

The UK-Liechtenstein tax deal

“No-names” negotiations and instructing a UK solicitor

It is now widely known that, on 11 August 2009, a ground-breaking deal was signed between the Government of the Principality of Liechtenstein and Her Majesty’s Revenue and Customs of the United Kingdom. This deal dramatically changes the way in which the UK tax regime can affect – and reach – private wealth held or administered in Liechtenstein.

The Liechtenstein Disclosure Facility

The terms of the deal include a special regime, the Liechtenstein Disclosure Facility or “LDF”, by which an individual with unpaid UK tax liabilities can put his UK tax affairs into a proper order, and thus can become fully UK tax compliant.

The LDF offers such an individual significantly more favourable terms, including a shorter taxable period, lesser tax penalties and the guarantee of no criminal prosecution, than would be otherwise available within the UK tax regime. For an individual eligible for the LDF, in the great majority of cases the LDF will offer a lower-cost tax deal than he could otherwise get.

This makes the LDF attractive for anyone with unpaid UK tax liabilities (whether he has existing links to Liechtenstein or not).

No-names negotiations

Another significant advantage of the LDF, not available elsewhere in the UK tax regime, is that the individual is allowed to approach Her Majesty’s Revenue and Customs (“HMRC”) and to open negotiations on a no-names basis. In effect, the individual can see what he will have to pay before he is required to commit himself to the disclosure process.

The anonymous approach and no-names negotiations are made through a UK professional representative. The key here is the role of the UK professional representative. In order for the “no names” negotiations to function, the individual must have a UK professional representative who will deal with HMRC on his behalf.

However, there is a catch. UK criminal legislation, aimed at preventing money laundering, places an

obligation on UK professionals to report clients in circumstances where the proceeds of crime are involved – including the proceeds of tax crimes, such as tax evasion. Such a report is made to the UK criminal authorities, not to HMRC – but obviously it undermines the whole purpose of “no names” negotiations, and there is every likelihood that the information will be shared by the criminal authorities with HMRC.

Legal professional privilege (‘LPP’)

The deal made by HMRC with the Liechtenstein Government does not bind the UK criminal authorities, nor does it affect the legal obligations of a UK professional under the UK money laundering reporting regime. The only available exemption, under which a UK professional would not be required to report the client, is where legal professional privilege (“LPP”) applies. LPP will only apply where the representative is a UK lawyer (most likely a solicitor), and where the client’s instructions have been provided for the purpose of giving advice, and in the right way.

In addition, the deal does not protect the client against HMRC’s very wide-ranging power, under UK law, to demand information from a third party, e.g. from a bank or adviser. While it is unlikely that HMRC would use this power in relation to an individual who was already in the process of making voluntary disclosure, it would be a significant risk if negotiations broke down or the client withdrew from the disclosure process. Again, the only available exemption that would protect the client here is LPP.

As a result, if an individual wishes to take advantage of the anonymous approach facility being offered by HMRC, it is important that the individual chooses the right representative, and provides instructions in the right way. The guidelines below show how the client can get the benefit of LPP protection, in relation to both anti-money laundering reporting requirements and HMRC’s power to demand information from an adviser.

Instructing a UK solicitor – financial institutions

The starting point will often be for the individual client's Liechtenstein service provider, such as a Liechtenstein bank, fiduciary or other financial institution, to approach the UK solicitor on behalf of one or more affected individuals. At this stage, the individual client may not wish to disclose his identity even to the UK solicitor – although if he does, the UK solicitor will be under a strict obligation of confidentiality.

It would be possible, and entirely proper, for the Liechtenstein financial institution (rather than the individual) to become the client of the UK solicitor. The financial institution will, in all but exceptional cases, have a legitimate interest in obtaining the UK solicitor's advice for itself. At this stage, it will not be necessary for the financial institution to disclose the identity of any underlying individual client to the solicitor, provided that the financial institution instructs and deals with the solicitor in the right way.

It will need to be clear, both in the solicitor's terms of engagement and in how the retainer is conducted, that the financial institution is acting as principal (i.e. on its own behalf), and not as an agent for a client. For example, the solicitor would take all his instructions directly from the financial institution, would obtain all the background facts directly from the financial institution and would submit his invoice to the financial institution for payment.

It would be best if the financial institution could instruct the solicitor to advise on the basis of generic type facts, such as a fact pattern common to a group of the financial institution's clients. However, it is not fatal if the fact pattern belongs to only one of the financial institution's clients.

The financial institution should take care not to suggest that it could be an agent – for example, if the financial institution tells the solicitor that it will need to refer a decision to "its client", or if the financial institution asks the solicitor to check certain facts with "its client". If the financial institution, perhaps inadvertently, does reveal that it is acting as an agent, then the solicitor will be required to identify and verify the underlying client and to carry out the usual "know your client" due diligence checks on that client. In this situation, LPP may not apply and the solicitor may have to make a report about the underlying client to the UK criminal authorities.

When acting for the financial institution, the solicitor should not have any contact with individual clients of that financial institution, until those clients are ready to instruct the solicitor themselves. Once the solicitor has given his initial advice, there will come a point when it will be desirable for the clients to instruct the solicitor directly, because there is a limitation on how much the solicitor can do while his client is only the financial institution.

While the solicitor's client is the financial institution, the solicitor will only be able to give advice – for example, on the likely tax costs involved in making disclosure. The solicitor will not be able to carry out any representation for a particular taxpayer – e.g. making an anonymous approach to HMRC. Also, the solicitor will not be able to carry out any transactions, such as restructuring the Liechtenstein assets.

Instructing a UK solicitor – individuals

In some cases, an instruction from a Liechtenstein financial institution may develop into a direct instruction from an individual taxpayer, e.g. after the solicitor has advised the financial institution on the likely tax cost of making disclosure, and the individual client wishes to proceed with the disclosure process. In other cases, the individual may wish to instruct the solicitor directly from the beginning. In either case, the solicitor will need to carry out the usual "know your client" due diligence checks on that client.

When the individual client is giving instructions to the solicitor, the client will be protected by LPP in relation to any past breaches of the UK tax laws that he discloses to the solicitor, even if those breaches are severe enough to amount to a criminal offence in the UK. This means that the solicitor will not have to report the client to the UK criminal authorities, or to comply with a demand for information from HMRC. However, the client must not give the solicitor any instructions that would amount to, or further, a criminal offence.

The following are examples of instructions where the client will be protected by LPP:

- > The client instructs the solicitor to advise him on becoming UK tax compliant after past breaches, and to represent him in making the proper disclosures to HMRC and negotiating the best deal with HMRC on past tax liabilities and penalties.
- > The client instructs the solicitor to advise him on how to become UK tax compliant after past breaches, e.g. the procedure, with the solicitor's retainer being limited to advice. In this case, the solicitor's retainer will end after the advice has been given, and the client himself will take responsibility for making the approach to HMRC.
- > The client instructs the solicitor to advise him on the likely tax costs of becoming UK tax compliant after past breaches, without seeking advice or representation on the disclosure itself. Again, in this case the solicitor's retainer will end after the advice has been given, and the client himself will take responsibility for making the approach to HMRC.
- > The client instructs the solicitor to advise him on whether his existing structures or assets in Liechtenstein are UK tax compliant. (The client will be protected by LPP even if the solicitor, on performing his analysis, concludes that there has been a breach of the UK tax laws.)
- > The client instructs the solicitor to provide him with a certificate, for the Liechtenstein financial institution's own compliance, that he is UK tax compliant. (The client will be protected by LPP even if the solicitor, on performing his analysis, concludes that he cannot provide such a certificate.)

What not to do

The following are examples of instructions where the client will not be protected by LPP (and therefore the solicitor may be obliged to report the client, and to comply with any HMRC demand for information):

- > Having decided to make disclosure to HMRC, the client must be committed to making full disclosure – the client must not instruct the solicitor to disclose only part of his affairs (i.e. to attempt to conceal the rest).

- > Having been advised that there has been a past breach of UK tax laws, the client must not inform the solicitor that he (the client) will not be making disclosure to HMRC. However, if the client simply ends the retainer and takes responsibility himself for making the disclosure, this will not trigger a disclosure obligation on the solicitor so long as the solicitor does not know, or have reasonable cause to suspect, that full disclosure will not be made.
- > Having been advised that there has been a past breach of UK tax laws, the client must not ask the solicitor to carry out any transactions in relation to the assets (e.g. to restructure the assets), unless he has already authorised the solicitor to disclose his name to HMRC and to the UK criminal authorities.
- > If the solicitor is aware of any past breaches of tax laws of countries other than the UK, the client must not inform the solicitor that he (the client) will not be making disclosure to the appropriate other country's tax authority.

Protecting information with LPP

When the client gives information to the solicitor in the course of his instructions, it is essential that this information is sent to the solicitor directly from the client himself. This is in order for the information to be protected by LPP.

Information sent to the solicitor by a third party, such as a Liechtenstein financial institution or another professional adviser, may not be protected by LPP. There is an easy solution to this – the third party sends the information to the client, who forwards it on to the solicitor.

There is no need for the client actually to compile the information – e.g. the financial institution can provide all the account statements, or an accountant or financial adviser can provide all the transaction details, to the client. All the client needs to do is forward it on – this can be as simple as forwarding an e-mail attachment.

The key is that, when the information is received by the solicitor, it comes directly from the client himself.

Future changes to LPP

This note has been prepared on the basis of the UK regime for LPP in force as at the date of publication (September 2009). The LPP regime is currently undergoing review and, therefore, this note is subject to any future changes in the UK law or practice relating to LPP.

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