# Corporate Governance – and Keeping Control Offshore

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## What is Corporate Governance?

- "*Ultimately, corporate governance is about the behaviour of boards and their directors*" (GFSC Finance Sector Code of Corporate Governance).
- Corporate governance is a formal expression of the components of good corporate practice against which shareholders and boards, as well as regulators, can better assess the degree of governance exercised over a company.
- The JFSC has not yet issued a code on CG but references as to the component parts of CG are evident in various parts of the regulations issued by the JFSC.
- Companies based in Jersey may seek to adopt corporate governance requirements set out in the locality of their centre of main interest (COMI) in order to demonstrate good practice, e.g. compliance with the UK Corporate Governance Code (as published from time to time) compliance with which would demonstrate discharge of CG expectations in Jersey.



## Components of Corporate Governance

Useful to look at the GFSC Code on CG which is structured around a set of 8 principles to provide an idea as to the infrastructure of CG.

Principles include the following:

1. **The board** – governance structure (to reflect the complexities of the business and its specific activities, strategies, risk appetite, policies, etc., role of chairman, composition of the board (balance of skills, responsibilities and a structure that does not cause an individual to, for example, unduly dominate decision making), committees of the board, delegation to management (need for a clear senior management structure but delegation not to absolve the board from overall responsibility for the sound governance of the company) and board meetings (sufficiently often to discharge duties)).
2. **Directors** – duties (acting intra vires), legislation and regulation (being conversant with the law and regulations), strategy (being responsible for the same), appointment, induction and reappointment of directors (i.e. a structured system for the appointment of directors and succession), commitment (sufficient time and understanding of the role to be discharged), performance evaluation (board scrutiny of its members), training and development.



## Components of Corporate Governance (2)

3. **Business conduct and ethics** – conflicts of interest, self-dealing and duties.
4. **Accountability** – object is to have a balanced assessment process for the company's position and prospects and for considering financial reporting and internal controls, e.g. strategic business management, audit and auditor rules, internal risk management structures, accounting for outsourced activity and annual business reviews.
5. **Risk management** – need for oversight of risk management including rules for attributing responsibility for risk (ultimately a board responsibility but possibly with the support of a senior executive responsible specifically for risk), strategy and policy (appetite, evaluation and management protocols), DR policy and contingency planning.
6. **Disclosure and reporting** – compliance with the law and regulations.
7. **Remuneration** – objective is that remuneration arrangements are structured fairly and responsibility and policies are consistent with effective risk management including avoiding policies that encourage excessive risk taking.



## Components of Corporate Governance (3)

8. **Shareholder relations** – satisfactory communication to shareholders and respect for rights of shareholders.

Likely that compliance with overseas codes in principal jurisdictions such as the UK will ensure that companies comply with domestic expectations, e.g. compliance with the UK Corporate Governance Code or the Association of Investment Companies Code of Corporate Governance (AIC Code) (the AIC Code is supported by the JFSC) and includes 21 principles, essentially covering the types of issues referred to above.

Increasing need for CG and resulting substance likely to cause "Jumbo" directors (directors who hold many directorships) to be more of a problem.

The CG infrastructure takes administration in the opposite direction to the "Sark lark" and "brass plate" activity and other practices of that nature.



## Centralising Control

- It is not axiomatic that having proper CG in place means that a company will, for example, be able to robustly assert that it is controlled in, say, Jersey, but there is a connection in that good CG should ensure that there is a predictable outcome on the issue of where a company is controlled.
- Under Article 123 of the Income Tax (Jersey) Law 1961, a Jersey company is resident in Jersey for tax purposes unless its business is "*centrally managed and controlled*" outside of Jersey in a country or territory where (a) the highest rate at which any company may be charged to tax on any part of its income is 10% and (b) the company is resident for tax purposes in that country or territory.
- The "central management and control" doctrine is well known and is essentially the place where decisions about the strategic policy and direction the company is taken (as opposed to the more day to day, operational issues).
- HMRC look to ascertain (a) who exercises CMC and (b) where, and in relation to (b), they look at whether it is the directors that exercise the CMC and if so, where, and if not them, who and where those individuals are located.

## Centralising Control (2)

- Locality of board meetings obviously relevant to CMC and ideally most, if not all, board meetings should be held in a single jurisdiction and to have sufficient meetings by reference to the activities of a company.
- It is important to ensure that what is done by directors is fully and properly documented but it is no less important to ensure that what is documented has actually taken place. Minutes should note the time and place of the meeting and who was present, and discussions minuted, to demonstrate substance rather than just form.
- Necessary that directors have sufficient knowledge and expertise in order to consider rather than merely follow proposals and reach a reasonable conclusion, e.g. difficulties may arise if the sector experience is not concentrated in the jurisdiction where taxation is not intended to occur.
- No key strategic decisions should be made outside of formal meetings of directors and where discretionary powers have been delegated to a person (including a director) those powers should only relate to day to day affairs and not key decisions.

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## Centralising Control (3)

- Need to avoid usurpation of the board by a single person who is the "guiding force" behind the company (also would be contrary to span of control considerations under FS regulations and CG principles).
- Key issue with usurpation is to demonstrate that if asked to do something that was not in the interests of a company, the directors of a company would not do it. As was noted in the case of *Untelrab Limited v McGregor and others (1996) STC 1*: "*That a determination [as to where the central management and control of a company actually abides] is a pure question of fact to be determined by a scrutiny of the course of business and trading…; that although a board might do what it is told to do it did not follow that the control and management lay with another, so long as the board exercised their discretion when coming to their decisions and would have refused to carry out an improper or unwise transaction; and that when deciding the issue…one should stand back from the detail and make up one's mind from the picture which the whole of the evidence presents."*

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## Centralising Control (4)

- These issues were of relevance in the case of *Mahonia (2004)* where the conduct of that Jersey company was considered in England in the context of the "Enron" scandal. Mahonia had been set up as a SPV to be a lending vehicle to an Enron entity and Mahonia received funding from parallel transactions between it and Chase Bank.
- The issue arose as to whether Mahonia was independent of Chase or controlled by it. Due to proper management by its directors, Mahonia was found to have not been controlled by Chase and the crucial finding was that the directors of Mahonia were free to decide whether to transact and (as the judge found) "*if there were elements of the transaction with which the directors were unhappy, I find that they would have sought amendment as they did from time to time or refused to agree to Mahonia's participation.*"

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## BEPS

- OECD's initiative on "Base Erosion and Profit Sharing" proposals moving ahead and elements of concern under BEPS include the artificial avoidance of permanent establishment status and demonstrating "economic substance" and "value exchange".
- According to the Chief Minister, there may be opportunities in Jersey under BEPs as more business may move to Jersey to demonstrate "real physical presence…and…substance".
- The issues of good CG, good practices with respect to keeping control offshore and future opportunity under BEPS all seem to coincide.

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