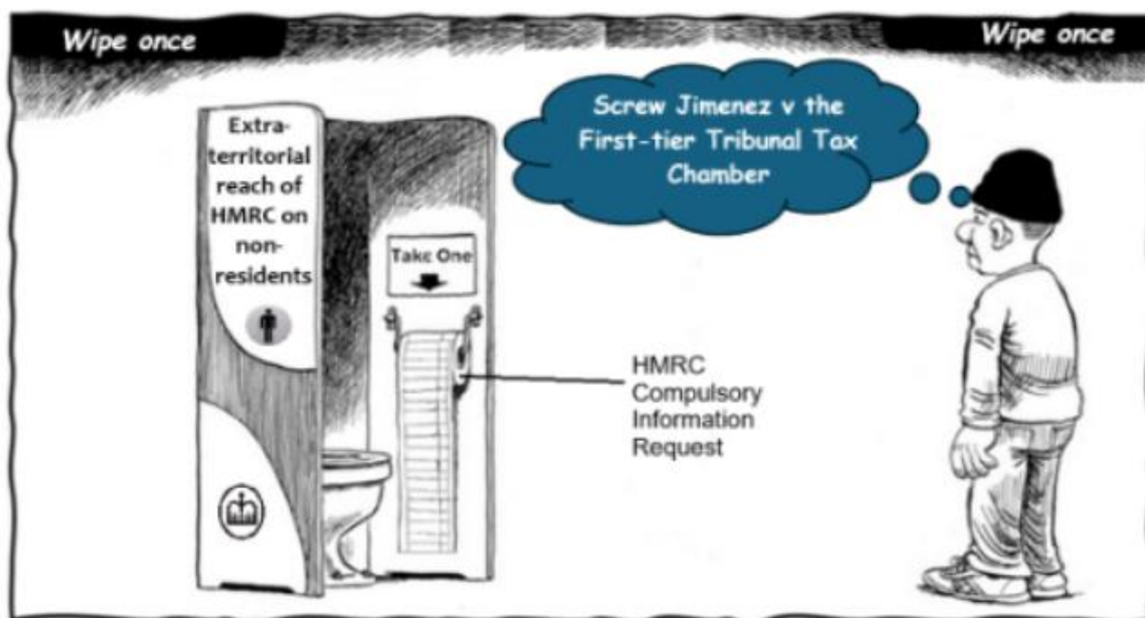

Can HMRC extraterritorially reach a non-resident submiting a fraudulent dormant UK company filing? The compulsory info request worth toilet paper?

Summary

- The UK court of appeal decided HMRC can issue information request on tax status to persons resident outside UK
- However, the court did not extend to requests of information to third persons in investigating the tax liability of the person
- If no information is obtained, HMRC may rely on tax treaties or teg MCAA to demand information
- If no such treaty exists, HMRC may penalise person by deducting penalties from any assets the person holds in the UK

What if a non-resident, establishes a UK company and files annually as a dormant company, despite the company being active. It has no income, account, income or assets in the UK. Assume it's not reportable by CRS if it's an Active NFE or PMIE owned by a Non Participating Custodial Institution.

Can HMRC issue information request to the director of the company? Can it use tax agreements or mutual assistance agreement in tax matters? Hint: No, if the non-resident is not 'sufficiently' connected to the UK.

The Jimenez v the First-tier Tribunal Tax Chamber

> The UK Court of Appeal determined that HMRC had power to issue a compulsory information request to an individual outside the UK for the purpose of checking that individual's tax position. The decision is silent about the extent to which HMRC can issue compulsory information requests to third parties outside the UK (ie, requests for the purposes of checking another person's tax position). The better view is that whether or not such a request will be valid turns on whether the third party is "sufficiently connected" with the UK.

> If the UK company registers for a GIIN, the UK tax authorities will know the entity exists. This does not disprove the company is dormant. The US FATCA definition of PMIE has no income test, but only the management of its assets by another FI. Where an entity has no operating history at the time its status an Investment Entity is being assessed, it will be regarded as a Financial Institution if it expects to meet the gross income threshold based on its business plans, such as the anticipated deployment of its assets and the functions of its employees.

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HMRC trying to use double tax agreements , or MCAA EoIR
will not help as HMRC does not have the bank account
details
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Introduction

- A Swiss resident establishes a UK limited company for international consulting, commissions, collecting Intellectual property income, or rental fees on properties. 51% of the assets as cash. The company is an Active NFE and is not subject to CRS. The UK company opens an account in, say, Singapore. Collects income/fees into this corporate account.
- Company is an Investment entity owned by a non-participating custodial institution with an investment portfolio of financial assets.

Dormant filings and dormant accounts cost not much more than a big mac and happy meal meal for the family

- The Swiss is a greedy pig and does not want to pay the reasonable 20% UK tax rate to HMRC
- Therefore he simply submits a dormant filing, which costs next to nothing
- Note the UK company does not require Economic Substance as it is resident in a taxable country.

Service	Price
Dormant Company Accounts	£44.99 →
Registered Office	from £71.99 per year →
Service Address	£20.99 per year →
4 Printed Share Certificates	£7.99 →
Company Filing Service	£172.99 per year →
Company Minutes	£7.99 →
Digital Company Register	£7.99 →
Director, Secretary, PCS Appointments	£28.99 →
Director, Secretary, PCS Removal	£28.99 →
Dormant Company Filing	£86.99 per year →
Officer and company address changes	£28.99 →
PAYE Registration	£71.99 →
Sole Trader Business Address	from £49.99 per year →
SH01 Allotment of Shares	£35.99 →
VAT Registration	£86.99 →
Apostille	£140.99 →
Certificate of Good Standing	£62.99 →

On the application of Jimenez v the First-tier Tribunal Tax Chamber and HMRC, the Court of Appeal determined that HMRC had power to issue a compulsory information request to an individual outside the UK for the purpose of checking that individual's tax position.

- The decision is silent about the extent to which HMRC can issue compulsory information requests to third parties outside the UK (ie, requests for the purposes of checking another person's tax position). The better view is that whether or not such a request will be valid turns on whether the third party is "**sufficiently connected**" with the UK (see below).
- The Court of Appeal did not comment on the First-tier Tribunal's practice of approving information requests in the relevant taxpayer's absence (ie, at an "ex parte" hearing). At first instance, the High Court had been critical of this practice, encouraging HMRC and the First-tier Tribunal to rethink their approach. That call for reflection now seems less likely to be heeded.

Background HMRC's compulsory information powers

HMRC has an impressive collection of powers available to it in support of civil investigations. As regards its powers to compel the production of documents and information, ***Schedule 36 Finance Act 2008*** confers on HMRC power to compel production from a person:

- for the purposes of checking **that person**'s tax position; and
- for the purposes of checking **another person**'s tax position.

Schedule 36 is silent about the **territorial scope** of those powers. In particular, it says nothing about whether the intended recipient of the notice must be present within the UK, **or resident within the UK**, for the powers to be operable.

It is of course the case, however, that a person can be a UK taxpayer without ever having set foot within the UK. This has been highlighted most recently by the imposition of a charge to capital gains tax on non-residents in respect of disposals of UK real estate.

As such, and although HMRC can ask the authorities in many foreign jurisdictions to obtain and transmit documents and information from persons within that foreign jurisdiction pursuant to various bilateral and multilateral treaties, it is conceivable that HMRC would want to issue a taxpayer or third party notice to a person outside the UK.

Territorial scope of statutes

- It is now relatively uncontroversial that the question of whether a statutory provision applies to persons or matters outside of the UK is a question of statutory interpretation.
- "*Unless the contrary intention appears... an enactment applies to all persons and matters within the territory to which it extends, but not to any other persons and matter. That principle is one of construction, underpinned by considerations of international comity and law.*"
- Another, related, general principle is that in the absence of, for example, a treaty providing for mutual assistance courts in one jurisdiction will not enforce the penal or revenue laws of another jurisdiction.
- That principle which relates to enforcement in a foreign jurisdiction does not, of course, prevent Parliament from enacting legislation with extra-territorial effect. A good example of Parliament enacting tax legislation with extra-territorial effect can be found in the case of An*dre Agassi v Robinson.*
- That case was concerned with a withholding obligation that arose in relation to payments made in respect of certain activities carried on in the UK by a non-UK resident entertainer or sportsman.
- A majority of the House of Lords held that no territorial limitation could be implied so as to limit the obligation of a person resident outside the UK and with no trading presence in the UK from the withholding obligation otherwise imposed upon them in respect of payments made to entertainers/sportsmen as described above, even in circumstances where the relevant payment was made outside the UK.

I. Decision of the High Court on Jimenez (which was subsequently reversed by Court of Appeal)

In *Jimenez*, First-tier Tribunal's approved the issue of a taxpayer notice to Mr Jimenez.

> The Notice had been sought by HMRC in support of a civil investigation into the residence status of Mr Jimenez in prior tax years.

> The taxpayer, Mr Jimenez, was a UK national who was living in Dubai. He had been a UK taxpayer in previous years and there existed a dispute between him and HMRC as to the period of his UK residency.

> As part of HMRC's investigations into his tax returns, HMRC issued a notice under Schedule 36 requiring the taxpayer in Dubai to provide them with certain financial information and a schedule of his visits to the UK.

> The taxpayer contended that the issue of such a notice to him outside the UK was either contrary to the legislation or otherwise contrary to international law.

> In particular, the taxpayer argued that the provisions of Schedule 36 "must be construed by reference to international law and in conformity with a presumption that Parliament would not have chosen to confer powers on HMRC which could be exercised in breach of international law".

> That included not conferring a power on HMRC which might result "in the UK exercising an enforcement jurisdiction within the territory of another sovereign state".

At first instance the High Court held, in essence, that Schedule 36 does not have extra-territorial effect. On that basis, the High Court found that the decisions to approve and issue the Notice to Mr Jimenez in Dubai were unlawful, and the High Court made a "quashing order".

In summary, the High Court's reasoning was as follows:

- The purpose of Schedule 36 is to "*provide a credible and effective system of checking and investigating*" the tax position of putative taxpayers. That purpose did **not, however, lead inescapably to the conclusion that Parliament intended Schedule 36 to have effect outside the UK.**
- The argument that the purpose would be subverted if Schedule 36 did not have extra-territorial effect hence Parliament must have intended to legislate extra-territorially was undermined by **the existence of mutual assistance arrangements, including bilateral double tax treaties containing information exchange provisions**, which Parliament would have been aware of when legislating, and which provide a means for HMRC to seek information from abroad about a person's tax liability.
- The power to issue taxpayer notices has to be viewed against the backdrop of Schedule 36 as a whole. Schedule 36 contains a number of powers pertaining to the inspection of premises, and one would "*raise eyebrows*" at the notion that Parliament intended those powers to have extra-territorial effect.
- Further, Schedule 36 imposes sanctions for non-compliance. Such sanctions stray into the realm of extra-territorial enforcement which would infringe basic principles of international law.
- As usually happens when First-tier Tribunal's approval of a taxpayer notice is sought, the First-tier Tribunal's considered the matter in private, ie, with the benefit of submissions from HMRC, but in the absence of taxpayer concerned).
- The High Court's view was that, unless the First-tier Tribunal's is satisfied that allowing the taxpayer to attend might prejudice the assessment or collection of tax, theFirst-tier Tribunal's should consider requiring HMRC to provide the taxpayer with a summary of the representations that HMRC intend to make and/or allowing the taxpayer to attend the hearing.

II. Decision of the Court of Appeal

The Court of Appeal took a different view to the High Court, **allowing HMRC's appeal** against the quashing order.

- The Court of Appeal started at the same point as the High Court, approaching the issue as a matter of statutory interpretation, and accepted that the purpose of Schedule 36 was to supply HMRC with powers to verify a taxpayer's self-assessment position.
- The Court was not persuaded, however, that the fact Parliament most likely intended Schedule 36 *inspection* powers to be **limited in scope to premises within the UK** meant that *all* of the Schedule 36 powers, in particular, the power to issue taxpayer notices, were similarly limited in their international outlook.
- The Court noted that a large number of **UK taxpayers would be persons resident outside the UK**, and hence concluded it was inherently unlikely that Parliament had intended taxpayer notices to operate on an entirely domestic plane.
- Putting it another way, the subject matter of Schedule 36 (checking the tax liability of potential UK taxpayers) supplied a **sufficient connection** between the non-UK recipient of the taxpayer notice and the UK jurisdiction to justify the conclusion that Parliament intended to legislate in an extra-territorial fashion.

> In addition, the Court found that there was a strong public interest in allowing HMRC to issue taxpayer notices to persons outside the UK, not least since tax evasion often has a cross-border aspect to it.

Ramifications on taxpayers notices and tax treaties

- Most information exchange provisions in bilateral tax treaties are exercisable only once the requesting authority has exhausted its normal procedures under domestic law to obtain the information sought.
- Since the Court of Appeal has made clear that HMRC's domestic powers (ie, the power to issue a taxpayer notice) can be exercised cross-border, it follows that HMRC **should not make use of the relevant tax treaty information exchange mechanism (to obtain information and document from a taxpayer) until it has issued and sought to enforce a taxpayer notice.**
- Any attempt to use a tax treaty prior to HMRC exhausting its powers under Schedule 36 ought, therefore, to be susceptible to challenge or in any subsequent penalty proceedings.

Third party notices

- The Court of Appeal's decision was concerned only with the extra-territoriality of HMRC's power to issue taxpayer notices.
- The position in relation to third party notices was not addressed.
- The Court decided that section 2 "*extends extraterritorially to foreign persons in respect of documents held outside the jurisdiction* ***when there is a sufficient connection between the person and the jurisdiction***". The Court held that whether a "**sufficient connection**" existed was a fact sensitive issue to be determined on a case by case basis

  1. whether the third party is resident, incorporated, or engaged in activities, in the UK;

  2. whether the request relates to property held by the third party in the UK;

  3. whether the request relates to transactions entered into by the third party in the UK.

In practice, it may be difficult to enforce such notices.

Common misconceptions with dormant companies

- What is a dormant limited company? A fully dormant company is one that has no accounting history whatsoever. If a limited company does not trade throughout a filing year, then it will be dormant for that year.
- In many instances, people register companies with the sole intent of leaving them dormant.
- They can do this simply by not participating in any trading activity from the date of registration.
- If you plan to register a private company and leaving it dormant, then you will still need to inform HMRC of this.
- Benefits of dormant limited companies: there are numerous reasons as to why someone may elect to register a private company with the purpose of keeping it dormant.
- A dormant company registration can offer security benefits when protecting a trademark or brand name.
- You may have an idea for a business you wish to start in the future. Perhaps you wish to register the limited company to not only secure the name, but to let the company company limited by shares' age so that by the time you do want to begin trading, the limited company has a few years behind it.
- This is very useful when entering into contracts, as the older a company is, the more prestigious it looks.
- In this respect, a dormant private company registration can be advantageous over time, as it will incur a very small percentage of mandatory outgoing charges (payments for annual filing and dormant accounts).
- However, the company is an asset that you can sell for considerable money depending on the age, when you wish to discard of your dormant limited company.
- Some flat management companies remain dormant for the purpose of owning the head lease or the freehold of a property, and set up a resident association separately to deal with the expenses that it incurs.

Duration of a dormant company

- A company limited by shares can maintain a dormant status **indefinitely**, though the directors of dormant companies must still file dormant accounts with Companies House.
- Dormant private company accounts: you will still need to file annual accounts with Companies House.
- If the details of any of your members change throughout the accounting period, you will still need to state this on the in the annual account. A non-trading company is not a company type, but rather the status of a registered company.
- Any company in England, Wales, Scotland and North of Ireland can be dormant whether they are limited by shares or a company limited by guarantee.
- Therefore, the same rules will apply to the company whether it is dormant or not.
- Transactions in dormant companies: to be dormant, the private company can have no trading or accounting history, although some transactions are possible with trading companies.
- For example, a dormant limited company can pay for shares that a subscriber takes, if this is applicable in the memorandum and articles.
- Any fees that the companylimited by shares pays to the Registrar of Companies to change the company name or for the annual filing, as well as the payment for penalties, would still keep the company in the dormant status.
- Making a trading limited company dormant: it is possible to make a trading company dormant, usually by simply not trading throughout an accounting period and declaring the private company dormant at the end of that year.
- If you have a limited company and you wish to cease trading, but do not want to dissolve the company, making it dormant is always an alternative. However, one should always seek professional advice before doing this.

Making a company dormant

- A company limited by shares is dormant from incorporation until they trade.
- If you need to register a non-trading company, you simply register the private company and have no trading activity at all. When a limited company trades or has activity through the company account, then the status will be active.
- You will still be eligible for the filing of the dormant account, annual returns, and informing HMRC that you are dormant so that you do not have to pay any corporate tax.

Non-trading companies and dormant companies

- A non-trading company is different to a dormant company.
- Non- trading refers to the status of a limited company which is not doing any business, but has a trading history and accounting transactions, which means that in the legal sense, it is not dormant.

Managing a dormant company

- The officers of a dormant company are responsible for filing the statutory paperwork and filing the correct accounts.
- Limited companies must have a minimum of one physical director and a registered office address.

Submitting documents to Companies House

- The company members are responsible for submitting the mandatory company information with Companies House as and when it is due.
- Failure to comply could lead to severe consequences, including fines and prosecution as it is a criminal offence.
- If your company officers do not meet the deadline and file the information late, they will have to pay fines as a civil penalty.
- It is important to be prompt with the annual filing because the Registrar may assume that the company is no longer operational and may decide to strike it from the register completely. When the Registrar strikes a company from the register it will become the property of the Crown and will no longer exist.
- You will need to provide Companies House with up to date, accurate details regarding your company, and it should be available for public viewing.
- Companies House must know how to contact the company (the official registered office address where the company holds the records), the details of the members including shareholders.
- They must have a copy of the memorandum and articles of association, the accounting reference date, and all financial information regarding the company's annual accounts.

Dormant private companies with no trading history

- Dormant companies must file annual dormant accounts, which they can do electronically at Companies House.
- A company can become dormant by not trading throughout the current financial year, even if they have previous transactions in earlier accounting periods. You will not be able to file the form DCA if this is the case.

Trading fraudulently under a dormant company

- **There is a common misconception that directors can use dormant companies to conduct business without paying taxes.**
- In many examples, people register a company with the intent of leaving it dormant, and then conduct business overseas through the dormant company but clearing the money in their own country, separate from the company activity.
- This is the incorrect way to utilise a dormant company and in most instances, it is illegal.
- However, the question is how can HMRC become aware of this activity. HINT: It can't.

What if the UK dormant company is actually active and is a Professionally Managed Investment Entity (PMIE)?

1. The bank will insist that the UK company file for a GIIN with the IRS
2. As the company is tax resident in the UK, the GIIN will be registered through the UK portal
3. This will give the UK tax authorties a hint the company is not dormant.
4. **However, this is useless for the HMRC as the GIIN does not provide any bank account information if the comapny is not reportable for CRS.**

CRS FAQ Pg 11 Q.27 Reliance on publicly available information

- **Can Reporting Financial Institutions solely rely on the fact that an Account Holder is included in the FATCA FFI list to reasonably determine that such Account Holder is a Financial Institution pursuant to Section V(D)(1)(b) or Section VI(A)(1)(b)?**
- No. Section V(D)(1)(b) and Section VI(A)(1)(b) specify that the use of publicly available information is subject to the condition that such information can be relied upon to "reasonably determine" the status of the Entity. While the FATCA FFI list is included as an example in paragraph 12 of Section V of the Commentary, the mere inclusion of an Account Holder on the FATCA FFI list is not sufficient on its own to reasonably determine that such Account Holder is a Financial Institution for CRS purposes.

CRS FAQ pg 13 Q.4. Reliance on Model 1 FATCA IGA definition of Investment Entity for purposes of CRS

- **Can jurisdictions rely on the definition of Investment Entity used in the Model 1 FATCA IGA for the purposes of implementing the CRS?**
- No, the definition of Investment Entity in Article 1(1)(j) of the Model 1 FATCA IGA cannot be used for CRS purposes on its own, as it is less prescriptive than the definition of Investment Entity in Section VIII(A)(6). However, the definitions of the Model 1 FATCA IGA and the CRS can be read consistently. For example, the CRS definition includes a gross income test to determine whether an Entity is treated as primarily conducting as a business one or more of the activities described in subparagraph A(6)(a), or an Entity's gross income is primarily attributable to investing, reinvesting, or trading in Financial Assets for purposes of subparagraph A(6)(b), and could be used to interpret the less prescriptive aspects of the Model 1 FATCA IGA definition. The CRS definition is in fact based on the definition of Investment Entity in the US FATCA regulations, which may be used to interpret the Model 1 FATCA IGA definition.

Can new company be a PMIE if it has no operating history?

- Where an entity has no operating history at the time its status as a Custodial Institution or Investment Entity is being assessed, it will be regarded as a Financial Institution if it expects to meet the gross income threshold based on its business plans (such as the anticipated deployment of its assets and the functions of its employees).
- Consideration can also be given to any purpose or function for which the entity is licensed or regulated.

Summary

- The UK court of appeal decided HMRC can issue information request on tax status to persons resident outside UK
- However, the court did not extend to requests of information to third persons in investigating the tax liability of the person
- If no information is obtained, HMRC may rely on tax treaties or teg MCAA to demand information
- If no such treaty exists, HMRC may penalise person by deducting penalties from any assets the person holds in the UK

================================== END ==================================