

TAX TALKS

Australia's Tax News Podcast - The Podcast for Australian Tax Professionals

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26 | Offshore Tax Havens

Offshore tax havens facilitate aggressive tax planning, evasion, avoidance. Call it what you like. And so are a tricky, highly charged topic. It has become relatively easy to set up shop in a tax haven.

Offshore Tax Havens

People use offshore tax havens for different purposes, but often to avoid tax.

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Tax Haven

The word 'tax haven' is confusing since people and entities use offshore tax havens for various purposes.

There is the 'legal' use of tax havens by corporations or individuals. Large corporations register their headquarters in a low-tax jurisdiction and shift profits accordingly. In 2016 Google, Facebook and other US technology companies held an estimated US\$1.84 trillion of assets in offshore tax havens. Globe-trotting individuals also use offshore tax havens by actually becoming a tax resident there and hence reducing their tax bill. All this does not result in the actual breaking of any laws, but is a political issue. So doesn't affect our tax practices directly.

And then there is the use of tax havens by individuals to hide assets and often evade tax. An estimated US\$7.6 trillion or 8 per cent of global wealth is held offshore and a large proportion of that is probably to evade taxes.

Offshore Tax Haven

There is no single accepted definition of an offshore tax haven but any general definition would include five elements:

- 1) A foreign jurisdiction is involved.
- 2) An entity is incorporated under local (tax haven) law without any requirement to hold assets within the jurisdiction or have a locally resident director.
- 3) There is no publicly available register of shareholders or directors. And you have the right to secrecy of ultimate ownership.
- 4) Tax free status for any business, and
- 5) No requirement to file a tax return.

Most tax havens limit the company's activities to overseas activities. So you can hold as many overseas assets as you like in your international business company. But you can't open a local corner shop. Or any other local

business.

Agents and Intermediaries

The greatest challenge is finding a reputable registered agent or intermediary. There are a lot more intermediaries than registered agents. So when you search online, you will probably come across intermediaries rather than actual registered agents.

A registered agent is the one actually registered. The one with an actual address within the jurisdiction. They are the official agent holding the register of shareholders and directors.

An intermediary can be anybody. Intermediaries are usually lawyers or accountants – the ‘fixers’ – who set up offshore corporate structures. The intermediaries are usually not the registered agents in the offshore haven, but the ones doing the actual work.

ID

Upon incorporation of the international business company, the registered agents attend to KYC (Know your Client) on behalf of the offshore haven’s regulators.

The id requirements for directors are often more strict in offshore tax havens. In Australia there are no id requirement for company directors. Anybody can set up a company and doesn’t need to provide id. You could make your dog a director or a fictitious person. In tax havens the registered tax agent has to check id.

International Business Company

The international business company is the entity through which you set up shop in a tax haven. It is an offshore company formed under the laws of a ‘tax haven’ jurisdiction. Also known as international business corporation. International business companies usually have no residency and no assets in the actual tax haven.

Offshore Corporate Structure

The offshore corporate structure usually includes layering over several jurisdictions, nominee directorships and bearer shares to ensure secrecy while keeping clients in control of the assets. When layering, the ultimate ownership becomes opaque by adding multiple layers of corporate ownership and corporate directorships. A nominee director acts on behalf of another person following their instructions.

Director Duties

In Australia you can’t delegate director duties but in offshore tax havens you can. The nominee director gives power of attorney to the ultimate owner.

Ownership

Whoever holds the physical certificate of a bearer share owns the company. So actual ownership is impossible to trace.

Example

Let’s say Peter has cash on a Swiss bank account and wants to hide his identity. So he engages Fernando, an intermediary. Fernando sets up company A in Belize with bearer shares and makes his aunt Maria the nominee director. Fernando then gives the bearer shares to Peter.

He then sets up company B on the Cayman Islands and makes company A the director. Again, he gives the bearer shares to Peter.

And then Fernando sets up company C on the British Virgin Islands, makes company B the director and gives the bearer shares to Peter.

He gets Company C to set up a bank account somewhere in an offshore tax haven. The cash is then transferred to this bank account.

So company C holds the actual assets, in this case cash, but it could also be shares or property or any other asset. Company C gives a power of attorney to Peter to control the cash.

This layered structure is very hard for lawyers or the ATO to pierce through. Maria is the only natural person in this three level structure. And she sits at the very bottom, removed by two layers from the assets.

Legitimate uses

Historically, mutual investment funds, which attract investors from around the world, have registered themselves offshore to avoid the risk of double taxation of their surpluses.

This isn't necessarily a problem so long as the beneficiaries of the fund do pay income tax on the money they receive from the fund in their home country.

When it comes to off-shore trusts, some argue that they are necessary to safeguard the privacy of beneficiaries. There are some circumstances where one can imagine this is a legitimate argument.

Yet the problem is that it is easy to abuse the protection of privacy to facilitate tax evasion, money-laundering and other illegal endeavours.

British Virgin Islands

The British Virgin Islands are a popular offshore tax haven, since it is a British overseas territory and its highest Court is the Judicial Committee of the Privy Council in London. Of course, there are others. But let's use the BVI as an example.

There are four things you can get in the British Virgin Islands but not in Australia. These are:

- 1) In the BVI the identity of shareholders and directors is not publicly available unless volunteered or subject to Court order.
- 2) Bearer shares are permitted.
- 3) No requirement to lodge tax returns.
- 4) No law of ultra vires so there is no limit on usage of the company.

Summary

It has become relatively easy to set up shop in an offshore tax haven thanks to the internet and technology. But at the same time technology also helps the ATO. And jurisdictions share a lot more data now, making it easier to find hidden assets and income.

The Common Reporting Standard CRS (and FATCA for the US) are a big step forward for the ATO. But how far all this will succeed in piercing through the layering remains to be seen.

The next big frontier of offshore tax havens will be crypto currencies since these operate outside of the traditional banking system. And hence are outside of CRS and FATCA's reach.

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