39

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SOVEREIGN

report

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39

contents

introduction 3

4 european news

6 americas+ caribbean news

10 middle east, africa + asia news

12 fiscal news

14 legal news

16 in the press: **A Will is not the only way…**

17 profile: **HMRC reveals QROPS data**

18 contact + info

Editor Christopher Owen
Design Alan Pitchforth
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enquiries@kamilian.com
www.kamilian.com
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Happy Christmas and a prosperous New Year!

I take this opportunity to wish all our readers, clients and friends a very happy Christmas and a prosperous New Year. As we head to press with this edition of the Report there is much uncertainty over the financial health of the world, particularly in the Eurozone. For anyone lucky enough still to be making a profit it makes sense to use this time to maximise your return by getting your tax planning right. A review of your current structures may well pay dividends, so we encourage you to contact your nearest Sovereign office who can certainly help with this.

Bahrain office opens

I am pleased to report that our Bahrain office is now open under able stewardship of Nabil Khoury. His contact details are to be found on page 18 of this Report. Based in the magnificent World Trade Center complex in Manama, Bahrain is the most recent addition to our growing network in the Middle East. We expect to develop further in this region in the months to come.

Sovereign Art Foundation

The Sovereign Art Foundation has been particularly active in recent months. We launched the Sovereign African Art Prize in Jo'burg as part of the Johannesburg Art Fair, with the gala dinner and auction held at Tokara Wine Estate in Stellenbosch. This inaugural event, the first pan-African art prize, was won by Hassan Hajjaj from Morocco for his work "Rubbish Odalisque" (see below). He received US$25,000 prize money and the opportunity of a three-month residency at the Nirox Foundation in SA. All proceeds raised are pledged to The African Arts Trust.

"Rubbish Odalisque" by Hassan Hajjaj

chairman

In Europe, this year's event took place in Istanbul, which is fast becoming one of the world's most important art centres. The €25,000 prize was won by Bulgarian artist Kamen Stoyanov for his work "Guys, this not L.A. but it's a cool place too". The gala dinner and auction, held in a disused textile factory, was attended by over 500 people. We raised a significant amount that is being donated to the local Acik Kapi Foundation, which uses the arts as therapy and rehabilitation for young orphans.

As we prepare for Sovereign Asian Art Prize, the next issue of *The Sovereign Report* will contain a special supplement looking at the recent events held around the world. It will also profile just some of the good causes helped by the Foundation using the enormous amounts raised in recent years. On behalf of all the charities who benefited from its work, I offer my sincere thanks to all who have contributed to the Foundation in any way.

Family Investment Companies

Family Investment Companies (FICs) are the latest big news in UK estate planning but can be used by anyone, anywhere else in the world to equally good effect. FICs can enable families to pool investments, pass on wealth down the generations, retain control, keep taxes to a minimum and protect wealth. For a more in-depth review of FICs, please take a look at my *Daily Telegraph* column, reprinted here for *In The Press* on page 16.

And finally... Saying it with flowers

There seems to be no escape for Britain's top Revenue official Dave Hartnett, who has been accused of letting Goldman Sachs and Vodafone off multi-million-pound tax bills in undisclosed settlements. While the HM Revenue & Customs permanent secretary for tax was addressing the LexisNexis Tax Journal conference in the City of London, he was joined on stage by protestors dressed as executives from the aforementioned firms. They handed him bottles of champagne and flowers, saying "We love you Dave" and started singing "for he's a jolly good fellow, and so say Goldman Sachs".

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

European Commission to challenge Swiss tax deals

The European Commission said, on 27 November 2011, that it was set to challenge the bilateral tax agreements signed by the UK and Germany with Switzerland, which are intended to settle long-running disputes over tax evasion by UK and German nationals holding cross-border accounts with Swiss banks.

EC lawyers have concluded that both bilateral deals, which maintain traditional Swiss banking secrecy by regularising accounts without disclosing individual identities, are incompatible with existing EU rules. UK chancellor George Osborne has been told that he must renegotiate with Switzerland or face a writ at the European Court of Justice. Germany, which is facing domestic political pressure over its deal, is also seeking to initiate a new round of talks with Switzerland.

Under the agreements reached in August and due to enter into force in 2013, persons resident in the UK and Germany would be given one chance to make an anonymous lump-sum tax payment to settle retrospective tax liabilities. The tax rate would vary from 19% to 34% of the assets, depending on the duration of the client relationship as well as the initial and final amount of the capital. The assessment period would begin in 2000. Alternatively, clients could disclose their banking relationship in Switzerland to their home tax authorities.

Swiss banks would be required to make advance "guarantee" payments of CHF 500 million ($700 million) and CHF 2 billion ($2.8 billion) to the UK and German tax authorities respectively. These payments would be offset by the incoming withholding tax payments under the schemes and refunded to the banks.

In order to prevent new, undeclared funds from being deposited in Switzerland, the UK authorities would be permitted to submit up to 500 requests for information per year, while Germany would be permitted 750 to 999 requests for an initial two-year period.

Switzerland regards the bilateral treaties as a blueprint for agreements with other EU members, such as Italy and Greece, but the EC contends that the UK and Germany had no right to agree bilateral deals that, in parts, contradict the EU Savings Tax Directive and the existing EU-Swiss tax agreement and undermine the negotiating mandate given to the EC.

The EU is committed to a multilateral automatic exchange of information system, whereby countries hand over confidential data on demand to support tax evasion investigations. The US has also rejected offers of a withholding tax deal, having already secured data from more than 4,000 UBS bank clients.

"The Commission has been very clear that areas covered by EU legislation must not be included in bilateral agreements between member states and third countries," said a spokeswoman for EU tax commissioner Algirdas Semeta. "We will work to remove the parts that impinge on EU law."

Sovereign Comment

At the time of going to press the future of these agreements is in doubt, but they provide further confirmation, if any were needed, that the European authorities are pursuing untaxed assets in Swiss banks with the same zeal as their US counterparts. As we have long advocated, simply maintaining cash balances in undeclared bank accounts abroad is not tax planning. Anyone concerned about their own position should contact their nearest Sovereign office without delay to take steps to regularise their situation.

EU to begin on STD expansion

ECOFIN, the EU Economic and Financial Affairs Council, approved, on 12 July 2011, proposals from the European Commission to begin negotiating changes to agreements signed in 2004 by Switzerland, Liechtenstein, Monaco, Andorra and San Marino on the taxation of savings income received by European Union (EU) residents under the Savings Tax Directive.

The proposed changes would amend the equivalent procedures in these third-party countries to close current loopholes, to expand the application of the withholding tax, or automatic exchange of information, on a wider range of savings instruments such as pensions and life insurance products.

The revisions cover a number of areas, including taxation of interest payments channeled through intermediate structures, expansion of "interest payment" to include income from financial products substantially similar to debt claims and level treatment of investment funds irrespective of their legal forms.

Sovereign Comment

The proposed amendments are in addition to more far reaching changes to the Savings Tax Directive that have been discussed by all member states in recent years. As reported in previous editions, the original Directive did not apply to bank accounts held in corporate names but this is likely to be considered under any future revision. ECOFIN's focus has of course been on the wider Eurozone problems in recent months. It remains to be seen how swiftly pressure can be brought to bear on these states and others in terms of widening the scope of the Directive.

Isle of Man Foundations Act gains Royal Assent

Manx Treasury Minister Eddie Teare announced, on 16 November 2011, that Royal Assent had been given to a new Foundations Act, which provides for the establishment of foundations on the Island. Each foundation must be on a public register and have a local registered agent.

Foundations resemble trusts but also have a separate legal personality, similar to that of a company, thereby permitting holders of assets to have more direct involvement. Foundations also offer greater familiarity to those from civil law countries, as well as opportunities in commercial legal structures.

Jurisdictions such as the Isle of Man have been pushing to create foundation structures at a time when trusts, typically a feature of Anglo-Saxon law, have seen some of their benefits erode in places such as the UK. Jersey enacted a foundations law in 2009. Guernsey is drafting a similar law.

The Limited Partnership (Legal Personality) Act 2011 also received Royal Assent and came into force on 18 October 2011. This provides any new limited partnership, registered under the Partnership Act 1909, with the option of adopting a legal personality that is separate from that of its partners.

Transitional provisions included in the Act allow existing limited partnerships six months from the date on which the legislation was enacted in which to make an election to continue in existence as limited partnerships with separate legal personality.

Malta launches new high net worth individuals' scheme

Maltese Finance Minister Tonio Fenech announced, on 15 September 2011, a new high-net-worth individuals' scheme designed to attract people to Malta who will also contribute to the local economy.

It replaces the permanent residence scheme, which was suspended at the start of the year. Existing permanent residents will not lose their status unless they sell their property.

Under the new rules, property bought by foreigners will have to be worth a minimum of €400,000 (or €20,000 a year in rent), up from the previous minimum of €116,000, and purchasers will have to spend a minimum of 90 days per year living in Malta.

EU nationals will have to have recognised health insurance and pay an application fee of €6,000 to cover fees the government will incur to do the "fit and proper" test to check whether the applicant is "desirable". They will also have to pay 15% tax on foreign income and standard tax on any local income. The minimum tax payable will be €20,000 a year and €2,500 tax per dependent.

Non-EU residents will also have to keep renewing their visa every three months or post a financial bond of €500,000 and €150,000 per dependent, to acquire permanent residency after five years, at which time the money will be paid to government. The minimum tax payment will be €25,000 a year.

Fenech said that people who purchased property and never visited were abusing the previous scheme and its name had created legitimate expectations under EU laws on what it meant to be a permanent resident. Further, people who purchased property were entitled to other rights given to Maltese citizens and the potential future liabilities were great.

Sovereign Comment
The sudden withdrawal earlier this year of the previous Maltese residency scheme came without prior warning. It is good to see the government replacing it with a new set of rules, albeit that they are somewhat more onerous than those pertaining under the earlier version. Sovereign has considerable experience in preparing such residency applications as indeed it has for alternative jurisdictions around the world. Should you be considering residency in a new country as part of your planning, contact your local Sovereign office for more details of the schemes both within Europe and further afield.

ECOFIN postpones vote on "zero-10" tax systems

The European Council of Ministers failed to ratify, as anticipated, the recently-revised "zero-10" tax regimes of Jersey and the Isle of Man, after they were removed from the EU Economic and Financial Affairs Council's (ECOFIN) agenda for its meeting on 30 November 2011. The schemes will not now be formally adopted until January, said a spokeswoman.

Under zero-10 regimes, most businesses pay no corporation tax, while some sectors, such as banks, pay 10% and a few pay 20%. (The EU Code of Conduct Group on Business Taxation announced a review of Jersey and the Isle of Man's zero-10 schemes in 2009 in response to pressure from some EU member states, which viewed them as harmful.

ECOFIN had been expected to approve the revised zero-10 corporate tax schemes, following the recommendations of the Code of Conduct Group, which in September found them to be compliant with the EU code provided that the deemed distribution provisions in Jersey and attribution regime for individuals in the Isle of Man were both removed. As a result of these amendments, residents who are shareholders of island companies will pay personal income tax on any unallocated company profits.

On 29 October, the Code of Conduct Group also announced that its review into Guernsey's zero-10 corporate tax regime introduced in January 2008 – would restart. The Code of Conduct Group began its review in 2009 after the UK Treasury raised concerns about the regime not being compliant with the EU code. It has been on hold since May 2010 after Guernsey's parliament gave assurances that it would revise the strategy.

Sovereign Comment
The governments of the UK Crown Dependencies are eager to see the zero-10 issue resolved as soon as possible, to end the uncertainty about their corporate tax regimes. Despite this further delay, it is pleasing to see that the Code of Conduct Group has accepted their amendments and a resolution is in sight. As in the case of Gibraltar, reported in the last issue, clarity on the matter can only lead to a positive outcome.

Guernsey proposes new Image Rights Register

The Guernsey parliament approved, on 29 September 2011, a policy letter proposing the creation of the world's first Image Rights Register, which will enable registration of a registered personality right, a property right, which would also provide rights in the registered personality's associated images.

Registerable features of a qualifying personality will include a personal name and any other associated distinguishing indications – such as voice, signature, photograph, character or likeness – which identify the personality uniquely.

Qualifying personalities will include any living or deceased natural person and could extend to some non-living entities, such as fictional characters. A registered personality right relating to a living personality will have indefinite duration and can continue to exist after their death subject to regular renewal or validation of registration on the Register.

There will be creation of exclusive ownership rights which may be enjoyed and protected by the holder of a registered personality right and which may be assigned and otherwise dealt with as personality, subject to relevant registration requirements.

Drafting time was estimated at about four months and the Commerce and Employment Department, which put forward the plans, said it hoped the legislation would be in place before the London Olympics in 2012.

BVI moves to automatic exchange under EU Savings Tax Directive

The BVI government gazetted, on 12 July 2011, the Mutual Legal Assistance (Tax Matters) (Automatic Exchange Information) Order 2011, which changes the way that the jurisdiction complies with the EU Savings Tax Directive (STD).

The STD was designed to facilitate the exchange of information on individuals' savings income between the tax authorities of EU member states. EU member states were also required to implement the Directive in their offshore dependencies. The UK is responsible for implementation in its overseas territories and crown dependencies, including the BVI.

For a transitional period, when the STD was introduced in 2005, Austria, Belgium and Luxembourg were permitted to withhold tax from savings income payments instead of exchanging information. This option was also extended to the other participating countries and territories, and the BVI government elected to implement the withholding tax. The rate of withholding tax was set at 15% from 1 July 2005, rising to 20% from 1 July 2008 and reaching 35% from 1 July 2011.

The new Order provides that from 1 January 2012, the withholding tax option will no longer be available to BVI-based paying agents. As such, BVI institutions will be obliged to disclose the minimum information to the BVI Inland Revenue, which in turn will comply with the information exchange policy under the directive.

The minimum information required for these purposes comprises: the identity and residence of the beneficial owner; the name and address of the paying agent; the account number of the beneficial owner or, where there is none, identification of the debt claim giving rise to the interest; and information concerning the interest payment.

The changes will be most relevant to individuals who are resident in an EU member state and who maintain savings accounts with banks in the BVI. It will apply as of the tax year commencing 1 January 2011.

Sovereign Comment

This item should be read in conjunction with the piece on renegotiating the terms of agreements signed back in 2004 under the original terms of the Directive (see Europe page of this issue). It is interesting to note the BVI's switch to automatic exchange of information although, given its relationship with the UK, it is perhaps not altogether surprising. The attitude of jurisdictions such as BVI to any material changes relating to companies under the Directive should prove critical to the ultimate success of the European initiative. Future editions of *Sovereign Report* will provide regular updates.

americas+ caribbean

IRS nets $2.7 billion from offshore accounts

The US Internal Revenue Service announced, on 15 September 2011, that the 2011 Offshore Voluntary Disclosure Initiative (OVDI) had attracted 12,000 applications before its expiry the previous week, pushing the total number of voluntary disclosures up to 30,000 since 2009.

In total, the IRS said it had collected $2.2 billion so far from the 15,000 people who participated in the original 2009 Offshore Voluntary Disclosure Programme (OVDP), reflecting closures of about 80% of the cases. A further 3,000 applicants had come in after the deadline, but were allowed to participate in the OVDI, which gave US taxpayers with undisclosed assets or income offshore a second chance to get compliant with the US tax system and avoid potential criminal charges.

The IRS had so far collected an additional $500 million in taxes and interest as down payments for the 2011 programme — a figure that did not yet include penalties – to bring the total collected through the offshore programmes to $2.7 billion.

The two disclosure programmes also provided the IRS with a wealth of information on various banks and advisors assisting people with offshore tax evasion, which the IRS said it would use to continue its international enforcement efforts.

"By any measure, we are in the middle of an unprecedented period for our global international tax enforcement efforts," said IRS Commissioner Doug Shulman. "We have pierced international bank secrecy laws, and we are making a serious dent in offshore tax evasion."

US Treasury postpones FATCA implementation

The US Treasury announced, by Notice 2011-53 of 14 July 2010, that implementation of the Foreign Account Tax Compliance Act (FATCA), which targets non-compliance by US taxpayers through foreign accounts, would be deferred by one year.

Under FATCA, enacted on 18 March 2010 as part of the Hiring Incentives to Restore Employment (HIRE) Act, foreign financial institutions (FFIs) with US customers and foreign non-financial entities with substantial US owners must disclose information regarding US taxpayers directly to the IRS (Internal Revenue Service). Failure to disclose information will result in a requirement on non-US financial intermediaries to withhold a 30% tax on US-source income.

The FATCA reporting obligations were scheduled to come into force in January 2013. But the US government has come under pressure from foreign governments to dilute its provisions due to the compliance burden they would place on financial institutions. On 6 April, Algirdas Semeta, head of the European Commission's tax policy office, wrote to the US Treasury criticising FATCA's "onerous" disclosure provisions for European banks.

The US Treasury has now deferred the schedule by a year. The reporting requirements will begin in 2014. Withholding tax on dividends and interest will also be delayed until January 2014, while withholding tax on gross proceeds of asset disposals will be postponed until January 2015.

But FATCA's special due diligence requirements – which require banks to identify certain "high-risk" US accounts worth more than $500,000 – will take effect in 2013.

Sovereign Comment

Despite delaying the effective date for implementation, the proposed FATCA rules are likely to prove cumbersome and expensive to introduce for internationa practitioners everywhere. The affect on US taxpayers with financial assets overseas remains to be seen. A number of Sovereign offices around the world report that several banks with whom they deal now refuse to establish, or even continue holding, accounts for US nationals as a result. The FATCA rules combined with pressure on banks abroad, especially Switzerland, appear to be forcing financial institutions to consider that the risks of unwelcome attention from the US authorities simply do not justify the risk, as they see it, of managing such relationships for American clients.

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Curaçao approves new package of corporate measures

The Curaçao Parliament approved, on 15 September 2011, legislation as part of the island's tax reform process following the 2010 dissolution of the Netherlands Antilles that resulted in Curaçao becoming an autonomous country within the Kingdom of the Netherlands. The changes will generally come into force on 1 January 2012.

Although the overall tax regime remains broadly the same as that of the former Netherlands Antilles, certain areas have been specifically amended to improve the investment climate and boost international competitiveness.

The corporate income tax rate of 34.5% will be reduced to 27.5% and, although no draft legislation has been presented, the government intends to further reduce the rate to 15% for 2013 and 2014. Under the new rate, the current 70% participation exemption would result in an effective tax rate below 10%, potentially triggering anti-avoidance rules in other tax jurisdictions. The exemption will therefore be reduced to 63%, for an effective tax rate of 10.175%.

The reform measures provide for a new "transparent limited liability company" that is disregarded for Curaçao corporate income tax purposes, with all of its income and assets allocated to its shareholders. Transparency will be granted only upon application to either a public limited liability company (NV) or a private limited liability company (BV). This must be submitted by or on behalf of the company's board of directors and must contain a written power of attorney from each shareholder. If transparent status is granted, the company will not be eligible for benefits under a tax treaty.

To increase the flexibility of Curaçao private foundations, which are currently not subject to tax on income unless they carry out active business operations, the reform measures include a provision that will allow a private foundation to opt to be treated as an entity subject to corporate income tax at a rate of 10%. This is designed to make foundations more attractive for use in organisational structures involving jurisdictions that impose a subject-to-tax requirement and will also allow a foundation to benefit from the participation exemption.

Curaçao also plans to enact a Trust Ordinance that will make it possible to establish a trust under a trustee's authority for beneficiaries or for a particular cause. When this legislation becomes final, trusts will be able to elect to be subject to a corporate income tax rate of 10% (as is the case for private foundations under the reform measures).

The Netherlands Antillean Guilder is to remain in place for 2011, but the government intends to replace it with the Dutch Caribbean Guilder.

Sovereign Comment

Referred to locally as "10.10.10", last year's changes that saw the dismantling of the former territory known as Netherlands Antilles will inevitably result in differences in approach. Of particular interest is the change to the tax treatment of the Curaçao private foundation, which may provide new planning opportunities for a tried and tested vehicle.

americas+ caribbean

St Kitts & Nevis boosts Citizenship Programme

A government-approved development is now giving applicants under the St Kitts & Nevis Economic Citizenship-by-Investment programme the option to sell back their investment for the purchase price at the end of the "must hold" period.

Established in 1984, the programme imposes no residency requirements and permits visa-free travel to over 80 countries; moreover, St. Kitts & Nevis has no wealth tax, income tax or inheritance tax. Qualifying investors are simply obliged to invest a minimum of US$350,000 in designated real estate in St. Kitts & Nevis, which must be held for statutory five-year period.

Under a new scheme, investors can purchase a redeemable shares priced at US$400,000 within a designated development on St. Kitts. In exchange for a guaranteed option to re-sell the property back to the developer after five years, the applicant renounces any income or dividends from the company. On expiry of the "must hold" period, they can sell back their share or choose to retain ownership, at which time they will be entitled to revenue produced by the property.

Sovereign Comment

Dual citizenship passports can provide added freedom and flexibility in the best of times. In the worst of times they can offer you and your family with invaluable protection against political or economic instability in your home country. Contact your nearest Sovereign office should you wish to learn more about this particular scheme. We are able to put you in touch with the promoters directly.

ECSC changes Civil Procedure Rules

A number of changes came into force on 1 October 2011 to the Civil Procedure Rules of the Eastern Caribbean Supreme Court (ECSC), which regulate procedure in civil and commercial proceedings in all of the OECS States – Anguilla, Antigua, Dominica, Grenada, Montserrat, St. Lucia, St Kitts & Nevis, St Vincent & the Grenadines and the BVI.

The ECSC rules are loosely based on the English CPR, but with significant modifications. The new changes take the form of extensive revisions to the CPR, together with the implementation of ten new Practice Directions.

The key change is the broader provision for service out of the jurisdiction, and new provisions that permit the Court to dispense with service in an appropriately exceptional case, or to make an alternative order in relation to the "mode of service".

This will be of interest to those litigating in the OECS States, particularly the BVI where the majority of the 800,000-plus registered companies are managed by persons overseas but where service out of the jurisdiction upon their shareholders and directors has not previously been specifically provided for.

Similarly, the Insolvency Act 2003 provides for summary remedies against delinquent office holders, and the means by which preferences or transactions at undervalues might be impeached, yet there has been no obvious mechanism by which such claims might be served out of the jurisdiction.

Sovereign Comment

The effect of these changes is that it is likely that there will be a number of potential litigants, who would previously have been advised that they were unlikely to obtain permission to serve a claim form out of the jurisdiction, who will now be able to seek remedy through the BVI Courts.

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South African external company registration

The new Companies Act, which came into force on 1 May 2011, requires that a foreign company must register as an "external company" within 20 business days after it first begins to conduct business or non-profit activities in SA. This may impact the way foreign investors conduct business in the country.

A foreign company will be regarded as "conducting business" under the new Companies Act if: it is a party to one or more employment contracts in SA; or it is engaging in a course of conduct or it has engaged in a course or pattern of activities in SA over a period of at least six months that would lead a person to reasonably conclude that the foreign company intended to continually engage in business within SA.

Under the previous legislation, a foreign company was simply required to register as an external company within 21 days of establishing a "place of business" within SA – defined as "any place where the company transacts or holds itself out as transacting business and includes a share transfer or share registration office". Under this definition, it was possible for foreign companies to operate in SA without registering as an external company.

The new requirement means that practically every foreign company employing individuals in SA must now register and raises the question as to whether registration as an external company for company law purposes could automatically result in the creation of a permanent establishment (PE) for corporate income tax purposes.

South African residents are taxed on their worldwide income and a company will be treated as resident if it is incorporated, established or formed in SA, or if it is effectively managed in SA. Non-residents are taxed on a source basis. If the foreign investor were resident in a South African tax treaty partner country, they would be subject to tax in SA only if it has a PE in SA.

Sovereign Comment

This is one of the reasons why Sovereign rarely suggests external company registration of an offshore company. It is better to place an SA company as the owner of the property or activity in SA, with a shareholding externally, rather than have direct ownership or activity in SA by the offshore company. Foreign investors should consider carefully the potential corporate income tax implications of the South African external company law rules and obtain advice.

39

Hong Kong companies exceed 900,000 mark

The number of companies registered in Hong Kong at the end of June this year reached above 900,000 for the first time, according to figures released by the Company Registry on 17 July 2011.

The total number of active local companies registered was 912,242 as at 30 June 2011, up 48,480 from the end of 2010, while a total of almost 78,000 new local companies were registered during the first half of this year, an increase of 8.5% over the new companies registered in the second half of 2010 and 15% over the first half.

"The number of new companies incorporated continued to rise in the first six months of this year, with a monthly record averaging around 13,000," said Registrar of Companies, Ada Chung.

In the first half of 2011, 402 non-Hong Kong companies also established a place of business in Hong Kong to bring the total number registered to 8,342 by end-June.

Sovereign Comment

Passing such a milestone would have been impressive in any specialist corporate jurisdiction. Of particular note is that Hong Kong cannot be considered in any way to be an "offshore" territory; still the results speak for themselves. Sovereign has a commitment to Hong Kong – indeed Sovereign's second largest office by staff numbers is located there. Contact your closest Sovereign office for more details on the benefits of incorporating in this most exciting, and growing, jurisdiction.

Revised Indo-Swiss tax treaty comes into force

The revised Indo-Swiss tax treaty, which will allow India to seek specific bank information in cases related to tax evasion, came into effect on 10 October 2011. Under the previous treaty, India could only seek bank details in relation to tax fraud cases.

"It contains provisions on the exchange of information in accordance with international standards applicable at present," said the Swiss Federal Department of Finance.

The provisions of the agreement will apply in India to income originating in tax years that start on or after 1 April 2012. In Switzerland, they will apply to income originating in tax years that begin on or after 1 January 2012. In the case of the exchange of information, the provisions will apply to information referring to tax years that start on or after 1 January 2011.

The Swiss Parliament approved the revised treaty on 17 June and, under Swiss rules, bilateral tax treaties are subject to public scrutiny for a period of 100 days, which ended on 6 October. India signed an agreement with Switzerland to revise the treaty in August 2010.

Data from the Swiss National Bank shows that total deposits of Indian individuals and companies in Swiss banks stood at about $2.5 billion at the end of 2010.

With the issue of black money hidden abroad by Indians being used to target his government by opposition parties, Indian Prime Minister Manmohan Singh called, at the G-20 summit in Cannes in November, for the world's 20 leading economies to take the lead in agreeing to automatic exchange of tax related information with each other without any discrimination for tax evasion or fraud.

India has adopted a three-pronged approach to tackle black money. First, it has completed negotiation of Tax Information Exchange Agreements (TIEAs) with 16 tax havens. Second, it has initiated the process of negotiation with 75 countries to broaden the scope of the 'Exchange of Information' Article in double tax treaties, either by way of protocols to existing treaties or new treaties. As of September, negotiations or renegotiations with 40 countries were completed.

Finally, section 94-A of the Income Tax Act 1961, now empowers the government to designate any territory outside India, in case of lack of effective exchange of information, as a notified jurisdictional area. Transactions with residents of such territories are subject to higher withholding, certain disallowances and transfer pricing regulations.

Offshore Yuan trade in Hong Kong grows

Hong Kong chief executive Donald Tsang said, on 11 November 2011, the Special Administrative Region was "making good progress" as China's premier offshore global trading centre for the yuan.

Speaking on the sidelines of Asia-Pacific Economic Cooperation (APEC) meetings in Hawaii, Tsang said deposits had reached 622 billion yuan ($97 billion) by the end of September and he estimated that trade settlement handled by Hong Kong banks would exceed 1.5 trillion yuan this year.

"Since the launch of renminbi (yuan) banking in Hong Kong in 2004, the scope of business and the pool of renminbi liquidity have expanded rapidly," he said. "We are making good progress."

Hong Kong's role as the premier offshore centre for the yuan trade was outlined in China's 12th five-year plan earlier this year and China is understood to be stepping up efforts to increase overseas use of the yuan, partly to reduce the country's exposure to the US dollar and to allow the currency to take on a greater global role in line with its trade profile.

The move has been welcomed by China's key trading partners such as the US, which say the yuan is undervalued, making Chinese exports cheaper on world markets and thereby gaining an unfair trade advantage.

Hong Kong introduced yuan bonds in 2007 and yuan trade settlement in 2009. Banks in Hong Kong can now offer a range of yuan services to personal and corporate customers.

"We look forward to playing a full and pivotal role in the gradual liberalisation of the mainland currency," Tsang said. "Not only will this firm up Hong Kong's financial services sector in times of global uncertainty, it will, I believe, provide stability and opportunity to the global financial system."

Beijing has recently taken small steps to relax controls on the currency and increase its use in global trade as it tries to reduce China's exposure to the dollar.

Last month, authorities announced rules to allow foreign companies to use yuan raised overseas to invest in China, which analysts said was a positive step for increasing cross-border flows in the currency. Singapore has voiced its ambition to become the secondary yuan trading centre after Hong Kong, as the Chinese currency gains broader global usage.

China extends social security contributions to foreigners

China's Ministry of Human Resources and Social Security finalised and promulgated, on 8 September 2011, rules that require foreign individuals working in the country to contribute to China's social security system. The rules applied as from 15 October 2011.

As a result, all foreign individuals who legally work in China under a work permit, residence permit or permanent residence certificate must participate in the Chinese social security system, unless an exemption is provided under a social security totalisation agreement between China and the home country of the individual.

Employers must report relevant information relating to foreign individuals working in the PRC to the local social security authority in a timely manner and employers are required to register all qualifying foreign individuals working in China with the local social security authority within 30 days from the date an application is made for a work permit.

In addition to foreign individuals that have work and residence permits, the final rules require individuals who have obtained permanent residence status in China to participate in the social security scheme.

Sovereign Comment

These rules will have a significant impact on multinationals, especially those with many foreign employees/assignees, whether hired locally or under secondment arrangements, and will create additional costs and administrative burdens. They also, however, also provide a legislative basis for foreign individuals who plan to work in China for a longer period to participate in the social security system and to benefit from the schemes in the long term.

China currently only has one totalisation agreement – with Germany – although negotiations are underway with other major jurisdictions. As a result, most foreign individuals will have to participate in the PRC social security system. Residents from Hong Kong, Taiwan and Macau were included in the draft rules, but omitted from the final rules, so it is uncertain as to whether they fall within the scope of the new rules.

Hong Kong clarifies Chinese dividends withholding rate

The Hong Kong Financial Services and the Treasury Bureau announced, on 4 July 2011, that the HK Special Administrative Region government had received a response from China's State Administration of Taxation to clarify the tax payable to the mainland for dividends paid by mainland companies to individual investors in Hong Kong.

A Bureau spokesman said: "The reply of the State Administration of Taxation notes that when non-foreign investment companies of the Mainland which are listed in Hong Kong distribute dividends to their shareholders, the individual shareholders in general will be subject to a withholding tax rate of 10% with reference to the arrangement for the avoidance of double taxation signed between Mainland China and Hong Kong. They do not have to make any applications for entitlement to the above-mentioned tax rate.

"For shareholders who are residents of other countries and whose home countries have reached an agreement with China on an applicable withholding tax rate higher or lower than 10%, they have to follow the bilateral tax agreement in paying tax in connection with dividends paid by Mainland companies listed in Hong Kong."

The Stock Exchange of Hong Kong is to issue a letter of explanation to listed companies.

Sarkozy call to ostracise "tax havens" at G-20 Summit

French president Nicolas Sarkozy called on 11 jurisdictions, including Switzerland and Liechtenstein, to be ostracised as "tax havens". He named them in a speech at the conclusion of the Cannes G-20 summit on 4 November 2011.

"We do not want any more tax havens," said Sarkozy. "The message is very clear, countries which persist in being tax havens will be ostracized by the international community."

A communiqué issued by the French Presidency of the G-20 summit, said the OECD's Global Forum on Transparency and Exchange of Information for Tax Purposes had identified 11 jurisdictions with serious shortcomings: Antigua and Barbuda, Barbados, Botswana, Brunei, Panama, Seychelles, Trinidad and Tobago, Uruguay, and Vanuatu did not have a suitable legal framework for the exchange of tax information and did not qualify for the phase 2 review; Switzerland and Liechtenstein did not qualify for phase 2 until they remedied certain deficiencies identified by the Global Forum.

"The G-20 countries have solemnly recommitted to promote compliance with the international tax and financial information exchange standards and to use all the countermeasures available to them to combat tax havens and non-cooperative jurisdictions that do not comply with these standards," said the statement.

"In tax matters, the countermeasures include tax penalties on counterparties in transactions with tax havens. Taking this action forward, the G-20 has called on the FATF and the OECD to step up their joint work on corporate and trust transparency in tax and money laundering matters."

All the G-20 governments signed up to the Multilateral Convention on Mutual Administrative Assistance in Tax Matters. Drawn up by the OECD and the Council of Europe, the Convention includes automatic exchange of information, multilateral simultaneous tax examinations and international assistance in the collection of tax due. It also imposes safeguards to protect the confidentiality of the information exchanged. Previously only seven of the G-20 members had signed.

Jeffrey Owens, director of the OECD's centre for tax policy and administration, said: "Now that the G20 countries have led by example, we expect other countries to sign the convention," he added. "As the membership expands, so the effectiveness of the convention will increase. Over the coming months we will be working with developing countries so that they will rapidly be in a position to sign the convention."

A survey of 20 countries conducted by the OECD showed that earlier measures to deter tax evasion had resulted in 100,000 individuals paying a total of $14 billion in unpaid tax on assets worth between $120-150 billion. "That is just the tip of the iceberg." said Owens.

France introduces new tax on high incomes

The French government announced, on 24 August 2011, that it is to impose an extra tax of 3% on annual income above 500,000 euros (US$721,000). The tax increase came after some of France's wealthiest citizens called on the government to tackle its deficit by raising taxes on the rich.

French Prime Minister Francois Fillon said the new tax would remain in place until France reduces its budget deficit back within the EU's intended limit of 3% of GDP, which should occur in 2013. France plans to trim its public deficit to 5.7% this year, 4.6% next year and 3% in 2013.

"This is a rigorous policy that will allow France to remain relaxed," Fillon said. "Our country must stick to its [deficit] commitments. It's in the interest of all French people."

Sixteen executives, including Europe's richest woman L'Oreal heiress Liliane Bettencourt, posted an open letter on the website of the French magazine Le Nouvel Observateur in which they offered to pay a "special contribution" in a spirit of "solidarity". Other signatories Christophe de Margerie of oil firm Total, Frederic Oudea of bank Societe Generale and Air France's Jean-Cyril Spinetta.

They said: "We, the presidents and leaders of industry, businessmen and women, bankers and wealthy citizens would like the richest people to have to pay a 'special contribution'. When the public finances deficit and the prospects of a worsening state debt threaten the future of France and Europe and when the government is asking everybody for solidarity, it seems necessary for us to contribute."

Sovereign Comment

We certainly live in interesting times when citizens volunteer to pay more tax! We cannot be sure how influential the group's suggestion was on the government's decision to impose this special tax. Nevertheless, it is certainly the case that thus far France has avoided much of the civil unrest seen in other European states as austerity budgets become the norm in order to reduce the massive debts that have built up in almost every EU country. We have also reported in recent editions on other developments in France, particularly as they result to foreign property owners.

39 fiscal

Jersey amends tax 'cap' to attract more HNWIs

The States of Jersey approved, on 23 July 2011, amendments to its 1(1)k regime for high net worth individuals to remove the distinction between income earned in Jersey and that realised elsewhere. It was argued that the tax differential discouraged wealthy individuals from keeping and investing their wealth on the island.

Under the revised regime, new 1(1)k residents will be taxed at 20% on the first £625,000 of all of their worldwide income and 1% on all income thereafter. They are also required to pay a minimum tax liability of £125,000.

Previously, 1(1)k's paid 20% on all of their Jersey-sourced income, as well as on just the first £1m of their foreign-sourced income. After that, they paid only 10% on the next £500,000, and 1% on the remainder. Additionally, the minimum amount they were required to pay was £100,000.

Jersey treasury minister Philip Ozouf said this would make for "a simple and competitive tax structure to encourage high net worth individuals to bring their investment and businesses to Jersey."

Sovereign Comment

Readers should refer to the news item on the Europe page for latest details of the HNWI residency scheme in Malta. A number of European centres – Gibraltar being another – are keen to attract new wealthy residents to their shores because such people are generally considered to "be good" for the local economy. Jersey's amendments to its rules are clearly aimed at attracting individuals who will actually reside in the island and invest in the local economy at a time when the global economic crisis has put revenues under pressure.

European Commission sets out plans to eliminate double taxation

The European Commission adopted, on 11 November 2011, a Communication setting out its plans to eliminate double taxation – and double non-taxation – of EU residents by member states which, it said, contradict the spirit of the single market.

Currently under EU law, there is nothing to oblige Member States to prevent non-discriminatory double taxation and the Commission said existing measures such as bilateral and multilateral double tax treaties did not provide adequate protection for citizens and businesses due to various shortcomings – too narrow scope, lack of uniformity in provisions, administrative burdens and long time-lines for dispute resolution.

A public consultation carried out by the Commission found that more than 20% of reported cases of double taxation of businesses were worth over €1 million, while for individuals, more than 35% of double taxation cases were worth more than €100,000.

Algirdas Šemeta, Commissioner for Taxation, said: "Double taxation is one of the biggest tax obstacles to the Internal Market, and can no longer be overlooked."

As an immediate first step to strengthen existing legislation against double taxation, the Commission adopted a simultaneous proposal to improve the Interest and Royalties Directive. This aims to reduce the instances of one Member State levying a withholding tax on a payment, while another Member State taxes the same payment.

Other areas in which the Commission intends to propose specific solutions to double taxation problems include cross-border inheritance tax in the near future and dividends paid to portfolio investors later on.

The Commission will also work on other possibilities to help eliminate cross-border double taxation, such as creating an EU Forum to develop a code of conduct on double taxation and a binding dispute resolution procedure for unresolved double taxation cases.

With regard to double non-taxation, which causes considerable losses to public revenues, the Commission said it would launch a consultation to gauge the full scale of the problem. On the basis of this consultation, it would determine the most appropriate and effective measures and come forward with solutions next year.

The Commission will submit the Communication on Double Taxation to the European Parliament, Council and European Economic and Social Committee for discussion and the Interest and Royalty Directive proposal to Council and the European Parliament.

Portugul Budget targets offshore companies and property

Portugal's "austerity Budget", announced on 14 October 2011, contained a number of proposed measures targeting offshore companies, and a document proposing rectification to the 2003 general property reform.

The Municipal Tax (IMI) rate charged on a property held by a company in a blacklisted jurisdiction is to be raised from 5% of the tax department value to 7.5%, while the Property Transfer Tax (IMT) levied on the acquisition of property by a blacklisted company is to increase from an 8% flat rate to 10%.

The time limit for tax corrections involving blacklisted jurisdictions is also increased from the standard term of four years to 12 years, while the time limit for tax collections is increased from eight years to 15 years.

Together with the Budget was a document proposing rectification to the 2003 general property reform, which established a 10-year period to achieve a general revaluation for tax purposes of all property in Portugal. This is to satisfy a promise made to the EU and IMF in return for economic assistance that a general revaluation should be concluded by the end of 2012.

As from 1 January 2012, current rules to value existing property will be revoked and there will be a general revaluation of all properties that have not been revalued since 1 January 2004 and that, as of 1 December 2011, are not undergoing revaluation under the IMI Code (CIMI).

It will not be obligatory for the property to be visited for revaluation purposes and the new values will come into effect on 31 December 2012 for payment of IMI in 2013. There will be a 30-day period for lodging an appeal. A second valuation, at the taxpayer's expense, must be made within 60 days of original notification.

Sovereign Comment

Many properties that have been registered with the same title holder for many years including those held by companies could see a dramatic increase in the tax value. Fortunately there has been a "capping" limit written into the legislation whereby any increase in the IMI payable for the years 2012 and 2013 is limited to the greater of either €75 or one-third of the difference between the IMI payable following the general valuation and that due for the year 2011.

Spain to reinstate temporary wealth tax

Spain's "wealth tax" (Impuesto Sobre el Patrimonio) was reintroduced, on 17 September 2011, for tax years 2011 and 2012 by temporarily repealing a 100% "tax allowance" that has been available since 2008. The new measures also provide new thresholds for application of the tax.

The Spanish wealth tax is based on the net assets held as of 31 December each year, and the rate ranges from 0.2% to 2.5%. Residents are subject to the wealth tax on their worldwide assets, while non-Spanish tax residents are subject to the wealth tax only for the assets located in Spain.

The reintroduction targets the richest people (around 160,000 resident taxpayers), so the minimum taxable wealth levels have been raised substantially to ¤700,000 per person, plus a maximum of ¤300,000 per person for their habitual residence (applicable only to residents).

The wealth tax is collected by the different "autonomous communities" in Spain, which are authorised to modify the minimum tax exemption, rates and allowances.

Sovereign Comment

As this edition goes to press, Spain has just elected a new government under Mariano Rajoy whose Partido Popular was swept into power mainly as a result of opposition to harsh new austerity measures. We await the new government's financial plans with considerable interest.

Cayman fund directors each found personally liable for $111 million

The Grand Court of the Cayman Islands, on 26 August 2011, found two directors of a failed hedge fund guilty of "wilful neglect or default" in exercising their supervisory powers as directors and, for the first time, made them personally liable for corporate losses. They were ordered to pay $111m each in damages to the fund's liquidators.

In *Weavering Ltd v Peterson & Ekstrom*, the Weavering Macro Fixed Income Fund had been incorporated in the Cayman Islands in 2003 as an open-ended investment company with a share listing on the Irish Stock Exchange (ISE). The investment manager was Weavering Capital (UK) Ltd, which was indirectly owned and controlled by Magnus Peterson, a former head of global trading at Swedish bank SEB.

In March 2009 the Fund went into liquidation after it emerged that $637m out of the $639m actively traded was held, in breach of the fund's investment criteria, in a single position with another Weavering vehicle based in the BVI, also controlled by Magnus Peterson.

ISE rules required the appointment of two independent directors to the board. Peterson appointed his younger brother, Stefan Peterson, and their 79-year-old step-father, Hans Ekstrom. Established as a limited company, the fund's directors were fully indemnified in respect of corporate losses, unless as a result of a director's "wilful neglect or default".

The Court heard that Peterson and Ekstrom "went through the motions of appearing to hold regular quarterly board meetings" and "provided an 'administrative service' in that they signed documents or took responsibility for documents when asked to do so by Magnus Peterson without making any enquiry or attempt to understand their content."

The Court found that Peterson and Ekstrom had wilfully neglected their duties as directors or defaulted in their discharge of them. Being aware of the existence of a duty to supervise the fund's affairs, they had done "nothing, and carried on doing nothing for almost six years". They had failed to discharge their duties by "signing whatever documents that were put in front of them without reading them, or, if they did read them, without applying their minds to their content."

The net losses flowing from this failure were assessed by the court be not less than $111 million. Damages were awarded against each defendant in that sum.

Sovereign Comment

This case demonstrates the importance that should be placed on the duties provided by company directors across the financial services sector. Perhaps this story – and those staggering fines – is of most interest to independent third party corporate directors and indeed firms such as Sovereign, but it should also be considered by clients who resent the close involvement of third-party directors into the affairs of companies they are asked to manage. It is likely that this result will be used in the future as a case study when discussing such matters with clients.

39 legal

UK Court of Appeal rules on *Huitson and Shiner*

The UK Court of Appeal handed down, on 25 July 2011, its judgments in Huitson and Shiner – two cases where the claimants argued that retrospective changes to the taxation of foreign partnerships were contrary to the European Convention on Human Rights and the free movement of capital guaranteed under the EC Treaty.

In both these cases, the individuals had entered into marketed tax avoidance schemes that involved the use of the UK-Isle of Man tax treaty and legislation then in force to generate income from UK activities that were free of UK income tax. The legislation was changed in 2008 to close the loophole and was given retrospective effect.

In dismissing both applications, the Court of Appeal stated that the purpose of the retrospective amendments was to give effect to "a justified fiscal policy" of maintaining a fair approach to all taxpayers in the UK. In balancing the rights of the general body of taxpayers against those of the claimants, the court decided that the liability to pay tax arising under the retrospective legislation was no more an infringement on the rights of the claimants than the usual obligation on ordinary citizens to pay tax in the country in which they are resident.

Regard was also paid to the fact that the tax treaty was used to avoid to income tax entirely on that portion of the income earned by the claimants through the trusts.

New Zealand Supreme Court backs taxman

The NZ Supreme Court affirmed, on 24 August 2011, a lower court's holding that two orthopedic surgeons who conducted their practices through corporate and family trust structures had avoided tax by diverting salary to company income taxed at a lower rate.

Two orthopaedic surgeons, Ian Penny and Gary Hooper, declared annual incomes of between NZ$655,000 and NZ$832,000 in the years prior to the hike in the top personal tax rate to 39% in April 2000. After that date, they declared personal incomes of between NZ$100,000 and NZ$120,000, while channeling the rest through companies they had established to employ themselves, and distributing that income to their families through family trusts.

The tax authorities contended that the salaries paid to the men were artificially low and that the use of the structures in this manner constituted a tax avoidance arrangement under the Income Tax Act 1994 (ITA). The authorities made assessments increasing the taxable incomes of both men for the 2002, 2003 and 2004 tax years. The total tax avoided amounted to no more than NZ$90,000 each, but the principles saw the case go all the way to NZ's highest court.

In 2009, the High Court sided with the taxpayers, holding that the ITA did not require the taxpayers to derive the practice's profits as personal income, but last year a majority of the Court of Appeal reversed the decision and held that the incorporation of the practices and the payment of salaries at artificially low levels constituted tax avoidance.

The Supreme Court agreed. The finding of tax avoidance turned on the "single step" taken by both taxpayers to place themselves on "each side of the employment contract relationship (as controlling director of the employer and as employee) in setting an artificially low level of salary which had the effect of altering the incidence of taxation".

"If the setting of the annual salary is influenced in more than an incidental way by a consideration of the impact of taxation, the use of the structure in that way will be tax avoidance," the judges said.

Gaines-Cooper loses appeal over residency

The UK Supreme Court dismissed, on 19 October 2011, the appeal by international businessman Robert Gaines-Cooper against the Court of Appeal's decision that he was a resident of the UK despite spending most of his time in the Seychelles.

The dispute centred on IR20, which was the UK revenue's guidance on what constitutes residency for tax purposes. Gaines-Cooper claimed to have followed the guidance and stayed out of Britain for a sufficient number of days every year to qualify as a non-resident.

But the Revenue argued that counting days was irrelevant because Gaines-Cooper had not left Britain "permanently or indefinitely" by making a distinct break, which meant he was resident. He had maintained extensive social and domestic ties to the UK, including a family home in Henley-on-Thames and a UK-based collection of Rolls-Royces, as well as making regular visits that included Royal Ascot and shooting parties.

The Supreme Court, by a 4-1 majority, dismissed Gaines-Cooper's appeal on the grounds that a "proper construction" of IR20 did not support his case and the argument that the Revenue had departed from the IR20 guidance was "far too thin and equivocal".

Although the guidance on how to achieve non-residence "should have been much clearer", it considered that a sophisticated taxpayer would have concluded that he had to make a "distinct break" from the UK in order to become non-resident.

Lord Mance dissented; saying no requirement for "a distinct break" had been expressed and other factors, including the day-count proviso, pointed away from such a requirement.

Gaines Cooper said in a statement: "The judgment I have received today is a disappointment to me and to my family. I also consider it to be a blow for all UK taxpayers who have relied on HMRC's published guidance when planning their tax affairs. My next step is to seek the views of my legal advisers with a view to referring my case to the European Court."

Sovereign Comment

Although the Supreme Court ruling could affect the outcome of hundreds of cases that are still in dispute, the issues at stake may soon be only of historic interest. The UK Treasury released, on 17 June 2011, two major consultation documents: one proposing the establishment, for the first time, of a statutory residence test (SRT) for tax purposes; the other, proposing an increase in the annual tax charge for long term non-domiciled individuals that are resident in the UK.

39 legal

Importance of substance for Cyprus structure

A Russian court found, on 30 June 2011, that a common royalty scheme – which involved a Cyprus company as an intermediary licensing vehicle between a BVI holding company and a Russian operating entity – had no business substance. It concluded that the Cyprus company was interposed merely in order to gain access to unjustified tax benefits.

In Russia, the judicial concept of an "unjustified tax benefit" is similar to a General Anti-Avoidance Rule and is primarily used to challenge purely artificial structures where the only aim is to obtain a tax benefit that is not justified by a sound business purpose.

In case No. 60-32327/2010-!8, the Russian tax authorities assessed, during a tax audit of the years 2006-2008, whether a Russian corporate taxpayer had incorrectly deducted more than RUB470m (USD15m) for a trademark. The payments had been made to a BVI company through a Cypriot sub-license company.

The BVI company had purchased the trademark from a Russian individual, who was a director of the parent company of the taxpayer. Prior to transferring the trademark, the Russian companies had not paid royalties for its use. The BVI company had granted a non-exclusive right to use a trademark to a Cypriot company, which then granted the non-exclusive right to use the trademark to the Russian taxpayer. The initial royalties far exceeded the purchase price of the trademark.

The Federal Arbitration Court of the Urals Circuit stated that, in such a case, a thorough investigation must be conducted as to whether or not such a series of transactions has a purpose other than merely tax savings. The findings of the lower courts in the taxpayer's favour had not been so substantiated.

The Court took into account information obtained through Interpol that the beneficial owner of the Cypriot company was a woman cohabiting with the former owner of the trademark, such that it could be deemed to be affiliated. As a result, it dismissed the decisions of the lower courts and remanded the case to the trial-court level for consideration de novo of the issues involved in this dispute.

Sovereign Comment

This case shows once again how vital it is for any "royalty routing" scheme to be structured correctly. In particular, it shows the importance of demonstrating proper substance and that the relationship between the owners of the companies must be carefully considered. Our Cyprus office has extensive experience in establishing structures in this area and it more important than ever that the right questions are asked at the outset in order that the right solution is offered.

Swiss Supreme Court finds UBS disclosure lawful

The Swiss Federal Supreme Court ruled, on 15 July 2011, that the disclosure of UBS customer data by the Financial Market Supervisory Authority (FINMA) to the US Department of Justice was lawful. This reversed the decision of the Swiss Federal Administrative Court and upholds FINMA's order.

In February 2009, FINMA ordered that the data of 255 UBS customers be disclosed to the US DoJ as a protective measure under articles 25 and 26 of the Banking Act. It proceeded on the basis that, if this data had not been disclosed, the US Department of Justice would have filed an indictment against UBS that could have caused the bank to collapse and had serious repercussions for the Swiss economy.

UBS customers filed a claim in the Swiss Federal Administrative Court, which in January 2010 declared FINMA's decision to be unlawful. FINMA appealed to the Swiss Federal Supreme Court.

The Swiss Federal Supreme Court confirmed the legal opinion of the Swiss Federal Administrative Court that the Swiss Banking Act did not provide sufficient legal grounds for encroaching on banking secrecy, but said that government authorities could, in the absence of a specific legal foundation, act on the basis of the "general police powers clause" to avert serious imminent risks to fundamental legally protected interests.

The Court held that this applied to FINMA, as far as it acted in agreement and with the consent of the Swiss Federal Council.

39

in the press:

A Will is not the only way...

A version of this article by Sovereign Group chairman Howard Bilton first appeared in The Daily Telegraph.

Nobody likes to dwell on his or her own mortality. In the UK, two-thirds of people die without leaving a will. I presume the figure is similar in other countries. In the majority of cases this may not be too much of a problem – there is little to bequeath and it automatically goes to the next of kin. But for those with large, complex estates, it would be a major problem. Fortunately such people generally take a little more care over their wealth and how it is passed on.

The alternative to a will is generally a trust. Trusts can have huge advantages because they allow the distribution of the wealth to be controlled by the trustees over a long period – so that children do not suddenly get a huge lump sum of cash or, should a surviving spouse remarry, to ensure that the bulk of the capital is preserved for the deceased's heirs and chosen beneficiaries.

Setting up a trust also forces the "settlor" to put their affairs in order early by transferring the assets to the trustees, thereby avoiding the worry, expense and delays of probate. Even a simple estate can cost up to 6% of its value in fees to administer and rarely takes less than two years to resolve. This benefits nobody – apart from the lawyers. Trusts provide a means of avoiding all that.

The disadvantage of a trust is that it involves… well… a level of trust. Assets have to be passed over to trustees and the settlor loses control. In a previous article I wrote about the joys of private trust companies. These provide a method of setting up a trust and retaining a good degree of control. They remain attractive and are being used increasingly by the sophisticated client.

There is another option and one that is increasingly being used by UK-domiciled persons who are restricted in their ability to transfer assets into trust by the 20% lifetime inheritance tax charge that applies to substantial transfers. Known as Family Investment Companies (FICs) in the UK, they can also be referred to as Common Law Foundations, because they are similar to the civil law foundation found in Liechtenstein and elsewhere but much easier to understand by those from common law systems.

An FIC is a company. Companies are usually limited by shares, which have three important characteristics: the right to vote and therefore control the company; the right to receive income in the form of dividends; and the right to the capital and the underlying assets owned by the company. Usually a share carries all three rights but it is also possible for it to carry only one or two of these three. By splitting the rights and obligations we can create interesting results.

For example, Mr. A is a UK national living in Hong Kong. He does not intend to spend the rest of this life in Hong Kong, so is almost certainly UK-domiciled and subject to UK IHT on his worldwide estate. His first preference would be to pass the assets into trust to avoid UK IHT but this would attract the 20% charge. He could of course gift his assets away and, provided he lives for at least seven years, avoid UK IHT and the 20% charge – but that would leave him reliant on his beneficiaries. Neither alternative is attractive.

Instead we set up an FIC. Mr. A is issued with all the voting shares and therefore keeps total control. He also retains, jointly with his wife, the income producing shares because he wants to maintain their lifestyle. The capital shares can be given away to his wife and children whilst he is in good health. This structure means that all his assets are conveniently held together so his executors do not have to locate, take control of and administer them according to the will. UK IHT is massively reduced because he has given away the capital seven years before death. The income producing shares will have some value but minor compared to the capital shares. Sweet and simple.

This type of structure would be effective for most persons who are in danger of being subject to inheritance tax or estate duty in their home country or anywhere else in the world. There is no estate duty in Hong Kong but residents will often have estate duty considerations in their county of birth and assets are frequently charged to estate duty in their country of location irrespective of who owns them. An FIC can remove these liabilities because the company does not "die" so there is no change of ownership.

The FIC will also be of relevance to those who have parents back in their home county with wealth to pass on. We frequently asked whether we can help reduce estate duties. Funnily enough the beneficiaries are often more concerned about this! There is nothing to stop a UK resident from setting up one of these structures. For most it will not give income or capital gain tax advantage without further planning but that is not the aim. It is a way of eradicating, or considerably reducing, estate duties.

An FIC can further be refined by using a company limited by guarantee or a company limited by both guarantee and shares. Most people will be familiar with guarantee companies even if they do not know it – they are the basis of most clubs and societies. When you join a club you become a member (for life or as long as you maintain membership), rather than a shareholder, of a company limited by guarantee. If the voting and income rights of an estate are therefore held by members rather than shareholders, those rights would expire on their death and new members could be elected, effecting a transfer without the need for further procedure or probate. Hybrid companies, which can issue both shares and memberships, therefore permit the various rights and obligations to be packaged to suit the circumstances of the family.

FICs are the latest big news in UK estate planning but can be used by anyone anywhere else in the world to good effect. They don't remove the need for a will, because there will always be personal assets outside the structure, but they do provide a convenient and relatively cheap and simple method of dealing with the bulk of a person's estate.

HMRC QROPS data: Australia, New Zealand and Guernsey dominate market

Data from Her Majesty's Revenue & Customs (HMRC) shows that during the first half of 2011 there were more pension transfers into Qualifying Recognised Overseas Pension Schemes (QROPS) in Guernsey than any other jurisdiction worldwide.

The HMRC figures show that of the total number of pension transfers out of the UK into QROPS between 1 January and 30 June 2011, 32% went into QROPS based in Guernsey. New Zealand was the second most popular destination at 28%, Australia third on 20% and then the Isle of Man at 5%, followed by Hong Kong and Malta both on less than 1%, with the remainder a combination of smaller numbers to a variety of other centres.

HMRC made a series of changes to the UK pension system from 6 April 2006 – known as "A" day. The overhaul included withdrawing the existing agreements for the transfer of UK pension rights to overseas schemes and meant that, in effect, this would only be possible if the receiving scheme was recognised by HMRC as a QROPS. However, there has been a lack of independent data about the marketplace until the HMRC released these figures following a freedom of information request.

The figures show that the value of funds transferred into QROPS globally was £121.5 million in 2007, before trebling to £358 million in 2008 and then rising to £366 million in 2009 and £471 million in 2010. That took the cumulative total of funds transferred of more than £1.3 billion by the end of last year and it is projected that the amount transferred during 2011 could pass the £500 million mark.

The HMRC figures for numbers of transfers from 2007 through to the end of June 2011 show that 47% have been made to Australia, 23% to New Zealand and 10% to Guernsey, followed by 2% to the Isle of Man, 1% to Hong Kong and less than 1% to Malta, with the remainder a combination of smaller numbers to a range of other centres.

Guernsey differs from Australia and in part New Zealand, in that it is primarily a "third country" QROPS destination, meaning that most of the QROPS transferred to the Island are for individuals who have left the UK to live elsewhere, such as in Europe or Asia.

Australia's QROPS market is comprised almost exclusively of those going to the country to live, while the New Zealand transfers are a mixture of third-country QROPS and those of individuals moving permanently from the UK to New Zealand.

Peter Niven, chief executive of Guernsey Finance, the promotional agency for the Island's finance industry, said: Since the QROPS regime was established back in 2006, it has been clear from anecdotal evidence that the industry has seen massive growth and that Guernsey has become one of the leading jurisdictions globally however, our understanding of the market has been limited by the lack of independent data. Therefore, the publication of these figures is long overdue but hugely welcomed and of course, it is very pleasing to see that Guernsey leads the way in terms of numbers of transfers at the present time.

> "Our understanding of the market has been limited by the lack of independent data. Therefore, the publication of these figures is long overdue but hugely welcomed."

Sovereign Trust (Channel Islands) Ltd (STCIL) is the Guernsey operation of The Sovereign Group. STCIL is licensed by the Guernsey Financial Services Commission for the provision of fiduciary services. In addition to corporate and trustee work, the company provides a complete range of professional and highly tailored pension services to private individuals and companies.

QROPS is a form of pension based outside the UK that is recognised by the British authorities as being eligible to receive transfers from registered UK pension funds. People who are living inside or outside the UK can transfer their deferred company and personal pensions to a QROPS.

Any pension can be transferred as long as an annuity has not been purchased or, if it is a final salary scheme, that the pension has not commenced. Better still, where the pensioner has not been resident in the UK for five complete and consecutive fiscal years, HMRC restrictions on how income and capital are spent no longer apply.

Anyone considering retiring overseas and becoming resident in a foreign jurisdiction or country for five years or more would benefit from considering a QROPS. The amount of tax you pay on income and capital received from your QROPS will be

determined by the taxation of the country in which it is based and you are resident. These laws vary from country to country but many are more favourable to pensioners than those in the UK.

British pensions that can be transferred to a QROPS include former employers occupational schemes (but not final salary or defined benefit schemes already inpayment); Superannuation Schemes; Executive Pension Schemes; Self Invested Personal Pension Schemes (SIPPSs); Small Self Administered Schemes (SSASs); Section 226 Personal Pension Schemes; Section 32 Pension Transfers and Personal Pensions.

The best option for you will depend on your personal circumstances and it makes sense to take professional advice that can take account of your individual needs and objectives.

Percentage of total numbers QROPS transferred (Source: HMRC)

Jurisdiction:	2007 to 31.06.2011	First half of 2011 only
Australia	47%	20%
New Zealand	23%	28%
Guernsey	10%	32%
Isle of Man	2%	5%
Hong Kong	1%	<1%
Malta	<1%	<1%
Others combined	17%	15%

Value of Funds Transferred into QROPS

Year	Value of funds transferred (£m)
2010	471.37
2009	366.68
2008	358.06
2007	121.49

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Contact

ABU DHABI
Vik Pangam
Tel: +971 2 495 2786
ad@SovereignGroup.com

BAHAMAS
Alan Cole
Tel: +1 242 322 5444
bh@SovereignGroup.com

BAHRAIN
Nabil Khoury
Tel: +973 17 151615
bahrain@SovereignGroup.com

BRITISH VIRGIN ISLANDS
Rudsel Lucas
Tel: +1 284 495 3232
bvi@SovereignGroup.com

CHINA
Frederik van Schalkwyk
Tel: +8621 6103 7089
china@SovereignGroup.com

CURACAO
Rudsel Lucas
Tel: +59 99 465 2698
cu@SovereignGroup.com

CYPRUS
Richard Melton
Tel: +357 25 733 440
cy@SovereignGroup.com

DENMARK
Jan Eriksen
Tel: +45 4492 0127
dk@SovereignGroup.com

DUBAI
John Hanafin
Tel: +971 4 448 6010
dubai@SovereignGroup.com

GIBRALTAR
Ian Le Breton
Tel: +350 200 76173
gib@SovereignGroup.com

RegisterAnAircraft.com
Brian T. Richards
Tel: +350 200 44620
rana@SovereignGroup.com

RegisterAYacht.com
Gabriel González
Tel: +350 200 51870
ray@SovereignGroup.com

Sovereign Accounting Services
Valery Filiaev
Tel: +350 200 48669
sasgib@SovereignGroup.com

Sovereign Asset Management
Richard Foster
Tel: +350 200 41054
sam@SovereignGroup.com

Quest Sovereign Insurance Services
Geoff Trew
Tel: +350 200 52908
sis@SovereignGroup.com

GUERNSEY
Rob Shipman
Tel: +44 (0)1481 729965
ci@SovereignGroup.com

HONG KONG
Jacques Scherman
Tel: +852 2542 1177
hk@SovereignGroup.com

Sovereign Accounting Services
Tel: +852 2868 1326
sashk@SovereignGroup.com

ISLE OF MAN
Diane Dentith
Tel: +44 (0)1624 699 800
iom@SovereignGroup.com

MALTA
Thomas Jackson
Tel: +356 21 228 411
ml@SovereignGroup.com

MAURITIUS
Ben Lim
Tel: +230 403 0813
mu@SovereignGroup.com

MONACO
Registered foreign trustee under Monaco Law 214
Tel: +44 (0)20 7389 0644
info@SovereignGroup.com

THE NETHERLANDS
Susan Redelaar
Tel: +31 (0)20 428 1630
nl@SovereignGroup.com

PORTUGAL
Nigel Anteney-Hoare
Tel: +351 282 340 480
port@SovereignGroup.com

SEYCHELLES
Neil Puresh
Tel: +248 321 000
sc@SovereignGroup.com

SINGAPORE
Joe Cheung
Tel: +65 6222 3209
sg@SovereignGroup.com

SOUTH AFRICA, Cape Town
Coreen Hayman
Tel: +27 21 418 2170
sact@SovereignGroup.com

SOUTH AFRICA, Jo'burg
Noelle McKean
Tel: +27 83 707 7269
sajb@SovereignGroup.com

SWITZERLAND
Dr Norbert Buchbinder
Tel: +41 (0)21 971 1485
ch@SovereignGroup.com

TURKS & CAICOS ISLANDS
Rudsel Lucas
Tel: +1 649 946 2050
tci@SovereignGroup.com

UNITED KINGDOM
Simon Denton
Tel: +44 (0)20 7389 0644
uk@SovereignGroup.com

Editor Christopher Owen
Design Alan Pitchforth
Publisher Kamilian Limited
enquiries@kamilian.com
www.kamilian.com
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www.pioneerprinter.com

SovereignGroup.com

39

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