

**T**his issue we are pleased to announce several new developments:

#### URUGUAY

In September we incorporated SOVEREIGN TRUST (URUGUAY) LIMITED which will operate out of offices located in Montevideo and Buenos Aires.

In addition to providing the usual company and trust formation and management services the new enterprise will also establish and manage Uruguayan companies and assist in establishing operations within the free trade zone in Uruguay.

An official opening is planned for 11 November in Montevideo and all clients and friends are most welcome to come and help us celebrate.

#### BAHAMAS

As mentioned in the last issue we are in the process of opening offices in Nassau, Bahamas. SOVEREIGN (BAHAMAS) LIMITED was incorporated in August and we are now in the final stages of the licensing procedure which we expect to be completed before the end of the month.

#### DENMARK

There has been tremendous interest in the new Danish holding company regime (*see page 6 last issue*) and in response we have accelerated plans to open offices in Copenhagen and are in the process of establishing SOVEREIGN (DENMARK) Aps.

More details will follow later.

#### EUROMONEY TRAINING

Sovereign have formed a joint venture with Euromoney training to provide, on an exclusive basis, speakers for Euromoney's seminars on International Tax Planning and Offshore Centres.

The first of a series of three to five-day training courses was held at The Regent Palace Hotel in London (21–25 June) when Professor William Byrnes and Howard Bilton delivered a five-day intensive course to a group of industry professionals. Further three-day seminars will take place in Hong Kong (6–9 December) and in Singapore in the early part of next year.

Part of the Euromoney/Institutional Investor Group, Euromoney Training is recognised

worldwide as a leading provider of specialist training to the banking and finance sector. Programmes are delivered by top trainers and market practitioners, supported by unparalleled information and research resources.

Each year Euromoney Training welcomes over 3,500 delegates to its training courses in London, Hong Kong, Singapore and New York. Attended by an international audience, these courses provide not only leading-edge training but also valuable networking and future trading opportunities.

In total, over 300 public training courses are held each year, in addition to extensive in-house training for banks and corporates.

Sovereign is pleased that our expertise in international and offshore tax planning has been recognised by one of the world's leading training companies.

#### PORTUGAL

The Sovereign Group is hosting an International Tax Planning Seminar on Friday 19 November 1999 at the Hotel Le Meridien, Rua Castilho, Lisbon.

This one-day seminar will centre around the use of offshore and onshore companies and trusts for effective personal and corporate tax planning structures, with particular reference to use of those techniques in Portugal.

The conference fee will be PTE75,000 (£250) + 17% VAT, with a 20% discount for early booking. Anyone interested in attending should contact our Portugal office on +351 282 342601.

#### SUBSCRIPTION

If you haven't already done so, then please don't forget to return the back page subscription form to us to ensure that you continue to receive future editions of this Report. There is no charge but we do need to hear from you if you wish to remain on the mailing list.



Howard Bilton BA(Hons)  
Barrister-at-Law (England, Wales & Gibraltar)  
Chairman of The Sovereign Group

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GIBRALTAR

**New rules for HNWIs brought into force**

Amendments to streamline the rules for High Net Worth Individuals (HNWIs) and Relocation of Executives Possessing Special Skills (REPSS) were brought into force on 19 August 1999.

HNWIs are reclassified as "Category II Qualifying Individuals" for tax purposes and the 30-day minimum requirement for HNWIs to reside in Gibraltar is removed. The requirement for HNWIs to maintain appropriate accommodation in Gibraltar, rented or owned, for their exclusive use is extended from seven to 12 months a year and, where appropriate, spouses and children of HNWIs can be included on the HNWI return in order to establish an aggregate family income. HNWIs are also to be allowed to carry on business from Gibraltar provided that the business is international.

Under the REPSS scheme, a second category has been created for qualifying individuals with income arising from their employment in Gibraltar below £50,000 pa (Category IV) who will be subject to maximum taxation of £5,000 pa. The previous tax ceiling for all qualifying individuals was £10,000 pa.

The employer of a Category IV individual is now required to take on a Gibraltar national at the same time. Qualifying individuals with a worldwide income of more than £50,000 pa are reclassified as Category III and subject to maximum taxation of £10,000 pa.

The UK parliament passed the Banking (Gibraltar) Regulations 1999 to allow the

"passporting" of banking services by Gibraltar-based banks to other EEA member states on the basis of their Gibraltar authorisation. It followed a review of the supervision of Gibraltar's banking sector last year by a team of independent experts from the Bank of England. The UK government agreed to insurance passporting for Gibraltar-based insurance companies in 1997. Passporting for investment services is still pending.

The European Commission is considering whether to take legal proceedings against Spain over the border delays caused by Spanish customs and police which are considered unacceptable at an internal EU border. But Spain, which claims sovereignty over Gibraltar, has insisted that the territory is a base for criminal activity and also claims that its tax revenues are compromised by Gibraltar's offshore banking regime.

**SOVEREIGN COMMENT**

The HNWI rules have been especially successful in attracting wealthy individuals to Gibraltar. The rates of tax payable in Gibraltar are considerably lower than the equivalent applicable rate in the competing territories of Jersey, Guernsey and Isle of Man and this, coupled with the idyllic climate of the area, has persuaded many wealthy individuals to make Gibraltar their domicile of choice.

Spain continues to posture about the issue of sovereignty over Gibraltar but this seems to have had little effect on the success of the international finance centre which continues to grow apace.

BRITISH OFFSHORE ISLANDS

**Legislation "unprecedented"**

UK Treasury minister Dawn Primarolo told a Select committee of the House of Commons that it would be "unprecedented" for the UK to legislate for the Crown Dependencies or Overseas Territories without their consent. But would not overtly state that the UK did not have the power to do so.

Primarolo, the UK Paymaster General, was giving evidence to the Select Committee on Treasury in her capacity as chairman of the EU's Code of Conduct Group on business taxation.

She said; "There is no legislation which formally sets out the extent of the powers of the parliament of the UK in relation to the Channel Islands. It would be unprecedented for the UK to legislate for the Overseas Territories or the Crown Dependencies without their agreement."

**SOVEREIGN COMMENT**

This statement may give some comfort to the British dependent territories who operate offshore centres and who are still digesting the possible ramifications of the OECD report and the UK government report entitled "Partnership For Progress & Prosperity" which recommends the imposition of tighter financial regulation and other measures which are seen as unhelpful to the development of their finance centres.

ISLE OF MAN

**Electronic Transactions Bill**

The Department of Trade & Industry has drafted an Electronic Transactions Bill intended as a first step to establishing the Isle of Man as an international centre for e-commerce.

Based on a draft Electronic Transactions Bill issued by the federal Government of Australia in January 1999, the draft Bill sets out to encourage and facilitate the use of information technology by removing legal constraints and doubts affecting the use of electronic communications.

It is intended to put e-commerce and paper-based commerce on the same legal footing and remove any legal impediments to the use of electronic communications with public authorities.

SWITZERLAND

**OECD warning**

The OECD warned the Swiss government on 5 August 1999 that it would come under increasing pressure from foreign tax authorities to provide banking information as Swiss bank secrecy laws made the use of fiduciary accounts "attractive to non-resident individuals desiring to evade taxes in their country of residence".

IRISH REPUBLIC

**Irish government to appoint inspector to Cayman bank**

The High Court has granted an application to serve papers on Ansbacher (Cayman) Ltd, the Cayman Islands bank which lodged millions of pounds in Dublin banks on behalf of Irish residents.

It is a preliminary move to the appointment of a High Court inspector and follows completion by authorised officer Gerard Ryan of an 18-month inquiry into the Cayman bank.

The secretive Ansbacher deposits, which were in existence from the 1970s and at one stage held IR£38m, were kept in Guinness & Mahon Bank and Irish Intercontinental Bank in Dublin. They contained funds belonging to a number of senior Irish figures, including former prime minister Charles Haughey.

Ryan was authorised to investigate Ansbacher (Cayman) last year. He is continuing to conduct inquiries into Irish Intercontinental Bank and Guinness & Mahon Bank, Cayman-

registered Hamilton Ross Ltd and College Trustees, a Guernsey company which handled trusts for Irish residents. All are connected with the Ansbacher deposits.

The Irish Revenue is also expected to apply to the High Court for permission to examine Ansbacher deposits held by Irish residents. According to a recent report by the auditor general, there were approximately 400 accounts in the name of Guinness Mahon Cayman Trust, subsequently Ansbacher (Cayman) Ltd. All but about 30 of them were foreign currency accounts.

Until new powers were conferred on the Revenue in the last Finance Act, it needed to know an account-holder's name before it could examine a bank account. Under its new powers, the Revenue can apply to the courts for permission to examine accounts where tax-evasion is suspected even where the account holder's identity is not known.

## BRITISH VIRGIN ISLANDS

**Code of Conduct (Service Providers) Bill drafted**

A draft Code of Conduct (Service Providers) Bill 1999 to give mandatory statutory status to the existing voluntary Code of Conduct for BVI-licensed service providers has been drafted and circulated for consultation.

The draft Bill is to be given legislative priority together with the Information Assistance (Financial Services) Bill which is to establish procedures concerning access to information about companies in response to regulatory enquiries.

Under the proposed legislation, disclosure is only to be permitted within defined structures under the authority of the High Court and only when public interest and other criteria have been satisfied.

**SOVEREIGN COMMENT**

These measures have been rushed through in part in response to the OECD and other reports referred to earlier. BVI remains the leading offshore jurisdiction of the world in terms of number of incorporations and is now keen to be seen as being regulated to the highest standard.

## CARIBBEAN

**Caribbean Court of Justice to replace UK Privy Council**

Prime Ministers of former British colonies in the Caribbean agreed in July to create a regional Court of Justice to replace the UK Privy Council as a final court of appeal.

The proposal, which would involve a panel of judges drawn from the participating jurisdictions, was approved by the attorney generals at the Caricom Summit in Trinidad and a preparatory committee has been appointed to complete arrangements for its establishment.

It is claimed that the new court will be able to deal with wider issues than the Privy Council, such as the settlement of trade disputes between members, but it is also viewed as a reaction to the protracted process of appeals which has frustrated efforts of governments in the region to execute capital punishments.

**SOVEREIGN COMMENT**

It is hoped that a Caribbean court of appeal will speed up the decision making process but whether the new court will be viewed with the same degree of respect as the UK Privy Council remains to be seen.

## UNITED STATES

**Russian money-laundering investigation centres on the Bank of New York**

An international investigation into suspected Russian money laundering, centred on the Bank of New York (BoNY), has sparked inquiries in the USA, UK, Switzerland, Russia and France. It was reported that the bank may have been used to transfer up to US\$15bn from suspect Russian sources since early last year.

The initial investigation concerned Benex International, a company registered in New Jersey. Financial institutions from Russia, UK, China and Australia had sent or received funds totalling billions of dollars through business accounts at BoNY run by Benex.

In August police raided the London home of Lucy Edwards, BoNY vice-president in London with responsibility for eastern Europe, and her husband Peter Berlin, an officer of Benex International. Both are Russian born. Edwards has been dismissed. Benex has been linked to Arigon, a Channel Islands firm understood to be controlled by Semyon Mogilevich, a Russian based in Hungary suspected of involvement in drugs and arms trafficking and prostitution.

Investigators are also examining the links with BoNY and a second alleged Russian mafia boss, Grigori Lutchansky, who was suspected of laundering money through European banks in the early 1990s using a series of companies in the Channel Islands and Isle of Man controlled by a company called Nordex, then based in Vienna.

Another BoNY employee, US-based senior vice-president Natasha Gurfinkel Kagalovsky, has been suspended. Her husband Konstantin Kagalovsky is a former deputy chairman of Menatep, a Russian bank which failed last year. Avisma, a Siberia-based titanium producer in

which Menatep formerly had a controlling interest, has filed an action in the US against a group of US shareholders who, it alleges, inherited and maintained a "tolling" scheme to divert profits through companies in the Isle of Man, Dublin and the US set up by Valmet, a financial services group based in the Isle of Man and partly owned by Menatep.

Swiss investigators are also believed to be looking into Runicom, the Gibraltar-based trading arm of Russian oil giant Sibneft. Runicom, which is owned by companies set up by Valmet, also set up a Swiss subsidiary, initially based at Valmet's Geneva office.

French authorities are understood to have opened an inquiry into the use of Eurobank, a Paris-based subsidiary of the Russian central bank, through which it channelled up to US\$1.2bn of IMF money to a company in Jersey although Russia and the IMF say there is no evidence that any of the funds were misused.

Jim Leach, chairman of the US Congress banking committee, has estimated that the sums laundered from Russia through Western banks over the past five years could total more than US\$100bn.

**SOVEREIGN COMMENT**

All companies working in the offshore sector and elsewhere in the financial services industry have long since been required to adopt "know your customer" principles and effect due diligence on their clients to international standards.

Whilst Sovereign recognises the desire for clients to maintain privacy, clients and prospective clients must expect to answer detailed questions about their background and the nature of the business which they wish to undertake.

## BAHAMAS

**Bahamas Securities Industry Act brought into force to aid establishment of BISX**

A Securities Industry Act to facilitate the establishment of a Bahamas International Stock Exchange (BISX) was brought into force in June. It is due to be operational for the domestic market by the end of this year with international trading scheduled to commence by the middle of next year.

The exchange, which expects to benefit from the affordable cost of international secondary listings, will be privately-owned and operated. Bahamas-based traders were invited to apply for membership by September.

A further invitation will be extended to foreign-based traders prior to the launch of international trading next year.

The BISX will be supervised by the Securities Commission of the Bahamas. This will supersede the Bahamas Financial Services Board which was created in 1996 to oversee development.

The contract to operate the trading systems has been awarded to a Canadian firm, EFA Software, which runs the Alberta Stock Exchange.

**SOVEREIGN COMMENT**

The Sovereign Group is in the final stages of establishing an operation in the Bahamas which will trade under the style "Sovereign (Bahamas) Ltd". The company has applied to become a founder member of the BISX.

NEW ZEALAND

**Court rules key "Winebox" findings invalid**

The New Zealand High Court has ruled that some of the key findings of the so-called "winebox" Commission of Inquiry into corporate tax fraud in the Cook Islands were invalid.

The inquiry under Sir Ronald Davison was set up in 1994 following the appearance of documentation – known as the "winebox" documents – concerning a series of 1980s Cook Islands tax deals by several New Zealand companies which, it was claimed, were evidence of fraud and tax evasion.

In its final report in 1997, although questioning the ethics of the transactions, the Commission decided that there was no fraud in the "winebox deals" and concluded there was therefore no incompetence on the part of the Serious Fraud Office and Inland Revenue Department for failing to find it.

But the judicial review of the inquiry found that Davison, had erred in relation to the "Magnum" transactions, one of the four main schemes covered by the commission.

Firstly, he had erred in concluding that the doctrine of acts of State prevented him from inquiring into the validity of the tax certificates issued by the Cook Islands Government.

He had also erred in his approach to ss99 and 301 of the Income Tax Act 1976 (concerning tax avoidance and the obligation on taxpayers to disclose all information about the amount of tax credits). It was not enough to look at one aspect in isolation: the subsequent reimburse-

ment of the tax charged should have been disclosed as well.

His fourth error lay in concluding that there was no evidence of fraud or tax evasion. The court emphasised that a finding of evidence was not tantamount to a finding that fraud or tax evasion was proved but that the commission was led by error of law to find that the suspicions concerning the tax certificates were unfounded.

Winston Peters MP who first prompted the inquiry said the High Court decision, which invalidated both Davison's harsh criticism of himself and his finding that the Revenue and SFO were not incompetent in their investigations of the Magnum deal, was a "complete vindication". He is calling on the government to reopen the inquiry.

Prime Minister Jenny Shipley said she expected the Inland Revenue and the Solicitor General to look "very carefully" at the ruling and decide whether any further action was needed.

**SOVEREIGN COMMENT**

This ruling will serve as a further blow to the Cook Islands which have recently been the subject of much negative comment regarding asset protection structures set up in the jurisdiction. The US courts, in particular, have been extremely critical of the Cook Islands trust legislation and the asset protection schemes promulgated thereunder.

HONG KONG

**NPC overturns HK ruling**

The Chinese parliament overturned a landmark decision of the Hong Kong Court of Final Appeal that all children of Hong Kong residents were eligible to live in the territory. It also criticised the court for not seeking its opinion first before issuing the judgement.

The US Congress is to seek testimony from experts on the issue after the US consul general in Hong Kong issued a statement of concern.

The ruling was referred in May to the Standing Committee of the National People's Congress in Beijing by the Hong Kong government which claimed that implementation would allow 1.6m Chinese migrants into Hong Kong.

Tung Chee-hwa, Hong Kong's chief executive, said the clarification from the NPC was "a giant step towards resolving a very difficult problem". Under Hong Kong's constitution, the Basic Law, China promised Hong Kong's executive, judiciary and legislature a high degree of autonomy in administering the territory after the 1997 handover.

**SOVEREIGN COMMENT**

The decision by the Chinese Parliament to overturn a decision by the Hong Kong Court of Final Appeal has been highly criticised in Hong Kong and abroad. However, it should be noted that it is not thought that a similar procedure exists in relation to commercial or fiscal decisions made by the Hong Kong courts and therefore this decision should have no effect on the commercial centre of Hong Kong.

MAURITIUS

**Mauritius Finance Act brought into force**

The Finance Act 1999 was brought into force on 29 July. The principal change affecting offshore activities is that non-resident beneficiaries of an offshore trust are to be exempt from tax from the next financial year.

Other changes contained in the Act include:

- the special 50% income tax relief scheme for expatriate employees will be limited to four years;
- the government is to adopt a flexible approach to investment incentives for multinationals investing a minimum of US\$40m in a project of "unique dimension";
- work permits to professionals are to be fast-tracked;
- the 50% special tax relief presently granted to expatriate employees in specific sectors is extended to cover non-resident Mauritians taking employment in these sectors.

The Companies Act 1984 is also to be amended to provide for the concept of golden shares and treasury shares and to provide for publication in the press of the names of compa-

nies which do not submit their annual returns.

Tax treaties have been ratified this year with Belgium and Mozambique. Treaties with Russia and Lesotho have been signed and are awaiting ratification. Treaties with Malawi and Vietnam have been agreed and are awaiting signature. Treaties are currently being negotiated with Canada, Greece, Portugal and Uganda.

**SOVEREIGN COMMENT**

The tax treaties signed by many offshore jurisdictions are coming under increasing pressure but Mauritius seems to have been successful in negotiating new tax treaties which can be accessed by the Mauritius "offshore" resident company. This type of company pays 15% tax but gets a credit, or deemed credit, equal to 90% of the underlying tax paid abroad. In effect this gives a maximum tax rate of 1.5%. This type of company can be extremely useful in any tax planning exercise which involves investment in or out of any country with which Mauritius has signed a tax treaty.

UNITED ARAB EMIRATES

**Abu Dhabi signs agreement on new offshore centre**

The Abu Dhabi Free Zone Authority has signed a 50-year concession agreement with Emirates Global Capital Corporation (EGCC) to develop an offshore financial and commodities market on the island of Saadiyat.

The US\$3.3bn programme will be the first investment opportunity fully open to outside businesses. A domestic and global initial public offering is scheduled to be launched before the end of this month.

The Authority hopes to establish Saadiyat Island as a regional financial and commodities centre bridging time zones between Europe and Asia.

**SOVEREIGN COMMENT**

Sovereign have recently opened an office in Abu Dhabi to service the United Arab Emirates and this announcement will generate further interest in the region as an important centre for tax planning.

## UNITED KINGDOM

## Trust transfer invalid

The Court of Appeal held that a scheme involving the transfer of shares owned by the taxpayer into a Liechtenstein trust fund was invalid under the anti-avoidance provisions of s478 of the Income & Corporations Taxes Act 1970.

In *Inland Revenue Commissioners v Botnar*, the taxpayer, former Nissan UK chairman Octav Botnar, had exchanged shares in Datsun (UK) Ltd for shares in a Guernsey Company, O Botnar Ltd. He then directed that those shares be held in a Liechtenstein trust in favour of classes of beneficiaries from which he and his wife were specifically excluded.

The High Court found that although Botnar did not benefit from the trust, its trustees could have set up a second trust from which he might benefit. It ordered Botnar to pay £68m in respect of assessments to income tax for the years from 1974 and 1989. Botnar died in Switzerland last year. The appeal was continued by his Swiss lawyer.

The Court of Appeal accepted that the powers on which the Crown relied be exercised so as to confer on Botnar a “power to enjoy”. The conclusion of the commissioners that income was dealt with as to be calculated to enure of the benefit of Botnar was therefore reasonable.

## SOVEREIGN COMMENT

As with the Anderson case referred to on this page, this case shows that attempts to transfer assets away which, in fact, leave the settlor or transferor in a position of partial or whole control will be looked at extremely suspiciously and are likely to fail.

## BAHAMAS

## Free-standing Mareva ruling

The Court of Appeal, reversing the decision of the High Court, held that it had no jurisdiction to grant a free-standing Mareva injunction where there is no substantive cause of action against the defendant.

In *Meespierson (Bahamas) Ltd & Others v Grupo Torras SA & Another* (Civil Appeal No 41 of 1998), the appellants were six trust companies incorporated in the Bahamas. The respondents, claimants in a UK action, initially obtained a world-wide Mareva injunction in the London High Court. This was subsequently discharged but by an originating summons the respondents sought a Mareva injunction and disclosure orders against the appellant companies in the Bahamas.

The Court of Appeal, following *Siskina [1979] AC 210*, held that there was no substantive claim in existence by the respondents against the appellants anywhere in the world and no decision could be found where a Mareva injunction had been granted in such circumstances.

## UNITED STATES

## US Court of Appeals attacks Cook Islands asset protection trust

The Ninth Circuit Court of Appeals upheld the ruling of the District Court for the District of Nevada in finding a couple in contempt for refusing to repatriate moneys from a Cook Islands asset protection trust.

In *Federal Trade Commission (FTC) v Affordable Media & Others (No. 98-16378)*, a husband and wife, Denyse and Michael Anderson, were involved in a telemarketing scam that raised at least US\$13m from investors before it collapsed.

The Andersons' US\$6.3m commission had been placed in a Cook Islands trust created in July 1995. They were named as co-trustees of the trust, together with AsiaCiti Trust Ltd, a company licensed to conduct trustee services under Cook Islands law.

In 1998, the FTC filed a complaint in the US District Court for the District of Nevada which issued an ex parte temporary restraining order against the defendants and entered a preliminary injunction requiring the Andersons to repatriate any assets held for their benefit outside the US.

The Andersons instructed AsiaCiti to comply but AsiaCiti notified them that the temporary restraining order was an event of duress under the trust, removed the Andersons as co-trustees and refused to provide accounts or repatriate the assets.

The FTC sought an order of contempt against the Andersons. The Court rejected their assertion that compliance with the repatriation provisions of the trust was impossible and ordered the Andersons taken into custody for contempt. The Andersons appealed.

The Court of Appeals affirmed that the District Court's finding, indicating that it believed that the Andersons remained in control of the trust. It said that their position as protectors allowed them to control the trust by allowing them to appoint new trustees and determine conclusively whether an event of duress was occurring or not.

The Court was particularly mindful of an unsuccessful attempt by the Andersons to resign after the issue of the Temporary Restraining Order. This attempted resignation, the court said, indicated that the Andersons knew that, as the protectors of the trust, they remained in control of the trust and could force the foreign trustee to repatriate the assets.

The Court of Appeals said: “Given the nature of the Andersons' so-called ‘asset protection’ trust, which was designed to frustrate the power of US courts to enforce judgments, there may be little else that a District Court judge can do besides exercise its contempt powers to coerce people like the Andersons into

removing the obstacles they placed in the way of a court.”

In a separate action the High Court of the Cook Islands ruled in favour of AsiaCiti Trust Ltd over its refusal to repatriate trust assets to the US at the request of the settlors, on the grounds that to do so would have breached the terms of the trust instrument.

The Andersons' imprisonment in the US ended with their agreement to remove the existing Cook Islands trustee and to appoint FTC, Inc. – a corporation formed by the FTC – as the new (sole) trustee.

The Andersons' also attempted to cause an amendment of the trust so as to benefit an “excluded person”, and to cause the appointment of FTC, Inc. as successor trust protector.

The Cook Islands trustee applied to the court for directions as to the validity of the documents. It contended that all were done under duress. Such changes, if made under duress, would be contrary to the trustee's mandate of conserving and protecting trust property for the benefit of the beneficiaries.

The court held that the documents purporting to remove the Cook Islands trustee, as well as appoint a new trustee and a new protector, were invalid, on the grounds that the FTC was an “excluded person” in terms of the trust deed. As such, it could not benefit from the trust fund.

Resignations by the settlors as protectors, were, in contrast to the view taken by the Ninth Circuit Court of Appeals, accepted by the court as valid.

## SOVEREIGN COMMENT

The decision by the US court shows that the onshore jurisdictions will do everything in their power to frustrate aggressive asset protection schemes entered into by citizens within their control. What this case does not determine, despite some industry comment to the contrary, is that trusts are not a legitimate asset protection planning tool if used in a responsible and proper manner.

In this case it was clear that the assets transferred into trust remained under the effective control of the Andersons at least until problems arose.

Trusts are unlikely to protect assets unless the settlors are prepared to give up control to the trustees and they are set up well in advance of any liabilities arising and in advance of facts and circumstances occurring which may give rise to liabilities.

A proper trust structure is generally effective in protecting assets as long as it is set up at a time when the settlor has no liabilities or contingent liabilities and the trust is properly administered by the trustees.

## EUROPEAN UNION

**Deadlock in EU savings tax and predatory corporate tax issues**

Finnish finance minister Sauli Niinistö proposed that EU finance ministers should agree a deal on EU-wide savings taxes and predatory corporate tax regimes in time for the EU summit in Helsinki in December.

The savings tax issue is currently being delayed by a dispute with the UK government over exemptions for foreign-currency eurobonds and with Luxembourg over a tax break for investment funds to prevent capital fleeing to non-EU centres.

The UK government, which threatened to veto the proposed tax unless a way was found of exempting institutional investors in international bonds, had promised to deliver compromise proposals to the European Commission by the end of June but the drafting has been held up by disagreements over the formula to be used.

The Finnish presidency cancelled a high-level meeting of EU treasury officials in July when the UK government again failed to produce a compromise proposal and convened an unprecedented four meetings of EU tax experts in September in an effort to make serious progress before the Helsinki summit.

Luxembourg has also insisted that investment funds, which would fall under the scope of the proposed savings tax if more than 50% of their assets were held in fixed-income investments, should be exempted.

But the European parliament has voted against the proposal.

Finland has called on EU governments to consider the scope for exempting mutual investment funds and Niinistö told Ecofin ministers that both issues should be resolved at the informal meeting of EU finance ministers in Turku on 10 September.

The tax package to be agreed in Helsinki comprises the proposed 20% withholding tax, a voluntary code of conduct to stop member states “poaching” investors through special business tax incentives, and a law making it easier to transfer interest and royalties across borders without incurring double taxation.

**SOVEREIGN COMMENT**

The EU proposals on withholding tax are set to be introduced into all EU states and “all territories under their control”. It is thought, therefore, that the withholding tax would have to be introduced into all the British dependant territories – which includes most of the Caribbean offshore centres – and also the islands closer to home including Gibraltar, Isle of Man, Jersey and Guernsey.

If these measures are introduced it is thought that they would precipitate a flood of capital and bank deposits to centres outside EU control such as the Bahamas, Mauritius etc. The delay in the introduction of such a measure is good news for the affected centres.

## HONG KONG

**HK appeal court applies *Ramsay* principle**

The Hong Kong Court of Appeal, by a majority of two to one, reversed the decision of the High Court in the *Shiu Wing* case holding that the *Ramsay* principle applied to the facts of the case.

In *Shiu Wing Ltd & Others v Commissioner of Estate Duty*, the plaintiffs – three Isle of Man companies – applied for a declaration that no estate duty was payable in respect of certain transactions designed to transfer ownership of shares in Hong Kong companies and land situated in Hong Kong to discretionary trusts outside Hong Kong.

The plaintiffs sought a declaration that no estate duty was payable because the gifts were all gifts of property situated outside Hong Kong. The Commissioner of Estate Duty, relying on the principle contained in *Ramsay v IRC* argued that the underlying reality of the transactions was that they were gifts of the property purportedly sold, and that this property was situated in Hong Kong.

In granting the declaration, the High Court held that although the *Ramsay* principle applies even where the relevant legislation contains its own anti-avoidance provisions, it was not possible to apply it to reconstruct the transactions as gifts of property situated in Hong Kong. The loans were not therefore shams. The Commissioner appealed.

Reversing the decision, the Court of Appeal held that where there is a single composite transaction into which steps are inserted that had no business purpose apart from tax avoidance, the inserted steps may be disregarded for tax purposes, and the charging provisions applied to “the end result”.

**SOVEREIGN COMMENT**

If upheld by the Court of Final Appeal, the decision will have significant implications for the artificial forms of estate planning that have become widely used in recent years in Hong Kong. Many schemes might then be open to attack.

## EUROPEAN UNION

**EC to extend money laundering rules**

The European Commission adopted a proposal to extend the scope of EU laws to combat money laundering to cover lawyers, real estate agents and casinos. It is aimed at discouraging criminals from shifting money laundering activities from banking and financial services to other sectors, particularly in the run up to the single currency in 2002.

The proposal would extend the scope of the 1991 directive under which financial institutions must ask all customers to provide identification at the start of a business relationship or when a single transaction or a series of related transactions exceed Euro15,000.

Existing EU rules only oblige member states to combat the proceeds of drug trafficking although nearly all member states have introduced national legislation to cover the proceeds of all crimes.

## UNITED STATES

**IRS to target US expats**

The IRS is to step up efforts to crack down on tax evasion by US expatriates who fail to file their obligatory US income tax returns. It plans to run cross-checks with tax returns when expatriates apply for new US passports.

The IRS believes it is losing several billions of dollars a year from the three million US expatriates worldwide who have failed to file tax returns. It says it will particularly target expatriates in the UK, Canada, Mexico, Germany, Italy, Hong Kong, Australia, Israel and Switzerland where the most tax is owed by US citizens.

A recent study based on information from 1,000 passport renewals found that only 600 replied and only 83 of those 600 had filed a tax return.

The Joint Committee on Taxation released a set of recommendations in late July which would require details of transactions to be disclosed to the IRS within 30 days after the transaction closes and again when the tax return is filed.

The main proposal is to collect a 40% penalty from any corporation that has tax benefits disallowed from a transaction which the government considers to be “a corporate tax shelter”.

**SOVEREIGN COMMENT**

The IRS are probably the most aggressive tax collection body in the world. Sovereign has established a specialist tax planning unit, based at Regent University, in order to give expert advice on all international tax planning matters but particularly those with US connections. We believe that our expertise in international tax planning is unrivalled anywhere in the world.

## A Letter from Hong Kong

Hong Kong has experienced a torrid time since the handover to China, but this has been the result of economics rather than politics. **MICHAEL FOGGO** of Sovereign Trust International in Hong Kong, examines the highs and lows and looks to the future.

There was considerable speculation leading up to the 30 June 1997 handover. Many commentators feared a mass exodus, an end to the rule of law and to the region's political and economic stability. However, the change of sovereignty had rather less impact than the Asian economic crisis from which Hong Kong now seems to be recovering.

### STOCK MARKET

The Hang Seng index reached its record high (16,673) just after the change of sovereignty. The Asian financial crisis then hit and the market fell to below 7,000. A HK\$30 billion package of special relief measures announced in June 1998 helped but Hong Kong is still facing a major challenge: consumer spending declined for the first time since the 1974 oil crisis and overall investment receded in 1998 after achieving double digit growth for four successive years. The end result was a 5.1% real term fall in GDP in 1998.

*“Consumer spending declined for the first time since the 1974 oil crisis and overall investment receded in 1998 after achieving double digit growth for four successive years”*

During the crisis the market was attacked by speculators borrowing in Hong Kong dollars to push up interest rates then selling short. The HK SAR government countered this attack by buying over HK\$100 billion worth of stock: this strategy worked and now a special committee has been established to manage the government's considerable portfolio. Today the Hang Seng index stands at just below the 14,000 mark.

### PROPERTY

Historically it has been claimed that Hong Kong property has been considerably overvalued. Prior to the handover all property, commercial and residential, was at a premium but prices in general more than halved and rental values in the office sector fell 35%.

The reduced property prices have resulted in a “strategic realignment” and prices now appear to be recovering.

### TOURISM

Visitor arrivals in 1998 (9.5 million) were down on 1997 (10.5 million) but the general consensus was that the 1997 figures for tourism were artificially high due to the handover. The 1998 figure for visitor arrivals shows Hong Kong is still seen as a worthwhile tourist destination.

### FINANCE CENTRE

The Organization for Economic Co-operation and Development (OECD) issued a report in which they made 19 wide-ranging recommendations to address the problems of “harmful tax practices”.

Hong Kong, though, has a system which taxes only Hong Kong-source income and, unlike many traditional tax havens, gives no special concessions to non residents. It has a high standard of regulation and transparency (names of directors and shareholders are filed for public inspection at the Companies Registry) and this should mean that Hong Kong won't have to make sweeping changes to its tax system to comply with the OECD's initiatives.

*“Hong Kong does not levy tax according to residence so it is also a jurisdiction from where foreign companies of all descriptions may be administered without tax consequence whilst still enjoying access to one of the world's most efficient banking systems”*

There are considerable advantages to registering foreign companies under Part XI of the companies ordinance. There is no stamp duty on transfer of shares, simplified administration and more lenient tax treatment.

Hong Kong does not levy tax according to residence so it is also a jurisdiction from where foreign companies of all descriptions may be administered without tax consequence whilst still enjoying access to one of the world's most efficient banking systems.

### TRUST SERVICES

In light of the various attacks on the traditional offshore jurisdictions there has been renewed interest in Hong Kong as a situs for trust business. Hong Kong is quite correctly perceived as having excellent infrastructure, first rate banking, accountancy and legal expertise and a large body of trained professionals.

Many of these attributes are, at least in part, absent from many offshore jurisdictions. Previously professionals might have been reluctant to use Hong Kong for long term trust business because of the worries about the change in sovereignty. Now Hong Kong has been seen to be working under Chinese rule as before and as the territory will still be subject to English law for another 48 years, many professionals now believe that it may be the ideal trust jurisdiction.

Hong Kong does have legislation which regulates the affairs of trust companies but various loop-holes in the legislation mean that that it is relatively easy to legitimately avoid submitting to the registration process. All companies incorporated in Hong Kong which wish to use the word “trust” or “trustee” in their name must submit to registration but there is nothing to stop a company undertaking trust business without being registered as long as it refrains from using these words in the name. Changes to the registration procedures, which would include the closure of this loop-hole have been proposed.

### FUTURE INITIATIVES

Looking to the future, external exports to the USA and Europe have grown. The economic growth on the mainland, as Hong Kong's number one market, is forecast to grow at 7%. This alone presents wide-ranging business opportunities for Hong Kong and the government project an overall growth in GDP of around 0.5% for 1999.

In March, Microsoft chairman Bill Gates confirmed his company's intention to participate in Hong Kong's cyberport initiative, a HK\$13 billion high-tech development project aimed at attracting IT and multi-media investment to a 26 hectare site on Hong Kong Island.

*“The project is expected to begin in 2002 and will be completed five years later generating 4,000 construction jobs and more than 12,000 IT-related positions”*

The project is expected to begin in 2002 and will be completed five years later generating 4,000 construction jobs and more than 12,000 IT-related positions. Eight companies have so far signed letters of intent to become tenants at the cyberport, including Hewlett-Packard, IBM Corp., Oracle Corp., Hua Ley, Pacific Convergence Corp. (a joint venture between PCG and Intel Corp.), Softbank, Cybase Inc. and Yahoo Inc.

### CONCLUSION

Hong Kong remains one of the great financial centres of the world and despite – or indeed because of – the Chinese take-over looks set to remain the leading business centre for the Asia region. The attacks on the traditional offshore centres by the OECD, the UN, the EU and the British Government will increase the attractiveness of Hong Kong as a tax planning jurisdiction and may well make it the jurisdiction of choice. We believe that Hong Kong has the brightest of futures.



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