SovereignGroup.com

SOVEREIGN REPORT 43

Abu Dhabi, **Bahamas**, Bahrain, **British Virgin Islands**, Cayman, **China**, Curaçao, **Cyprus**, Dubai, **Gibraltar**, Guernsey, **Hong Kong**, Isle of Man, **Malta**, Mauritius, **Portugal**, Seychelles, **Singapore**, South Africa, **Switzerland**, The Netherlands, **Turks & Caicos Islands**, United Kingdom.

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Introduction

Season's Greetings

Welcome to the latest edition of Sovereign Report – the final one for 2014. Traditionally this is the time of year to review the 12 months just passed and to look forward to a new year and the inevitable challenges it will bring...

The times they are a-changin'

Readers cannot have failed to notice the number of different but inter-related stories in recent issues in respect of enhanced rules for reporting, beneficial ownership and the exchange of information. These new requirements are being driven by the G-20 countries, via the OECD, and are being implemented on a truly global basis. As a consequence they will be unavoidable.

Many readers may already have been dealing with the markedly tougher regulatory and reporting requirements brought in by the new US FACTA regime, which came into force on 1 July. Given the rate of progress made by the OECD in 2014 and the ambitious targets that have been set for implementation, likely it will not be long before we are all grappling with the realities of the new Common Reporting Standard and automatic exchange of information.

Sovereign's structures have never relied on secrecy and we are committed to ensuring that both we, and our clients, remain in full compliance with national and international rules, despite the extra cost and time involved. Any readers concerned about their position as a result of any of such developments should contact their nearest Sovereign office without delay.

In view of this international agenda it is perhaps not surprising, as we also report in this issue, that the BVI government has initiated a strategic review of its financial services industry. No doubt other jurisdictions are doing or will have to do the same, as they seek to adjust to this new environment. Further consolidation and specialisation by offshore financial centres is inevitable. We will be reporting more on this in future issues.

Improved communications

We will of course try to make any transition as painless as possible for clients and will keep you fully informed of developments. To this end Sovereign has been attending to its communication capabilities. As part of this process, many of you will have received e-shots alerting recipients to developments in China and our residency and citizenship programme. We hope these are helpful in highlighting both potential issues and potential opportunities. We have also initiated a programme to upgrade our website to provide clients with an improved online platform. This should be coming on stream during 2015.

Beneficiaries of The Sovereign Art Foundation getting their hands dirty at a creative workshop.

Sovereign Art Foundation (SAF)

The Sovereign Art Foundation has just closed entries for the 2014-15 Sovereign Asian Art Prize. We received over 350 entries from leading artists in the Asia-Pacific region, who have all been carefully selected by independent curators. The work of the 30 short-listed finalists will be exhibited in Hong Kong in March and auctioned at our gala dinner in May. The proceeds from the evening will go towards helping disadvantaged children.

This year SAF will be focusing its efforts on building its own grass roots programme – Make It Better – in Hong Kong assisting children who live in appalling conditions and have very little opportunity or hope.

If you would like more information or would like to stay up to date with The Sovereign Art Foundation's activities and events, please email art@SovereignArtFoundation.com.

Sovereign news

As the year draws to a close, several offices are expanding in terms of their staff numbers – in some cases this means relocating to new offices. Additionally, I am delighted to announce Bernadette Fulton's recent appointment as Managing Director of our Mauritius office.

I hope you enjoy this edition and on behalf of my Sovereign colleagues in all corners of the world, I extend season's greetings to all our readers and their families and wish you all a happy, prosperous and, above all, well planned 2015.

Howard Bilton
Chairman of The Sovereign Group

UK publishes draft Bill on "beneficial ownership"

The UK government introduced a draft Bill – the Small Business, Enterprise and Employment (SBEE) ¬Bill – to parliament on 25 June 2014, which includes proposals to set up a central registry of the real owners of companies and trusts. This was a key pledge made by Prime Minister David Cameron during the UK's presidency of the G8 last year.

The aim of the Bill is to "enhance the reputation of the UK as a trusted and fair place to do business by increasing transparency around who owns and controls UK companies; and help deter and sanction those who hide their interest in UK companies to facilitate illegal activities or who otherwise fall short of expected standards of behaviour". The UK will encourage other jurisdictions, including its Overseas Territories and Crown Dependencies, to follow suit.

The Bill will require UK companies to obtain and hold adequate, accurate and current information on their beneficial owners, who are termed in the draft legislation as "people with significant control" (PSCs). A PSC is any individual who ultimately owns or controls more than 25% of a company's shares or voting rights, or who otherwise exercises control over the company or its management. Where a qualifying beneficial interest in a company is held through a trust arrangement, the trustee(s) or any other individual(s) exercising effective control over the activities of the trust, will have to be disclosed.

Companies will be required to maintain a register of PSCs, which will contain information on the beneficial owners' full name, date of birth, nationality, country or state of usual residence, residential address, service address, date on which they acquired control over the company and details of the nature of that control. This register will be kept available for public inspection via the company, with the exception of residential addresses. All the information must also be provided to Companies House, where it will be accessible publicly, with the exception of residential addresses and full dates of birth.

Companies will be given statutory tools to help them obtain this information, including the ability to serve notice on a person. They will also be required to update the information if they know or might reasonably be expected to have known that a change to their beneficial ownership has occurred. PSCs will be required to inform the company of any changes to the information recorded in the register.

New companies will be required to provide an initial statement of beneficial ownership on incorporation and will not be registered at Companies House unless this information is provided. Companies will then be required to confirm that the information held at Companies House is correct at least once every 12 months, detailing all changes that have occurred in-year.

The registry is intended to provide a single source of information to support national and overseas law enforcement and tax authorities' investigations; support financial institutions and other regulated professional bodies as they carry out anti-money laundering due diligence checks on companies; and allow all those who engage with a company – investors, suppliers or customers – to identify with whom they are really doing business.

The measures will be discussed in Commons Committee, after which the Bill will go to the House of Lords for debate. The Bill also prohibits the issue of bearer shares, limits the use of corporate directors and introduces new measures for the disqualification and punishment of unfit directors.

Sovereign Comment

These proposals and others being mooted around the world are part of a worldwide crackdown the use of corporate structures for secretive or illicit activities. As an industry leader, Sovereign fully supports the rationale, if not necessarily the scope of the proposed requirements. It should be noted that the above suggestions go considerably further than any previous initiatives and the time and effort required to maintain such records will be significant. This may lead to higher costs for companies if they are to remain fully compliant. Further developments will be reported in future editions.

Cyprus brings new Alternative Investment Funds Law into force

The Alternative Investment Funds Law of 2014 (AIF) was brought into force with publication in the Official Gazette on 25 July 2014. The Law, which replaces and repeals the International Collective Investment Schemes Law 1999 (ICIS), was enacted by the Cyprus parliament on 10 July.

The AIF Law updates the funds regime in Cyprus and aligns it with the latest EU directives on asset management, with a focus on transparency and investor protection. It sets out rules for the authorisation, ongoing operations, transparency requirements and supervision of AIFs in Cyprus and regulates the role and responsibilities of their directors, custodians and external managers.

An AIF is defined as a collective investment undertaking that raises external capital from a number of investors with a view to investing it in accordance with a defined investment policy for the benefit of those investors, and that has not been authorised as a UCITS. The Law provides for two classes of AIF: "unlimited", which are available to any number of investors, including retail; and "restricted", which are available only to up to 75 well-informed or professional investors subject to a €125,000 minimum investment.

AIFs may be structured as variable or fixed capital companies, as limited partnerships, or as a mutual fund. The unit trust structure provided for by the ICIS Law is no longer available. The AIF Law also introduces new structuring options, such as umbrella structures with multiple investment compartments, and permits public offerings of shares of AIFs. Securities issued by AIFs may also be listed.

The role of depositary is no longer restricted to credit or banking institutions and may, subject to specified conditions, be undertaken by other entities. This may provide more flexibility for AIFs such as private equity and real estate funds, which are not investing in financial and money market instruments.

Under the previous regime, international collective investment schemes were regulated and supervised by the Central Bank of Cyprus. The AIF Law provides that the Cyprus Securities and Exchange Commission (CySEC) will be responsible for the regulation and supervision of AIFs, bringing all investment products, asset managers and investment firms under a single regulatory body.

Switzerland amends key law on foreign requests

The Swiss Federal Council brought the revised Tax Administrative Assistance Act (TAAA) into force on 1 August 2014. This permits Swiss banks to respond to a wider range of administrative assistance requests concerning their foreign clients and is intended to bring Switzerland into compliance with developing international standards and OECD recommendations.

The revised TAAA includes a new provision that envisages a procedure for, in exceptional cases, deferred notification of persons entitled to appeal. This would apply to administrative assistance requests already submitted by 21 March 2014. It also sets out more precise specifications regarding group requests, which would apply to requests submitted after 1 February 2013.

However, the TAAA explicitly states that the Swiss authorities will not consider a request if "it constitutes a fishing expedition" or "if it violates the principle of good faith, particularly if it is based on information obtained through a criminal offence under Swiss law".

On 1 July 2014, Switzerland and the European Union initialled a mutual understanding on business taxation that is designed to end a bilateral dispute that has resulted in friction and threats of countermeasures from the EU since 2005.

Under the accord, the Swiss Federal Council reaffirmed its intention to propose abolishing certain tax regimes within the framework of the third series of corporate tax reforms, particularly those that provide for different treatment of domestic and foreign revenue. It further reaffirmed that new tax measures will be based on international standards.

The European Council has criticised the Swiss tax treatment of holding and domiciliary companies at a cantonal level. No cantonal corporate taxes are currently levied against Swiss-based holding and domiciliary companies on revenues derived from business conducted outside Switzerland. The EU confirmed its intention to lift any countermeasures taken as soon as the regimes in question have been abolished.

Sovereign Comment

As with other similar initiatives reported elsewhere in this edition, Sovereign's clients can be reassured that we remain fully compliant. Any readers who might be concerned about these changes should contact their closest office at the earliest opportunity. It is reassuring to note that "fishing expeditions" will not prove successful although it remains to be seen how the violation of good faith issue is dealt with in practice. It is also reassuring that Switzerland is seeking to resolve tensions with the European Union and avoid potential sanctions.

HMRC to miss target unless LDF sees "dramatic" pickup

The Liechtenstein Disclosure Facility (LDF) must see a "dramatic" influx in declarations or HM Revenue & Customs will fail to meet its £3 billion target. The LDF has so far raised just £1 billion in regularised tax across 5,982 declarations, since it opened in August 2009.

If the facility continues to receive declarations at the current average size of £161,000, it will require a total of 12,000 new cases by its March 2016 closure date to meet the Revenue's target.

The LDF is an agreement between Liechtenstein and HMRC designed to give UK taxpayers with undeclared funds held in offshore bank or custody accounts with an opportunity to regularise their tax affairs on favourable grounds. Those with undeclared funds will receive a penalty of just 10% on any tax due and a guaranteed immunity from prosecution.

To make use of the LDF, an investor must link at least 20% of their assets to a Liechtenstein-based financial institution. Investors are also given an option to contact HMRC on a "no-names" basis to discuss their funds, and are not required to repatriate their funds after the facility has closed.

Sovereign Comment

HMRC must strengthen its communication of the advantages of the facility if it is to meet its target. Peter Carnell, consultant at Sovereign Group, said: "I have been very surprised at the facility's low uptake to date; the LDF covers assets from all over the world and offers immunity from prosecution, both making it far more attractive than any other disclosure agreements on offer. We have seen people come out nice and clean with no naming and shaming or prosecutions. If I was HMRC, I would have expected to have at least 20,000 registrations."

UK regulator withdraws "high risk country" list

5 September 2014, the UK Financial Conduct Authority (FCA) removed a list of "High Risk Countries" from its website following representations from the Cayman Islands government. It said that it did not plan to publish such a list in the future and has committed to a full review of the methodology.

The previously unpublished list of 95 countries was released by the FCA on its website on 18 July after it had entered the public domain following a freedom of information request in early July. The Cayman Islands was the only UK overseas territory and the only major offshore financial center classified as "high risk" for financial crime.

The Cayman Islands government said it was "astounded" to find Cayman on the list, despite its international compliance track record and high ranking in the assessment by the OECD's 2013 Global Forum on Transparency and Exchange of Information for Tax Purposes, which put Cayman on par with the UK and higher than most G8 countries. "The third-party data and assessments on Cayman's regime speak impartially and unambiguously regarding the strengths of our system," said Minister of Financial Services Wayne Panton.

The list was used by the FCA to evaluate regulated financial firms' anti-money laundering compliance. Financial institutions in the UK are required to develop their own country risk categories based on publicly available information. After learning of the FCA's internal high-risk country list, financial firms called for its publication to assist with their anti-money laundering efforts.

Gibraltar launches its first stock exchange

Gibraltar opened its first stock exchange on 1 November 2014, following authorisation by the Financial Services Commission of Gibraltar. The Gibraltar Stock Exchange, to be known as GSX, will list collective investment schemes known as open-ended funds. The full opening, when open-ended funds will be able to list on the exchange, will take place in the first quarter of 2015.

The GSX, which is chaired by former Gibraltar Financial Services Commission chief executive Marcus Killick, has been marketing its services over the last 18 months in Europe, Asia and the US and reported that it has already received "keen interest" from a number of applicants. The exchange will give funds greater exposure to investors in the European Union, while the listing process will benefit investors by requiring the funds to become more transparent.

Sovereign Comment

The opening of a stock exchange provides Gibraltar with an additional pillar and product offering to its expanding financial services sector and will provide infrastructure in further establishing Gibraltar as a leading EU finance centre.

European Council reaches final agreement on extending mandatory automatic exchange

The European Council reached a final unanimous agreement, on 14 October 2014, for an amended directive extending the scope of the mandatory automatic exchange of information between EU member state tax authorities to include dividends, interest and other income, such as account balances and sales proceeds, in line with the new global standard on automatic exchange of information adopted by the OECD and endorsed by the G20.

The amended directive will enable tax authorities to better combat tax evasion and to improve the efficiency of tax collection. The new amended directive should be transposed into national law by 1 January 2016 at the latest and should apply as from 2017 (except for a one-year transition period provided for Austria until 2018, during which time the EU savings directive will continue to apply in Austria). Tax treaties with third countries – Andorra, Liechtenstein, Monaco, San Marino and Switzerland – are to be amended accordingly.

UK doubles minimum investment for Tier 1 visa to £2 million

The UK government announced, on 16 October 2014, changes to the Tier 1 (Investor) visa regime. The changes became effective immediately for applications made after 6 November 2014. The most notable change is the increase of the minimum investment amount from £1 million to £2 million.

All the funds must now be invested in UK Government bonds, share capital or loan capital in active and trading UK registered companies. Under the previous regime, up to 25% was permitted to be invested in property. The requirement that a migrant's investment must be "topped up" if its market value falls is also being removed; instead migrants will only need to purchase new qualifying investments if they sell part of their portfolios and need to replace them in order to maintain the investment threshold. The provision under which the required investment sum could be sourced as a loan has also been removed.

Finally there is a new "genuine investor" test under which UK will refuse applications if there are reasonable grounds for believing that a third party is fronting the investment funds, if the funds were obtained unlawfully or the character, conduct or associations of a funding provider make approving the application contrary to the public good.

The UK Home Office approved 735 applications for UK residency permits from wealthy foreign investors from outside the EU in the year to June. This is up from around 500 in the previous year and just 100 in the year to 30 June 2009. In total, at least £2.2 billion has been invested by foreigners since 2009.

US Foreign Account Tax Compliance Act comes into force

The controversial US Foreign Account Tax Compliance Act (FATCA), first enacted in March 2010, was duly brought into force on 1 July 2014. It is intended to provide the Internal Revenue Service (IRS) with access to information – including account ownership, balances, and amounts – in respect of accounts held by US taxpayers in foreign financial institutions (FFIs) with a balance of over USD50,000.

US Deputy Assistant Secretary for International Tax Affairs Robert Stack said: "Over the past several years, FATCA has become the global standard in combating international tax evasion and promoting transparency. With FATCA agreements treated as in effect with nearly 100 jurisdictions, and more than 80,000 financial institutions already registered to comply with the IRS, the international support for FATCA is without question."

Foreign governments have two options for complying with FATCA: they can either enable their FFIs to enter into agreements with the IRS to provide the required information or they can themselves enter into one of two alternative Model Intergovernmental Agreements (IGAs) with the US. If FFIs do not agree to identify and report information on US account holders, FATCA requires payors to withhold a portion of certain US-source payments made to those FFIs.
Under a Model 1 agreement, FFIs report the relevant information to their respective governments, which then relay that information to the IRS. Under a Model 2 agreement, FFIs will provide relevant information directly to the IRS, with government-to-government cooperation serving to facilitate reporting when necessary to overcome specific legal impediments.

Generally, financial institutions in countries that have not signed intergovernmental agreements with the US must register with the IRS and enter into a so-called "FFI Agreement" or be subject to 30% withholding on certain payments from the US. Although FATCA has entered into operation, in order to as to "facilitate an orderly transition", the IRS has agreed to refrain from rigorously enforcing many of its requirements with regard to reporting, due diligence and withholding provisions during 2014 and 2015, provided that an FFI is making a good-faith effort to achieve compliance.

Sovereign Comment

Regular readers will recall the lengthy and at times tortuous passage that these proposals have endured since first being mooted several years ago. It is good to have some certainty now that the law has come into effect. Sovereign clients should be reassured in the knowledge that relevant group companies are fully compliant under FATCA new rules as FFIs. This will be of particular importance to clients who hold either US citizenship or US residency. Any questions on FATCA should be addressed to your closest Sovereign office.

BVI government reviews direction of financial services

The government of the British Virgin Islands announced, on 12 August 2014, that it had appointed management consultants McKinsey and Company to undertake a strategic review of the financial services industry. The aim is to protect, diversify and strengthen financial services – which currently provides 65% of government revenue – to ensure the long-term sustainability of the BVI.

The review will be undertaken in three phases to:

- Examine the BVI's existing legal and business environment to assess the health, quality and productivity of the financial services industry, as well as the suitability of current government strategies;
- Advise the government on managing, rebuilding and strengthening the BVI's systems and practices, as well as measures to protect the international reputation of the BVI;
- Develop a strategic framework and implementation plan that is designed to diversify the existing financial services model, create greater substance and attract value-added activities to the BVI.

BVI Premier and Minister of Finance, Dr Orlando Smith said: "Over the past two years I have led a number of initiatives which sought to critically look at our financial services industry and determine how we should position ourselves for the future. Throughout that period the industry has been subject to a number of shocks, which threaten the viability of what is our most important economic pillar.

"I am therefore pleased to have commissioned this latest engagement. I look forward to receiving the final implementation plan and the Territory being able to move forward strategically as a global financial services leader, with a stronger and more diversified financial services industry."

Sovereign Comment

This development is a welcome move for the BVI and one that may soon be repeated in other jurisdictions elsewhere. The demands facing territories that rely on the provision of financial services is becoming ever more challenging. In the case of BVI, it is clear from the figure quoted in this story just how critical this industry is to the BVI economy – and, by extension, to the UK which is ultimately responsible for its overseas dependencies and territories. We await the outcome of this McKinsey review with considerable interest, not least because of the pivotal role that BVI companies play worldwide.

US acts to rein in corporate tax Inversions

US President Barack Obama issued new rules, on 22 September 2014, to crack down on corporate inversions – a transaction by which US-based multinationals restructure so that their US parent is replaced by a foreign parent, in order to reduce their domestic tax bill and put non-US earnings beyond the reach of US authorities.

Thirteen inversion deals have been announced since the start of 2013 – including Burger King's $11.4 billion acquisition of the Canadian coffee shop chain Tim Hortons – which are together worth $178 billion. The new rules will stop non-US subsidiaries of inverted companies from making loans to their new foreign parent as a way to avoid paying US tax. They will further stop the new parents from buying overseas subsidiaries to free that cash from US tax.

The US Treasury is also making it harder for a US company to meet the current rules for inversion, which require shareholders of the foreign partner to own more than 20% of the new company. The new rules prohibit the use of certain assets to inflate the size of the foreign merger partner and also stop US companies from paying special dividends just before an inversion in order to reduce their own size, or spinning off part of their operations to shareholders for the same reason.

"We're taking initial steps that we believe will make companies think twice" before carrying out an inversion, said US Treasury secretary Jack Lew. "For some companies considering deals, today's actions will mean that inversions no longer make economic sense."

The Obama administration resorted to using its executive powers to curb inversions because Congress failed to agree on how to tackle them via legislation. The Treasury warned that it would continue to look for other steps to discourage inversions, and to review tax treaties.

"We've recently seen a few large corporations announce plans to exploit this loophole, undercutting businesses that act responsibly and leaving the middle class to pay the bill, and I'm glad that Secretary Lew is exploring additional actions to help reverse this trend," said President Barack Obama in a statement.

Sovereign Comment

This is a hugely topical issue, coming at the end of a year in which a great deal of attention has been focused on international corporate structuring, which has resulted in several high profile public companies being criticised for exploiting complex tax planning strategies. See a further news item in the Fiscal section of this edition for news of investigations by the EU into this practice. The US is taking executive action to reduce the attraction to domestic companies to employ corporate tax inversion as a strategy. The situation in the EU is more tricky due to European rules on freedom of movement but public opinion in this area is also likely to lead to a tightening of the rules in the years ahead.

Cayman introduces director registration regime

The Cayman Islands government brought the Directors Registration and Licensing Law, which provides for the registration and, in certain cases, licensing of individuals appointed as directors of Cayman "covered entities", into force on 4 June 2014. The law is designed to allow the Cayman Islands Monetary Authority (CIMA) to verify certain basic information in respect of directors of covered entities. It also contains separate licensing regimes for professional directors, who serve on 20 or more relevant boards, and for corporate directors of covered entities.

Covered entities are mutual funds regulated by CIMA under the Mutual Funds Law or companies registered as "excluded persons" under the Securities Investment Business Law. The Law extends to all directors of covered entities, wherever they are resident or incorporated, but does not apply to directors of other Cayman Islands companies or to directors of general partners, or to trustees, of covered entities.

Individuals acting as directors of existing covered entities were required to register with CIMA within three months from 4 June. CIMA can refuse to register applicants convicted of a criminal offence involving fraud or dishonesty, or who are the subject of sanctions from a regulator, self-regulatory organisation or professional disciplinary body. For new fund launches, a person who is proposed to be appointed as a director of a covered entity may not be appointed prior to being registered or licensed by CIMA.

Professional directors of existing covered entities are required to be licensed by CIMA and had three months from 4 June to register with CIMA. Applicants are subject to a "fit and proper" test. Exemptions from the licensing requirement apply to: directors, employees, members, officers, partners or shareholders of an entity holding either a Cayman Islands companies management licence or a mutual funds administrators licence; fund managers of a CIMA-regulated mutual fund that are registered or licensed by a prescribed overseas regulatory authority, provided that the individual is acting as a director through their relationship to that fund manager.

Corporate directors are either required to be registered as a Cayman Islands company or to be registered as a foreign company in Cayman. Existing corporate directors have six months from 4 June to comply. Corporate directors not already licensed under either a Cayman Islands companies' management licence or a mutual fund administrators licence, must be licensed by CIMA. Corporate directors must have at least two natural persons on their board that meet CIMA's fit and proper requirements and proposed new or additional appointees are required to be approved by CIMA.

Hong Kong and Macau commit to new OECD information exchange standard

The government of the Hong Kong SAR announced, on 15 September 2014, that it had committed to the OECD Global Forum on Transparency and Exchange of Information for Tax Purposes to implement the new global standard on automatic exchange of information.

In July this year, the OECD released a Common Reporting Standard for Automatic Exchange of Financial Account Information in Tax Matters (CRS), which called on governments to obtain detailed account information from their financial institutions and exchange that information automatically with the jurisdictions of residence of account holders on an annual basis.

Secretary for Financial Services and the Treasury, Professor K C Chan, said: "It is crucial for Hong Kong to adopt the latest global standard on tax transparency in order to maintain our international reputation and competitiveness as an international financial and business centre."

It was added that Hong Kong is committed to implementing the new global standard on a reciprocal basis with appropriate partners which can meet relevant requirements on protection of privacy and confidentiality of information exchanged and ensuring proper use of the data. Over 60 jurisdictions around the word have already committed to CRS implementation by 2017, or at the latest by the end of 2018.

The Hong Kong government said it had been enhancing its regime to meet the evolving international standard on exchange of information, including removing the domestic tax interest requirement in conducting exchange of information under comprehensive avoidance of double taxation agreements, and putting in place the legal framework for Hong Kong to enter into tax information exchange agreements with other jurisdictions.

The Macau SAR government also announced its support for the global new standard on 29 September 2014 and said it would soon initiate the legislative procedures necessary for the amendment of relevant domestic laws to ensure timely compliance with the new standard.

Sovereign Comment

These announcements from both SAR governments underline the importance attached by them to their financial services industries and the need to adhere to new international norms such as the OECD's CRS. Professor Chan's comments in particular are significant. Regular readers will be aware that Hong Kong has never been classified with other jurisdictions as a "tax haven". It is clear that the government is seeking to protect this position. Sovereign's Hong Kong office is one of the group's largest and we welcome this initiative, designed as it is to retain the Hong Kong's pre-eminence as Asia's leading business and finance centre.

Dubai introduces Qualified Investor Funds

The DIFC Laws Amendment Law 2014, which makes a number of significant changes to the Dubai Financial Services Authority's (DFSA) investment laws and regulatory regime, was brought into force on 21 August 2014.

The Collective Investment Law 2010 is amended to allow the creation of a new category of fund –Qualified Investor Fund (QIF) – available only to professional investors willing to make an investment of at least $500,000, which is reduced from $1 million minimum initially proposed by the DFSA in a draft of the rules for public consultation earlier this year.

An addition to the existing categories of funds available in the Dubai International Finance Centre (DIFC), the lighter regulation under QIF rules is specifically designed for higher net worth investors. QIFs are limited to 50 investors each and will be offered only through private placements. The new class of funds is expected to boost the DIFC's growth as a fund domicile.

The DIFC Laws Amendment Law also simplifies the structure and process for DFSA regulatory decisions and subsequent appeals. The DFSA will make all first instance decisions and must follow specified procedures designed to ensure its decisions are fair and reasonable. The Regulatory Appeals Committee (RAC), which used to hear appeals from DFSA decisions, will be abolished. Instead all appeals on DFSA rulings to be taken by Financial Markets Tribunal.

The DFSA's supervisory and enforcement powers have been further strengthened. A new provision prohibits misleading, deceptive, fraudulent or dishonest conduct related to financial products or services in the DIFC. The DFSA previously had the right to withdraw licences but has been given new powers to suspend a licence or registration for up to 12 months and to prohibit firms from using misleading names.

The current framework for the supervisory oversight of auditors in the DIFC is also improved by introducing the registration of audit principals, strengthening the rules on auditor independence and making other changes to ensure consistency with international auditing standards.

"They [the amendments] are considered desirable and appropriate for the maturity of the DIFC, given that it has now experienced a decade of operations. They also ensure that the regulatory regime continues to evolve to reflect best international practice," said Ian Johnston, chief executive officer of the DFSA.

Qatar financial centre offers new tax reliefs

The Minister of Finance enacted, on 18 June 2014, amendments to the Qatar Financial Centre (QFC) Tax Regulations and Tax Rules, which originally came into force in 2010, to reflect legislative changes elsewhere in the QFC. The revised legislation and regulations introduce new provisions to align the QFC Tax Regulations with the new rules for special purpose companies and holding companies that are within the definition of "special funding companies", which may elect for special tax exemption status.

Funds that make investment on behalf of a single family office are exempted from taxation and unregulated Qatari-owned entities can elect for a concessionary tax rate of 0% to apply to their operations within the QFC.

An incentive scheme for new QFC entities based on the effective use of tax losses is to be established, and fees paid by way of a distribution and other fees paid in priority to other distributions and performance fees under the special exempt status incentive are exempt from taxation. Management fees received from a registered fund or a special investment fund, which has elected for special exempt status, will not be exempted.

Other technical and administrative changes include an exemption from taxation for dividend income received by a QFC entity and for interest and other yields on public treasury bonds. Profits derived from intangible fixed assets including intellectual property, patents, trademarks or similar assets not registered in Qatar or the Riyadh Patent Office may now be considered local source income taxable in the QFC.

Definitions of partners of general and limited partnerships and members of limited liability partnership have also been introduced, as well as the term "disguised partners or members". There is a limitation on the deductibility of remuneration of partners, members and disguised partners or members around the "just and reasonable" test, in addition to the current deductibility cap.

Salman Al Thani, chief financial and tax officer at the QFC Authority, said: "These changes to our Tax Regulations and Rules following our latest review support the QFC's evolving strategy by ensuring alignment with structures such as holding companies and special purpose companies available in the QFC. Qatari-owned entities stand particularly to benefit and will now find it advantageous to set up structures in the QFC which previously they could only establish abroad."

Sovereign Comment

Regionally Qatar is working hard to enhance its own reputation in order to effectively compete in international financial services with other regional jurisdictions such as the UAE. Sovereign is keen to embrace the Qatari initiative and is already working to ensure clients are able to access new products and services available from Qatar. Further details can be obtained by contacting our Dubai office, details of which appear in the Contact section on the back page of this issue.

China issues new rules on reporting foreign participations

China's State Administration of Taxation (SAT) issued new rules (SAT Gong Gao [2014] No.38), on 30 June 2014, governing information requirements for foreign income and foreign participation. They were applied as of 1 September 2014.

Resident enterprises that have incorporated or participated in, or disposed of, an existing interest in foreign companies are required to complete a new Information Form on Foreign Participation of Resident Enterprise to provide information on foreign participation and foreign income if their direct or indirect participation in a foreign company exceeds 10% of share capital or share capital with voting rights.

Resident enterprises will also be required to report to SAT, within the same quarter of the year in which it occurred, when a direct or indirect participation in a foreign company is increased to exceed 10% or more, or decreased from 10% or more to below 10%.

The rules apply equally to Chinese permanent establishments or branches of non-resident companies deriving foreign income that is effectively connected with such establishments or branches.

Sovereign Comment

Our China operation has offices in Beijing and Shanghai and is able to advise on all aspects of Chinese corporate rules. Benefitting from many years relevant experience, specialist guidance can be given to foreign firms considering inward investment into this country of over 1.3 billion people. Compliance with every different series of rules and regulations is of vital importance, particularly given the lightning pace of development in the country and the regular changes to legislation. All Sovereign offices actively effect introductions to our China office to promote participation in this challenging but hugely rewarding market.

Dubai allows transfer of title to company as a gift

The Dubai Land Department (DLD) has advised that it will accept a transfer of a property from an individual or individuals to a Jebel Ali Free Zone (JAFZA) offshore company that is wholly-owned by a further offshore company as a "donation in kind contract" (gift), provided that the beneficial owners of both companies are the same as the property owners.

As a result the gift transfer fee of 0.125% of the value of the property will be applied rather than the standard fee prescribed for a sale and purchase contract, which is 4% of the total value of the agreement. The 0.125% fee is subject to a minimum of AED 2,000 (approx. US$545) and consent to the transfer must be obtained from both JAFZA and the DLD via a written request.

The primary advantage of using a JAFZA offshore company to hold property in Dubai is the avoidance of complex international inheritance procedures – particularly the potential application of Shari'ah law. Since 1 January 2011, the only offshore company that can own property in Dubai is the JAFZA offshore company. To ensure the asset is protected from local inheritance laws a BVI company layer is added, which falls under Common Law and simplifies the inheritance procedures significantly.

If the investors are husband and wife, both spouses can be made joint shareholders in the company. Children can also be introduced to the company in due course as a means of passing on the assets through the offshore company.

Sovereign Comment

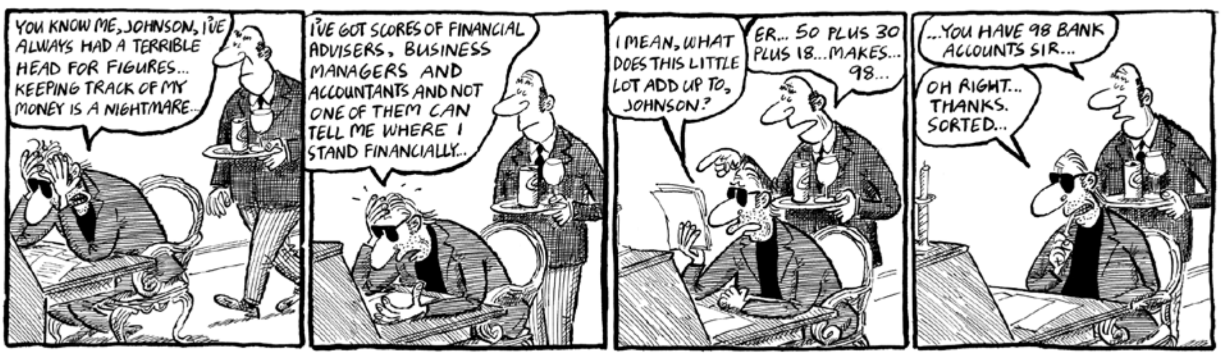
Having a company name on the title of the property provides additional confidentiality to the owner(s), while a corporate structure further offers a highly effective platform for joint investments. Application of the reduced 0.125% transfer fee is entirely at the DLD's discretion. If you are considering transferring a property to a corporate entity, Sovereign recommends you to take advantage of this concession at the earliest opportunity.

Seychelles, Singapore sign double tax treaty

9 July 2014, Singapore and Seychelles signed a double taxation agreement (DTA), which cuts withholding taxes and incorporates the internationally agreed standard for the exchange of information for tax purposes. The DTA allocates taxing rights between the two jurisdictions with regard to business income, income from shipping and air transportation, and provides for tax relief on different types of passive income.

Dividends paid by a company which is registered in one of the countries to a company or individual that is a resident of the other will only be liable for taxation in the other country, unless the beneficiary of the dividends, being a resident of one of the countries, has set up a permanent business establishment in the other country. Withholding tax on interest income is to be capped at 12%. Withholding tax on royalties is capped at 8% if the beneficial owner of the royalties is a resident of the other state.

The agreement will enter into force after the completion of domestic ratification procedures in both territories. This is the fourth DTA signed by Seychelles this year following agreements with Ghana, Kenya and Guernsey, bringing the total to 21.



OECD progresses move to new global standard for Automatic Exchange of Information

The new OECD/G-20 standard on automatic exchange of information was endorsed, on 29 October 2014, by all OECD and G20 countries as well as major financial centres participating at the annual meeting of the Global Forum on Transparency and Exchange of Information for Tax Purposes in Berlin.

Fifty-one jurisdictions signed a Multilateral Competent Authority Agreement that will activate automatic exchange of information, based on the Multilateral Convention on Mutual Administrative Assistance in Tax Matters.

Collectively known as the Early Adopters Group, they have committed to the first exchange of information in relation to new accounts and pre-existing individual high value accounts to take place by the end of September 2017. Information about pre-existing individual low value accounts and entity accounts will either be exchanged by the end of September 2017 or September 2018, depending on when financial institutions identify them as reportable accounts.

The OECD's new global Standard for Automatic Exchange of Financial Account Information in Tax Matters calls on governments to obtain detailed account information from their financial institutions and exchange that information automatically with other jurisdictions on an annual basis. A total of 89 Global Forum member jurisdictions have committed to implementing this Standard on a reciprocal basis with all interested jurisdictions.

The Global Forum is to establish a peer review process to ensure effective implementation. In 2015, jurisdictions will provide implementation plans so that a report can be made to the Global Forum plenary next year. Reviews are expected to start in 2016, as the legal and regulatory frameworks of jurisdictions committed to first exchanges in 2017 should be finalised.

Governments also agreed to raise the bar on the standard of exchange of information upon request, by including a requirement that beneficial ownership of all legal entities be available to tax authorities and exchanged with treaty partners.

The Global Forum invited developing countries to join the move towards automatic exchange of information, and a series of pilot projects will offer technical assistance to facilitate the move.

OECD Secretary-General Angel Gurria said: "The fact that so many jurisdictions have agreed today to automatically exchange financial account information shows the significant change that can occur when the international community works together in a focused and ambitious manner."

Even before the Standard has become operational, the drive toward greater transparency and better exchange of information is having a tangible effect on taxpayer behaviour. OECD analysis of voluntary disclosure programmes since 2009 shows that more than half a million taxpayers have voluntarily disclosed income and wealth previously undisclosed to their tax authorities and countries have realised more than €37 billion in revenue.

Sovereign Comment

The OECD's new Standard is just one of the international initiatives aimed at reducing the incidence of illegal tax evasion worldwide, although arguably it is the most effective. The story includes reference to the success of voluntary disclosure programmes that have been established in several states. The extra work and cost involved in complying with these initiatives is a matter of regret but Sovereign has always insisted that any structuring with which it is involved on behalf of clients is fully compliant and would withstand scrutiny by home tax authorities. Should any readers wish to review their own arrangements to ensure compliance with this initiative – and indeed others highlighted elsewhere in this edition, they are encouraged to contact Sovereign as soon as possible.

Hong Kong sign tax treaties with South Africa and South Korea

Hong Kong and South Africa signed a comprehensive double taxation agreement on 16 October 2014. It was the 31st treaty signed by Hong Kong. K C Chan, Secretary for Financial Services and the Treasury, said that it sets out the allocation of taxing rights between the two jurisdictions and will help investors better assess their potential tax liabilities from cross-border economic activities.

Currently, the profits of Hong Kong companies doing business through a permanent establishment in South Africa may be taxed in both places if the income is Hong Kong-sourced. Under the treaty, double taxation will be avoided in that any South African tax paid by the companies will generally be allowed as a credit against the tax payable in Hong Kong in respect of the income.

South Africa's withholding tax on dividend income will be reduced from 15% to either 5% or 10%, depending on the percentage shareholding; royalties, currently 15%, will be capped at 5%; interest will be capped at 10%.

Hong Kong also signed a tax treaty with South Korea on 8 July. Under the treaty, withholding tax on interest and royalties will be capped at 10%, and withholding tax on dividends will be reduced to 15 or 10%, depending on the percentage of shareholdings. Both treaties include provisions in line with international standards on the exchange of information in tax matters.

Russia excludes Malta from black list of offshore jurisdictions

The Russian Finance Ministry drafted, on 8 October 2014, a decree that will exclude Malta from its "black list" of offshore jurisdictions. The decision followed the enactment of the revised treaty between the governments of Russia and Malta, signed in May, for avoidance of double taxation and the prevention of fiscal evasion with respect to taxes.

In September, the upper house of the Russian parliament, the Federation Council, sent a set of draft laws on "de-offshorisation" to the lower house, the State Duma. If adopted, the new rules are expected to take effect from 1 January 2015.

The proposed changes substantially alter the tax environment for Russian individuals and legal entities that own foreign assets and introduce unprecedented rules into Russian law for assessing the income of Controlled Foreign Companies (CFCs), as well as for qualifying a foreign company as a Russian tax resident.

According to the Bill, companies incorporated in jurisdictions on the "black list" of the Russian Ministry of Finance will be regarded as Controlled Foreign Companies (CFCs) if Russian residents own, directly or indirectly, more than 10% of their shares. The law will apply to foundations, partnerships, partnership associations and other collective investment vehicles, although trusts are not yet specifically included.

Russian taxpayers who are "controlling persons" will be required to self-assess and include the CFC's profits as part of their own tax base, pro rata to their shareholding, and will then be taxed at the applicable rates for individuals and legal entities. Russian taxpayers will also have to declare all cases of direct or indirect ownership exceeding 1% of shares held in foreign corporations that are resident in any jurisdictions on the "black list".

To stimulate reporting, the Russian Tax Code is likely also to be amended to increase sanctions for non-disclosure or incomplete disclosure of information, as well as non-payment of the relevant tax.

Sovereign Comment

Since the dissolution of the former Soviet Union in December 1991, the number of Russian clients seeking to manage their affairs using international finance centres has multiplied in an extraordinary manner. It was perhaps inevitable given the pressure on Russia's tax revenues that attention would be paid to CFCs. It is very good news for Malta that it has succeeded in getting off the black list before any legislation comes into force. This is now the time to review arrangements in order not to fall foul of the amended rules, and to avoid the proposed increases in fines.

EU to investigate corporate tax codes in Ireland, Luxembourg and the Netherlands

The European Commission opened, on 11 June 2014, three in-depth investigations to examine whether decisions by tax authorities in Ireland, The Netherlands and Luxembourg with regard to the corporate income tax to be paid by Apple, Starbucks and Fiat Finance and Trade, respectively, comply with the EU rules on state aid.

The Commission has been investigating under EU state aid rules certain tax practices in several Member States following media reports alleging that some companies have received significant tax reductions by way of "tax rulings" issued by national tax authorities. The Commission said it did not call into question the general tax regimes of the three Member States but that tax rulings could involve state aid within the meaning of EU rules if used to provide selective advantages to a specific company or group of companies.

The Commission will examine if the three transfer pricing arrangements validated in the following tax rulings involve state aid to the benefit of the beneficiary companies:

- The individual rulings issued by the Irish tax authorities on the calculation of the taxable profit allocated to the Irish branches of Apple Sales International and of Apple Operations Europe;
- The individual ruling issued by the Dutch tax authorities on the calculation of the taxable basis in the Netherlands for manufacturing activities of Starbucks Manufacturing EMEA BV;
- The individual ruling issued by the Luxembourgish tax authorities on the calculation of the taxable basis in Luxembourg for the financing activities of Fiat Finance and Trade.

The Commission said it had reviewed the calculations used to set the taxable basis in those rulings and, based on a preliminary analysis, had concerns that they underestimated the taxable profit and thereby granted an advantage to the respective companies by allowing them to pay less tax. The Commission notes that the three rulings concern only arrangements about the taxable basis; they do not relate to the applicable tax rate itself.

Joaquín Almunia, Commission Vice President in charge of competition policy, said: "Under the EU's state aid rules, national authorities cannot take measures allowing certain companies to pay less tax than they should if the tax rules of the Member State were applied in a fair and non-discriminatory way."

Sovereign Comment

It is unfortunate that some elements of the press continue to treat any arrangement involving international corporate structuring as tax evasion – without considering the facts behind each case. This is particularly true in the US and Europe where political pressure relating to several high profile cases, some of which are mentioned in this story, has resulted in unjustified criticism of the firms involved. The implications for other companies, whilst not in the public eye could be significant. We shall follow these investigations and continue to report their findings in future editions.

Portugal introduces new Local Lodging Registration requirements

A new law published on 29 August 2014, which comes into effect on 27 November, makes it mandatory for any individual letting property for short-term tourism to register a business activity with the Portuguese Tax Department (Finanças) and register with their local council for Alojamento Local (AL).

AL registration has been in place for some time but the new law changes the procedure, including the necessity to prove the registration of a business activity – either business activity registration under CAE 55201 or 55204 (furnished accommodation for tourists) of Category B (sole traders) –by production of the appropriate form submitted to the Finanças. Those persons already registered under AL, must produce this form within 30 days of the law coming into force.

This change in reporting letting income can mean a substantial reduction in tax payable on income received. The calculation of tax will be based on turnover. The "Simplified Tax Regime" will apply, and thus tax payable will be based on a fixed amount of profit equal to 15% of the rental income. A flat tax rate of 25% will apply to that 15% profit which will determine a final tax rate of 3.75%.

This procedure does however require a disciplined and ongoing relationship between the property owner and the reporting party (probably your fiscal representative). Due to the nature of the new requirements the tax will be at a minimum but increased accounting fees will be incurred due to added workload.

Sovereign Comment

This is not all good news. Although it will benefit those with a letting income above €20,000, it may force some smaller accounts to cease letting because it will no longer be financially viable. Sovereign – Consultoria Lda with its staff of 14, including four qualified accountants, is capable of providing full assistance in this process covering the following services: fiscal representation; tax return preparation and filing; online invoicing and monthly reports compliance; and accounts and book keeping. Registration needs to be effected before the end of 2014 and thus we recommend that any person who may need assistance should make contact with Sovereign as soon as possible.

UK High Court finds inheritance tax liability on bequest to a Jersey trust

The UK High Court held, on 18 September 2014, that for a disposition in a will to a charitable trust to be exempt from inheritance tax, the trust concerned had to be subject to the jurisdiction of the UK courts.

In *Routier and Another v Revenue and Customs Commissioners*, Peter Routier and Christine Ann Venables, as executors of the estate of the late Beryl Coulter, were appealing against a determination by the Revenue and Customs Commissioners that the disposition of the residue of her will to a charitable trust – the Coulter trust – was liable to inheritance tax because the trust was governed by Jersey law.

Mrs Coulter died on 9 October 2007 and was domiciled in Jersey at the date of her death. Her will was dated 1 October 2004, and was stated to be governed by the law of Jersey. Probate was granted in the Probate Division of the Royal Court of Jersey on 25 October 2007. In her will Mrs Coulter left legacies to various people totaling £210,000, but HMRC took the position that the gift of the residue to the Coulter trust was not exempt from inheritance tax of between £591,724 and £633,571.

Section 23 of the UK Inheritance Tax Act 1984 provides: "(1) Transfers of value are exempt to the extent that the values transferred by them are attributable to property which is given to charities. … (6) For the purposes of this section property is given to charities if it becomes the property of charities or is held on trust for charitable purposes only, and 'donor' shall be construed accordingly."

The issue between the parties was whether the gift to the Coulter Trust fell within section 23(1) because it fell within the second limb of section 23(6), being a gift that was held on trust for charitable purposes only. The appellants argued that the plain words of subsection (6) indicate that all that was needed for the exemption to apply was that there was a trust and the trust's purposes were exclusively charitable purposes under UK law.

HMRC contended, however, that there was an implied requirement in both limbs of subsection (6) that the body of persons or trust (in the first limb) or the trust (in the second limb) were governed by the law of some part of the UK. It concluded that because the Coulter Trust was governed by the law of Jersey it did not qualify as a 'trust for charitable purposes only' for the purposes of either limb.

in dismissing the appeal, Mrs Justice Rose said subsection (6) of section 23 was only a definition section. The primary exempting provision was subsection (1), which referred only to property given to charities. The word "charities", as defined in section 989 of the Income Tax Act, clearly imported the requirement that the trust should be governed by the law of some part of the UK because it referred to bodies established for charitable purposes.

If parliament had intended to extend the scope of the exemption to overseas trusts, she found, it would have made that clear in subsection (1) rather than using a word that imported the requirement for a UK link. The expression "held on trust for charitable purposes" in section 23(6) of the Inheritance Tax Act 1984 required not only that the charitable purposes be UK law charitable purposes but that the relevant trust be subject to the jurisdiction of the UK courts as well.

ECJ rules on application of "free movement of capital" to Overseas Territories

The European Court of Justice (ECJ) found, on 5 June 2014, that the imposition of dividend withholding tax on distributions made by two Dutch companies to their respective holding companies based in the former Netherlands Antilles was compatible with the European Union's (EU) principle of free movement of capital.

In *X BV and TBG Limited vs Staatssecretaris van Financien* (C-24/12 and C-27/12), the two Dutch companies argued that the 8.3% dividend withholding tax applied to their distributions was contrary to the EU principle of the free movement of capital, given that the Netherlands Antilles was at that time an overseas country and territory (OCT) of The Netherlands.

The ECJ noted that EU law did mention the Netherlands Antilles as part of the Kingdom of the Netherlands although the relevant provision did not refer to the application of the free movement of capital principle. It further noted a European Community (EC) decision concerning OCTs that prohibited "restrictions on the payment of dividends between the EU and OCTs."

However, the ECJ held that, because the withholding tax on dividends to the Netherlands Antilles was "intended to prevent excessive capital flow towards the Netherlands Antilles and to counter the appeal of that OCT as a tax haven", it should be allowed, provided that the national court found that the withholding tax was "combating tax avoidance in an effective and proportionate manner."

"European Union law must be interpreted as not precluding a tax measure of a Member State which restricts movements of capital between that Member State and its own OCT whilst pursuing the objective of combating tax avoidance in an effective and proportionate manner," the ECJ found.

Sovereign Comment

This is an interesting case and raises the question of the EU's relationship with other OCTs and dependent territories. There are several examples where EU countries impose withholding tax when payments are made to jurisdictions they consider "offshore". Cyprus was a case in point even after it joined the EU in 2004. Gibraltar is excluded from this risk given its particular status within the EU. The relevant article describes the territory as one "for whose external relations a Member State is responsible". At present, this arrangement only applies to the UK and Gibraltar.

ECJ strikes down Dutch fiscal unity rules

The European Court of Justice (ECJ) ruled, on 12 June 2014, that Dutch legislation governing the formation of consolidated tax entities was in breach of the European Union's (EU's) principle of freedom of establishment.

The Dutch fiscal unity regime allows groups of companies to file a single tax return and offset losses incurred by one company in the group against profits of another, therefore calculating Dutch corporate income tax on a consolidated basis. Under the current fiscal unity regime, where Dutch companies have a linking company – whether parent or intermediary company/companies – in another Member State, it is not possible for such consolidation to take place.

In a combined ruling handed down in SCA Group Holding BV and others (C-39/13, C-40/13 and C-41/13), the ECJ ruled that under Article 49 read with Article 54 of the Treaty on the Functioning of the European Union (TFEU), a member state cannot prevent a resident parent company from forming a single tax entity with a sub-subsidiary merely because the sub-subsidiary is held though a non-resident company that does not have any permanent establishment (PE) in the Netherlands. Similarly, it may not prevent single entity tax treatment to resident sister companies in circumstances where the common parent is a non-resident and does not have a Dutch PE.

According to the ECJ, the Dutch fiscal unity rule "creates a difference in treatment between, on the one hand, parent companies the seat of which is in the Netherlands ... and, on the other hand, parent companies which also own subsidiaries in the Netherlands but have their seat in another Member State and are without a permanent establishment in the Netherlands."

The ECJ noted that parent companies resident in the Netherlands may "set off the losses of their loss-making subsidiaries against the profits of their profit-making subsidiaries." However, non-resident parent companies with Dutch subsidiaries but without any PE in the Netherlands are "excluded from benefiting from the tax entity and, therefore, from the cash-flow advantage which the tax entity bestows."

The ECJ could find no valid grounds to justify this either by an objective difference of situation or by a public interest consideration based on the coherence of the tax system including the double use of losses.

Italian Supreme Court overturns Dolce and Gabbana tax convictions

Italy's Supreme Court overturned, on 24 October 2014, tax evasion convictions and 18-month jail terms against fashion designers Domenico Dolce and Stefano Gabbana.

They were accused of having transferred control of their brands to a shell company in Luxembourg in 2004 and 2005 to avoid paying Italian taxes. Prosecutors had argued that setting up the Luxembourg company Gado – an acronym of the designers' surnames – while the operation was being managed and controlled of Italy was a bid to defraud the state.

Dolce and Gabbana were originally accused of tax evasion of around €1 billion. In June 2013, they were found guilty of evading taxes totalling €200m and given 20-month jail sentences, which they appealed. In April this year an Italian appeals court upheld the guilty verdict.

However, the Supreme Court annulled the conviction, declaring that the prosecution case was "unfounded", and ended the case. "We have always been honest and we are extremely proud of this recognition by the Italian court of justice. Viva l'Italia," the two designers said in a statement.

Sovereign Comment

You might think "all's well that ends well" – but has it? Whilst these two unrelated cases demonstrate that the taxman and prosecutors do not always win, it's difficult to say to what extent the successful defendants will feel like celebrating. Press attention has focused on the legal costs but the intangible costs may have been even greater. Firstly there is the reputational cost to two globally recognised brands; second, the "opportunity" costs that result from an uncertain future and the diversion of energy; finally, there is the "emotional" cost – Dolce and Gabbana were actually convicted in Italy's lower courts while Weil was indicted, declared a fugitive, arrested and extradited. Both cases demonstrate the need for robust, compliant and well-documented planning from the outset.

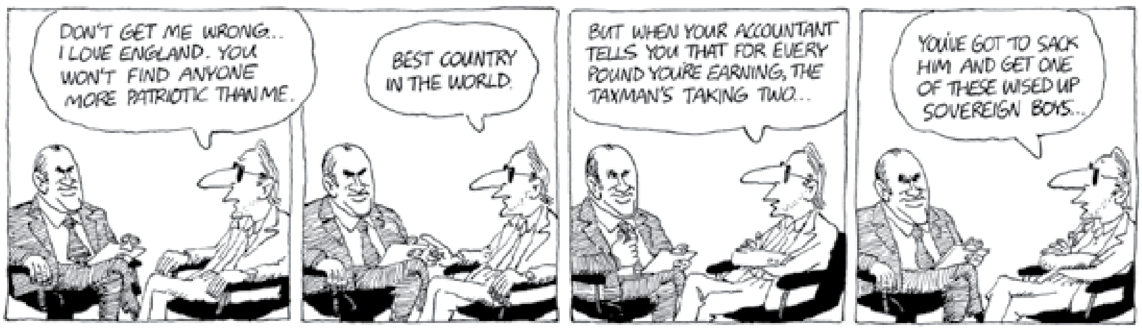
Former senior Swiss banker cleared on US tax charges

Raoul Weil, former head of wealth management at UBS, was acquitted in a federal court in Florida on 3 November 2014 of helping wealthy US customers hide $20bn in offshore accounts. The verdict is a setback for the US tax authorities.

The jury took just over an hour to reach its verdict after a three-week trial ended abruptly, when the defence declined to call any witnesses and asserted that the prosecution had failed to make its case.

Weil was formerly the third most senior banker at UBS, which paid $780m in 2009 to settle allegations made by the US Department of Justice that it had abetted tax evasion. It also handed over 4,450 names of US clients.

Weil was declared a fugitive from US justice in 2009 but, after leaving UBS, worked openly as chief executive of an independent Swiss asset management firm. He was arrested in Italy while on holiday in 2013 and agreed to be extradited to the US.



Whatever you do, don't lose art

A version of this article by Sovereign Group chairman Howard Bilton first appeared in B Beyond, a magazine for leading philanthropists, art collectors and outstanding achievers.

The readers of this esteemed organ are a sophisticated bunch and its content focuses quite heavily on art, so I am assuming that most, like me, are collectors of art. If I'm correct in that assumption, then I hope an article dedicated to maximising the value of your art collection and maintaining it for future generations should be of more than passing interest.

Most B Beyond readers will travel extensively and many will probably also own multiple homes. This necessarily makes life more complicated. There will be different considerations depending both on where the art collector is domiciled and resident and on where their art is actually hanging. An article that tried to cover every different eventuality in every different country would, of course, end up being a very lengthy book. I don't wish to detain you that long so for the purposes of this article I will be writing with particular reference to UK law. The details will therefore be UK-specific but many of the issues will be universal.

The UK charges inheritance tax (IHT) at 40% – over and above the personal allowance of £325,000 – on all assets located in the UK, irrespective of the domicile or residence of the owner. Art that is hanging on a wall in the UK is deemed to be a UK-situated asset. Nasty. It is even worse for those individuals who are actually domiciled in the UK. They are subject to UK IHT on their worldwide assets, so they would be liable to pay the 40% on the value of their art collection wherever it is located. It could even be the case that the country where it is located also wants to charge IHT or estate duty on the same asset.

An exception is made if an artwork is owned by a non-domiciled individual and is situated in the UK only for public display or cleaning and restoration, but this provision is unlikely to apply in most cases. With capital taxes it is by no means certain that a credit would be given for tax paid in one country against tax due in another so it is possible that two charges can occur on the same asset, virtually wiping out its value to anybody other than the tax man. Not good.

Many long term residents of the UK who have never formally acquired a UK domicile my still discover that they have been "deemed domiciled" – and are therefore subject to UK IHT on their worldwide estates, even though they still pay capital gains and income taxes according to the very generous rules applicable to non-UK domiciled persons. A deemed domicile will occur if a person has spent 17 out of the last 20 years resident in the UK. This can often catch out long-term UK residents.

One way to eradicate UK IHT is to bequeath the assets to a recognised charity. Art collectors often tend to be of a philanthropic persuasion so it is quite common for collections to be left to a public gallery or museum. In theory the IHT exemption would apply to a gift to any such institution because most museums are established with charitable status. It would also fall within the "public display" provision noted above but, until recently, UK legislation only applied the exemption to gifts to UK charities.

European law has since extended this provision to any charity in the European Union but it is by no means certain that the exemption would apply to bequests to institutions further afield, even if it was a charity under its domestic legislation. A solution to this problem may be to set up your own EU-registered charity and make the gift to that. The charity could then loan or gift the collection as it saw fit.

Those collectors who prefer to retain their art collection within the family would still be liable to pay IHT in the UK unless it can be effectively planned out. The standard planning is to transfer the art to discretionary trust, thereby placing it outside the former owner's estate for IHT. The trust would then be at liberty to dictate what should happen to the art both now and after the death of the owner (known as the "settlor" in legal argot). Excellent. The problem is how to get the property into trust.
A simple gift would be subject to the lifetime IHT rules in the UK and would therefore attract an immediate charge of 20% of the current value of the artwork or collection. Further, the transfer would be deemed to be a "sale" for capital gains tax (CGT) purposes. If the owner was resident in the UK, CGT would be payable on the difference between the acquisition price and current value.

" Failing to take considered and timely action in respect of your art collection could be a profound mistake. "

Non-UK domiciled persons can eradicate this potential CGT charge by first transferring the art to an offshore company and then gifting the shares in the offshore company to a trust that is based outside the UK. Once this transfer has been accomplished, the art would no longer be an UK asset and so no CGT charge would apply.

Another way of circumventing the 20% charge would be to have the trust purchase the art. Sales do not attract the 20% charge but CGT would apply unless the owner was non UK resident at the time of the sale. There are currently plans to extend the CGT regime to include non-UK residents transferring UK real estate interests but these proposals do not extend to a sale of chattels such as art.

There are a number of hidden traps depending on the status of the settlor of the trust. For instance, it could be that the trust is deemed subject to a ten-yearly charge of up to 6% of the assets held. Various "anti-avoidance" rules can also be brought into play if the settlor continues to "enjoy" the art by hanging it on their wall without making any payment or providing other valuable consideration. In this case, the gift could be deemed incomplete and the art remaining within the donors estate for IHT purposes. Both potential traps can be avoided with care.

The only remaining option is a good taxidermist and an electric rocking chair – which actually doesn't sound too far fetched in the context of modern British art.

Failing to take considered and timely action in respect of your art collection could be a profound mistake. The major auction houses frequently have estate sales where a major art collection is sold on the death of the owner. You may even have brought art from just such a sale. This may be because the beneficiaries of the estate have little interest in the collection but often it is simply because they need to generate cash to pay the IHT bill. A little planning now can be of huge benefit to your family or other beneficiaries.

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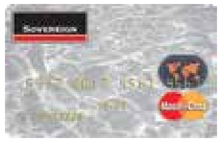

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