

Don't leave your family in financial dead end when you die

Howard Bilton

Most people prefer not to think about their death, but failing to do so and plan appropriately can be an expensive business. Not for you because you are dead. It is your family that ends up losing out. If you are young, healthy and single stop reading now. If you have a spouse and/or some children, pay attention.

After the abolition of estate duty in Hong Kong, many people mistakenly believed they no longer needed to consider estate duties, or inheritance taxes as they are called in some places. For most wealthy Hong Kong residents that is not true. Most have investments outside Hong Kong and those assets often will be subject to "death taxes" by the country in which they are located irrespective of who owns them.

Obviously, the older you get the more important it is to have your affairs in order but unfortunately people die young so it is never too early to start. Unless you know when you are going to die, start now or as soon as you have assets of a value which will attract tax.

Consider the example of Joe Sixpack, a British national and a long-term Hong Kong resident, who has:

- A nice London pad worth £2 million (HK\$22.4 million)
- A collection of fine wines stored in London worth £150,000

- A holiday home in Spain worth €3 million (HK\$30.1 million)
- A large portfolio of shares in US public companies which have not gone bankrupt (yet!) valued at US\$2.5 million
- A property in Hong Kong valued at HK\$40 million in which he lives with his American wife

The first fact to note is that as Mr Sixpack is a British national, he might well be considered domiciled in the United Kingdom despite his long-term residence in Hong Kong. If he is, his worldwide estate would be subject to Britain's inheritance tax at a rate of 40 per cent (the first £300,000 is exempt).

Ordinarily, transfers between husband and wife are exempt from the British inheritance tax but only if both parties are domiciled in Britain. As Mrs Sixpack is a US national, she will almost certainly not be domiciled

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in Britain, so the tax will bite. It is possible to establish an alternative "domicile of choice" outside Britain and thereby rid yourself of the liability to British inheritance tax on your worldwide estate but it is extremely unwise to assume that liability is not there.

Even if Mr Sixpack was not domiciled in the United Kingdom, his assets in Britain would still be subject to the 40 per cent inheritance tax due to their situs (ie, they are located in that country for legal purposes). So 40 per cent of the value of the property and the fine wine will have to be paid to Britain's taxman irrespective of his domicile. We believe the taxman is wealthy enough as it is but he does seem to be increasingly desperate for money these days. The portfolio of shares in the US would be subject to the American inheritance tax.

The property in Spain would be subject to Spanish inheritance tax and also "forced heirship" laws, which mean Mr Sixpack is forced to leave a third of the property to the spouse, a third divided equally among the children and the remaining third is the estate which you can do with as you please. That may not be as Mr Sixpack wishes and is an additional consideration over and above the tax that would be payable in Spain.

The Hong Kong property would not be subject to estate duty in Hong Kong because there is none. If he is



domiciled in Britain, the whole estate would still be subject to that country's inheritance tax. Also his estate may be double-taxed. Just because you have paid death duties in the country of the situs of the asset does not necessarily mean that Britain will not tax the estate again on the same asset. In this case, that double jeopardy exists in relation to all assets other than the Hong Kong property.

Mrs Sixpack is likely to think rather less fondly of Mr Sixpack if he leaves all these problems for his executors to fix as not only will the tax have to be paid but it will probably take a minimum of two years to com-

plete the probate process in all the countries involved and have the assets released. Only after that can the executors transfer the assets (or dispose of the assets and release the proceeds of the sale) to Mrs Sixpack and the rest of the heirs named in the will.

The good news is that to a certain extent, estate taxes are voluntary. They are a lot easier to plan against than most forms of tax. In simple terms, the correct strategy is to transfer the various assets to a company or companies appropriately selected for the jurisdiction in question and then place the shares of all those different companies into a foundation,

guarantee holding company structure, trust or the like.

By doing this, you convert the different assets into the interest in the holding structure which can be carefully structured to avoid any need for probate and, in many cases, any need to pay inheritance tax. Transferring the assets to such structures would usually represent a sale of each asset, so capital gains tax may be payable in its country of situs (not in Hong Kong because there is no capital gains tax) so I suppose the only good news to come out of the credit crunch is that values are likely to be historically low, so now is a good time to do it.

What is clear is that you either pay the capital gains tax or your estate pays the death tax. One way or the other the taxman gets you, but while you are alive you can take steps to minimise or eliminate both. Why leave it to chance or to your nearest and dearest to sort out when they are most vulnerable and least equipped to deal with these matters?

If Mr Sixpack is indeed still domiciled in Britain, he would still be taxed on the value of his interest in the holding entity so it is not the perfect solution for him but for most other nationalities it may well be no more complicated than the above. If Mr Sixpack is unsure about his domicile, he needs to straighten it out, the sooner the better.

Of course, none of the above really applies to US nationals because they pay full American taxes for as long as they hold a US passport.

That seems unfair, but somebody's got to pay to invade Iraq!

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