

OFFSHORE TRANSACTION COMPANIES THEIR USES AND OPERATIONS

Moore Stephens, Jersey specialises in the provision of management and administrative services to international transaction companies. The purpose of this paper is to highlight how such companies could be of benefit to your international trade and explain how they would be operated.

Why set up an offshore transaction company?

Offshore transaction companies are used for a wide variety of functions. In essence, an offshore transaction company co-ordinates the trade between two or more overseas locations by receiving and raising invoices and arranging for the direct delivery of goods or services from the supplier to the end customer, with legal title passing through the offshore company.

In general, the reason for operating an offshore transaction company is to accumulate funds or profits in a tax free, politically stable location. This is achieved either by the receipt of commission payments for providing an agency service, or, if the offshore transaction company acts as principal, by retaining profits representing the mark-up on each transaction.

Some specific uses of offshore transaction companies:

- Provide a trading entity for businesses based in countries with high level of political or economic instability, or with restrictive legislation such as exchange controls. The offshore transaction company can allow the legitimate accumulation of retained profits in a stable and unrestricted environment.
- Earn profits in a low tax jurisdiction allowing tax-free accumulation.
- Earn profits in an entity not required to publish or submit annual accounts.
- Provide employment services for short, medium or long-term contract employees working away from their country of origin and salaries and other benefits may be paid free of tax.
- Receive commissions earned overseas in a low tax jurisdiction. Income may not have to be remitted back to the parent company's country of residence.
- Earn and retain discounts on major capital purchases enabling retention of funds offshore.
- Provide a trading base close to Europe for suppliers or customers located in remote locations.
- Act as a ship chartering, aircraft leasing, film-making, property development or mining company.

How a transaction company works

To be effective, a transaction company must be managed and controlled by its directors in the chosen jurisdiction. Moore Stephens has a dedicated team that specialises in the administration of transaction companies.

The most basic structure involves three parties; a supplier, the intermediary transaction company and a purchaser or end customer. Depending on how the arrangement is to operate, the supplier or the purchaser will have established the structure. Both forms are considered below:

i) Supplier structure

A supplier wishes to trade internationally and earn/retain profits offshore. This may be to reduce local tax liabilities or to accumulate international trading income outside domestic restrictions such as exchange controls.

Goods or services are sold by the supplier to an offshore company, managed and controlled in Jersey. The company then sells those goods or services to the end customer but delivery is made direct from the supplier to the customer. Only legal title and payment need pass through the offshore company. An example of a typical transaction is as follows:

- a) Details of the order are transmitted to the offshore transaction company, from the supplier. Necessary information includes;

- Product specification
 - Purchase and sale prices
 - Shipment date
 - Shipment terms
 - Payments terms
 - Documents required
- b) The offshore transaction company prepares documentation to place an order with the supplier.
 - c) The supplier issues an order confirmation to the offshore company.
 - d) The offshore company receives an order from the purchaser.
 - e) When the goods are ready for despatch, all documentation except the purchase invoice is sent direct to the customer. The purchase invoice is sent to the offshore transaction company.
 - f) Upon receipt of the purchase invoice the offshore transaction company raises a sales invoice, which it transmits to the customer by including, where appropriate, the agreed mark-up representing offshore profit.
 - g) The goods are despatched direct from the supplier to the end customer.
 - h) On the due payment date the customer transmits funds in settlement of the sales invoice to the offshore transaction company.
 - i) Upon receipt of the funds the offshore transaction company transmits settlement of the purchase invoice to the supplier retaining the profit element offshore.

A typical method of transmitting documentation to the offshore transaction company is by facsimile.

ii) Purchaser structure

In this case, a purchaser may have negotiated particularly attractive discount terms or competitive prices and wish to retain those discounts offshore. This could apply to goods purchased as normal trading stock or capital acquisitions on which annual tax allowances may be claimed.

In addition to possible tax benefits, an offshore transaction company may also assist by retaining accumulated funds offshore, outside domestic restrictions such as exchange controls.

An example of a typical transaction is as follows:

- a) Details of items to be purchased are transmitted by the purchaser to the offshore transaction company by fax (see ia), "The supplier structure").
- b) The offshore transaction company places an order with the supplier.
- c) The supplier issues an order confirmation to the offshore company.
- d) When the goods are ready for despatch the purchase invoice is sent to the offshore transaction company. All other documentation is sent direct to the purchaser
- e) Upon receipt of the purchase invoice, the offshore transaction company raises a sales invoice, which it transmits to the purchaser, ensuring that where applicable, discounts receivable are added back so that the sales invoice reflects the gross market value of the goods.
- f) The goods are despatched direct from the supplier to the purchaser.
- g) On the due payment date, the purchaser transmits funds in settlement of the sales invoice to the offshore transaction company.
- h) Upon receipt of the funds, the offshore transaction company transmits settlement of the original purchase invoice, less any discounts, to the supplier. Profits and discounts are retained offshore.

Once again, a typical method of transmitting documents to the offshore transaction company is by facsimile.

Letters of Credit

Given that individual consignments can be of significant value it is essential that the offshore transaction company is paid in full for the goods delivered. Similarly, the company must ensure it pays only for the goods received.

Letters of credit can assure this. As there is certainty of payment associated with this form of settlement, suppliers can offer extended credit terms to their customers and purchasers can gain better control over their terms of trade by improving credit terms or obtaining price discounts.

Our dedicated team has extensive experience in all aspects of letters of credit, through a number of international and UK clearing banks based in Jersey and is more than happy to discuss your specific requirements in addition to other methods of payment, which may be beneficial to your business.

Although extremely valuable, particularly when trading with developing economies, letters of credit are an expensive means of securing payment. Bank charges are based on the value of the consignment. Bank drafts which are payable on presentation of delivery documents offer an alternative to letters of credit and provide added security of payment at a reduced cost; the supplier lodges the documents with the customer's bank and the consignment can only be released upon acceptance of the draft. This method of payment is much more straightforward than letters of credit, but still ensures that goods have been despatched before payment is made. If using this method it is important to use reputable international banks.

Taxation issues

i) Jersey

The company will be classed as International Service Entity. As the ultimate owners will be outside of Jersey, there will be **no** taxation payable in the Island on any income from sources outside Jersey and bank interest received on Jersey accounts. The company can accumulate income entirely free of Jersey tax and can receive or remit dividends or pay interest without any requirement to withhold tax. There is no need to submit accounts or tax returns to the local authorities.

ii) Country of parent company's residence

Before any structure is put in place, it is essential that the tax rules of the parent be reviewed to ensure the structure is effective. Of key significance are transfer pricing and general anti-avoidance provisions, which could look through the offshore company and treat any transactions as being directly between the supplier and the end customer.

We always recommend that specific tax advice is taken concerning offshore transaction companies and would be happy to assist through the Moore Stephens International Network.

iii) Repatriation of profits

Before establishing a transaction structure the treatment of repatriated profits must be established. Some tax authorities apply very favourable tax treatment to such dividends while others may apply more penal rates of tax. Specific advice should be taken in the country in which you are ordinarily resident for tax purposes.

Jurisdiction

Moore Stephens, Jersey manages companies that are registered in various jurisdictions such as Jersey, Guernsey, the Isle of Man, the British Virgin Islands and the Cayman Islands. We use these different companies because of their specific characteristics, which we are able to combine with the technical skills of our team to offer our clients a service designed for their specific needs.

Ownership of your company

As a consequence of the Jersey requirement for probate, when the owner of a Jersey company dies, we recommend that you do not directly own shares in your Jersey Company, but through a trust – details are available on request.

Fees and Costs - Formation and Ongoing

We appreciate that it will be important for you to have a good indication of the administration costs so you can evaluate if an offshore transaction company would be worthwhile. We would, therefore, need a full profile of company's likely level of activity so we can provide an accurate quote. Whilst not exhaustive, the following is an indication of information required:

- Number of transactions, both incoming and outgoing
- Payment methods e.g. open account, bank drafts, letters of credit
- Countries where the company will conduct business
- Any salient information which you consider may have an impact on the work levels

Moore Stephens Jersey is part of Moore Stephens International, which is regarded as one of the world's major accounting and consulting networks consisting of 351 independent firms with 630 representative offices and some 21,000 people across 98 countries.

This information sheet provides a brief outline only and is not comprehensive as such and should you require further specific advice, please contact either Clive Barton or Kathy Gillen:

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