ABACONDA MANAGEMENT GROUP

INTERNATIONAL TAX COMPLIANCE

ESSENTIAL GUIDE FOR BOARDS OF THE DIRECTORS OF INTERNATIONAL COMPANIES

Table of Contents

INTRODUCTION 3
DEALING WITH OFFSHORE COMPANIES 3
INTRA-CORPORATE STRUCTURING 4
CORPORATE ADMINISTRATION AND TAX LIABILITIES....6
ACCOUNTING, BOOKKEEPING AND TAX LIABILITIES....7
TAX EVASION AND TAX CONSULTANCY 7
TAX QUESTIONS FOR THE BOARD 8
MOVE YOUR BUSINESS, BUT DON'T SPREAD IT 9
Appendix 1 10
Appendix 2 12
Appendix 3 13
Appendix 4 14
Appendix 5 15
Appendix 6 16
Appendix 7 17

INTERNATIONAL TAX COMPLINCE: ESSENTIAL GUIDE FOR BOARDS OF THE DIRECTORS OF INTERNATIONAL COMPANIES by Ed KRUGER and Cyrill KRUGER

Abaconda Management Group Ltd

556 Cameron Rd, Office 3, Tauranga South, Tauranga, 3112, New Zealand

PO Box 13645, Central, Tauranga, 3141, New Zealand

+64 9 88 9 2277

info@abaconda.info

www.abaconda.info

Neither this brochure nor our website provides neither tax, nor legal or accounting, investment or any other professional advice. Please do not confuse the information given in our brochures, websites and communications with a professional consultation. This brochure should not be construed as a solicitation or offering of any service by Abaconda Management Group Ltd.

© All rights reserved. Abaconda Management Group Ltd.

Introduction

Today more than ever, global trade is carried out by an extensive network of international companies which operate across numerous jurisdictions, with over half of the world's entire quantities of trade being executed by multinational companies. This new reality has grown out of the need for economic development of the modern world and global social development. However, in the process of profit creation the Boards of Directors of international companies may have, in some cases, lost sight of the dividing line between legal means for the avoidance of extra tax payments and illegal methods of evading tax liabilities. Despite century standing tax practices which were clearly defined by the terms "legal" and "illegal", the modern business world is now faced with the newly rising paradigms such as "legal, but unacceptable". Keeping in mind that the Board of Directors is responsible for each action taken by the company, we are providing this brochure, aimed at offering help and assistance to international entrepreneurs to avoid commonly encountered mistakes, misconceptions, pitfalls and errors.

Today more than ever, global trade is carried out by an extensive network of international companies which operate across numerous jurisdictions, with over half of the world's entire quantities of trade being executed by multinational companies.

DEALING WITH OFFSHORE COMPANIES

An "offshore company" is a commonly used term in international business, but one which does not have a commonly agreed upon definition. Only a decade ago an offshore company was regarded as an international business entity registered in one of a select few small island nations, providing beneficial tax treatments for international owners. Nowadays the term "offshore company" encompasses specific structures and methods of using foreign corporations or national laws, which provide specialized and specific rules for particular business situations. As a result, companies registered in even the most reputable countries of the OECD could now be regarded as being used in "offshore practice" (Appendixes 1- 6)

According to the regulations of most countries, companies dealing with offshore partners must identify them in their own due care and due diligence procedures. However, what are the main factors for the Board of Directors in identifying offshore structures?

- As a general rule, offshore companies are formed in a country other than their owner's jurisdiction, with no particular economic reason for doing so.
- As a general rule, offshore companies do not conduct business in their country of registration.
- As a general rule, offshore companies do not control their activities from their country of registration.

- Often companies which could be identified as offshore, hold their operational bank accounts in a country different to their head office location, and different to their country of corporate registration.
- Often the company is represented by an individual who holds no position on the Board of Directors, and operates under a Power of Attorney.

If the Board of Directors can identify at least two of these characteristics in an operational partner, they should recognize that in most cases tax authorities will qualify such partners as offshore companies.

How significant or dangerous is such a judgment from tax authorities? For practical purposes, it all depends on the course of action that the Board of Directors is willing to take in dealing with particular partnering offshore companies.

The Board and the owners of the company must have a clear understanding that rules of dealing with a partnering offshore company remain the same in any genuine business situation.

It is a common, albeit misguided, view that it is illegal to deal with offshore companies. There are no rules or regulations stopping anyone from dealing with an offshore company (outside of the typical rules regarding illegal activity). However, in conducting business with offshore companies, the Board must take extra precautions to ensure:

- the legitimacy of planned transactions, and
- that there are valid economic and business reasons for the transactions.

In most cases, the Board is recommended to identify the final beneficiary of the offshore company, and to obtain some strong guarantees from them regarding any future transactions. The Board must also understand that a failed transaction with an offshore company could be classified as unlawful negligence or failure to exercise an adequate standard of care.

The Board and the owners of the company must have a clear understanding that rules of dealing with a partnering offshore company remain the same in any genuine business situation. Even if both partnering companies have the same owners, they are both bound to provide adequate securities for joint transactions. The only possible legal exception to these common rules arises if the partnering companies operate in an intra-corporate structure and their accounts are consolidated.

INTRA-CORPORATE STRUCTURING

In the contemporary business environment most entrepreneurs operate a number of corporations, which could be located across several different countries. This situation is perfectly normal, and in most countries there are no restrictions to the right of the business person to establish business entities in overseas jurisdictions. However, this level of ease is regulated by the reporting systems of the entrepreneur's country of residence. In most cases, state tax authorities are eager to have full information about the business person’s interests in overseas enterprises, or details of any bank accounts opened in their name or under the name of the companies controlled by them.

Intra-corporate structures are often closely connected with the use of offshore companies, and connections like these must be closely monitored by the Board. As an example, the so-called global phenomenon of "round tripping" *(for further illustration, please see Appendix 3)* is the most known gray

method of using offshore structures in intra-corporate administration. The scheme involves a series of fund transactions, under which:

- tax obligations are avoided or evaded on profits raised in the country of residence,
- the specified funds are transferred to an offshore company, as an asset of such a company, and
- the offshore company “reinvests" the funds back into the country of residence.

As an illustration, according to publically available information, 40 percent of all inward Foreign Direct Investment (FDI) to India comes from the tiny island nations of Mauritius, the British Virgin Islands (BVI), Cyprus, the Cayman Islands, and Bermuda, while half of the outward FDIs from India are invested into companies registered in Singapore, Mauritius, Cyprus, and Switzerland.

Nearly 50 percent of the outward FDIs from Russia are received by companies registered in Cyprus and the BVI. At the same time, close to 80 percent of Russia’s inward FDIs are from Cyprus and the BVI.

About half of China inward FDIs are made by companies registered in the BVI and Hong Kong, while 80 percent of all outward FDI flows from China are directed to Hong Kong, the BVI, and the Cayman Islands.

Hong Kong received 80 percent of its FDI inflows from China and a select number of tax haven jurisdictions, mainly the BVI. At the same time 96 percent of the FDI outflows from Hong Kong are directed back into these countries.

Despite the overwhelming number of transactions between these jurisdictions, there is no significant evidence of merger and acquisition (M&A) operations between business entities registered in these countries. It is also important to note that the majority of the inbound and outbound FDIs are directed as loans and credit operations, which are in most cases unsecured by any means.

Without a doubt, most of the round tripping operations originate as intra-group transactions, and, in good practices, such transactions must be recorded under the group's consolidated account, which does not happen in the majority of cases. As a result these operations may be classified by international tax authorities as a mechanism of illegal tax evasion.

Despite the simplicity and ease of identifying such schemes, round tripping has become one of the most commonly used methods of tax avoidance, tax evasion and money laundering.

How can the Board of Directors ensure that they are not involved in round tripping, or fund piping?

- All financial transactions, and especially credit transactions with offshore companies, must be properly documented and secured.
- If there are any unsecured financial operations between two companies, then the Board of Directors must consolidate the accounts of these companies, or provide clear and economically viable reasons as to why the situation arose, and what type of other securities are in place.

As a general rule, if the companies operate under the management of the same beneficial owner (or group of owners) dealing on the same market, and with joint business interests, the record keeping of these companies must be consolidated. Despite a common misconception, the lack of any "visible" consolidation does not mean that this consolidation does not exist, but it does mean that the beneficial owner did attempt to hide some financial transactions and/or evade their tax obligations.

The Board of Directors must pay particular attention to the beneficial owner of their partnering offshore company. The practice of using nominee directors and shareholders has been recently clarified by the OECD, and nominee owners and managers are no longer accepted by tax authorities as the real beneficial owners, as long as they cannot enjoy the final benefits created by the company.

In dealing with a company with nominee shareholders, the Board of Directors must ensure that the shareholders (under the right economic conditions) regularly received dividends from the company, and that such dividends are properly recorded in the financial statements.

As a rule of thumb, the Board of Directors must ensure that any intra-group operations:

- Be properly recorded.
- Have obvious economic reasons.

The lack of reasoning or documentation behind financial and trading transactions with partnering companies will be a clear indication to tax authorities of numerous possible tax offences.

CORPORATE ADMINISTRATION AND TAX LIABILITIES

The Board of Directors must take all necessary steps to guarantee the required levels of timely corporate administration. In some cases, the lack of appropriate documentation behind the administration could be judged by tax authorities as an indication of possible tax evasion.

The responsibility for compliance with national and international report keeping rules does not lie with one particular Director, but with every member of the Board of Directors. In addition, each Director has the responsibility to operate in good faith for the company, and could be charged with offences such as dishonesty, misconduct, fraud, etc.

The responsibility for compliance with national and international report keeping rules does not lie with one particular Director, but with every member of the Board of Directors.

To err on the side of caution, the Board of Directors must:

- Hold regular meetings of the Board.
- Adequately record the Minutes of the Meetings of the Board.
- Keep all original copies of the minutes in the Registered Office of the company.
- Ensure that an Annual General Meeting (AGM) is held in a regular manner.
- Ensure that an appropriate level of communication is maintained with the management of the holding company or its subsidiaries.

The Board also holds the responsibility to ensure that the accounting and booking of the company is in full compliance with national regulations. In most cases, the Board must also ensure that the company's accounting and bookkeeping records and full documentation of trading operations are kept at the Registered Office. The Board is responsible for keeping these records for a number of years, even after the official closure of the company. As a rule of thumb, not keeping the necessary documentation in the Registered Office will be considered by tax authorities as a clear indication of misconduct. The lack of

meetings or communications between members of the Board will also be an indicator of improper management, and/or the creation of “grey directors”, or the use of nominee directors.

Even if national regulations allow the company to skip holding an Annual General Meeting, in good business practice, the Board must ensure that an AGM is held, and the Board should supply full information about the company’s activities to its shareholders. The Annual General Meeting for the consolidated group of companies should be considered as an absolute necessity.

ACCOUNTING, BOOKKEEPING AND TAX LIABILITIES

Most companies have a clear understanding of their responsibility to keep adequate accounting records. Unfortunately, the rules regarding the timely manner of preparation and maintenance of accounting records are often neglected. From the point of view of tax authorities, a properly operating company cannot prepare its accounting reports only once or twice a year, and a lack of day-to-day management records is a clear indicator of abnormal or even illicit company operations, which will often lead to allegations of tax evasion.

An obvious indicator of abnormal behavior is also a lack of communication between the Board and their accountants. In a normally operating company, there should not be any "agents" between the accountants and the directors, as regular reports and accounting can be a primary indicator of the health of the business.

In a normally operating company, there should not be any "agents" between the accountants and the directors, as regular reports and accounting can be a primary indicator of the health of the business.

The timely preparation of the yearly financial statements and (if required) audit are also an important indicator of the Board's commitment to upkeep appropriate accounting standards. Any financial statements issued more than six months after the end of the fiscal year, often hint to the tax authorities that the Board has no genuine reasons to check the financial information of the company, and/or have double accounting.

TAX EVASION AND TAX CONSULTANCY

Tax consultants are highly demanded professionals in the present day market. Unfortunately, the excess demand for professional consultants leads to an overwhelming supply of unqualified specialists. In order to select the proper tax consultant, the Board must ensure that:

The consultant is a member of a *national* professional body, and is committed to upholding the utmost standards of the respective body.

The consultant has the necessary experience and qualifications needed to provide appropriate and adequate solutions.

As a majority of the under qualified consultants provide roughly the same advice, the Board must take notice of any solutions which contain one (or more) of the following commonly offered schemes, as in most cases they are tantamount to tax evasion:

- Having or issuing loans or any other financial obligations, with no credit or asset checks.
- Having or issuing loans or any other financial obligations that are to be paid off by future earnings.
- Operations whereby the company receives an unreasonable amount of tax deductions.
- Opening accounts in offshore banks, in countries where the company holds no direct business interests.
- Operating your own business through a Letter of Authorization, issued by somebody else, probably an individual in one of the offshore jurisdictions.
- Financial or business transactions lacking economic reasons, and/or transactions with disproportionately large tax benefits.
- Involvement in transactions with tax exempt charitable organizations.
- Involvement in transactions with entities with accumulated tax losses.
- Artificial transactions with offshore companies, and/or companies with offshore bank accounts.

TAX QUESTIONS FOR THE BOARD

Despite the fact that the Board could be heavily dependent on the advice of an external consultant, the ultimate responsibility for each and every transaction in which the company is involved, continues to rest with the Board. It is logical to say that any transactions for which the company is involved in must be discussed and be accepted by the Board. For each of these transactions precautions need to be taken by the Board to ensure full compliance with tax laws and anti-money laundering regulations. In this regard, what are the major questions that the Board of Directors must ask, and receive a clear answer for?

- Are the tax results of the operation in line with the commercial results of the operation?
- Does the proposed arrangement include any artificial structuring which does not reflect a standard method of achieving the same commercial result?
- Is any element of the proposed operation included solely for the purpose of achieving an additional tax benefit?
- Is any element of the proposed operation included with no sound commercial purpose?
- Does the proposed transaction comply with standard arms length principals and with good practices of transfer pricing procedures?
- Has the entire Board of Directors agreed upon the proposed transaction, and is it recorded in a written resolution?
- Does the legal description of the proposed transaction reflect the actual nature of the operation?

> For each of these transactions precautions need to be taken by the Board to ensure full compliance with tax laws and anti-money laundering regulations.

If the Board does not have satisfactory answer to any one of these questions, then it should be consider that such an operation falls under the definition of tax evasion or money laundering, and in some circumstances, will be treated as such by tax authorities.

MOVE YOUR BUSINESS, BUT DON’T SPREAD IT

The information in this brochure is intended for small and medium sized international enterprises, which are too often over reliant on external advice, and are guided by commonly seen misinterpretations. Unfortunately, in the contemporary business world, the formation of a company in another country is no longer seen as a business expansion only. Quite the opposite, creation of numerous companies in offshore jurisdictions may often lead to the allegations of tax evasion.

When your business is ready to expand internationally, or when your business is reasonably dissatisfied with the economic conditions in your present country of residence, then you can move your business, or part of your business, to a country with more favorable economic conditions. However, your interests in the new country must be consolidated with your existing operations (unless the trade of each business is thoroughly different by nature, and there are absolutely no intra-group transactions between them), and you must provide full administrative and management efforts to operate the new company.

… you can move your operations to any country in the world, and your company could migrate to almost any jurisdiction in the world, but there is no sound reason to create offshore companies with the hopes of evading tax obligations.

To summarize, you can move your operations to any country in the world, and your company could migrate to almost any jurisdiction in the world, but there is no sound reason to create offshore companies with the hopes of evading tax obligations. Surprisingly, in the current business environment, it can be much cheaper to comply with international and national tax regulations, rather than paying for unreasoned tax advice, nominee services, and offshore commissions, while creating “grey” structures, which could still be easily identified by tax authorities. You should always remember that intentional tax evasion and tax fraud are serious offense, and can be subject to serious consequences, even prosecution.

Appendix 1

Brazilian Blacklist, 2010

For the purpose of this list (which is deemed to be a "black-list"), the Brazilian tax authorities included the countries or dependencies that, according to the Brazilian Government, do not impose tax on income or, in which the applicable income tax rate is equivalent to any percentage varying between zero and 20% (maximum), as well as whose national legislation does not allow access to the information regarding the capital stock structure or ownership of the legal entities organized under the laws of any such jurisdiction. The current list comprises the following jurisdictions:

1. Andorra
2. Anguilla
3. Antigua and Barbuda
4. Netherlands Antilles
5. Aruba
6. Ascension Island
7. The Commonwealth of The Bahamas
8. Bahrain
9. Barbados.
10. Belize
11. The Bermuda Islands
12. Brunei
13. Campione d`Italia
14. Channel Islands (Alderney, Guernsey, Jersey and Sark)
15. Cayman Islands
16. Cyprus
17. Singapore
18. Cook Islands
19. Costa Rica
20. Djibouti
21. Dominica
22. United Arab Emirates
23. Gibraltar
24. Granada
25. Hong Kong
26. Kiribati
27. Labuan
28. Lebanon
29. Liberia
30. Liechtenstein
31. Macau
32. Madeira Island
33. Maldives
34. Isle of Man
35. Marshall Islands
36. Mauritius Island
37. Monaco
38. Montserrat Island
39. Nauru
40. Niue Island
41. Norfolk Island
42. Panama
43. Pitcairn Islands
44. French Polynesia
45. Qeshm Island
46. American Samoa
47. Eastern Samoa
48. San Marino
49. Saint Helena Island
50. Saint Lucia
51. The Federation of Saint Kitts and Nevis
52. Saint-Pierre and Miquelon Island
53. Saint Vincent and the Grenadines
54. Seychelles
55. Solomon Islands
56. The Kingdom of Swaziland
57. Switzerland
58. The Sultanate of Oman
59. Tonga
60. Tristan da Cunha
61. Turks and Caicos Islands
62. Vanuatu
63. U.S. Virgin Islands
64. British Virgin Islands

- in the case of Luxembourg, the regime applied to the entities incorporated in the form of holding company (Luxembourg Holding Company)
- in the case of Uruguay, the regime applied to the entities incorporated in the form of Sociedad Financiera de Inversion (SAFI), which is the Uruguayan Financial Service Corporation which will exist until December 31, 2010
- in the case of Denmark, the regime applied to the entities incorporated in the form of holding company (Danish Holding Company)
- in the case of Netherlands (Holland), the regime applied to the entities incorporated in the form of holding company (Dutch Holding Company)
- in the case of Iceland, the regime applied to the entities incorporated in the form of International Trading Company (ITC)
- in the case of Hungary, the regime applied to the entities incorporated in the form of the offshore KFT, which is the acronym for Korlátolt Felelõsségû Társaság (the Hungarian Limited Liability Corporation)
- in the case of the United States of America, the regime applied to the entities incorporated in the form of Limited Liability Company (LLC) whose equity participation is formed by non-residents, which are not subject to the US federal income tax, such as Delaware, Nevada, Florida and other US states which adopt a similar regime
- in the case of Spain, the regime applied to the entities incorporated in the form of Entidad de Tenencia de Valores Extranjeros (ETVE), which is the International Spanish Holding Company and
- in the case of Malta, the regime applied to the entities incorporated in the form of International Trading Company (ITC) and International Holding Company (IHC).

Appendix 2

Denmark Blacklist, 2010

The Tax Ministry of Denmark considers the following jurisdictions to be tax havens (September, 2010):

1. Austria
2. Andorra
3. Anguilla
4. Antigua & Barbuda
5. Aruba
6. Bahamas
7. Bahrain
8. Barbados
9. Belize
10. Cayman Islands
11. Cook Islands
12. Cyprus
13. The U.S. Virgin Islands
14. British Virgin Islands
15. United Arab Emirates
16. Netherlands Antilles
17. Dominican Republic
18. Gibraltar
19. Grenada
20. Guatemala
21. Guernsey
22. Hong Kong
23. Isle of Man
24. Isle of Sark
25. Jersey
26. Latvia
27. Liberia
28. Liechtenstein
29. Lithuania
30. Luxembourg
31. Macau
32. Maldives
33. Marshall Islands
34. Monaco
35. Montserrat
36. Nauru
37. Niue
38. Panama
39. Samoa
40. San Marino
41. Switzerland
42. Seychelles
43. Singapore
44. St. Kitts and Nevis
45. St. Lucia
46. St. Vincent and the Grenadines
47. Tonga
48. Turks and Caicos Islands
49. UK
50. Vanuatu

Appendix 3

Australia Blacklist, 2011

Secrecy jurisdictions of concern and no effective exchange of information with Australia:

1. Andorra
2. Bahrain
3. Cyprus
4. Hong Kong
5. Liberia
6. Liechtenstein
7. Luxembourg
8. Panama
9. Seychelles

Appendix 4

France Blacklist, 2010

Non-cooperative countries and territories ("NCCTs"), considered as not respecting international standards in the fight against tax fraud and tax evasion (The Amended Finance Act for 2009).

1. Anguilla
2. Belize
3. Brunei
4. Costa Rica
5. Dominica
6. Grenada
7. Guatemala
8. Cook Islands
9. Liberia
10. Marshall Islands
11. Montserrat
12. Nauru
13. Niue
14. Panama
15. Philippines
16. St. Kitts and Nevis
17. St. Lucia
18. St. Vincent and the Grenadines

Appendix 5

Spain Blacklist, 2010

Therefore, as of October 2010, Spain's tax haven list now includes the following territories:

Asia Pacific:

1. Bahrain,
2. Brunei,
3. Hong-Kong,
4. Macao,
5. Singapore,
6. Northern Mariana Islands,
7. Solomon Islands,
8. Vanuatu,
9. Fiji

Europe and Middle East:

1. Cyprus,
2. Gibraltar,
3. Principality of Liechtenstein,
4. Principality of Monaco,
5. Isle of Man,
6. Channel Islands,
7. Republic of San Marino,
8. Lebanese Republic,
9. Jordan,
10. Republic of Liberia

Africa:

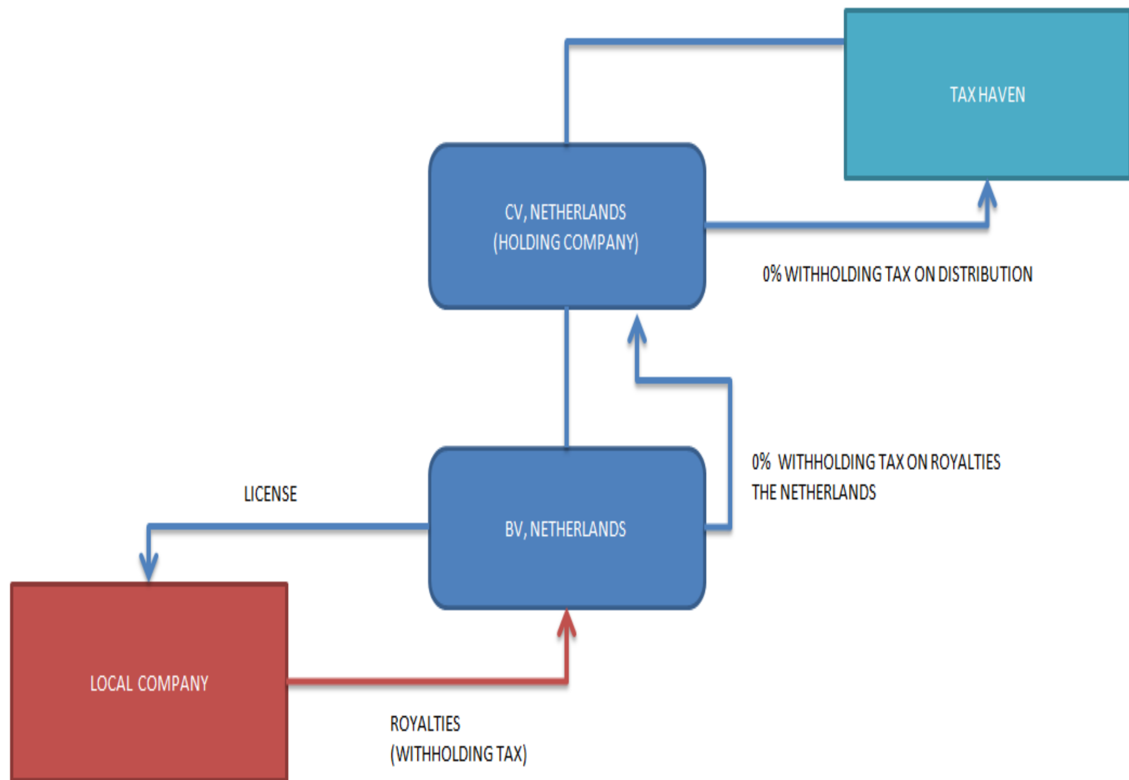
1. Oman,
2. Republic of Seychelles,
3. Mauritius,
4. Republic of Nauru

America and Caribbean:

1. Dominican Republic,
2. Republic of Panamá,
3. Anguilla,
4. Antigua y Barbuda,
5. Bahamas,
6. Barbados,
7. Bermuda,
8. Cayman Islands,
9. Cook Islands,
10. Dominican Republic,
11. British Virgin Islands,
12. US Virgin Islands,
13. Saint Vincent and Grenadines,
14. Saint Lucia,
15. Montserrat,
16. Falkland Islands,
17. Grenada,
18. Turks and Caicos

Appendix 6

Commonly seen EU holding company structure, which could be considered as a tax evasion scheme.



Appendix 7

Commonly seen round-tripping structure, which could be considered as a tax evasion scheme.