14

issue fourteen

SOVEREIGN

report

contents

Sovereign Trust (Gibraltar) Limited is licensed by the Financial Services Commission – Licence No: FSC 00143B.

Sovereign Trust (Isle of Man) Ltd is licensed by the Isle of Man Financial Supervision Commission as a Corporate Services Provider.

Sovereign Trust (TCI) Limited is licensed by the Financial Services Commission – Licence No: 029.

Sovereign Group Partners LLP is regulated by the FSA – No. 208261.

UK Budget

For many years we have been expecting a review of the rules on domicile which govern liability to UK inheritance tax. The Inland Revenue has published an extensive background paper that sets out the current UK rules and summarises the similar in 29 other countries. But there is no indication of the form or timing of any legislative changes, so in essence there is no news on this issue (see European page 4).

New measures have been introduced with immediate effect to counter plans aimed at draining capital gains out of non-UK resident trusts. These techniques were generally known as ‘flip flops’. There is also legislation to prevent tax-avoidance schemes involving the use of relevant discounted securities (RDS).

The EU Savings Directive

It has just been announced that the Cayman Islands has successfully obtained a ruling from the European Court of Justice that the EU cannot impose an obligation on it to implement the proposed savings tax Directive. The court also ruled that the UK was not legally required to impose the Directive on the Cayman Islands. This might seem a significant victory but it looks increasingly clear that the UK aims to impose the Directive irrespective of any obligation and, if it lacks the constitutional power, may resort to other tactics (see Fiscal page 8).

The EU continues to release statements suggesting that the US has agreed to adopt legislation equivalent to the EU savings tax Directive. We believe that this is not the case and that the EU legislation is incompatible with US laws in various areas.

In the latest bizarre twist to the tale of this Directive, Italy has announced that it will not agree to implementation unless it gets concessions on milk quotas!

Gibraltar tax reforms

As we go to press Gibraltar appears to have given approval by the EU for its proposed tax reforms which will abolish corporation tax in Gibraltar and, instead, will impose both a property and pay-roll tax equal to 15% of profit on those companies renting offices and employing staff in Gibraltar. At the same time Gibraltar intends to abolish the exempt and qualifying companies and make those companies subject to the normal tax regime in Gibraltar. Most, if not all, exempt and qualifying companies will not be renting offices and employing staff in Gibraltar so will not be liable to any tax. Gibraltar still has to convince the Commission that the new regime does not represent state aid (which was the reason the EU required Gibraltar to abolish the exempt and qualifying companies) but this latest approval marks a significant step forward.

chairman

Portugal - changes in tax in property

The Portuguese Government has announced tax changes affecting property. As of 2004, inheritance tax, gift tax, Sisa (land transfer tax) and Contribuicao Autarquica (Municipal tax or “rates”) are all to be abolished. Sisa and rates will be replaced with a new tax designed to raise an equivalent amount of revenue but the form this will take is not yet clear.

We will circulate further details to clients who own Portuguese property as soon as things become clearer.

Hong Kong and SARS

I am pleased to report that we still have a full complement of staff despite the spread of Severe Acute Respiratory Syndrome (SARS). We recently received a medical bulletin from the Hong Kong government that suggested that the virus was killed by "a solution of 70% alcohol and a diluted solution of bleach". We are endeavouring to adhere to a strict regimen, at least with regard to the first ingredient in this formula. Please bear with us!

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

UK issues consultation paper on non-domicile status

The Treasury and Inland Revenue jointly issued a background paper on the tax treatment of non-domiciled individuals in the UK. Chancellor Gordon Brown underlined his interest in reform by highlighting the discussion paper in his Budget speech on 9 April. It examines the current rules by which individuals who are resident but not domiciled in the UK are only subject to income tax and capital gains tax on non-UK income and gains remitted to the UK. It also looks at the treatment of temporary residents in 29 other countries around the world.

Up to 100,000 people could be affected by any changes to the tax rules. These include 65,000 people who claim non-domicile status and a further 33,000 who are UK residents but get tax concessions because they typically stay in the UK for three years or less.

A review was announced in the last Budget. The paper makes no specific proposals and gives no indication of the government's intention but the Labour party pledged to close the loophole around non-domicile status in 1994. The most likely option would require foreigners to start to pay tax on their overseas income if they remain in the UK for a certain period of time.

The paper reveals that some 16,000 individuals declared foreign earnings totalling £800 million which were not liable to tax because they were not remitted to UK. It also said some wealthy foreigners who claim non-domicile status have been living in the UK for as many as 40 years.

Future decisions about any reform, it said, would be based upon principles that tax rules should be fair, support economic competitiveness, and be transparent and easy to operate. The paper invites comments on whether the current rules:

- establish an appropriate degree of connection with the UK to give an obligation to pay tax on worldwide income;
- ensure that an appropriate contribution to the Exchequer is paid by those with a temporary connection with the UK;
- provide objective criteria for determining when a temporary or long term connection with the UK is severed, suspended or restored;
- support the internationalisation of labour markets and ensure the competitiveness of UK firms.

The Budget also introduced, with immediate effect, measures to counter a capital gains tax avoidance technique by which trust gains could be "drained out" of offshore trusts by transferring property to a new settlement and taking out borrowing equal to the funds transferred. The new rules seek to trace trust gains back to the original trust where payments are made to beneficiaries and, to counter future variants, the Revenue announced that trust gains might only be "drained out" where there have been payments to beneficiaries who are charged to tax.

Measures to counter tax avoidance by using artificial losses on relevant discounted securities (RDS) – securities that may be redeemed at a certain premium – will also be included in the Finance Bill. A number of schemes have been developed to exploit this legislation by producing RDS's that are disposed of at a loss which is matched by a non-taxable gain.

The Finance Act 2002 denied tax relief where an RDS was issued by a connected person. The new measures will prevent relief for losses where the disposal occurs on or after 27 March 2003 and trustees will no longer be able to carry forward losses on the disposal of an RDS.

14 europe

Switzerland amends tax treaty with US

Switzerland and the US have revised the interpretation of the provision for administrative assistance under the Swiss-US tax treaty of 1996 to allow the US more access to client information in cases of suspected tax evasion.

The new agreement provides that the US will be able to request information in tax cases even if the statute of limitations on such cases have been reached under Swiss law and Switzerland must provide administrative assistance in cases which exhibit the same degree of illegality as tax fraud.

The definition of "tax fraud" is extended to mean conduct:

- that is established to defraud individuals or companies, "even though the aim of the behaviour may not be to commit tax fraud;
- that involves the destruction or non-production of records, or the failure to prepare or maintain correct and complete records, that a person is under a legal duty, tax or otherwise, to prepare and keep as sufficient to establish the amount of gross income, deductions, credits, or other matters required to be shown by such person in any tax return, if the person has not properly reported such amounts in any such tax return;
- by a person subject to tax in the US that involves the failure to file a tax return or an affirmative act that has the effect of deceiving the tax authorities.

Sovereign comment. Sovereign specializes in advising US citizens on legitimate and IRS-compliant structures which can and do allow the US citizen or resident to be fully compliant in the US but still avoid being taxed on profits such as those generated on a Swiss bank deposit.

Malta votes to join the EU

Malta voted to join the European Union in a referendum on 8 March. The smallest of the 10 countries that have completed membership negotiations, it was the first to hold a referendum seeking public endorsement for EU membership by May next year.

Fifty-four percent of voters said yes to EU membership on a turn out of 91 percent. But the referendum is non-binding and will have to be validated by a general election.

Prime Minister Eddie Fenech-Adami called an election for 12 April, four days before Malta is scheduled to sign the accession treaty.

Meanwhile the EU will press ahead and admit only the Greek sector of divided Cyprus after the breakdown of United Nations-led talks on reunification at The Hague on 10 March. UN secretary-general Kofi Annan abandoned negotiations after Greek Cypriot and Turkish Cypriot leaders failed to agree on a plan to hold simultaneous referenda in both parts of the island at the end of March, just in time for the signing of the accession treaties by the EU's 10 new members on April 16.

Sovereign comment

It is thought that Malta's advantageous tax system already complies with EU requirements so we are not expecting too many changes as a result of Malta's accession to the EU. As a reminder, Malta has a unique system of taxation of International Trading Companies and International Holding Companies. The headline rate of tax is 35% and high levels of tax are actually paid by these companies but the shareholders are able to reclaim most of that tax leaving a net rate of tax of between 0% and 6%. The fact that tax is actually paid by the company means that, at present, there is no pressure on the advantageous tax treaties negotiated by Malta through which these advantageous types of companies continue to be able to benefit.

Caribbean offshore centres call for re-negotiation of OECD agreements

Antigua, the Cayman Islands, St Vincent & the Grenadines and Panama have complained to the OECD that concessions on banking secrecy granted to three EU countries could negate their OECD agreements. They have called on the OECD to re-negotiate their letters of commitment to exchange information.

On 21 January the EU agreed to exempt Belgium, Luxembourg and Austria from automatic exchange of information under its proposed savings tax directive and allow them to instead impose a withholding tax until 2011 (*see Fiscal page 8*). The concession was granted because the three states had refused to break bank secrecy rules unless Switzerland and other key non-EU jurisdictions also agreed to implement similar measures.

Antigua's chief negotiator Sir Ronald Sander, in a letter to the OECD's secretary-general, Donald Johnston, said: "It is now patently and blatantly obvious that no level playing field exists and that jurisdictions, such as Antigua and Barbuda, that have committed to participate in the OECD's global tax forum are being placed at a severe disadvantage."

He called for a meeting of the OECD's global tax forum, made up of OECD and non-OECD members, so that all jurisdictions can collectively decide whether there is any basis for further commitment to the OECD's initiative to eliminate tax competition.

But the OECD says it is standing by its harmful tax competition initiative and that the protests by the four jurisdictions do not take full account of all aspects of the programme. The commitments made by 31 OFCs deal with the exchange of information only when there is specific request by an overseas investigator rather than the automatic exchange of information proposed by the EU.

OFCs that signed letters of commitment are: Anguilla, Antigua, Aruba, the Bahamas, Bahrain, Belize, Bermuda, the British Virgin Islands, the Cayman Islands, the Cook Islands, Cyprus, Dominica, Gibraltar, Grenada, Guernsey, Isle of Man, Jersey, Montserrat, the Netherlands Antilles, Malta, Mauritius, Niue, Panama, Samoa, St Kitts & Nevis, St Lucia, the Seychelles, St Vincent, San Marino, the Turks & Caicos Islands and the US Virgin Islands. Seven jurisdictions on the OECD's blacklist – Andorra, Liechtenstein, Liberia, Monaco, the Marshall Islands, Nauru and Vanuatu – decided not to make the commitment.

Sovereign comment

There is clearly mounting resistance to the OECD proposals but, in our view, exchange of information upon request is already here. The US has already signed Tax Information Exchange Agreements (ITEAs) with many OFCs and intends to sign with all OFCs before the end of the year. It is perfectly feasible for any country with a tax treaty with the US (nearly everyone) to request the US to obtain information under its ITEA and exchange that information under the tax treaty. As always, it is our very firm view that good tax planning does not, and should not, rely upon confidentiality but should be "revenue compliant". There are still many offshore structures which can be used to mitigate tax but such arrangements will almost always necessitate doing more than setting up a simple offshore company. Saving tax legitimately is never simple, if it was then nobody would pay tax!

Estimated EU directive could cost Cayman US$70 million

A leading UK economist has estimated that the Cayman Islands could suffer a US$70 million loss on account of the proposed EU savings tax directive which would require the reporting of all interest payments on savings held in the Cayman Islands by EU residents.

Professor Sir James Mirrlees of Cambridge University, a Nobel prize winner for economics in 1996, estimates that the additional reporting burden could cost banks up to US$30 million a year, while the demand for financial services could fall by up to US$50 million if the directive is implemented. The overall economic cost would be "unlikely" to exceed US$70 million a year.

"The directive will change the relative attractiveness of investing in the Cayman Islands rather than, say, Hong Kong or Singapore," said Sir James. "That is bound to induce many investors to hold less of their wealth in the Caymans and more in other countries not subject to the directive… The brute fact is that the expected return on investment, net of tax, for many Europeans placing their funds in the Caymans will be less than the expected return in a non-reporting country, also with no withholding tax."

Sovereign comment

Sir James' comments are correct. The proposed EU savings tax Directive affects not only accounts held within the EU but also within territories under their control. This means that most OFCs will be affected including Netherlands Antilles, Gibraltar, Isle of Man, Channel Islands, Cayman, BVI etc. Investors will almost certainly prefer to have their savings held in independent jurisdictions such as the Bahamas and Hong Kong which may be huge beneficiaries of this Directive. Implementing the directive will be expensive and many clients will object to their account information being automatically exchanged with their home tax authority even if there is no suggestion of tax evasion or avoidance. People, quite rightly, believe they have a right to some privacy.

Bahamas launches online company registration service

The Bahamas has launched a Registered Agent Information System, through which registered agents are able to incorporate international business companies and perform a range of other corporate services electronically, in a secure environment.

In addition to the incorporation of IBCs, services available to agents licensed by the Inspectorate of Financial & Corporate Service Providers (FCSP) or under the Banks & Trust Companies Regulations Act (BTRA) will include name reservations, enquiries and reports, file downloads and maintenance, and filing of electronic documents.

Full computerisation of all aspects of the Registrar General's office is expected to be completed within the next two years. The government also tabled four Bills in January to provide for the development of electronic commerce. The new legislation will set the rules for commercial transactions, the protection of intellectual property rights, security, interconnectivity, and the privacy and confidentiality of consumer information.

Sovereign comment. The new government in the Bahamas is making a concerted effort to regain the ground lost through ill-considered legislative changes in recent years. The number of new incorporations during 2002 was 3,458, the lowest for 10 years, compared to a peak of 18,697 in 1997. Loss of confidence in the jurisdiction is certainly to blame. Despite having an office in the Bahamas, Sovereign has advised clients to use a different jurisdiction until certain issues were clarified. We believe that the Bahamas is now, again, an excellent jurisdiction in which to incorporate.

Hong Kong Budget sets out to tackle fiscal deficit

Tax rates were increased across the board in Hong Kong's Budget on 5 March as finance minister Antony Leung Kam-chung attempted to close the widening gap in the government's finances, now estimated at HK$70 billion.

Headline tax increases included a 1% rise in income tax to 16% and a 1.5% rise in company profit tax to 17.5%. These are expected to generate an extra $6.8 billion in revenue per annum. At the same time, measures to curb expenditure, by $20 billion to a target of $200 billion per year, included a 6% cut in civil service pay and reductions in overall welfare spending by 11.1%.

The Budget measures will not substantially reduce the deficit this year, but Leung said they will at least stop it from growing. Hong Kong has registered fiscal deficits in four out of the past five years and operating deficits in the past five years. The Medium Range Forecast anticipates continued fiscal deficits before returning to fiscal balance by 2006-07. The situation is the same for the operating deficits.

Revenue concessions included amending the Inland Revenue Ordinance to exempt offshore funds from profits tax and extending exemption from the fixed stamp duty of $5 to unit trust funds domiciled in Hong Kong.

To enhance the environment for financial services, the government said it will strive to improve the corporate governance standard of listed companies by implementing the Corporate Governance Action Plan. To foster the development of retail bonds and other financial products, it will introduce a Bill to amend the Companies Ordinance by July to simplify the procedures for the registration and issue of prospectuses. It will also make tax proposals to assist the development of the bond market and the fund management industry.

To enhance the insurance industry it is examining turning the office of the Commissioner of Insurance it into an agency independent of the government in line with international regulatory trends.

Sovereign comment

Although the rate of corporation tax has increased in Hong Kong it is still the case that tax is only payable on Hong Kong-source profit. It is still perfectly possible to do business through a Hong Kong company in such a way that it does not produce any Hong Kong-source profit so the effective rate of tax is zero. Hong Kong companies must file full audited accounts with the Hong Kong Inland Revenue Department (IRD) and at that time need to claim that profit revealed in those accounts is not taxable and support that claim with hard evidence. Generally this does not have to be repeated in subsequent years as the IRD will thereafter accept that the company profits are not taxable unless and until the working method changes. Hong Kong is not a member of the OECD or considered by the OECD as a tax haven. It is also not affected by the proposed EU Savings Tax Directive. As such, we believe that Hong Kong may be the OFC both now and in the future. Others seem to agree. The number of new companies incorporated in Hong Kong last year was 46,554, up from 38,258 the previous year.

14 asia+ pacific

FATF not to impose counter-measures on the Philippines

The Financial Action Task Force (FATF) decided not to apply any countermeasures to the Philippines following the enactment on 7 March of Republic Act No. 9194 to amend the Anti-Money Laundering Act of 2001. But the Philippines is to remain on the FATF's list of non-cooperative countries and territories (NCCTs) until such time as the new legislation has been implemented effectively.

In February the FATF took the serious step of recommending that its members impose additional counter-measures against Philippines due to the failure of the Philippines to enact legislation to address previously identified deficiencies in their anti-money laundering regime. It called upon the Philippines government to enact the appropriate legislative amendments by 15 March 2003 or face counter-measures.

FATF President Jochen Sanio said: "This is a significant success for the FATF and the Philippines in the fight against money laundering. Close monitoring of implementation issues will be crucial in determining an appropriate time for the Philippines' removal from the NCCT list."

For current list of NCCTs see Legal Page.

Singapore Budget introduces tax incentives

Finance minister Lee Hsien Loong announced a series of tax incentives aimed at attracting foreign trusts and encouraging intellectual property business in the Singapore Budget on 28 February.

All foreign trusts will now be exempt from income tax and all trust administration services provided to foreign trusts will be zero-rated for goods and services tax purposes. Qualifying trusts must be held by non-residents or foreign companies.

The government will also exempt from tax foreign income in the form of dividends, branch profits and services income from 1 June 2003, from jurisdictions with tax rates of at least 15%.

Other measures will make it more attractive to create and hold intellectual property in Singapore, such as the automatic grant of writing-down allowances for expenditures incurred in acquiring intellectual property.

These include extending the unilateral tax credit scheme to royalties remitted from non-treaty countries from the financial year beginning on 1 April 2004 and granting automatic writing-down allowances over a five-year period for capital expenditure incurred in the acquisition of intellectual property from 1 November 2003.

Two new structures, limited partnerships, which are typically used for private equity and fund investment activities, and limited liability partnerships, often used for professional and business investment activities, are to be introduced in 2004.

The government is to remove the requirement that private companies must appoint secretaries with professional qualifications. They must, however, still appoint a company secretary. Audited accounts will no longer be required for dormant companies and for exempt private companies with annual turnovers below a threshold of S$2.5m, rising to S$5m after one year.

US Court of Appeals makes determination on sham trusts

The US Court of Appeal affirmed the decision of the US Tax Court which had held that the foreign trustees of a foreign trust that had supposedly received the profits of a US business as its owner were no such thing and could be ignored as such because the trust was a sham. As a result the taxpayer and his wife were personally liable for tax on the income purportedly earned by the trustees as owners of the business in the years 1994 to 1996, as well as for negligence penalties for failure to pay the tax when due.

In the case of *Robert A. Lund & Others v. Commissioner of Internal Revenue* the US Court of Appeals in San Francisco held that the Tax Court had correctly applied a four-factor test to determine that the Zero Gee Trust lacked economic substance:

- Lund's relationship to the trust property (his computer consulting business) did not differ materially before and after he formed the trust and granted the business to the trust;
- the trust did not have independent trustees;
- no economic interest passed to the named beneficiaries of the trust;
- Lund did not honour restrictions imposed by the trust or by the law of trusts.

The indicators that Zero Gee lacked economic substance were that, after placing his computer consulting business in the trust, Lund had purportedly transferred his entire beneficial interest, valued at between US$1 million and $2 million, to a foreign corporation without any consideration whatsoever. Lund also had essentially unrestricted use of trust property and obtained bank loans and credit for the consulting business using property as collateral.

At the same time, the trustees of Zero Gee had performed no meaningful work, had received only $3,600 per year for managing the trust and Lund had continued to operate and control the business. The named beneficiaries of Zero Gee had received only token payments despite a net trust income of over $1.2 million and the fact that Zero Gee had reported distributions equal to its entire income.

Sovereign comment

The situation illustrated here will not be untypical of the many so-called trust arrangements that have been set up over the last 20 or 30 years. Too often trusts have been sold as products and have been badly drafted, badly set-up and badly managed to the extent that, like this arrangement, they will be considered as shams if they come under any sort of scrutiny. Trusts are an extremely powerful planning tool which carry a whole host of advantages. But, if they are to be effective, it will necessarily involve the settlor losing legal control and some degree of actual control. If control is retained then it isn't a trust. Time and time again we are seeing trust arrangements called trusts which are nothing of the sort. Beware of the trustee who promises too much! Such arrangements will fail if attacked by creditors, the tax authorities or anybody else for that matter.

Jersey Royal Court declares trust void for uncertainty

The Royal Court declared a settlement void because there was insufficient certainty as to the beneficial interests after the replacement trustee applied for an order as to the proper construction of the settlement.

In *Re. The Double Happiness Trust*, the settlement had been drafted in the Hong Kong office of accountants Grant Thornton in 1997. No legal advice was taken. The result, said the Court, "is a vivid illustration of the dangers of non-lawyers drafting trust deeds."

In order for a trust to be valid, there must be certainty as to the subject matter, the beneficial interests and the beneficiaries. In this case, said the Court, there was some difficulty in respect of certainty of beneficiaries. The definition was by no means clear and there was complete confusion and inconsistency in the deed concerning "beneficiaries" and "named beneficiaries". Even greater difficulty lay in establishing the beneficial interests.

The Court, in a judgment given on 10 December 2002, said it was reluctant to allow a trust to fail for uncertainty because of poor drafting. Despite many errors and inconsistencies, it could detect an intention in the main body of the trust deed that the trust fund was to be held upon the trusts set out in Schedule Two, but found it impossible to construe Schedule Two so as to provide sufficient certainty as to the trusts which were being created.

In the circumstances, said the Court, it had no alternative but to declare that there was therefore insufficient certainty as to the beneficial interests and the settlement must be declared void.

Sovereign comment

Trust lawyers around the world will be smiling at this one. The larger accountancy firms often have departments which act as trustees and hold themselves out as having expertise in trust matters but frequently, and not unsurprisingly, do not have the necessary legal skills to draft trust deeds in-house. The consequences of having a trust declared void are serious. Presumably the trust was set up for tax reasons and, presumably, the benefits sought will not now have been achieved. Sovereign employs a large number of lawyers to prepare our trust documents. Where necessary we seek outside expertise and opinion. When setting up a trust always make sure that an experienced lawyer has drafted the trust deed.

FATF update list of NCCTs

The Financial Action Task Force (FATF) removed Grenada from its list of Non-Cooperative Countries & Territories (NCCTs) as a result of the implementation of significant reforms to its anti-money laundering system.

It also withdrew the application of additional counter-measures with respect to Ukraine after the recent enactment of comprehensive anti-money laundering legislation that addresses the main deficiencies identified in 2001 and reaffirmed last December.

The current list of NCCTs comprises: Cook Islands, Egypt, Guatemala, Indonesia, Myanmar, Nauru, Nigeria, Philippines, St. Vincent & the Grenadines, and Ukraine. The FATF called on its members to update their advisories requesting that their financial institutions give special attention to businesses and transactions with persons, including companies and financial institutions, in listed countries or territories, to take into account the changes in the list. It will review the situation of each NCCT at its next Plenary meeting in June.

Sovereign comment. The list of NCCTs is reviewed periodically and countries can be added or and others removed. The effect of being branded as an NCCT is that it makes it very difficult for residents of that country to open bank accounts and deal with financial institutions. Banks are now required to obtain a large amount of due diligence information on any new customer so starting a new relationship with any bank or financial institution is difficult enough. Attempting to start that relationship if you are a resident of a country branded as an NCCT adds extra difficulty as the bank is bound to be extra cautious and will generally require extra information and documentation.

EU Finance Ministers fail to adopt fiscal package

EU Finance Ministers failed to secure a final agreement on the fiscal package – the savings tax Directive, the Code of Conduct on business taxation and the Directive on interest and royalties – at an EcoFin Council meeting in Brussels on 19 March. Agreement was blocked by Italy in an unrelated dispute over milk quotas.

With the exception of Italy, all member states endorsed the political agreement reached in the Council of Ministers on 21 January and reaffirmed their commitment to adopting the fiscal package as soon as possible. Italy's objections may force the EU to delay introduction of the package by a year to 2005.

Under the proposed savings tax Directive, twelve member states are to implement automatic exchange of information concerning interest income derived from savings in another member state from 1 January 2004, the date of implementation of the directive, with Austria, Belgium and Luxembourg applying a withholding tax on savings held by residents of other member states rising to 35% by 2010 and sharing the revenue with the country of residence.

These three Member States are to move to automatic exchange of information, if and when, certain third countries, principally Switzerland and the USA, agree to exchange of information upon request with respect to savings income in accordance with the OECD Agreement on Exchange of Information on Tax Matters. Dependent and associated territories of member states are also to apply the same arrangements.

The agreement under negotiation with Switzerland, to apply the same rates of retention and withholding as Belgium, Luxembourg and Austria and to share the revenue with the country of residence, will serve as a basis for similar arrangements with Liechtenstein, Andorra, Monaco and San Marino. The 35% withholding rate will remain after each has adopted exchange of information on the OECD standard.

An extension to Switzerland of the Directive on interest and royalties between parent companies and subsidiaries abroad was accepted by all the member states, but Spain was granted a concession permitting it to negotiate a bilateral tax treaty.

All member states except for Belgium accepted the Code of Conduct on business taxation, which provides for the dismantling of 66 tax measures with harmful features (40 in EU member states, 3 in Gibraltar and 23 in dependent or associated territories) by 2005 at the latest. Belgium secured agreement that the specific tax regime for enterprises in "co-ordination centres", which were authorised until 2000, should continue to apply until 2010.

Sovereign comment

The continued haggling over the fiscal package among EU member states and between third parties has led to great uncertainty and has thrown up a number of potential anomalies, particularly in relation to those OFCs which are dependent and associated territories of member states. Only when, and if, the package is finally adopted will it be possible to start assessing the full impact. We will continue to monitor the situation.

14 fiscal

Gibraltar lobbies UK on EU Savings Tax Directive

Chief Minister Peter Caruana said he had been unable to persuade the UK government to permit Gibraltar to apply the same withholding tax system granted by the EU to Austria, Luxembourg and Belgium under the proposed savings tax Directive.

The UK wants its overseas territories and dependencies to automatically exchange client information with an EU member when interest payments are made to residents of that EU country. After a meeting with UK officials on 7 February, Caruana said Gibraltar's proposal had met with a "negative" response. He noted that Gibraltar would not decide on whether to mount a legal challenge until the EU completes the final draft of the directive. "Our EU status means that our finance centre must remain responsive to events outside Gibraltar's control," he said. "Unavoidable challenges have to be accommodated as well as possible and new opportunities seized."

Sovereign comment. Gibraltar is not alone in wanting to introduce a withholding tax instead of automatic exchange of information. The Channel Islands and the Isle of Man are all considering requesting that they be allowed to follow the withholding tax route. Interestingly, the directive would not affect UK residents opening accounts in Gibraltar because Gibraltar is considered part of the UK. Also, as things stand, the directive only appears to apply to individuals, so accounts opened in the name of a company (presumably incorporated outside the EU) would not seem to fall under the terms of the directive. But we can expect further protocols to be added which would affect any entity beneficially-owned by an EU resident.

Manx Budget continues reduction of corporate taxation

The Isle of Man Budget effectively extended the 10% rate of corporate tax to all resident trading companies by moving the threshold at which the higher rate of 15% becomes payable to £100m from £500,000. The income tax higher rate for company non-trading income and non-residents remains at 18%.

The Budget, delivered on 18 February, contained a package of measures to stimulate and develop the funds industry by: extending the existing zero rate tax regime and VAT exemption on fund managers' profits and fees to both fund administrators and to managers of Experienced and Professional Investor Funds. It also introduced an Overseas Funds Exemption such that an overseas fund may be administered in the Isle of Man without "dual regulation" where it is incorporated in a jurisdiction having an appropriate regulatory framework.

Further measures included a concession and relocation package to assist companies requiring to bring key employees to the island, and an increase in non-resident company duty from £830 to £1,000. No change was proposed to the fees for exempt companies or other international entities. These will remain at £430 per annum.

The Budget measures are expected to be in place by the summer. Other measures in the pipeline include changes to the Partnership Act to help attract funds established as Limited Partnerships; and changes to the Companies (Transfer of Domicile) Act to facilitate the easier migration of funds to the Island from other jurisdictions.

Sovereign comment

The Isle of Man's intention is ultimately to reduce the rate of corporation tax paid by resident companies to zero so as to achieve a unified system of taxation in which there is no distinction between resident, non-resident and exempt. The Budget has again increased the duty payable by non-resident companies. The objective is to encourage non-resident companies to convert into exempt companies so that they have a resident director and company secretary.

Yacht registration in the 21st Century

The Sovereign Group has further augmented the range of its wealth management services with the addition of Register A Yacht.com, a Gibraltar-based specialist with over 20 years experience in yacht registration and offshore company management.

In the past, if you wanted to register your yacht under the British flag, you could choose any British Port of Registry – the procedure for registration would be the same in each. When the formalities had been completed you could sail away, holding a British Registration Certificate, or "blue book" as it is commonly known, and flying the Red Ensign without having to worry about any further paperwork.

But increasing international maritime regulation combined with numerous changes in legal and fiscal regimes around the world, have made the process of owning and registering a yacht ever more sophisticated. British Ports of Registry now have different rules in place and each offers its own advantages and disadvantages.

Advantages of the British flag

Registering a yacht in a British port entitles it to fly the respected British flag. This brings with it international recognition, prestige and the full protection of the Royal Navy and world-wide network of British Consular offices.

The British flag also means British law, which may be beneficial should legal disputes arise. It may also make financial institutions feel more comfortable about lending on the security of British-registered yachts because the documentation is based on a familiar and proven system of law.

Broadly speaking, British Ports of Registry will permit the registration of yachts that are owned by nationals of EU member states. But by owning a vessel through a company anyone can obtain the advantages of British registration indirectly. Corporate ownership may also provide other benefits including privacy, confidentiality and asset protection.

Legal and fiscal issues

Before registration there are certain factors that should be taken into consideration. These include whether the yacht has any liens or mortgages on it, whether it is already registered in a foreign registry and whether it is liable to payment of VAT.

The VAT question often causes confusion. Regardless of the ownership of the flag, if the yacht is for use in EU waters and the beneficial user is an EU resident then the yacht is liable to pay VAT. If the beneficial user is not an EU resident then VAT-free temporary importation is still available.

If the yacht being bought or sold has already paid VAT then it is important to ensure that the sale of the yacht takes place within the EU. This will preserve its VAT paid status.

Registration procedures

The registration procedure itself is relatively straightforward. The first step is to submit the proposed names to the appropriate Registry. When these are cleared and reserved, a tonnage measurement survey must be carried out by a recognised classification society.

"Owning and registering a yacht has become ever more sophisticated".

"Through a company anyone can obtain the advantages of British registration".

If the yacht is new, a builder's certificate is required. If it is second hand, a notarised bill of sale is required together with previous bills of sale establishing a five-year chain of title.

All the documentation must be submitted to the Registry which then issues a "carving and marking note" for the vessel. This note has to be verified and returned to the Port of Registry which will then issue the British registration certificate, the 'blue book'.

Most British Ports of Registry require non-resident owners to appoint a locally-based representative agent to attend to the renewal of registration on behalf of the owner. In Gibraltar the registration is renewed on an annual basis; in UK mainland ports the registration is renewed every five years.

Those familiar with matters maritime will know that time and tide do not wait. Completion of the yacht may be delayed, or weather, holiday or crewing considerations may come into play before everything is in place. If this happens, some registries – Gibraltar is one – will issue a provisional registration for the yacht, provided the proposed name is available and clear title to the yacht can be proved. The provisional registration is for three months and allows the yacht to move freely while the formalities for full registration are completed.

Register A Yacht.com

Sovereign's new specialist makes yacht registration easy. Register A Yacht.com will manage the process of registration to ensure that the correct procedures are followed and the right forms submitted. British ports of registry are the preferred and recommended choice, but yachts and commercial vessels can be registered in any of the world's registers, according to the individual's requirements.

Register A Yacht.com provides a comprehensive marine service, which includes arranging the radio licence, insurance, registration of a change of ownership or name of a yacht, and the transfer of a yacht to another British Port of Registry. It can also liaise with agents and brokers during the selling or buying process and arrange for delivery of all the documentation needed to complete the deal successfully.

The Sovereign Group is also able to call upon the resources of Sovereign Law member R A Triay & Co, a Gibraltar-based law firm headed by maritime law specialist Raymond "Monchi" Triay.

If you would like to find out more about Register A Yacht.com, please contact us at Suite 2B, Mansion House, 143 Main Street, Gibraltar (Tel: +350-51870) or visit the website: www.registerayacht.com

information

For more information on the services provided by The Sovereign Group, please visit our website: **www.SovereignGroup.com** or contact your most convenient Sovereign office listed below.

Bahamas: Tennille Darville
Tel: +1 242 322 5444
Fax: +1 242 325 8445
bh@SovereignGroup.com

British Virgin Islands: Susannah Musgrove
Tel: +1 284 495 3232
Fax: +1 284 495 3230
bvi@SovereignGroup.com

Cyprus: Vassos Hadjivassiliou
Tel: +357 22676519
Fax: +357 22679079
cy@SovereignGroup.com

Denmark: Jan Eriksen
Tel: +45 44920127
Fax: +45 43690127
dk@SovereignGroup.com

Germany: Dr Norbert Buchbinder
Tel: +49 (0)911 92668–30
Fax: +49 (0)911 92668–39
de@SovereignGroup.com

Gibraltar: Stuart Stobie
Tel: +350 76173
Fax: +350 70158
gib@SovereignGroup.com

Sovereign Asset Management Ltd Chris Labrow
Tel: +350 41054
Fax: +350 41036
sam@SovereignGroup.com

Hong Kong: Michael Foggo
Tel: +852 2542 1177
Fax: +852 2545 0550
hk@SovereignGroup.com

Isle of Man: Paul Brennock
Tel: +44 1624 699800
Fax: +44 1624 699801
iom@SovereignGroup.com

Malta: Mark Miggiani
Tel: +356 21 339 218
Fax: +356 21 322 531
ml@SovereignGroup.com

Mauritius: Ben Lim
Tel: +230 208 1747
Fax: +230 208 1736
mu@SovereignGroup.com

Netherlands: Susan Redelaar
Tel: +31 (0)20 428 1630
Fax: +31 (0)20 620 8046
nl@SovereignGroup.com

Portugal: Nigel Anteney-Hoare
Tel: +351 282 340480
Fax: +351 282 342259
port@SovereignGroup.com

South Africa, Cape Town: Timothy Mertens
Tel: +27 21 418 4237
Fax: +27 21 418 2196
sact@SovereignGroup.com

South Africa, Johannesburg: Paul Woods
Tel: +27 11 886 7728
Fax: +27 11 781 3083
sajb@SovereignGroup.com

Spain: Richard Melton
Tel: +34 952 764168
Fax: +34 952 825637
spain@SovereignGroup.com

Turks & Caicos Islands: Paul Winder
Tel: +1 649 946 2050
Fax: +1 649 946 1593
tci@SovereignGroup.com

United Arab Emirates: Kevin O'Farrell & Cecilia D'Cunha
Tel: +971 4 3976552
Fax: +971 4 3978355
dubai@SovereignGroup.com

United Kingdom: Simon Denton
Tel: +44 (0)20 7389 0555
Fax: +44 (0)20 7930 1151
uk@SovereignGroup.com

Sovereign Group Partners LLP Gerry Scanlon, Neil Pidgeon & Hugh de Lusignan
Tel: +44 (0)20 7389 0655
Fax: +44 (0)20 7930 0502
capital@SovereignGroup.com

Sovereign Accounting Services Stephen Barber
Tel: +44 (0)20 7389 0644
Fax: +44 (0)20 7930 4749
sas@SovereignGroup.com

United States of America: William H. Byrnes
Tel: +1 305 579 5344
Fax: +1 305 579 5345
usa@SovereignGroup.com

Sovereign Education William H. Byrnes
Tel: +1 305 474 2468
Fax: +1 305 474 2469
edu@SovereignGroup.com

Uruguay: Walter Otero
Tel: +598-2 900 3081
Fax: +598-2 900 1932
uy@SovereignGroup.com

contact

Editor: Christopher Owen
Publisher: Kamilian Limited
Tel/Fax. +44 (0)20 7266 9920
Email: report@kamilian.com
Website: www.kamilian.com
Printer: Pioneer Printers Limited

SOVEREIGN

SovereignGroup.com

14

SOVEREIGN

www.SovereignGroup.com