and implement appropriate systems and controls. The risk-based approach is central to the UK anti-money laundering regime and means that the steps required of a regulated firm should be proportionate to the risk perceived by the business. Civil penalties will remain and the government consulted on whether regulators should have the power to impose additional penalties. The impetus behind the move is to ensure that the regulations continue to deliver an effective and proportionate anti-money laundering regime, in particular to ensure the UK financial system is a hostile environment for money laundering and terrorist finance, while minimising the burdens they impose on businesses.

The Law Society welcomed the Treasury's plans to hold a consultation and described it as a 'victory for proportionality'. The Law Society called for the abolition of the criminal offences under the Regulations in the 2009 House of Lords inquiry and the 2009/10 review of the Regulations. It is lobbying for a more proportionate anti-money laundering regime and urged solicitors to respond to the consultation (which closed on 30 August 2011).

Responding to the government's announcement, Law Society chief executive Desmond Hudson said that:

> while firms will still need to conduct due diligence and report suspicions of money laundering, they will no longer need to fear a criminal conviction if a passport they have on file goes out of date

> or if they did not get the right number of utility bills or bank statements for every director of a company they are instructed by... We believe it will help law firms take a more risk-based approach so that they allocate resources more effectively rather than slavishly following a ticked box approach. Equally, this is by no means a suggestion that firms can go soft on anti-money laundering compliance.

The consultation will not affect the criminal penalties for money laundering under the Proceeds of Crime Act 2002 or the obligations of firms to report suspicious activity to the Serious Organised Crime Agency.

Equitable liability replaced by new 'special relief' for oppressed taxpayers

In the past, where customers had no statutory remedy to adjust an excessive adjustment or displace a determination because the time limit for submitting a return had passed, HMRC would, in some cases, be prepared not to pursue their legal right to recover the full amount due. This practice was known as 'equitable liability.' The purpose of the equitable relief liability concession was to provide a 'relief of last resort' for certain taxpayers, particularly those vulnerable taxpayers who were unable to fully engage with the tax system (for example, where customers were suffering from a temporary or sporadic illness, including mental illness).

HMRC was only prepared to consider applying equitable liability where it was clearly demonstrated that:

- the liability assessed or determined was greater than the amount that would have been charged had the returns, and necessary supporting documentation, been submitted at the proper time; and
- acceptable evidence was provided of what the correct liability should have been.

In such cases, HMRC would accept a reduced sum based on the evidence provided, if, in their view, it would be unconscionable to pursue recovery of the full amount.

From 1 April 2011, equitable liability was replaced by a new statutory special relief. Special relief is a form of overpayment relief that can only apply to amounts charged in HMRC determinations for income tax self-assessment or corporation tax self-assessment where no other statutory remedy is available. HMRC has published its guidance to officers in respect of the new relief. The guidance is particularly relevant to taxpayers who have received income tax or corporation tax determinations from HMRC and whose tax affairs have been in arrears for several years. As a result of the changes, HMRC will no longer accept new requests for equitable liability, but will still continue to consider those claims for equitable liability received before that date.

Taxpayers will still be able to make a late appeal against amendment or assessment if they have a reasonable excuse for not having appealed within time or if they apply to the tribunal. There is no right of appeal against an HMRC determination where a customer has not submitted a self-assessment return. Instead, taxpayers who disagree with the determination should displace it by submitting a self-assessment return. From 1 April 2011, taxpayers who are out of time to make a self-assessment to displace a determination, and are unable to claim overpayment relief, may be able to claim special relief.

How it works

A person (individual or company) who has received a notice to make a return must do so by the filing date. Where this obligation is not met, HMRC has the power to raise a determination of the liability due and unpaid to the best of their knowledge and on the basis of the information available to them. Where HMRC issues such a determination, the sum on it becomes the amount that is legally due to be paid. There is no right of appeal against a determination. However, submission of the return will displace the determination and the determined amount of tax will be automatically amended to the return amount, provided the return is received within the relevant time limits.

If these time limits are not adhered to, subject to what follows, a person may claim special relief if HMRC has made a determination in the absence of a return for a year of assessment or accounting period, and:

- the person is out of time to displace the determination; and
- they are unable to claim overpayment relief.

The Law Society called for the abolition of the criminal offences under the Regulations in the 2009 House of Lords inquiry and the 2009/10 review of the Regulations

Unlike claims for overpayment relief, there is no time limit for claiming special relief. Also, special relief is not automatically excluded whenever:

- a person knew, or ought reasonably to have known, that they had some other means of correcting an overpayment or over-assessment but they failed to use those other means within the relevant time limit; or
- HMRC has already taken court action to recover amounts due under a determination, unless the person was present or was legally represented during the proceedings, or an agreement was reached to settle the proceedings.

In addition, to qualify for special relief, a person must satisfy both the remaining requirements for overpayment relief and must meet three further conditions that reflect HMRC's former practice regarding equitable liability. These three conditions are as follows:

- In the opinion of the Commissioners, it would be unconscionable for HMRC to seek to recover the amount that has been charged by a determination, or refuse to repay it if it is has already been paid. HMRC's guidance states that 'unconscionable' means 'completely unreasonable' or 'unreasonably excessive'. HMRC cannot simply disregard the time limits for making a self-assessment if it appears a determination might be excessive. Further circumstances must exist that make it unconscionable to recover the full amount due under the determination, or not to repay an amount already paid. Such circumstances could be temporary or sporadic illness (including mental illness), non-receipt of notices or insolvency.

- The person's tax affairs are otherwise up to date, or arrangements have been made to the satisfaction of the Commissioners to bring them up to date as far as possible.

- The person has not previously claimed special relief or sought equitable liability (whether or not relief was given).

The Enforcement Insolvency Service is responsible for determining whether a claim to special relief can be accepted and, in particular, whether these three conditions are met.

Special relief is intended as a final and exceptional remedy where it would be unconscionable for HMRC to pursue tax that is legally due. HMRC has a duty to Parliament and customers generally to collect the tax due under relevant tax law and to ensure that the tax system is operated fairly.

In order to qualify for Business Property Relief, it is necessary to establish that there is indeed a 'business' at all.

Is Business Property Relief (BPR) available for owners of a group holding company?

The Chartered Institute of Taxation (CIOT) has published its correspondence with HMRC concerning the availability of BPR for shareholdings in the holding company of a group of companies (where the holding company has made loans to the trading subsidiaries).

BPR is available where whole or part of the value transferred by a transfer of value is attributable to the value of the relevant business property. The relief operates by treating the whole or part of the value transferred as reduced by 100% (s104 Inheritance Tax Act 1984 (IHTA 1984)). Section 105(3) IHTA 1984 sets out a test where BPR is not available, ie all shareholdings potentially qualify for BPR unless the business of the company consists wholly or mainly of certain excluded activities. This section would preclude most group structures. However, there is an exception in s105(4)(b) IHTA 1984 for holding companies. This exception does not focus on the group as a whole but on the business of each separate company in that group. The nature of each company's business is looked at, starting with the business being carried on by the holding company.

A typical scenario would involve a holding company (HoldCo) whose main activity is holding shares in trading subsidiaries (so that the HoldCo does not fall within s105(3) IHTA 1984). In addition to its shareholding in the trading subsidiaries, the holding company may also have made intra-group loans to the trading subsidiaries. In order to qualify for BPR, it is necessary to establish that there is indeed a 'business' at all.

The crucial test as to whether BPR applies is whether the business of HoldCo consists predominantly of being a holding company of one or more companies (s105(4) IHTA 1984). There is a definition of 'holding company' in s1159 Companies Act 2006 (CA 2006) that simply refers to a company being a subsidiary of another company (its 'holding company') if the holding company:

- holds a majority of votes in the subsidiary;

- is a member of the subsidiary and has the right to appoint and remove the majority of its board of directors; or

- is a member of it and controls… a majority of the voting rights in it.

Schedule 6 of the Companies Act 2006 contains some further amplification of the above tests but does not alter the substance of s1159 CA 2006.

CIOT queried whether the incorporation of s1159 CA 2006 into s105(4)(b) IHTA defined 'holding company' or 'the business of being a holding company'. CIOT states that this distinction is important because if s1159 CA2006 provides an exhaustive definition of the business of being a holding company, then other activities (such as loans to subsidiaries) presumably do not form part of the business. Conversely, if the business of being a holding company is a wider concept, then providing loan finance to subsidiaries would, in CIOT's view, be treated as an ordinary activity that many holding companies would undertake. CIOT prefers the latter view but put forward this query to HMRC, although, in its opinion, the wider definition still lacks clarity as to what the business of a holding company consists of. CIOT has suggested that the business of a holding company would include the following activities:

- holding shares in subsidiaries;

- co-ordinating the activities of those subsidiaries by means of voting control and the ability to control the subsidiary boards;

- provision of loan and other finance to those subsidiaries;

- providing strategic direction and oversight of the activities of subsidiaries, and ensuring that the subsidiaries work together to achieve a common aim;
- monitoring the financial performance of subsidiaries, providing a 'treasury' function and co-ordinating guarantees and cross-group collateral;
- providing a structure to allow ring-fencing of the activities of the subsidiaries, nurturing new higher-risk activities within the limited liability offered by subsidiaries, reorganising the businesses of subsidiaries as they change and grow; and
- managing relations with shareholders on behalf of all subsidiaries.

HMRC's response of 10 January 2011 acknowledged that s1159 CA 2006 defines the structural relationship between a holding company and a subsidiary in terms of control and voting rights, but agreed that applying this definition to IHTA 1984 did not provide any definition as to what the business of that holding company may be. HMRC confirmed that in determining what the main business of a company is, it looks at the activities undertaken by it to ascertain whether it falls within the provisions of s105(4)(b) IHTA 1984 and, in doing so, applies the factors set out in *Farmer & anor (executors of Farmer, deceased) v Inland Revenue Commissioners* [1999].

However, HMRC agreed with CIOT that the activities listed above are indicative of the business of a holding company. HMRC confirms that if these or similar activities predominate, and the group subsidiaries are themselves non-investment companies, then BPR would normally be available for shares in the holding company. In relation to intra-group loans, these are regarded as non-investment where the loans are used by the subsidiaries for the purposes of their non-investment businesses and the amounts are reasonable in the context of the group business as a whole. ■

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Farmer & anor (executors of Farmer, deceased) v Inland Revenue Commissioners
[1999] STC (SCD) 321

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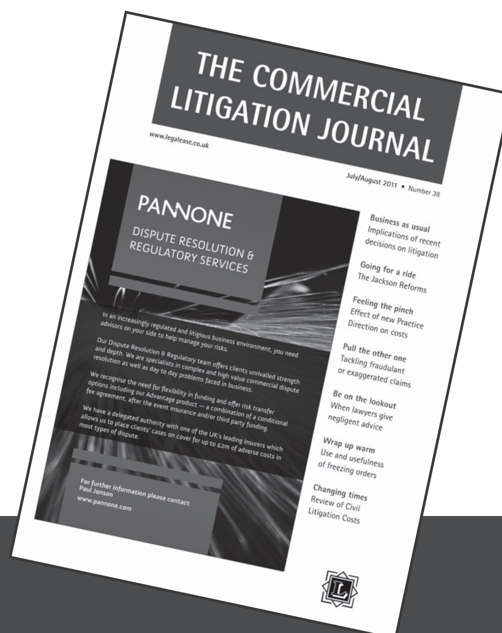

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