Company Residence and Management and Control: How to Navigate the Pitfalls

Robert Field | 26 April 2016

A company will be treated as UK tax resident if it is incorporated in the UK. It will also be treated as tax resident if it is centrally managed and controlled from the UK. Two cases, in particular, illustrate the issues involved.

In *Wood v Holden* (2006) the taxpayer won, demonstrating that on the facts the company was managed and controlled from outside the UK. Then in 2009 came a victory for the Revenue in the *Laerstate* case. The *Laerstate* decision itself was not surprising, for the reasons analysed below, however it does serve as a useful reminder of all the things one must, and all the things one must not, do in order to ensure that a company does not become resident in the UK by reason of its management and control. The two cases together repay close study when addressing this particular aspect of UK tax theory.

The bare facts of *Laerstate*: *BV v Revenue and Customs Commissioners* are as follows:

Laerstate was a company incorporated in the Netherlands, and so resident there under Dutch law. It had two directors during the period in dispute – a Mr Bock and a Mr Trapman. Mr Bock acquired all the shares in the company in December 1992. At the time he was arranging finance from a German bank to fund the acquisition of £150m of Lonrho shares, by way of subscription (the subscription shares) and an option to acquire £50m of shares from a company controlled by Tiny Rowland (the option shares). The subscription shares were acquired by Laerstate using the funding organised by Mr Bock and in February 1993 he took up a role as joint managing director and CEO of Lonrho. In early 1996 Anglo American Corporation of South Africa Limited (Anglo) offered to buy Laerstate's option shares. Laerstate exercised its rights to buy the option shares and sold them on to Anglo in November 1996, Mr Bock having resigned as a director in August of that year. The UK Revenue issued assessments of Advance Corporation Tax and Corporation Tax on chargeable gains against Laerstate in November 1997, having concluded that it was resident in the UK by reason of its management and control.

Counsel for Laerstate tried to demonstrate that all 'acts of central management and control' of the company had taken place outside the UK, with a list of events and locations. However, while the Revenue accepted that in cases where a company is managed through board meetings then where the board meets is likely to be relevant to the question of central management and control, there is a prior question to be answered – were the decisions about the company made at board meetings at all? Mr Bock had accepted that board meetings were not really meetings at all and no discussion had taken place. The consequence, said the Revenue, was that this was a

case where the board did not function as such and all the business decisions had been made by a dominant director who was also the company's 100% shareholder and resident in the UK at the time. The question was therefore whether Mr Bock urged and persuaded his co-director, Mr Trapman, who then made decisions; or whether Mr Trapman had simply abdicated his responsibility in relation to the management of the company.

The Tribunal considered that Mr Bock's activities in relation to Laerstate while in the UK did not amount to "ministerial matters or good housekeeping", as contended by the company. On the facts, Mr Bock's activities went much further and amounted to strategic decision-making on the company's behalf. During the lead-up to the exercise of the option to "put" the Lonrho shares by way of sale to Anglo, Mr Bock made an unfortunate reference to "my shares" and the Tribunal concluded that Mr Bock told Mr Trapman to exercise the option and Mr Trapman did so without giving the matter any particular consideration. In contrast with *Wood v Holden*, Laerstate was not able to claim that the board was in possession of even an absolute minimum of information upon which it could base a decision, and then made one (even if mistaken or ill informed).

The *Laerstate* case is an object lesson in how *not* to run the affairs of a company in such a way that it is effectively managed and controlled outside the UK. The evidence summarised by the Tribunal is clear:

- Mr Bock's own diary clearly showed that he had been in the UK when a large number of critical decisions were taken;
- The board did not actually meet until March 1996, so the minutes of prior board meetings appeared to be Mr Bock having a meeting with himself. Moreover, the Tribunal found that although Mr Bock had actually been at three meetings, the minutes did not record this;
- Mr Bock carried on all relevant negotiations and instructed London solicitors, who reported to him alone;
- Mr Trapman was a mere cipher. He was not provided with information that enabled him to come to decisions, he simply did as he was told.

How does one ensure that this debacle does not happen to you? It is all about proper corporate governance and following due process, even though this means a more onerous compliance regime than would be observed in relation to a UK resident company.

Don't

- simply pay lip service to the place where the board meets;
- have a majority of UK resident directors, or even an equal number of UK resident and non-resident directors;
- allow UK based board members to phone in to meetings from the UK;
- rely on the services of non-UK directors who do not have the necessary skills and experience to make informed decisions, unless they can clearly demonstrate that they put their minds to the decision-making process;
- allow a controlling shareholder or anyone else to run a company's affairs without reference to the board. Such a person can advise, exhort and persuade – but

ultimately the board must make the decisions;

- rely on board minutes prepared in advance. Pre-prepared board minutes are essential to the completion of any transaction, of course; however, the minute of a meeting in which the decision to undertake the transaction is a critical document and must demonstrate that the board has applied its mind;
- allow board members to involve themselves in strategic decisions in the UK without reference to the board.

Do make sure that

- the composition of the board, and the location where board meetings are to take place, are appropriate for the business of the company. Business happens in real time and the board may have to convene at short notice;
- it is clear what decisions in relation to the company's affairs amount to "central management and control". Typically these will be decisions about buying or selling an asset, or dealing with finance;
- it is clear to everyone involved that only the board can take strategic decisions and that its meetings will be outside the UK;
- if UK residents are to be on the board, they are prepared to travel to board meetings outside the UK;
- the board meets regularly, in keeping with the nature of the company's business;
- the board has the information that enables it to make informed decisions on matters of strategy and policy;
- copies of the information provided to, and considered by, the board are kept;
- full minutes of board discussions and decisions are retained. Sound or video recordings of board meetings taking place can put the decision-making process beyond doubt;

If you require further information on anything covered in this briefing please contact Robert Field (robert.field@farrer.co.uk); +44(0)20 3375 7574 or your usual contact at the firm on 020 3375 7000. Further information can also be found on the Tax page on our website.