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STOP PRESS: EU and Switzerland finally agree on implementation of EU Savings Directive

At the time of going to press it has just been reported that Switzerland has reached agreement with the EU to implement the EU Savings Directive, having been given assurances that it can retain a measure of its banking secrecy.

At a meeting in Brussels on 19 May, the two sides gave official endorsement to nine agreements which, in addition to the savings tax Directive, would bring Switzerland into the Schengen passport free area in 2006-2007 and enhance co-operation in areas such as the fight against fraud. They are expected to be signed in the autumn.

A compromise deal was struck whereby Switzerland signed up to the Schengen accord, which currently provides for co-operation against fraud in the area of indirect taxation. But Switzerland will not be bound if the EU member states decide in the future to extend the agreement to cover co-operation against fraud in the area of direct taxation.

Countries such as the UK and Germany have sought an EU-wide savings tax deal for years. But the Directive, which gives member states a choice between levying withholding tax and exchanging banking information, is dependent on third countries, such as Switzerland, and relevant dependent or associated territories, such as the Cayman Islands, Channel Islands, and BVI, agreeing to apply equivalent or the same measures from the same date.

EU finance ministers meet in June to decide whether such agreements are in place and whether to proceed with the 1 January 2005 schedule for implementation. The good news is that the Directive only appears to affect accounts held by individuals and not by companies and trusts.

New Singapore office

Sovereign Trust (Singapore) Pte Limited has now been incorporated and has commenced business operating from 96A, Club Street, Singapore 069464. The office will be headed up by Richard Wilson who was formerly one of our resident directors in Mauritius. For contact details, see *page 10*.

chairman

We elected to open an office in Singapore to service the growing South East Asia market and the increasing demand for the incorporation and management of Singapore companies. Singapore is regarded as a safe jurisdiction because it is not affected by either the OECD's report on harmful tax competition or the EU Savings Tax Directive. Nor is it an OECD member, so it has not come under pressure to implement exchange of information provisions. Many clients have contacted us asking whether we can set up banking arrangements in Singapore and this new office will assist with those matters.

Sovereign Art Foundation

The Foundation held its annual charity dinner at Cine Citta restaurant in Hong Kong on 11 May to mark the conclusion of the 2004 Sovereign Contemporary Asian Art Prize. The first prize of US$10,000 was presented to Jeffrey Aranita, and the US$4,000 second prize to Christopher Ng. Voting to decide the third prize was concluded on 7 May, and was won by Simon Birch, a popular local artist, after a very close contest. It was announced that the third prize would be renamed "The Schoeni Art Prize" in memory of Manfred Schoeni, an advisor to the Foundation and a personal friend, who was tragically murdered in the Philippines days beforehand.

After the prize giving, works by the top 30 finalists (apart from the first and second prize winners) were auctioned off to raise money for the Foundation. Funds raised will be used to fund scholarships and grants for emerging Asian artists and further the general aims of the Foundation to raise the awareness of Asian art and artists.

Thanks to all who contributed, particularly Tiffany and Michelle, to a great evening and helped make this first Annual Art Prizes such a great success.

Howard Bilton BA(Hons)
Barrister-at-Law (England, Wales & Gibraltar)
Professor of Law, St. Thomas School of Law, Miami, USA
Chairman of The Sovereign Group

EU plans to restrict use of Offshore Financial Centres

The European Commission said curbs on the use of offshore centres and special purpose vehicles would be introduced after the collapse of Italian food giant Parmalat. They will be part of its Action Plan to modernise company law and enhance corporate governance in the EU, which was launched last May. The Commission said it hoped the proposals would be adopted by mid-2005.

EU internal market commissioner Frits Bolkestein told the European Parliament he would be submitting proposals to revise the EU's company law Directive on statutory audits. It would also accelerate work on three corporate governance proposals covering the role of non-executive directors, collective responsibility of all board members for financial and important non-financial statements, and full disclosure in company accounts of offshore "special purpose vehicles".

Only the southern section of Cyprus joined the EU on 1 May 2004, after Greek Cypriots rejected a settlement plan put forward by the UN in a referendum held on 24 April. The UN plan was a last bid to secure reunification before accession to the EU but Greek Cypriot leaders urged voters to reject it. Some 76% of Greek Cypriots voted against the UN's peace plan, while 65% of Turkish Cypriots, who live in Northern Cyprus, approved it, opening the door for economic aid to them from the UN and the EU after decades of isolation. Only Turkey currently recognises the government of Northern Cyprus.

The southern section of Cyprus became part of the EU together with the Czech Republic, Estonia, Hungary, Latvia, Lithuania, Malta, Poland, Slovakia and Slovenia.

The Commission has sent formal requests to Italy, Portugal, Greece, Sweden, Luxembourg and France to implement the second Anti-Money Laundering Directive. Adopted on 4 December 2001, it was due to be in force across all member states by 15 June 2003.

The Directive commits member states to combat laundering of the proceeds of a wide range of serious crime and extends the coverage of the first Directive from the financial sector to a series of non-financial activities and professions. These include external accountants and auditors, real estate agents, notaries, lawyers, dealers in high value goods and auctioneers.

Sovereign comment

We do not believe that there is anything inherently wrong in a company choosing to use offshore structures as part of its overall tax or other planning arrangements. Such vehicles can be used entirely properly and legally, but equally they can be used for illegal purposes. In our opinion, it is therefore pretty pointless to pass a law stating that it is illegal to do something illegal. We also note that yet again the woes of Parmalat are being blamed on the offshore sector when the alleged fraud was carried on in Italy and elsewhere.

18 europe

Jersey announces major tax reform proposals

Jersey has issued proposals to abolish company tax for both resident and non-resident companies and to introduce a sales tax to compensate for lost revenue. The move is intended to bring the tax regime into line with OECD and European Union initiatives to curb "harmful tax competition".

In proposing a zero corporate tax rate, Jersey is following the Isle of Man. Guernsey is expected to follow suit. The three UK crown dependencies believe the zero rate is vital to compete with Ireland, which set its corporate tax at 12.5% last year.

Senator Frank Walker said: "Every country in Europe has VAT. There are very strong reasons for Jersey to introduce some form of sales tax."

Sovereign comment. All the major offshore jurisdictions who have tax for residents but not for non-residents are having to revise their systems and most are looking at introducing a unitary system which does not distinguish between entities owned by residents and those owned by non-residents. Gibraltar, subject to finally getting EU approval, is looking to introduce a zero tax system and make up the revenue by imposing an employee tax and a property tax. Neither would impact upon most existing companies owned by non-Gibraltar residents. The Isle of Man was the first jurisdiction to announce that it would be introducing zero tax across the board so it is no surprise that Jersey is following that lead.

UK Budget cracks down on tax avoidance

UK Chancellor Gordon Brown announced, as part of the Budget on 17 March, a new disclosure measure requiring those who devise and market certain avoidance schemes to provide the Inland Revenue with details in advance.

Brown said he did "not at this stage intend to introduce" a general anti-avoidance rule, as has been implemented in Australia and Canada. Instead he chose to follow the US approach, which relies on voluntary disclosure. Under the new measure, advisers will have to provide a description of the scheme and the tax consequences. The Revenue will register the schemes and allocate reference numbers. Taxpayers using such a scheme will have to include its registration number on their tax returns. Where schemes have been devised in-house or offshore, the onus will fall on the taxpayer to provide details to the Revenue. The measure targets schemes and arrangements based on financial products and employment-based products.

The Chancellor also moved to close certain specific loopholes: companies that realise capital from partnerships face a charge to corporation tax; individuals may no longer use life insurance policies to generate deficiency relief; individuals and trustees will not gain tax benefit from stock lending transactions involving UK equities; individuals may not avoid income tax by manipulating the market value of strips of government bonds.

Sovereign comment

We do not believe that these measures affect Sovereign and its clients. Our London operation would generally only pass out information which might lead to the sale of a product or scheme by one of our offshore offices which, being outside the UK, would not be covered. The new legislation will obviously be a bigger problem for practitioners who are based in London or who have a substantial presence in London. This may give Sovereign a competitive advantage.

BVI introduces Virgin Islands Special Trusts Act

The British Virgin Islands has introduced three new pieces of trust legislation. The Virgin Islands Special Trusts Act, Trustee (Amendment) Act and Property (Miscellaneous Provisions) Act received first reading on 28 August 2003 and second and third readings on 30 September. They will come into force when they receive Royal Assent.

The Virgin Islands Special Trusts Act provides a structure for ownership of a business. Designated shares will be held on "trust to retain", and the trustee's duty to hold the shares will override any duty to maximise the value of assets. They will thus be covered against liability for any resulting decline in the value of the trust property. Unless authorised to act by trust beneficiaries in certain carefully defined circumstances, trustees will be barred from exercising their power as shareholders to interfere in the management of the company. Trusts which are created under the proposed Virgin Islands Special Trusts Act, will be known as “VISTA” trusts.

The Trustee (Amendment) Act includes provisions relating to dealings between trustees and third parties, charities, the BVI’s “conflict of laws” rules, and a new regime for “purpose trusts”.

The most significant aspect of the Property (Miscellaneous Provisions) Act is a provision which abolishes the requirement that deeds executed by individuals need to be sealed.

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Sovereign comment

The new VISTA trusts could prove extremely popular. Clients who own substantial shares in private companies often wish to settle those shares into trust for tax or dynastic reasons, but this can create a dilemma for trustees. A trustee should always seek to diversify the portfolio of investments under their control and this can be incompatible with holding a large share of a private company as the major or sole asset of the trust.

Trustees also need to keep a close watch on the business activities of the company and interfere where necessary. But many settlors object to interference from the trustees during their lifetime.

VISTA trusts may be the ideal vehicle to hold the shares of a private company and provide settlors with all the tax and dynastic planning benefits, without the inconvenience of trustee interference which may be entailed with a standard trust.

Turks & Caicos assistance to overseas regulators

The Supreme Court held that the US Securities & Exchange Commission (SEC) was an overseas regulatory authority within the meaning of the Overseas Regulatory Authority (Assistance) Ordinance 2001 (the Ordinance) and could be assisted by the TCI Financial Services Commission (FSC).

In *Muir Woods Investment Group v The Licensing Committee of the FSC*, the SEC sought the assistance of the FSC to obtain documents and information regarding a number of international business corporations (IBCs). The FSC wrote to the company managers of the IBCs concerned, citing the Ordinance and requesting that they divulge the information sought, including details of the directors, officers and beneficial owners. The IBCs contested the request on the basis that the SEC was not an overseas regulatory authority to which assistance could be given and that, even if it was, the Ordinance did not permit such details to be divulged in the manner sought.

The court found that the term “overseas regulatory authority” includes any foreign authority exercising such functions and therefore held that the SEC did qualify and could be assisted by the Financial Services Commission. It also held that the Ordinance overrode the Confidential Relations Ordinance and the confidentiality provisions of the Companies Ordinance. The FSC was therefore entitled to demand and be given the information sought, and to pass it on to the SEC.

Although the point was not at issue in the case, the court emphasized that the competent authority has to be satisfied, before it can assist, that the assistance is not requested by the overseas regulatory authority for the purposes of any functions directly or indirectly relating to assessing, imposing or collecting tax.

Sovereign comment

It is interesting that the court held that it would not have ordered the release of the information if it was in relation to a tax matter. But this is somewhat academic as the OECD requirements for exchange of information, which are due to be implemented, would include the need to exchange information on such tax matters.

Bahamas issued guidance on unidentified customers

The Central Bank of the Bahamas (CBB) issued, on 17 February, guidelines for banks and trusts on submitting information on customers they have not properly identified under the anti-money laundering rules.

The guidelines relate to customers which banks and trust companies had prior to 29 December 2000, when new identification procedures came into effect under the Financial Transactions Reporting Act, amended last year. Financial institutions were required to verify the identity of such customers by 1 April 2004. In cases where they have not, the bank or trust company were obliged to notify the CBB by 30 April. Under the legislation, the CBB has the power to order banks or trust companies to freeze the customers’ accounts until verification of identity has taken place.

Sovereign comment. Before there was a legal requirement to identify customers, many banks and trust companies required very little information on their clients. But those days are gone, and no bank or trust company will now take on a client without performing due diligence. Providing information is time consuming and can be a source of irritation to the honest client but regrettably there is no way round this and, in this new era, full and frank disclosure is vital before any financial transactions can take place. Most jurisdictions are relying upon financial institutions to put their house in order without resorting to legislation. This new guideline in the Bahamas will force clients to provide the documentation.

China rejects direct elections for Hong Kong

The National People's Congress Standing Committee (NPCSC) voted, on 26 April 2004, against allowing direct elections for the post of chief executive of the Hong Kong Special Administrative Region (SAR) in 2007 and for the Legislative Council in 2008.

The NPCSC, China's legislature, said it had interpreted the Basic Law, effectively Hong Kong's constitution, and found that only China's central government had the authority to decide when, and if, electoral reform was needed in Hong Kong.

The current chief executive, Tung Chee-Hwa, was appointed directly by the Chinese government. The NPCSC's decision followed submissions by Tung asking it to determine whether "methods for selecting the chief executive in 2007 and for forming the Legislative Council in 2008 may be amended".

Hong Kong's Basic Law provides for full elections for the post of chief executive by 2007, but the NPCSC expressed "concern" to Hong Kong's government that electing the chief executive by universal suffrage in 2007 would go against the Basic Law's principle of "gradual and orderly progress". Pro-democracy advocates also want voting rights to be broadened to include all 60 members of the Legislative Council.

In his Budget statement on 10 March, Hong Kong Financial Secretary Henry Tang declared his support for a future sales tax in the territory but offered up no major tax changes for the current fiscal year, relying instead on economic growth and reduced spending to keep the SAR's deficit in line. Tang delayed making a decision on the sales tax until the end of the year. Implementation would take another three years, he said.

Sovereign comment

There was never much likelihood that China would allow any real level of democracy in Hong Kong. One of China's complaints about the outgoing British colonial rule was that there had been no element of democracy in the government of Hong Kong during the 150 years of its existence, so why were they trying to introduce it shortly before they left? The democratic process in Hong Kong is little more than a veneer and it is unlikely that this will change in the foreseeable future. Despite that, Hong Kong remains stable and flourishes economically. It is generally considered to be the place with the greatest financial freedom in the world and with the least barriers to setting up and running a business. English law on commercial matters continues to prevail and will do so until 2047.

18 asia+ pacific

Indonesia revokes tax treaty with Mauritius

High level diplomatic talks are underway in a bid to restore the Mauritius/Indonesia tax treaty, after notice of termination was sent by the Indonesian Embassy in Tanzania in February. According to the terms of the treaty, termination will take effect on 1 January 2005.

The reasons given for the termination of the treaty were that Mauritius is being utilised by non-Mauritian citizens who form conduit companies to invest in Indonesia. This Indonesia regards as an abuse of the treaty.

A letter has been sent requesting permission for a delegation including the Minister for Financial Services, the Financial Secretary and the Commissioner of Income Tax to travel to Jakarta for urgent talks.

Sovereign comment. The Mauritius government seems to be quite optimistic about the chances of reinstating its treaty with Indonesia but, until matters are clarified, investors in Indonesia would be wiser to look for another suitable treaty. Useful jurisdictions to establish an investment company would include Netherlands, Singapore, UAE or the UK. All these have excellent treaties and companies can be structured to pay zero or minimal rates of tax on income received from Indonesia whilst enjoying reductions in the normal levels of tax withheld in Indonesia.

Australian Tax Office targets tax haven schemes

The Australian Tax Office (ATO) has set up a special taskforce to tackle "abusive tax haven arrangements". The Taskforce will look at financial dealings between Australian taxpayers and the 38 OECD-listed tax havens. It will also focus on Switzerland because of bank secrecy issues.

The Tax Office said it was mainly focusing on schemes where people use a tax haven's secrecy laws to hide assets and income that should have Australian taxes paid on them.

The type of schemes targeted for special attention are those which try to:

- create deductions in Australia;
- avoid tax on tax haven income;
- provide access to tax haven funds on which no Australian tax has been paid.

"Although there are some above board business reasons for dealing with tax havens – currency dealings, insurance, hedge and mutual funds management and offshore investment – the tax office is looking at arrangements designed to avoid or evade Australian taxes," said a statement issued on 23 February 2004.

The Tax Office estimates an average of A$10 million is transferred daily to tax havens of which "only a small proportion requires further review". It said it was not generally concerned with ordinary trade, tourism and financial business or private transactions with entities or individuals located in tax havens.

Sovereign comment

Our often-repeated view is that any arrangement designed to save tax should be capable of withstanding legal scrutiny. But we also recognise that such scrutiny rarely occurs without a substantial cost in terms of the time and effort. Australians may therefore prefer to make arrangements within a jurisdiction which is not on the OECD tax haven list – Hong Kong, Singapore and the UAE would be the obvious candidates. Sovereign does provide tax planning services to Australian nationals and residents but always backs them up with a legal opinion from a reputable Australian law firm indicating that all arrangements are legitimate, compliant and permissible under current Australian tax legislation.

UK Court of Appeal gives beneficiaries right to sue

The Court of Appeal dismissed an appeal against the decision of the High Court not to strike out a claim brought by the beneficiaries under a trust, alleging negligence by an accountant in connection with the establishment of that trust.

In *Hughes & Others v Colin E G Richards*, the infant children of David and Alison Hughes, as the beneficiaries under a trust created by the parents, sued the defendant, Colin Richards, alleging negligence in the establishment of the trust. Richards applied for the striking out or dismissal of the children's claim. The High Court refused the application. Richards appealed.

Richards, a chartered accountant, had advised the Hughes to set up an offshore trust fund to avoid income tax on royalty payments which they wanted to invest to provide for their children's education. A trust was registered in Liechtenstein with a Swiss bank as trustee, and a Swiss trading company was formed to which the Hughes sold the benefits of the royalty agreement. But the tax withheld was not recovered nor, under the tax treaty with Switzerland, was it recoverable.

No sums were paid out of the trust to or for the benefit of any of the children, the Swiss trading company was put into liquidation and the trust was struck off. The monies were largely absorbed by the costs, fees and charges, and tax liabilities. The children brought an action claiming Richards owed them a duty of care to use reasonable skill and care in the performance of an investment and monitoring retainer. They also alleged negligence and breach of duty in that the scheme he devised was unsuitable.

Richards applied to have the children's claim struck out or dismissed on the grounds that third party beneficiaries of a transaction could not sue solicitors who were negligent in carrying out the transaction. The High Court refused, holding that there was no decided case where these non-binding observations had in fact been applied to defeat a claim. The Court of Appeal agreed, saying that the relevant area of law was still subject to some uncertainty and developing. It was highly desirable that the facts should be found so that any development of the law should be on the basis of actual and not hypothetical facts.

Sovereign comment

The question of whether an advisor owes any duty of care to the beneficiaries remains to be decided at trial. Generally, a lawyer would only owe a duty of care to whoever instructs him. That was clearly not the beneficiaries of the trust. The trustees owe a duty of care to the beneficiaries and, in fact, to nobody else, but they are not a party to this action and it was not their fault that the scheme was unsuitable.

Guernsey court orders bank to disclose accounts

The Court of Appeal of Guernsey upheld freezing and disclosure orders against a bank in relation to an account held by a company which was alleged to have defrauded US investors of millions of dollars through fake wine futures and debt notes.

In *Seed International Ltd v Tracey & Others*, given on 18 December 2003, the plaintiffs were 13 US-based doctors or dentists who invested in wine or other enterprises of Seed International, a Cayman Islands' company. In November 2002 they were granted an *ex parte* freezing order by the Guernsey court in respect of US$6.1m assets held by Seed within Guernsey. The orders were made in support of substantive proceedings in the Netherlands. Seed sought to have the injunctions set aside.

On 3 November 2003, the Royal Court ruled that the freezing order should remain in place. It also ordered Royal Bank of Scotland International to disclose all documents relating to accounts held by Seed, including details of transfers in and out. Seed appealed, arguing either that there should be no disclosure order or that its terms should not have been wider than the associated freezing order.

The Court of Appeal held it was clear that there was jurisdiction under the Law Reform (Miscellaneous Provisions) (Guernsey) Law 1987 to make a disclosure order, ancillary to a freezing order, even where there was no proprietary claim. Further, it found the arguments in favour of making some form of disclosure order were overwhelming. Seed had or had had assets in Guernsey. Seed had had large sums in the Netherlands, which were no longer there. Without disclosure, the freezing order would be "toothless".

It also found that the Guernsey courts had jurisdiction to make a disclosure order with an ambit wider than that of the freezing order. If monies had been moved by Seed out of Guernsey, it was clearly in the interests of justice that the plaintiffs should know, at the least, to which bank account or other place outside Guernsey Seed had moved its money.

Sovereign comment

Guernsey, like all offshore jurisdictions, tries hard to ensure that its confidentiality laws are not used to try and evade justice. Where ordinary people have lost money the courts will generally try to assist in the tracing of those funds.

FATF removes Ukraine and Egypt from non-cooperative list

The Financial Action Task Force (FATF) announced, at its plenary meeting in February, the removal of Ukraine and Egypt from its list of Non-Cooperative Countries and Territories (NCCTs), following substantial reforms.

The list of countries currently designated as NCCTs are the Cook Islands, Guatemala, Indonesia, Myanmar, Nauru, Nigeria and Philippines. The FATF called on its members to maintain their advisories requesting that their financial institutions give special attention to businesses and transactions with persons, including companies and financial institutions, in these listed countries.

The FATF also decided to maintain the current counter-measures against Myanmar and Nauru, citing a lack of sufficient progress to justify their removal. But Nauru has been removed from the OECD's list of uncooperative tax havens after submitting a letter of commitment to exchange information on tax matters through bi-laterally negotiated tax information exchange agreements with OECD member countries. Nauru will exchange information on criminal tax matters in the first tax year after 31 December 2003. Exchange of information on civil tax matters will become effective for the first tax year after 31 December 2005.

Only Andorra, Liberia, Liechtenstein, the Marshall Islands and Monaco now remain on the OECD's list of uncooperative tax havens.

Portuguese property Municipal Tax

Demands received in respect of 2003 Municipal Tax have confirmed the worst fears for many owners who still hold property in the name of listed "offshore" companies. Despite hope that there might be some form of deferral of the punitive 5% municipal tax rate applicable to those properties, the demands have been arriving with that rate in place.

There are many anomalies amongst the tax demands being received. Some have been charged the normal rate for non-offshore held property, some have been charged 5% but the calculation of actual tax payable is much less than that. However many have been charged the full 5% tax payable, giving, in some cases amongst our own clients, a tax payable in excess of Euros7,000.

On the assumption that these anomalies will eventually be resolved and unpaid tax collected, and also on the basis that unpaid municipal tax can eventually lead to a forced judicial auction of the property concerned by the tax department to recover tax due, it is obvious that all owners of offshore-held property need to address these issues as soon as possible and definitely before the end of the current year.

Due to the changes in revaluation of property for tax purposes, in the majority of cases a transfer back to ones own name by way of sale, or indeed other notarial act, can also lead to large liabilities for tax based on a presumed capital gain at 25% of the calculated gain.

For most property owners therefore, the only real option is to make the company acceptable to the tax authority by moving its place of registration from "black listed" to "non-black-listed" by what is known as "re-domiciling" the company. Re-domiciliation is often the simplest and cheapest way of addressing the problem and also leaves the owner with the original advantages of corporate ownership.

The level of work involved in re-domiciliation is high and the process will normally take at least two months, so clients would be advised to consider their own situation and start the process early and certainly no later than September this year to avoid passing the 31st December 2004 "deadline" and being charged the punitive tax in respect of this current year.

Sovereign comment

Last year Sovereign was contacted by numerous clients who had delayed making a decision until it was too late to redomicile their company to avoid the tax last year. As a result, many clients then decided to wait and see what would happen this year and have not yet made a decision on how to proceed. They may be faced with another year's penalty tax unless they act now. Many clients had hoped that the legislation would go away or there would at least be an amnesty on its imposition. Neither occurred and it is most unlikely that there will be any further changes now. Any person with a company managed by Sovereign or by another company manager who needs assistance in this respect should contact Sovereign's Portuguese office.

18 fiscal

Tax survey finds global trend of decreased tax rates persists

KPMG said its annual Corporate Tax Rates Survey indicated that rates on average continued a general trend downwards. The 30 member countries of the OECD had an average corporate tax rate of 29.96% in 2004, a fall from 30.9% in 2003. EU member countries had an average tax rate of 31.32%, compared to 31.84% in 2003.

Cyprus and Ireland had the lowest corporate tax rates among 69 jurisdictions surveyed. Cyprus' corporate tax rate was 10% and 15% depending on the amount of a company's chargeable income. For the years of assessment 2003 and 2004, companies with a chargeable income over CY£1 million (about US$2 million) became subject to an additional 5% tax on the amount over CY£1 million.

Ireland's corporate tax rate was 12.5% although a 10% rate still applied to certain active trading income from defined existing manufacturing companies and the qualifying income of International Financial Services Centre and Shannon-based companies. The special rate will expire between 2003 and 2010.

Costa Rica had the largest reduction in taxes, by 16.7% from 2003 to 2004, giving the country a corporate tax rate of 30% (36% in 2003). Hong Kong increased its rate to 17.5% in 2004 from 16% in 2003 but remained the Asia-Pacific jurisdiction with the lowest corporate tax rate. Singapore's government reduced the general corporate income tax rate to 20% on income from the 2004 financial year onward in the latest budget.

Tax administrations form joint operational unit

The tax administrations of Australia, Canada, the UK and the US have started discussions to form a joint operational unit to increase cooperation on cracking down on "abusive tax transactions". The commissioners of the four tax administrations agreed to meet in Washington to discuss the launch of the joint task force.

"While tax administrations operate primarily within their own borders, many abusive tax transactions employ strategies that cross borders and many of the promoters of these transactions operate globally without regard to national boundaries," the Australian taxation office announced on 16 March 2004.

The office said setting up a joint task force would help the four countries to: share expertise, best practices and experiences in the field of tax administration to identify and better understand abusive tax transactions and emerging schemes, as well as those who promote them; and exchange information about specific abusive transactions and their promoters and investors under existing bilateral tax treaties.

Sovereign comment

These countries seem to want to halt any attempt to mitigate or avoid tax. Our view remains the same as always: there is no harm in trying to reduce tax, but it is vital that any and all arrangements are legal and compliant, and that all necessary declarations and reporting are carried out in the home country of the taxpayer. Offshore companies and trusts will nearly always play a part in any tax mitigation exercise but will rarely be the whole solution and will not work by themselves. Sovereign has great expertise in advising residents of all four countries on tax planning which is both legitimate and compliant, but also effective.

OECD issues 2004 Tax Haven Report

The OECD reported that its member states had made major progress in eliminating harmful tax practices, by modifying or abolishing more than 30 of the 47 preferential tax regimes identified by the OECD in 2000 as potentially harmful.

According to the 2004 Progress Report on the Project on Harmful Tax Practices, issued by the OECD's Committee on Fiscal Affairs in March, 18 regimes have been abolished or are in the process of being abolished, 14 have been amended so as to remove potentially harmful features, and 13 have been found not to be harmful after further examination.

Only two regimes, Switzerland's so-called 50/50 practice (previously referred to as the Administrative Company regime) and Luxembourg's 1929 Holding Company regime, on which proposals for modification are currently before the Luxembourg Parliament, are to be the subject of further discussion this year. Both these countries abstained from approving the OECD's original report on harmful tax competition in 1998.

The OECD modified its original criteria for identifying a harmful tax regime in 2001 following sustained criticism from non-OECD countries and a shift in US government support following the election of President Bush. Low or no taxes and ring-fencing from the domestic economy were dropped, leaving lack of transparency and no effective exchange of information as the only determining criteria.

The full list of the 47 potentially harmful regimes identified in 2000 and the conclusions drawn by the OECD, are summarised below, grouped according to industry designation. In cases where a regime is in the process of being eliminated, the OECD has deemed it to be abolished provided that: no new entrants are allowed into the regime, a definite date for complete abolition of the regime has been announced; or where the regime was transparent and permitted effective exchange of information.

The OECD reviewed a number of new regimes introduced since 2000. The Netherlands' advance pricing agreement/ advance tax ruling practice and the Belgium advance tax rulings practice were examined and found not to be harmful.

The Report also examined the progress of 41 non-OECD jurisdictions that were identified as tax havens and said that only five were still refusing to cooperate – Andorra, Liberia, Liechtenstein, the Marshall Islands and Monaco. But the OECD admitted that it was aware that a number of financial centres – particularly Hong Kong and Singapore – had not been a part of this exercise and that within the OECD there were widely diverging practices.

The report said OECD members should feel free to consider applying coordinated, unilateral "defensive measures" to "effectively neutralise the deleterious effects of harmful tax practices".

Future work with those low-tax jurisdictions that had agreed to cooperate would involve: monitoring newly-introduced preferential tax regimes; developing and implementing the transparency and exchange of information standards and the establishment of a level playing field; intensifying discussions with other non-OECD jurisdictions to gain their compliance with the principles of the project; and improving access to bank information for tax purposes.

The relevant jurisdictions are: Anguilla; Antigua & Barbuda; Aruba; the Netherlands; The Bahamas; Bahrain; Belize; Bermuda; the British Virgin Islands; the Cayman Islands; the Cook Islands; Cyprus; Dominica; Gibraltar; Grenada; Guernsey; Isle of Man; Jersey; Malta; Mauritius; Montserrat; Nauru; Niue; Panama; Samoa; San Marino; the Seychelles; St Kitts & Nevis; St Lucia; St Vincent & the Grenadines; Turks & Caicos; the US Virgin Islands; and Vanuatu.

Antigua and St Vincent announced in October 2003 that they would no longer take part in the process. The two jurisdictions said they were suspending their commitments because the European Union's recent savings tax compromise with several OECD members undermined the concept of a level playing field.

INSURANCE

Australia (offshore banking units) – not harmful;
Belgium (coordination centres) – abolished;
Finland (Aland captive insurance regime) – abolished;
Italy (Trieste financial and insurance centres) – abolished;
Ireland (international financial centres) – abolished;
Portugal (Madeira international business centres) – abolished;
Luxembourg (provisions for fluctuations in reinsurance companies) – amended to remove potentially harmful features;
Sweden (foreign non-life insurance companies) – abolished.

FINANCE AND LEASING

Belgium (coordination centres) – abolished;
Hungary (venture capital centres) – not harmful;
Hungary (preferential regime for companies operating abroad) – abolished;
Iceland (international trading companies) – abolished;
Ireland (international financial service centres) – abolished;
Ireland (Shannon airport zones) – abolished;
Italy (Trieste financial services and insurance centres) – abolished;
Luxembourg (finance branch regime) – amended to remove potentially harmful features;
Netherlands (risk reserve regime for international group financing) – abolished;
Netherlands (intragroup financing regime) – amended to remove potentially harmful features;
Netherlands (finance branch regime) – amended to remove potentially harmful features;
Spain (Basque Country and Navarra coordination centres) – abolished;
Switzerland (administrative companies) – still under review.

FUND MANAGEMENT

Greece (mutual fund and portfolio investment companies) – not harmful;
Ireland (international financial service centres) – abolished;
Luxembourg (management companies, 1929 holdings) – still under review;
Portugal (Madeira international business centres) – abolished.

BANKING

Australia (offshore banking units) – not harmful;
Canada (international banking centres) – not harmful;
Ireland (international financial service centres) – abolished;
Italy (Trieste financial service centres) – abolished;
Korea (offshore activities of foreign exchange banks) – abolished;
Portugal (external branches in Madeira business centres) – abolished;
Turkey (Istanbul offshore banking regime) – abolished.

HEADQUARTERS REGIMES

Belgium (coordination centres) – abolished;
France (headquarters centres) – amended to remove potentially harmful features;
Germany (monitoring and coordinating centres) – amended to remove potentially harmful features;
Greece (offices of foreign companies) – abolished;
Netherlands (cost-plus rulings) – amended to remove potentially harmful features;
Portugal (Madeira international business centres) – abolished;
Spain (Basque Country and Navarra coordination centres) – abolished;
Switzerland (administrative companies) -- under review;
Switzerland (service companies) – amended to remove potentially harmful features.

DISTRIBUTION ACTIVITY

Belgium (distribution centres) – amended to remove potentially harmful features;
France (logistic centres) – amended to remove potentially harmful features;
Netherlands (cost-plus and resale minus rulings) – amended to remove potentially harmful features;
Turkey (Turkish free zones) – not harmful.

SERVICE CENTRES

Belgium (service centres) – amended to remove potentially harmful features;
Netherlands (cost-plus rulings) – amended to remove potentially harmful features.

SHIPPING

Canada (international shipping regime) – not harmful;
Germany (international shipping regime) – not harmful;
Greece (shipping offices) – not harmful;
Greece (shipping regime law 27/75) – not harmful;
Italy (international shipping regime) – not harmful;
Netherlands (international shipping regime) – not harmful;
Norway (international shipping regime) – not harmful;
Portugal (international shipping register of Madeira) – not harmful.

MISCELLANEOUS ACTIVITIES

Belgium (ruling on informal capital) – amended to remove potentially harmful features;
Belgium (ruling on foreign sales corporation activities) – abolished;
Canada (non-resident-owned investment companies) – abolished;
Netherlands (ruling on foreign sales corporation activities) – amended to remove potentially harmful features;
Netherlands (ruling on informal capital) – abolished;
United States (foreign sales corporation regime) – abolished.

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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: Alan Cole
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: Mike Jones
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: Stuart Stobie
Tel: +852 2542 1177
Fax: +852 2545 0550
hk@SovereignGroup.com

Isle of Man: Paul Brennock
Tel: +44 (0)1624 699800
Fax: +44 (0)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

Singapore: Richard Wilson
Tel: +(65) 6222 3209
Fax: +(65) 6222 1525
sg@SovereignGroup.com

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

South Africa, Johannesburg: Alex Burger
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: Tennille Darville
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: Noel Otero
Tel: +598-2 900 3081
Fax: +598-2 900 1932
uy@SovereignGroup.com

contact

Editor: Christopher Owen

Publisher: Kamilian Limited
Email: report@kamilian.com
Website: www.kamilian.com

Printer: Pioneer Printers Limited
Website: www.pionprint.com.hk

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