

TAX

# Nowhere to hide

The call for tax transparency is being echoed around the globe, with 'midshore' centres like Bahrain and the UAE emerging as reputable, regulated and tax efficient jurisdictions



In 'midshore' jurisdictions like Dubai, the tax benefits offered to foreign investors are not ringfenced from the domestic economy

by Mark Lazell

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**A** 2012 book entitled *Offshore Apocalypse - The Collapse of the Tax Haven Industry*, written by a team of tax-law academics, auditors, compliance officers and lawyers, describes in detail the drawn out demise of the offshore tax haven.

For decades, offshore companies enabled business to be conducted globally away from prying eyes, including tax authorities. Though technically legal, these structures were often suspected to be conduits for money laundering and tax evasion, their activities and the identities of the company owners hidden behind a wall of secrecy provided by the laws of the offshore jurisdiction.

Things have changed, however. Following intense efforts led by the

Organisation for Economic Co-operation and Development (OECD) to clamp down on offshore practices, tax authorities and banks in jurisdictions around the world are now sharing information. And these changes are opening up new opportunities for well regulated, tax efficient, bona fide trading hubs such as Bahrain and the UAE.

"Shell companies and sparsely-staffed affiliates in exotic tax havens are no longer acceptable," stresses Thomas Hanzely, the managing director of BBD Enterprises, a Bahrain-based tax, corporate structuring and management consultancy.

"It is unlikely that real value is created in these locations, and it is likely not feasible establishing real operations there that could create value and hence attract profits," he adds.

With the coming of the 'offshore apocalypse', the UAE and Bahrain are among a clutch of so-called 'midshore'

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centres poised to capitalise.

"They are no or low tax jurisdictions that offer a good mix of factors investors take into account when setting up overseas businesses - an educated and skilled workforce, good infrastructure, a stable legal system and the rule of law, investor-friendly business environment and a good double tax treaty network," explains Gergely Demetrovics, BBD's head of tax & compliance.





► “The tax benefits they offer to foreign investors are not ring-fenced from their domestic economies,” Demetrovics notes. “These locations can facilitate operations currently run in high tax jurisdictions, which would then generate profits in a no tax environment - without the risk of being adversely affected by anti-avoidance and transparency measures promoted by the G20, the OECD and various governments around the globe.”

The origins of the global transparency drive date back to 1998, when the OECD published a report on harmful tax competition. Global financial crises which followed put further pressure on governments to raise tax revenues. In 2013, the OECD and the G20 club of major economic powers, which includes Saudi Arabia, adopted the 15-point BEPS [Base Erosion and Profit Shifting] Action Plan to address growing concerns among OECD and non-OECD countries about the risks to tax revenues, tax sovereignty and tax fairness that BEPS behaviours pose, in particular when these results lead to unanticipated double non-taxation.

“It was an initiative which has gained further momentum by the public outcry against multinationals using complicated tax planning techniques, as well as various financial institutions helping wealthy individuals hide their assets offshore,” says Demetrovics.

He says the first step into a world of transparency is FATCA [US Foreign Account Tax Compliance Act], a US tax law with direct impact on all US individuals, businesses and any other entities with US ties.

“FATCA makes it virtually impossible for US persons to conceal assets held in offshore accounts and shell corporations,” he explains. “All financial institutions worldwide are, or will, shortly be providing detailed information about account holders and their banking activities to US authorities on an automatic basis and without the client’s knowledge, which means investigation and possible prosecution for all non-compliant clients and bankers/banks,” Demetrovics adds.

FATCA is also relevant for GCC governments, financial institutions and citizens.



During the OECD Peer Review process, Qatar and Bahrain were viewed as ‘largely compliant’

“Banks and other financial service providers can be held liable for maintaining banking relationships with non-compliant customers (including tax non-compliant ones),” the BBD Enterprises executive points out.

“This is a risk banks want to avoid fiercely. Since formal compliance with local and international laws is unlikely to be enough to protect them from criminal prosecution and penalties, these institutions are putting their own, even more stringent measures in place, which may lead them to voluntarily inform local and foreign authorities if deemed necessary, without informing the client.

“Customers, particularly high net worth individuals and corporates, are facing enhanced due diligence when opening or maintaining bank accounts. Once opened, accounts are being monitored continuously and suspicious or unusual transactions reported to authorities such as central banks, fiscal authorities and the police. Customers with complex structures and/or multiple offshore companies are subject to maximum scrutiny and reporting,

**‘All bank secrecy tools (tax havens, offshore entities, numbered accounts, nominees, trusts, foundations) are becoming useless or extremely limited in use’**

Thomas Hanzely

and we also see a lot of financial institutions ending banking relationships if the client’s structure is only perceived as non-compliant,” Hanzely continues.

He says FATCA will serve as a model for other countries, including those in the GCC, to obtain information about their tax payers and/or nationals.

“GCC countries are also opening up to similar international initiatives which facilitate co-operation among authorities to improve their ability to tackle money-laundering, tax evasion, tax-related crime and assist them in their investigation, litigation and prosecution efforts,” he explains.

**‘GCC investors are very conservative, including in their tax structures. The motto is as little exposure as possible. Some of them are sometimes quite surprised how exposed they are with ‘outdated’ tax structures’**

Gergely Demetrovics

the Intergovernmental Agreement (IGA) developed to facilitate FATCA’s implementation.

“The CRS contains the reporting and due diligence standard that underpins the automatic exchange of financial account information. This also means that there is (even) more compliance work in the pipeline for financial institutions,” he says.

Given that CRS effectively impacts every person in every jurisdiction, it has enormous implications from regulatory and technical/IT perspectives.

“We will have a tremendous amount of data floating around and it remains to be seen how this can be processed by the various authorities around the world. Questions such as the right to privacy, data protection etc need to be sufficiently addressed. Most of the structures were set up in order to preserve privacy and not necessarily to avoid paying taxes,” Hanzely stresses.

GCC countries are playing their part in this effort. As a G20 member, Saudi Arabia is actively supporting the BEPS project. The kingdom, along with Bahrain, Qatar and the UAE, are also participating in the so-called OECD Peer Review process, co-ordinated by the Global Forum, a grouping of 125 countries.

“Through an in-depth peer review process, the restructured Global Forum monitors that its members fully implement the standard of transparency and exchange of information they have committed to implement. It also works to establish a level playing field, even among countries that have not joined the Global Forum,” he continues.

Speaking at a recent meeting of the GCC branch of the International Fiscal

Association (IFA), a non-governmental, non-sectoral organisation based in the Netherlands, Ian Anderson, a senior consultant at the Doha office of the UK law firm Pinsent Masons, described Qatar’s experience of the OECD Peer Review process.

“The process focused Qatar’s mind on some of the areas which needed improvement, but fundamentally most of the law was in place,” explained Anderson, former director of tax at the Qatar Financial Centre (QFC).

“The team who came to Qatar to conduct the on site visit in Phase Two of the process spent a week reviewing everything. “Eight elements of the review process for Qatar were rated ‘compliant’, and two ‘largely compliant’. It felt at times that they were looking for faults. But at a final meeting in Paris involving 40 countries, Bahrain and Qatar were both viewed as ‘largely compliant’, which I think in the circumstances is an extremely good result.

Demetrovics says the winds of change blowing through the global financial and tax system has implications for GCC business owners having international operations.

“Tax is rather an annoying task to deal with and in some cases, their corporate and tax structures were set up a while back, totally legitimately,” says Demetrovics. “However, they have not been reviewed for many years as to whether they are still compliant or not. Hence, we see a lot of unnecessary tax exposure but also opportunity to restructure the businesses in a tax-friendly manner.

“GCC investors are very conservative, including in their tax structures. The motto is as little exposure as possible. Some of them are sometimes quite surprised how they are indeed exposed with some of the ‘outdated’ tax structures.”

He notes the risks associated with improper use of non-compliant tax structures.

“Contrary to common belief, financial damage (in the form of hefty fines, late interest payments, etc) is not the only hazard. Non-compliant taxpayers must foresee reputational risks, exposure to criminal prosecution and to other serious measures.” ■