

**THE DIRECTORS AND STAFF OF  
THE SOVEREIGN GROUP WOULD  
LIKE TO WISH ALL OUR CLIENTS  
AND FRIENDS A HAPPY AND  
PROSPEROUS NEW YEAR**

We are pleased to report that the only Millennium bug experienced within the organisation was flu, which affected a number of staff.

**ENCYCLOPAEDIA OF COMPANY  
AND TRUST LEGISLATION**

We are also pleased to announce an important new reference work which will be published by Kluwer Law and Tax International – the world's leading tax publisher.

The work will appear in the summer and will be in both print and electronic formats. The general editors will be Howard Bilton and William Byrnes and the work will cover all the important tax planning jurisdictions and provide a complete one stop database of information for the practitioner and business man. It will include the complete company and trust legislation of each jurisdiction together with commentary and relevant case law and planning notes.

**E-COMMERCE: LAW, TAX AND  
BUSINESS PUBLICATION**

Scheduled for publication in March, again by Kluwer, this will be another work produced by Sovereign. It will provide a comprehensive one-stop electronic and paper reference work for the practitioner. There will also be an abbreviated version geared specifically to the needs of the businessman and/or the consumer in the important new fields of e-commerce and e-business.

**EUROMONEY COURSES**

The recent five-day and three-day intensive Euromoney training courses run in conjunction with Sovereign have proved extremely successful and very well received by participants. Further Euromoney advanced international and offshore tax planning courses will be run as follows:

- 13–15 March in London
- 11–13 July in Singapore
- 21–23 August in London
- 4–6 October in Hong Kong

All courses will be delivered by Professors William Byrnes and Howard Bilton and will use a classroom format for a maximum of 15 participants.

**SOVEREIGN TRUST IN URUGUAY**

Around 500 invited guests attended a cocktail reception to mark the opening of Sovereign's new Uruguayan office which will provide representation to clients in the South American region. The office is located in the central business district of Montevideo at Sovereign Trust (Uruguay) Ltd, Andes 1365, Esc. 421, Edificio Torre de la Independencia, Montevideo, Uruguay. Contact details appear on the back page.



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

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GIBRALTAR

## New Ordinances come into operation

Amendments to the Companies, Limited Partnerships and Business Names Registration Ordinances were passed by the House of Assembly, together with a new Registered Trust Ordinance and new Redomiciliation Regulations. All are due to come into operation on 1 January 2000.

But a Bill for a Gibraltar Private Foundation Ordinance 1999 which would have provided for the establishment of private foundations in Gibraltar was vetoed by the UK government.

Based on the Austrian Foundation, the Bill was to provide the legislative basis for the establishment of foundations as vehicles for the holding of private assets endowed on the foundation for the benefit of identified persons or classes of persons.

The Companies (Amendment) Ordinance 1999 upgrades existing legislation to: permit a limited company to re-register as unlimited, or vice versa, and for a limited company to re-register as a limited partnership whilst maintaining continuity; abolish the requirement for a common seal; abolish the limitation on a company limited by guarantee that only a member may participate in profits; provide a new definition of authorised signatory; introduce a requirement for articles to be filed on the incorporation of any limited company.

The Registered Trust Ordinance 1999 provides for the registering of a trust deed where so required and for the keeping of an index of the trust names. The Redomiciliation Regulations

provide for a company to leave Gibraltar permanently and extend the list of jurisdictions permitted for redomiciliation.

The Limited Partnerships Ordinance is amended to require a limited partnership to have a registered office in Gibraltar and, if none of the partners is resident in Gibraltar, to appoint a secretary resident in Gibraltar.

The Business Names Registration (Amendment) Ordinance 1999 makes provision for annual notification and registration of business names first registered on or after 1 January 2000 and for the registration of Web sites established in or from within Gibraltar.

### SOVEREIGN COMMENT

Gibraltar has recently seen a marked increase in activity. Its status as a full member of the European Union makes it the ideal gateway for investment into Europe. The Private Foundations Ordinance has been shelved at the insistence of the British government who perceived it as a way round the 4th EU Directive which required all companies to file accounts at the public registry. This was not the intention of creating the new legislation and Gibraltar is in the process of persuading the British government of this fact. If the new Private Foundation Ordinance does pass into law it will provide a cheaper and more easily understandable version of the Liechtenstein Foundation and is something which has generated much interest. Further developments are awaited.

ISLE OF MAN

## New EIF category established

A new category of Experienced Investor Fund (EIF) was created under the Financial Supervision (Experienced Investor Fund) (Exemption) Order for persons sufficiently experienced to understand the risks associated with an investment in the fund.

No regulatory approvals are required to launch or add funds which can be incorporated or established in any jurisdiction, provided they are administered from the Isle of Man and make proper custodial arrangements.

An EIF can be established as an open-ended investment company, unit trust or limited partnership. No regulatory/licence fees are payable, no restrictions are imposed on promotion subject to the fund admitting only "experienced investors" and no prospectus is required. An EIF is exempt from tax in the Isle of Man and EIF managers in the Isle of Man are liable to only 5% tax on profits.

There is no limit to the number of investors in a EIF, no net worth tests or requirement for a

declaration of wealth. The minimum investment requirement per investor is US\$15,000.

A Limited Liability Companies & Financial Services (Amendment) Act has been brought into force to extend the range of commercial opportunities available for LLCs by removing the 30-year duration requirement.

The US no longer requires that domestic and foreign LLCs carry the certainty of limited duration to qualify for assessment to tax as a partnership. It has introduced a simplified system by which entities elect to be treated as a corporation or a partnership.

The amendment is intended to create new commercial opportunities for the use of LLCs, particularly as corporate capital vehicles for foreign investment into the Lloyds insurance market. Foreign "names" will be able to invest via corporate vehicle offering partnership-style management participation with limited liability and neutral tax treatment. It may also be an attractive vehicle for local professional incorporations.

JERSEY

## Edwards Review endorsed

The Task Force set up to assess the findings of the Edwards Review of Financial Regulation in the Crown Dependencies has endorsed the majority of its recommendations in a response published one year on.

Jersey has implemented, or has accepted with implementation in progress, Edwards's recommendations in all areas except: the control of trusts; public filing of audited accounts by private companies; disclosure of the beneficial ownership of foreign-incorporated companies.

The Task Force said it would welcome further regular independent evaluations of Jersey's regulatory standards in accordance with an agreed timetable. In the absence of a current international standard, it recommended that a review should be conducted every five years.

CYPRUS

## Belgian tax treaty ratified

A tax treaty was ratified with Belgium and came into force in December.

The withholding rates for dividends are 10% if the beneficial owner is a company which holds directly or indirectly at least 25% of the capital of the company paying the dividends, or 15% in all other cases. For interest it is 10%, but interest on deposits (not represented by bearer instruments) with a banking enterprise are exempted. There is no withholding tax on royalties. The treaty renegotiated by Cyprus with Russia came into force on 1 January 2000 (see *Sov Rep issue 1 page 6*).

### SOVEREIGN COMMENT

The previous Russia/Cyprus tax treaty provided for zero withholding tax on dividends, royalties and interest issuing out of Russia. It was thought that the renegotiated treaty would remove many of these benefits but that didn't happen so Cyprus remains THE jurisdiction of choice for investment in and out of Russia. Concerns remain that Cyprus may be the haven for the proceeds of organised Russian crime but this does not detract from its attractiveness as a gateway for legitimate business.

MALTA

## Range of PIFs expanded

The Malta Financial Services Centre is planning to expand its range of collective investment schemes under the Investment Services Act with the introduction of a new class of non-retail Professional Investor Funds (PIFs). Implementation was expected before 1 January 2000.

CAYMAN ISLANDS

Shipping Law enacted

A Merchant Shipping Law was brought into force. Based on the UK Merchant Shipping Act 1995, and other related UK legislation, it updates and streamlines existing Cayman Islands legislation and introduces new provisions.

Qualifications for owning a Cayman Islands vessel have been expanded to enable persons “both natural and corporate” from a wider global range to have access to the registry.

The Law also provides statutory protection for first mortgages where the mortgage contract contains a clause in the covenant prohibiting, without the consent of the first mortgagee, the creation of subsequent mortgages, the transfer of ownership or registration, or the voluntary deletion of the vessel from the register.

UNITED STATES

US indicts ex-BoNY staff

US authorities made the first arrest in connection with the alleged illegal transfer of US\$7bn of suspect Russian funds through accounts at Bank of New York. A former bank employee Svetlana Kudryavtsev was charged in the Manhattan Federal Court in November with lying to investigators.

The authorities are also expected to launch extradition proceedings against London-based former BoNY vice-president Lucy Edwards and her husband Peter Berlin. Both were charged in October with three counts relating to wiring money without the proper licences.

A third former employee, Russian Aleksey Volkov, was also indicted by the US authorities.

BRITISH VIRGIN ISLANDS

BVI targets financial crime

An Anti-Money Laundering Code of Practice and a Proceeds Of Criminal Conduct (Designated Countries & Territories) Order were approved in September.

The Anti-Money Laundering Code of Practice sets out guidance for all licensed service activities and establishes procedures for identification and verification of clients, record keeping and maintaining a register of money laundering enquiries.

The Proceeds Of Criminal Conduct (Designated Countries & Territories) Order provides that the Proceeds of Criminal Conduct Act 1997 applies to a court order made in a designated country or territory for the purpose of recovering payments or other rewards received in connection with money laundering.

UK OVERSEAS TERRITORIES

UK Govt to appoint independent analysts

The UK announced that it is to appoint independent analysts to carry out an in-depth review of financial regulation in its Caribbean Overseas Territories and Bermuda early next year.

The review was commissioned jointly with the governments of Bermuda, Cayman Islands, British Virgin Islands, Anguilla, Turks & Caicos Islands and Montserrat following the publication in March of a UK government White Paper entitled “Partnership for Progress & Prosperity”.

It will examine practices and legislation covering the banking, insurance and securities sectors, companies and trusts, independent regulatory authorities, international co-operation and anti-money laundering. It will also be responsible for determining whether further action is needed by any territory in order to meet these standards and prioritising recommendations.

Several of the territories’ governments expressed concern about the impact of new regulations proposed by the UK government and the pressure being exerted by the OECD for a review of the taxation regimes of jurisdictions which, according to the OECD, offer an unfair advantage and might be susceptible to international financial crime. The Overseas Territories contend that their financial services are well

regulated and that supervision is adequate. They believe that the attack by the OECD may cause economic damage and hope that the UK review will support their case.

The White Paper also announced the formation of an Overseas Territories Consultative Council, comprising UK Ministers with responsibility for Overseas Territories and the chief ministers or legislative council members from the Overseas Territories, which met for the first time in London in October.

Items discussed included the initiatives by international bodies such as the EU, the OECD and the G7/8 against offshore finance centres.

The UK government said: “All parties agreed that they understood each other’s aspirations and responsibilities better and the importance of the UK government’s commitments for the Overseas Territories arising from its international obligations.

“There was a useful review of progress in implementing the government’s offer of citizenship – although parliamentary time is yet to be made available for the necessary legislation.”

It was intended that the appointment of a company to undertake the review would be made by the end of 1999 and is to be completed by the middle of this year.

BAHAMAS

BISX private placement raises US\$5m

The Bahamas International Securities Exchange was incorporated on 23 September and a private placement to raise US\$5m of equity capital was fully subscribed. Regulations, including requirements for listing and licensing, are being finalised and were due to be approved and issued before the end of last year.

BISX, which will be privately-owned and operated, was offering 40 single shares at US\$125,000 each. The Securities Commission is currently vetting applications and is expected to approve the new shareholders this month. The capital is to be used to develop the domestic seg-

ment of the exchange which is expected to be operational early in the new year. A further ten shares have been set aside for a future offering to raise capital for developing the international segment which is due to be operational by the summer.

A consortium of PricewaterhouseCoopers (Bahamas) and UK-based BTA Consulting has been awarded the contract for setting up and developing BISX. BTA’s managing director Brian Taylor has been appointed as the first chief executive of the BISX and associate director Gouram Bose as its first chief operating officer.

TURKS & CAICOS ISLANDS

Proceeds of Crime Ordinance commences

The Proceeds of Crime Ordinance, Company Managers Licensing Ordinance and Mutual Funds Ordinance were all due to commence on 1 January 2000. Regulations and guidelines to accompany the Proceeds of Crime Ordinance have now been published.

The Regulations contain mandatory requirements for compliance with “know your customer” rules, record-keeping and staff training. The

guidelines are non-statutory advice as to matters which might give rise to suspicions.

The Financial Services Commission has issued a warning notice against Mercantile Capital Group, Datacorp Capital Securities and Pentagon Securities which claim to be securities brokers/investment advisers with offices in the island of Providenciales but which do not have any offices or staff in TCI.

MAURITIUS

White Paper proposes new Companies Act

The government has put out a White Paper on proposals for a new Companies Act to replace and update the Companies Act of 1984.

The proposed legislation is based on the New Zealand Companies Act 1993 but drawing on the BVI and Bermudan legislation which was used as a model for the provision of exempt offshore companies in the Mauritius International Companies Act 1994.

The Companies Act will provide the core company law provisions for domestic companies and will also introduce a number of new features including:

- one-step incorporation;
- one-shareholder companies;
- provision for no par value shares;
- new procedures for name reservation;
- removal of need to state objects;
- removal of the ultra vires principle;
- replacement of memorandum and articles by a constitution;
- purchase by companies of their own shares.

Separate statutes – a Securities Act and an Insolvency Act – will provide for additional regulation and proposals will be made to include provisions of the Mauritius Offshore Business Activities Act 1992 relating to companies described as “offshore companies” and to redesignate them as “external companies”.

Certain features of offshore companies such as the continuation in Mauritius of companies

which are incorporated elsewhere and the incorporation of limited life companies will be made available to domestic companies.

Also due to be tabled are amendments to the Non-Citizens (Property Restriction) Act and the Mauritius Citizenship Act in order to grant “Permanent Residents Status” to investors investing US\$500,000 in Mauritius in priority sectors including the Freeport, the Financial Services sector, operational headquarters, IT, film making and tourism.

Xavier-Luc Duval, a former partner of accountant Coopers & Lybrand, was appointed as the first Minister of Industry, Commerce, Corporate Affairs & Financial Services which, it is hoped, will serve to drive the offshore sector forward.

SOVEREIGN COMMENT

Mauritius has proved extremely successful in acting as a gateway for investment into India due to the extremely beneficial provisions of the Mauritius/India double tax treaty. Most funds which invest in India are based in Mauritius and Mauritius is now one of the world's largest investors into India. More recently Mauritius has signed a tax treaty with China and also has in place a treaty for the mutual protection of investments. The Mauritius government are very active in promoting the financial centre and the new measures are designed to enhance its attractiveness.

HONG KONG

Yam proposes financial recovery plan

Joseph Yam, chief executive of the Hong Kong Monetary Authority (HKMA), called for the building of a stronger financial system as Hong Kong and the region recover from the recent financial crisis.

The areas to be considered for the building of a stronger financial system were:

- prudent management of the international financial architecture;
- international reform in financial disclosure and regulation;
- regional monetary co-operation.

He said that Hong Kong was now recovering from a painful, 18-month recession and that the financial policies pursued by the government had helped Hong Kong pass through the period of crisis with minimal damage to its monetary and financial systems.

He also said that currency stability, under the linked exchanged rate system, was forcing the structural adjustments necessary to maintain and improve Hong Kong's competitiveness.

The HKMA's second overseas representative office opened in London last October. The

first such office was opened in New York in October 1996.

The London office will monitor European economic trends and foreign exchange and fixed income markets in the European time zone and will also provide the Convertibility Undertaking to overseas offices of licensed banks in Hong Kong that have opened clearing accounts with the HKMA.

Joseph Yam said the three HKMA offices in Hong Kong, London and New York would provide 24-hour coverage of the Convertibility Undertaking, demonstrating Hong Kong's commitment to the monetary rule of the linked exchange rate system.

SOVEREIGN COMMENT

As detailed in Michael Foggo's article which appeared in Sovereign Report No. 2, the Hong Kong economy is now surging ahead after suffering under the Asian economic crisis. At the time of writing the Hang Seng Index was approaching its all time high and most commentators predict further growth next year and beyond.

MALAYSIA (LABUAN)

IOFC to get “virtual” boost

A series of measures were announced to boost the Labuan International Offshore Finance Centre (IOFC) including provision for limited access for offshore banks to the ringgit loan market.

The Labuan Offshore Financial Services Authority (LOFSA) is to invest in a gateway on the Web to which companies operating in the IOFC will be linked so that customers have interactive access to financial products and services.

A virtual global exchange – to be known as the Labuan International Financial Exchange – is expected to be launched in March 2000. The Exchange will provide listing and trading facilities for a wide range of products, including mutual funds, bonds, derivatives, insurance-linked products and, possibly, intellectual properties.

SOVEREIGN COMMENT

The financial centre of Labuan was created primarily to attract business which it was thought would leave Hong Kong due to concerns over the 1997 change in sovereignty. Initially, Labuan had only limited success but has since attracted banks and other financial institutions wishing to access the Malaysian tax treaty network or who wish to invest in and out of Malaysia itself. Labuan has been little used for private client business.

SEYCHELLES

Treaty signed with China

A tax treaty with the People's Republic of China was signed in Beijing. It is hoped to bring it into operation early this year.

Royalties and interest are taxed at 10%, dividends at 5%. Capital gains are not taxable in the treaty country of which the alienator is resident, unless they derive from the alienation of immovable property. Capital gains are not taxable in the Seychelles.

Under the tax-sparing credit provisions of the treaty, for income which is exempt from tax either in China or Seychelles as a result of tax incentives, the tax credit for tax paid in either state is deemed to include the total amount of tax which would have been paid in either state in the absence of any incentives. No entities are excluded from treaty benefits.

SOVEREIGN COMMENT

The Seychelles is trying to replicate the success of Mauritius but has previously suffered from allegations of being a base for money laundering activity. The reduced levels of withholding tax provided for by the treaty are the same as those in the Mauritius treaty. It remains to be seen whether investors will be as ready to use this jurisdiction as they are to use Mauritius.

## UNITED KINGDOM

**Intent to defraud rulings upheld by Court of Appeal**

In *Regina v Dermot J Dimsey & Brian R Allen*, the Criminal Division of the Court of Appeal upheld a number of rulings obtained by the Inland Revenue against a Jersey accountant and a UK businessman.

Dimsey, an accountant in Jersey, was recruited by an engineer called Chipping to form nominee offshore companies in Jersey to facilitate the supply of aircraft parts to South Africa in breach of sanctions.

Dimsey, Chipping, Chipping's solicitor da Costa and Allen, a business associate, were convicted of cheating the Revenue and jailed. Dimsey was jailed for 18 months and Allen for seven years with an additional fine of £3m. They appealed.

Both submitted that as neither Chipping nor Allen were officers of their respective companies they could not be fixed with any criminal or other liability for failure to comply with the statutory obligation requiring a company which is liable to corporation tax to give notice to the Revenue that it is so chargeable.

In dismissing these appeals, the Court of Appeal held that failure to disclose was not an omission but a deliberate act intended to defraud the Revenue.

Dimsey submitted that the trial judge had misdirected the jury on the test for determining whether some of Chipping's companies were UK resident. The Court held that no difficult questions of central management and control arose because Chipping was not a consultant but undertook the day to day running of the business while Dimsey carried out the functions of administration in Jersey.

Allen submitted that as a shadow director he was not liable to tax in respect of benefits in kind and the provision of living accommodation. The Court held that the benefits were received in the UK and that Allen fell within the extended definition of director as someone in accordance with whose instructions the company was accustomed to act. He was therefore taxable.

**SOVEREIGN COMMENT**

This case again demonstrates that it is inadvisable to use "nominee" directors. Directors should and must be in control of the affairs of the company for which they act otherwise taxation problems will arise and, as can be seen from the above, there is also a danger that a tax problem gets turned into a criminal action. Criminal action will only normally result if the taxpayer rejects the chance to make a full and frank disclosure but clearly if such disclosure is going to be made and tax is still to be avoided the company must be properly set up and administered and must not be a sham arrangement.

## UNITED STATES

**Failure to turn over US\$7m trust assets lands former Wall Street whiz in jail**

Former Wall Street trader Stephan Jay Lawrence, was jailed for contempt by a federal bankruptcy court in Florida for failing to turn over US\$7m in an offshore trust.

Lawrence amassed an estimated personal fortune of US\$30m in the 1980s but his financial empire collapsed on "Black Monday" 1987 when he lost US\$50m in his trading account at Bear Stearns & Co.

In 1991 he set up a Mauritius trust for himself and his family a few months before a securities industry arbitrator ordered him to pay US\$20.4m to Bear Stearns. He retained certain powers over the trust, including the power to remove and replace trustees

When Bear Stearns pursued his assets in the federal district court in Miami, Lawrence filed for Chapter 7 bankruptcy. He listed more than US\$20m in debt and one tangible asset – a US\$400,000 property protected under Florida's homestead exemption.

He also listed the US\$7m trust in Mauritius but claimed he was dropped as a beneficiary in 1995 and was never a trustee.

In 1998 bankruptcy judge Thomas Utschig held that Lawrence had set up the offshore trust to protect himself from the judgment won by Bear Stearns in March 1991. In effect, it was a sham, prohibited under Florida law.

He was ordered to turn over the trust's assets and an accounting of its investments, but claimed he had lost a controlling interest in the trust when removed as a beneficiary in 1995 and was unable to comply.

Chief Bankruptcy Judge A Jay Cristol called his attempts to turn over the trust lame and jailed him for contempt of a civil court order. He said Lawrence would not be released from the Federal Detention Centre in Miami until he turned over the trust.

The court held that any type of impossibility defence to a contempt proceeding was invalid if the defendant was responsible for creating the impossibility. It also examined the factual issue of impossibility, and said that it did not believe that the debtor would part with a substantial part of his assets without retaining de facto control over them.

**SOVEREIGN COMMENT**

In the last issue of the Sovereign Report we gave details of the Anderson case. This is yet another incidence of US courts taking every opportunity to unwind "asset protection trusts". As suggested in the last issue this does not mean that trusts are not a useful way of protecting assets but it again emphasises the fact that the trust must not be a sham and that it must be set up at a time when the settlor has no outstanding liabilities which cannot be settled out of assets retained under his control and at a time when he does not know of any facts and circumstances which might lead to such a situation arising. If planning is undertaken early and has purposes other than only asset protection then a trust should still prove to be a most effective tax and asset protection planning tool.

There has been a proliferation of asset protection structures set up mainly for US persons at times when that type of planning is completely inappropriate. Many offshore jurisdictions initiated aggressive legislation designed to give protection to assets over and above that which would be afforded by a normal trust structure. In our opinion trusts are best set up in jurisdictions which do not have aggressive designer asset protection legislation as using such legislation does indicate a primary motive of asset protection and will, in most cases, be fatal to that plan.

## BERMUDA

**Swiss industrialist challenges validity of US\$2.7bn Bermuda-based trust**

Swiss industrialist Baron Hans Heinrich Thyssen-Bornemisza began legal proceedings in the Supreme Court to regain control of the family business worth US\$2.7bn from his son Georg.

The baron created a Bermuda-based trust in 1983 to keep the business together and avoid any disputes between the family about inheritance. The trust's beneficiaries are Georg, his eldest son and chief executive officer of the Thyssen-Bornemisza Group (TBG), and the baron's four other children by another four wives.

TBG – the main asset – earned US\$100m last year. The baron is attempting to dissolve the trust, claiming that since 1995 his son has not paid him the US\$20m a year that was agreed. The trial is expected to last up to a year.

**SOVEREIGN COMMENT**

It is quite unusual to find a settlor challenging the validity of a trust set up upon his instigation. Normally such challenges arise from aggrieved heirs, commercial creditors and spouses.

## FRANCE

## OECD moves against "harmful tax havens"

The OECD Forum on Harmful Tax Practices has completed its initial technical evaluation of the 47 jurisdictions identified in last year's *Report on Harmful Tax Competition* for review as potential tax havens.

The report set up the Forum to produce a list of tax havens in support of the drive by OECD governments to combat harmful tax practices and eliminate the adverse consequences which, it claims, those jurisdictions have on the world economy.

Its preliminary findings will be presented to the OECD's Committee on Fiscal Affairs, the senior tax policy body, at a meeting in January. Any list of tax havens is to be submitted to the OECD Council in June.

The identified jurisdictions will be encouraged to eliminate the harmful features of their regimes as part of an ongoing co-operative dialogue with OECD Forum. The OECD said that in situations where such discussions are unsuccessful, co-ordinated counter measures by OECD member countries are foreseen.

In October, the government of the Bahamas told OECD officials in Paris that the report lacked balance and discriminated against countries whose tax regimes the OECD had unilaterally declared to be harmful.

In a statement to the OECD it said that it found the application of the term "harmful tax havens" deeply offensive. The Bahamas had never had a tax on income and capital and did not hold the view that such taxes are inherently a natural component of an appropriate tax regime.

## SOVEREIGN COMMENT

The OECD report has faced much criticism. Both Switzerland and Luxembourg abstained and have already indicated that they will not support the report and will not be bound by its conclusions. The OECD's own Business and Industry Advisory Committee (BIAC) has also produced a scathing analysis of the report. Most of the criticism points to the fact that the OECD claim within their report that tax incentives are the primary or sole motivation for the location of business. Most commentators suggest that this is untrue and that many other factors contribute to the choice of location. The Bahamas, in particular, would argue that businesses locate there because of the local skill base and relative commercial freedom. Branches of US and other onshore-based corporations cannot gain tax advantage because offshore profits would almost certainly be taxed back onshore because the offshore subsidiary would be classified as a CFC. Despite the torrent of criticism the OECD is pressing ahead with its proposals. As can be seen above, a blacklist of tax havens will be published in June but in most cases a two year period of grace will be given before action is taken against a tax haven as long as it commits to introducing reforms in line with OECD recommendations. We imagine that most of the major offshore financial centres will give the necessary undertakings so any disruptive countermeasures will probably not come into effect until June 2003. We continue to monitor the situation closely.

## UNITED KINGDOM

## UK Treasury legislation targets "designer rate" tax regimes

The Inland Revenue brought in legislation to counter the use of "designer rate" tax regimes in Guernsey, Jersey, the Isle of Man, Gibraltar and Ireland which allow companies to bypass the UK's anti-avoidance legislation for Controlled Foreign Companies (CFCs).

The legislation is intended to prevent UK companies avoiding UK tax by diverting income to subsidiaries (CFCs) in tax havens and preferential regimes. It had immediate effect but will be formally introduced in this year's Finance Bill.

Existing CFC rules regarded a company as being in a tax haven or preferential regime if it is subject to a level of taxation less than 75% of what it would have paid had it been resident in the UK.

The new rules will set aside the 75% tax threshold to trigger CFC rules and instead require UK companies to pay an amount of CFC tax equal to any tax that would otherwise be avoided.

The regimes to which the legislation applies will be named in regulations and the legislation will allow further regimes to be named in future if necessary.

From 6 October, the legislation will apply to:

- Gibraltar – Income Tax Qualifying Companies.
- Guernsey – Bodies with International Tax Status.
- Ireland – Companies taxed in accordance with s448(7) of the Irish Taxes Consolidation Act 1997.
- Isle of Man – International Companies.
- Jersey – International Business Companies.

The UK said it would use all mechanisms at its disposal to press the Dependent Territories of Jersey, Guernsey, the Isle of Man and Gibraltar to change their tax treatment of companies in the way that they have already responded to requests to act against money-laundering.

## SOVEREIGN COMMENT

It is interesting to note that neither Malta nor Madeira appear on the list of regimes to which the regulations apply. In Malta the headline rate of tax is 35% but a system of credits and refunds mean that the effective rate is between 0% and 6%. In Madeira the SGPS company has a headline rate of tax of 36% but only 5% of income is taxable thereby giving an actual rate of 1.8%. It may be that both these jurisdictions can be utilised to avoid CFC classification by the UK.

## EUROPEAN UNION

## EU heads delay decision on withholding tax

Government heads at the Helsinki Summit on 10 December agreed to delay any decision on the proposed EU-wide withholding tax on non-resident savings for another six months pending further study by a high-level working group.

The move averted the complete collapse of a tax package, which includes measures to eliminate unfair business taxation and a directive on cross-border royalty and interest payments between associated companies, over the UK's insistence on securing an exemption for international bonds.

Failure to exempt bonds, the UK argues, would drive London's US\$3bn international bond market to non-EU financial centres.

The new working group will be examining the recent paper by Finland and the European Commission setting out plans to minimise the administrative burden on the international bond market as well as UK proposals for sharing information on suspected tax evaders with other member states' authorities.

The report of the Code of Conduct Group chaired by UK Paymaster General Dawn Primarolo, which examined more than 200 tax regimes in various EU countries, was presented to the Summit.

The Group found against 66 tax breaks operated by member states and their associated territories including Belgium, Denmark, Greece, Ireland, Luxembourg, the Netherlands, Portugal, Spain, Gibraltar, Aruba, BVI, Guernsey, Isle of Man, Jersey and the Netherlands Antilles.

## SOVEREIGN COMMENT

It is now thought unlikely that the UK will rejoin the European Monetary Union or adopt the single European Currency Unit within the foreseeable future. This may leave the UK better placed to continue to reject proposals for an EU savings tax and press for further exchange of information as an alternative way of assisting with tax collection. The present UK stance makes it very difficult for any of the recommendations of the Group to progress.

## Offshore Finance Centres – Prospects for 2000 and beyond

The phenomenal success of the offshore finance industry and the consequent proliferation of products and services have brought it under ever increasing international scrutiny. Sovereign Group chairman **HOWARD BILTON** examines the threat to OFCs and the industry's future.

The 1990s saw a phenomenal rise in the use of offshore structures. The BVI led the way with the number of incorporations peaking at about 50,000 per year. Other jurisdictions would claim that they won the battle for quality over quantity. The phenomenal success of the offshore jurisdictions has caused the competition – the onshore jurisdictions – to react and various developments over this and the coming years will affect all of us.

### ASSET PROTECTION

Asset protection trusts and schemes based on such structures were heavily promoted in the US and elsewhere.

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*Asset protection and planning is still alive and well but only if used responsibly and any trust should have some commercial purpose other than asset protection*

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Typically such schemes involved the transfer of assets into trust by a settlor who retained almost total control over those assets until he came under attack when he suddenly released all control to an offshore trustee. Often the schemes were set up after the settlor had entered into a risky business or was already aware of facts and circumstances which might lead to substantial debts which he would be unable to pay without the transferred assets.

The US and UK courts (page 5), in particular, have made it clear that they will do everything within their powers to ensure that both settlors and their advisors are heavily penalised for making or assisting in these fraudulent transfers and that such schemes cannot be used to avoid legitimate creditors.

Asset protection and planning is still alive and well but only if used responsibly and any trust should have some commercial purpose other than asset protection. Setting up trusts in jurisdictions which are well known for their designer asset protection legislation is a red flag to the onshore courts and, in our view, such jurisdictions should be avoided. It is also absolutely vital that the trust is properly and independently managed by the trustees and cannot be considered as a sham arrangement.

### TAX AVOIDANCE

Many countries are becoming increasingly aggressive in initiating anti-avoidance legislation which attempts to reduce or eliminate the benefits of international or offshore tax planning. Further legislation will undoubtedly

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*It may not be prudent to invite attention from the Revenue by revealing details of your tax planning arrangements but good planning should be able to withstand the scrutiny and should not rely solely on confidentiality*

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continue to be passed but loopholes will remain and tax mitigation will still be possible although more difficult. In particular, the confidentiality afforded by the offshore jurisdictions will be eroded and tax plans which rely on obscuring the facts will be unlikely to work in the future. It may not be prudent to invite attention from the Revenue by revealing details of your tax planning arrangements but good planning should be able to withstand the scrutiny and should not rely solely on confidentiality.

### OECD

The OECD's *Report on Harmful Tax Competition* remains at the forefront of the offshore news (page 6). The report has been heavily criticised by the OECD's own Business and Investment Advisory Committee (BIAC), by many of the offshore jurisdictions under attack and, indeed, by some of the OECD members, notably Switzerland and Luxembourg.

Despite this, some of the report's recommendations are bound to be implemented over the coming years. In June of this year a list of jurisdictions that the OECD categorise as tax havens will be published and the OECD will impose sanctions against those jurisdictions unless they commit to implementing the OECD's recommendations over the following two years. It is thought that most of the major reputable offshore financial centres will ensure that they avoid immediate sanctions but greater transparency, less confidentiality and better regulations will have to come.

### EUROPEAN UNION

The EU continues its attempts to introduce a 20% withholding tax on savings held within any EU member state or any territory under the control of an EU member state (page 6). This would affect most of the major offshore financial centres which have British connection and may lead to a flight of capital from these areas to independent jurisdictions such as Hong Kong and Bahamas. At the moment the EU recommendations cannot be implemented due to the veto by Britain which wants to protect the City of London Eurobond market. There does not seem to be any end in sight to the present stalemate.

### THE UNITED NATIONS

The UN is concerned to eliminate money laundering and will implement sanctions against any jurisdictions not on its white list of well-regulated countries. Many of the major offshore financial centres have already entered into a dialogue with the UN to ensure that they appear on the white list but other jurisdictions will face penalties.

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*Many of the major offshore financial centres (OFCs) are under UK control including the Channel Islands, Gibraltar, Isle of Man, Cayman and BVI*

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### UK OVERSEAS TERRITORIES

Many of the major offshore financial centres (OFCs) are under UK control including the Channel Islands, Gibraltar, Isle of Man, Cayman, BVI (page 6). The UK has made it clear that it wishes to see that highest standards of regulation in these jurisdictions and will conduct a review of them all over the coming year. Service providers will have to be licensed and will have to adhere to strict "all crimes" money laundering principles, with "all crimes" to include tax evasion, and "know your client" principles.

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*What is clear is that greater sophistication will be required in tax planning arrangements and it is unlikely that those who sell companies and trusts as a commodity rather than as a tax planning tool to be used in concert with well informed advice will survive very much longer*

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The OFCs may be a victim of their own success. Powerful countries and organisations have made it clear that they wish to curb the use of OFCs by unscrupulous individuals and criminals. At the moment there are a large number of unregulated service providers who promote aggressive, ill-thought-out planning techniques and those companies and firms will have to obtain licences, curb their activities or go out of business. We welcome these moves. What is clear is that greater sophistication will be required in tax planning arrangements and it is unlikely that those who sell companies and trusts as a commodity rather than as a tax planning tool to be used in concert with well informed advice will survive very much longer.



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Tel: UK +44 01702 474656. Fax: UK +44 01702 480729.

**BAHAMAS**

Tel: +1 242 322 5444  
Fax: +1 242 325 8445  
bh@sovereigngroup.com

**BRITISH VIRGIN ISLANDS**

Tel: +1 284 494 4527  
Fax: +1 284 494 4456  
bvi@sovereigngroup.com

**CYPRUS**

Tel: +357 2 676 519  
Fax: +357 2 679 079  
cy@sovereigngroup.com

**DENMARK**

Tel: +45 44920127  
Fax: +45 43690127  
dk@sovereigngroup.com

**GIBRALTAR**

Tel: +350 76173  
Fax: +350 70158  
gib@sovereigngroup.com

**HONG KONG**

Tel: +852 2542 1177  
Fax: +852 2545 0550  
hk@sovereigngroup.com

**JAPAN**

Tel: +81 3 3201 8008  
Fax: +81 3 3201 2002  
japan@sovereigngroup.com

**NETHERLANDS**

Tel: +31 (0)20 428 1630  
Fax: +31 (0)20 620 8046  
nl@sovereigngroup.com

**PORTUGAL**

Tel: +351 282 342601  
Fax: +351 282 342259  
port@sovereigngroup.com

**SOUTH AFRICA**

Tel: +27 21 418 4237  
Fax: +27 21 418 2196  
sact@sovereigngroup.com

**SPAIN**

Tel: +34 952 764168  
Fax: +34 952 825637  
spain@sovereigngroup.com

**TURKS & CAICOS ISLANDS**

Tel: +1 649 946 5056/7  
Fax: +1 649 946 5052  
tci@sovereigngroup.com

**UNITED ARAB EMIRATES**

Tel: +971 4 3976552  
Fax: +971 4 3978355  
dubai@sovereigngroup.com

**UNITED KINGDOM**

Tel: +44 (0)207 479 7070  
Fax: +44 (0)207 439 4436  
uk@sovereigngroup.com

**USA**

Tel: +1 757 363 9669  
Fax: +1 757 363 9668  
usa@sovereigngroup.com

**URUGUAY**

Tel: +598-2 900 3081  
Fax: +598-2 902 1246  
uy@sovereigngroup.com

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