



Is Anybody There?

Following HMRC's victory in the recent Laerstate case, it is now certain that merely holding Board meetings abroad will not ensure that an offshore company is treated as resident outside of the UK where the company has UK connections, such as controlling UK shareholders. The purpose of this Business Tax Update is to review some of the key principles established by the Laerstate case, and to consider practical ways in which the residence status of offshore companies can be safeguarded against attack by HMRC.

Outline of the Laerstate Case

In summary, the facts of the case were:

- In 1992, Dieter Bock ("DB") purchased a Dutch registered company, Laerstate BV (LBV). He became a director on that date in addition to the existing director (Johannes Trapman - "JT" - a Dutch resident), and was sole shareholder throughout the period 1993 to 1996.
- LBV subsequently purchased a substantial shareholding in Lonrho plc funded by a loan taken out personally by DB. Two months later DB was appointed joint managing director and CEO of Lonrho plc ("Lonrho"). Despite being based in London, DB spent more than half of his time outside of the UK during the years in question.
- It was established that under both Dutch company law, and LBV's Articles of Association, a single director could make a binding decision on behalf of the company.
- In 1996, LBV sold the shares in Lonrho to a third party at a profit. Some months prior to this DB resigned as a director, but remained as shareholder.
- HMRC subsequently raised an assessment on the capital gain earned by LBV on the share sale, on the basis that it was UK resident at the time the gain was made.

LBV appealed against the assessment on the basis that it was not UK resident as all key decisions had been made outside the UK, and further that the important decisions about the sale of the shares were taken by JT, who was not UK resident.

However the Court found that, although JT had the power to bind the company, it was DB who made the key decisions, and these decisions were simply "rubber stamped" by JT. The Court cited the following evidence to support its conclusions:-

- There was a period of 18 months when there were no Board meetings.
- Many of the Board meetings did not consider strategic issues.
- There was some doubt over the whereabouts of DB for certain meetings - although the records showed that he attended the meetings, other evidence demonstrated that he could not have been there.
- Advice relating to the share sale was given to DB by his solicitors at meetings in London, and by letters addressed to him (and not to JT), and DB negotiated the details of the transaction with the third party. It did not appear that JT was kept up to date with these events during the relevant time.

Accordingly, it was held that LBV was UK tax resident by virtue of being managed and controlled from the UK.

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Practical implications of Laerstate

The key principles of corporate tax residence arising from the Laerstate case for offshore companies are summarised as follows:

- The residence status of an offshore company is a question of fact, and it should not be assumed that central management and control is necessarily carried on where the Board meets.
- In determining an offshore company's residence status, the whole picture needs to be considered, including a general review of how the offshore company's trade is carried out. It will not be sufficient to simply move certain acts of management to different territories. HMRC will look at where the real decisions are made, and not just where they are purported to be made.
- Whilst signing Board resolutions outside the UK is important, this alone is not sufficient to constitute central management and control. Board meetings should take place regularly outside the UK, and should involve the discussion of real and strategic issues, and sufficient information should be made available to enable the participants to make informed decisions. In addition, the Board minutes should reflect the real business of the meeting, and should not be based on pre-prepared or pro forma minutes.
- All directors should be kept informed of developments even if they are not able to take part in all meetings, and they should be given sufficient information to enable them to form their own view on matters.
- Detailed records of the attendance at Board meetings should be maintained. It was a feature of the Laerstate case that HMRC required access to all the documents supporting travel arrangements, as evidence of attendance at offshore board meetings. This included diaries, travel documents and receipts. For UK directors, in particular, it is therefore necessary to show that any management decisions are made offshore, and they should, where possible, attend Board meetings in person, rather than by telephone or via signing written resolutions.
- Advice from third parties (such as accountants or solicitors) should be given to the offshore company, and not to a UK resident director. In addition, instructions to these advisers should come from the offshore company, and not from any UK resident entity as this may give the impression of decisions being made in the UK.
- Offshore companies should ensure that the majority of directors are non-UK resident, and that no strategic decisions or communications are inadvertently made in the UK, such as via computer, telephone or mobile telephone in the UK.

Next Steps

The best way to defend an attack from HMRC on the residence status of an offshore company is to ensure that appropriate procedures are put in place and for evidence of those procedures to be properly maintained. For example, the offshore company should:

- Hold regular Board meeting offshore which most, if not all, of the directors should attend.
- Make appropriate documentation available before the meeting so that the directors are properly briefed on the issues to be considered.
- Ensure that all strategic decisions are made offshore, and are not first decided onshore before being "rubber stamped" at a later meeting offshore.
- Ensure that directors keep detailed meeting attendance records, including all travel documents.

Conclusion

Whilst it is not possible to be absolutely certain of an offshore company's residence status under the current UK tax regime, there are useful steps which an offshore company with UK connections can take to provide it with the best chance of defending itself against a challenge to its residence status from HMRC. Nevertheless, it is clear HMRC will no longer accept that simply holding Board meetings outside of the UK is sufficient to establish that an offshore company with UK connections is not UK resident.

If you are interested in discussing these issues further, then please speak to your usual Rawlinson & Hunter contact

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