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SOVEREIGN REPORT

44

INTRODUCING...
SIMON GARVEEN

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

The Sovereign Art Foundation's *Make It Better* project uses the arts to help Hong Kong's underprivileged children build self-confidence, social awareness and engagement with their communities.

KUNG HEI FAT CHOY

That's Happy New Year in Cantonese. Last month the Year of the Sheep (or Ram or Goat) was welcomed in by the usual fanfare and the week-long festivities, not just in China but around the world as "CNY" becomes an ever more global celebration of Chinese culture. China continues its rapid economic development at home, while its foreign investment programme is making an increasing impact around the world – and not just in Asia, but in Africa and the Americas too. The economy has recently experienced fairly steep contractions in its annual GDP growth rate from the dizzying heights seen in recent years. Nevertheless China's GDP is still expected to grow at the rate 6.8% in 2015 and colleagues in our Sovereign China offices continue to see ever increasing levels of interest from around the world in investing in China. Our China entry services business continues to grow. Negotiating the local and national regulations in China is not uncomplicated but they are there to guide you through the maze.

CYPRUS

Regular readers will have followed the banking crisis in Cyprus with concern in recent years. A recently announced relaxation of capital movements is hugely welcome. Details can be found on the Europe pages of this edition. Clearly a large proportion of the island's economic difficulties relate to its close relationship with Greece. It is to be hoped that the new government in Athens manages to agree a way forward with the EU. Given this background, it is good to report that Sovereign's Cyprus office recently celebrated its 15-year anniversary. Despite the problems surrounding the banking sector, the jurisdiction continues to thrive. Robust royalty routing arrangements and an innovative citizenship programme are just two examples of what Cyprus has to offer.

KEE CLUB CHARITY HOUR TO "MAKE IT BETTER"

In February, KEE Club in Hong Kong hosted a cocktail fundraising event for The Sovereign Art Foundation (SAF) to re-launch its *Make It Better* project. The night was an incredible success and SAF raised US$15,000 in direct donations – a great result for a two-hour cocktail party.

The *Make It Better* project is expanding to include kindergarten and teenage children, and will focus on empowering young, underprivileged members of society through art. Underpinning the effort is an innovative collaboration between Hong Kong University, our highly experienced partner charities, and a diverse group of professionals and practitioners who, with SAF's backing, are intent on creating the preeminent "healing through art" programme in Hong Kong.

If you wish to volunteer or donate to the *Make It Better* project please email **Alex@SovereignArtFoundation.com**

SOVEREIGN PEOPLE

In the last issue I mentioned Bernadette Fulton's recent appointment as Managing Director of our Mauritius office. New premises have now been secured and more staff recruited in this increasingly important Indian Ocean jurisdiction, which is conveniently located between the African mainland and India. We have had an operation on Mauritius since 2000 and this expansion will enable us to better meet the worldwide demand for services there.

I would also like to extend a warm welcome back to Jacques Scherman, who is well known to many Sovereign clients. Jacques previously ran our Hong Kong office but has now returned home and will be based in our Cape Town office. He can be contacted at **jscherman@SovereignGroup.com**

SOVEREIGN FUND MANAGEMENT (SFM)

As many of our readers will know, implementation of the EU's Alternative Investment Fund Management Directive (AIFMD) has made it much more difficult for fund managers, particularly third country fund managers, to market their funds within Europe. I am pleased to announce that we have therefore created our own AIFM – Sovereign Fund Management (SFM) – to serve as an AIFM platform in Europe. SFM is incorporated and regulated in Gibraltar, which is part of the EU, and is therefore able to leverage the AIFMD passport opportunities for cross-border European distribution. For a fuller explanation see page 9.

IN THE PRESS

Finally, as this edition goes to print, policy makers around the world are pushing harder and harder on transparency, not least to boost their much-depleted revenues in the wake of the world financial crisis. In this, the politicians are being ably supported in their endeavours by the media which, in demonising the industry, continually fails to acknowledge that most planning is legitimate and compliant – just like it is onshore – and that ultimately the responsibility lies with the taxpayer. This is something we always stress to clients and I would invite you to turn to my article on page 17 of this edition.

Howard Bilton
Chairman of The Sovereign Group

EUROPE

Gibraltar announces legislative and regulatory overhaul

The Gibraltar government and Financial Services Commission announced jointly, on 28 January 2015, a complete overhaul of the legislative and regulatory framework for financial and professional services in Gibraltar. The aim is to streamline and rationalise over 80 different pieces of current legislation and multiple FSC guidance notes into one Act and a single accompanying regulatory handbook.

"(We are) working to establish Gibraltar as the EU domicile of choice across the full spectrum of financial services," the government said in a proposal document. "Critical to the achievement of this objective is efficient, robust and responsive regulation."

The project is an important part of the government's strategy for the development of the Gibraltar financial and professional services market and is a key component of the FSC's strategic programme published last October. The planned changes are set out in an 18-page document published on the FSC website.

Albert Isola, Minister for Financial Services and Gaming, said: "We will be putting in place a simpler, highly navigable legal framework, which will, together with our investment in strengthening the FSC, result in a more efficient and responsive regulatory regime building on enhancing the key elements of our reputation, regulation and speed to market."

SOVEREIGN COMMENT

We have long supported government efforts in Gibraltar to rationalise financial and professional services legislation and welcomed the introduction of the new Companies Act in 2014. Gibraltar enjoys a unique status – as part of the EU, Gibraltar-regulated firms are able to passport their services throughout the 28 nation bloc but Gibraltar's exclusion from the EU Customs Union means that there is no VAT regime in place. International advisers and their clients, in particular from Asia, recognise the growing importance of the jurisdiction and its potential across many different sectors.

Portugal changes rules on tax residency and taxation of trusts

Portugal has altered its rules concerning residency for tax purposes. For those arriving in or leaving Portugal from 1 January 2015, residence will be determined over a 12-month period before arrival or departure. Previously the basic rule was that a person would be considered tax resident if they spent more than 183 days in Portugal during the calendar (fiscal) year or had their principal place of residence in Portugal at 31 December.

The new rules still maintain the 183-day residency but that can now be in any period of 12 months – in other words spanning two calendar years if necessary. For the purposes of deciding length of stay, it is considered to be any day or part day in which the individual slept in Portugal.

In addition tax residency is assumed to have occurred as from the first day in which the person takes up permanent residency and a person's principal place of habitual residence rule applies is assumed as the fiscal domicile unless the person proves otherwise.

Also as of 1 January, a law was introduced to tax distributions from fiduciary structures, such as trusts and foundations, to Portuguese resident individuals. Where the beneficiary is also the settlor, the tax rate is 28% when, and only when, the income received is the result of the liquidation, revocation or termination of the trust and the distribution or refund exceeds the value of the assets that were originally settled to the trust fund when it was established. Where the recipient is a third party, it will suffer a stamp duty of 10% if, and only if, the asset or right acquired is situated in Portuguese territory at the acquisition date and no stamp duty exemption is available.

These changes may be significant for trust settlors and beneficiaries. For more detail contact Sovereign's Portuguese office please.

Fourth European AML Directive published in full

The full text of the fourth anti-money laundering directive (AMLD) was published for the first time on 27 January 2015 following its endorsement by the Economic and Monetary Affairs and Civil Liberties committees. If endorsed by the full European Parliament and the EU Council of Ministers, member states will have two years to transpose the directive into their national laws

The fourth AMLD will for the first time oblige EU member states to keep central registers of information on the ultimate "beneficial" owners of corporate and other legal entities, as well as trusts. These central registers were not envisaged in the European Commission's initial proposal, but were included by MEPs during negotiations.

The central registers of corporate and other legal entities will be accessible to: the authorities and their financial intelligence units without any restriction; to "obliged entities" such as banks conducting their "customer due diligence" duties; and also to the public although public access may be subject to online registration of the person requesting it and to a fee to cover administrative costs.

To access a register, a person will have to demonstrate a "legitimate interest" in suspected money laundering, terrorist financing and in "predicate" offences that may help to finance them, such as corruption, tax crimes and fraud. These persons, such as investigative journalists, could access information such as the beneficial owner's name, month and year of birth, nationality, country of residence and details of ownership. Any exemption to the access provided by member states will be possible only "on a case-by-case basis, in exceptional circumstances".

Central register information on trusts will be accessible only to the authorities and "obliged entities".

The text also clarifies the rules on "politically-exposed" persons" – people at a higher than usual risk of corruption due to the political positions they hold, such as heads of state, members of government, supreme court judges, and members of parliaments, as well as their family members. Where there are high-risk business relationships with such persons, additional measures should be put in place to establish the source of wealth and source of funds involved.

MEPs also approved a deal on a draft "transfers of funds" regulation, which aims to improve the traceability of payers and payees and their assets.

Swiss Federal Council consults on international exchange of tax information

The Swiss Federal Council launched two consultations on legislation to facilitate the international exchange of information in tax matters on 14 December 2014. One bill relates to the OECD/Council of Europe administrative assistance convention signed by Switzerland in 2013, while the other relates to implementing Swiss participation in the Multilateral Competent Authority Agreement on the Automatic Exchange of Financial Account Information (MCAA), which was signed by Switzerland on 19 November 2014.

The Council's decision to sign the administrative assistance convention and implement the global automatic exchange of information (AEOI) standard is in line with its strategy for a competitive Swiss financial centre, which includes the international standards in the area of tax and particularly those concerning transparency and the exchange of information.

The bilateral activation of the AEOI will be addressed in separate bills that will be submitted to the Federal Assembly for approval. Corresponding negotiations with the European Commission and possible partner states are under way or will commence in the near future.

The Federal Council is also proposing to make two declarations. Firstly, that Switzerland will generally inform affected persons about the forthcoming exchange of information and secondly, that Switzerland will not allow foreign authorities' requests to conduct tax audits in Switzerland. The issue of the countries with which Switzerland should establish the automatic exchange of information will be presented to parliament separately at a later stage.
Both consultations will run until 21 April 2015. The Federal Council's dispatches for the attention of parliament are expected in summer 2015, enabling parliament to debate draft legislation from autumn 2015. It is intended that the legislation should come into force from the beginning of 2017 with the first automatic exchange of information taking place in 2018.

SOVEREIGN COMMENT

After a difficult period in the last few years, much of it connected with Greece's well-known financial troubles, it is reassuring to note these positive developments from Cyprus. It is another sign that the jurisdiction is slowly returning to its former position as one of Europe's leading international finance centres. The note on the Chairman's Page of this edition points out that our Cyprus office is 15-years-old this year. The office is well placed to offer the full range of services that Cyprus has to offer, including the island's residency/citizenship programmes and royalty routing solutions. Contact George Ayiomamitis in Cyprus for more information.

San Marino Aircraft Registry ratifies Cape Town

The government of San Marino, the tiny Italian enclave near Rimini, ratified the Cape Town Convention on International Interests in Mobile Equipment on 1 January 2015. Known simply as "Cape Town" for short, it provides for a readily accessible online register of rights and prioritisation over aircraft and engines that is supervised by the UN's International Civil Aviation Organisation (ICAO) and is designed to facilitate the financing and acquisition of aviation assets.

Cape Town has now been ratified by nearly 50 jurisdictions worldwide. David Colindres, president of the San Marino Aircraft Registry (SMAR), said: "This ratification is very important as it gives value added and confidence to banks and leasing companies. The registration of interest in an asset such as an aircraft is considered to be best practice for owners, creditors, debtors, lessors, lessees, agents and others in protecting their financial interest in such an asset."

SOVEREIGN COMMENT

San Marino's aircraft registry has reported good progress since its re-launch in 2012. Ratification of the Cape Town Convention is another important step in its development. Aviation news from San Marino and the other international aircraft registries is covered in our e-newsletter Airborne, which is published monthly by Sovereign's aviation division. To be included on the mailing list, contact RegisterAnAircraft.com. Details are on the back page of this Report.

Cyprus relaxes restrictions on capital movement

The Finance Ministry published, on 8 December 2014, Decree 32 under Articles 4 and 5 of the Enforcement of Restrictive Measures on Transactions in Case of Emergency Law of 2013, which has further relaxed restrictions on capital movement. Under the Decree:

- Central Bank of Cyprus approval is no longer required for payments or transfers of funds abroad up to €2 million (previously €1 million);
- The transfer of deposits or funds abroad up to €10,000 (previously €5,000) is now freely permitted;
- Physical exports of euro notes or foreign currency notes are permitted up to €6,000 (previously €3,000) per natural person, per journey abroad.

Capital controls were imposed on the island's banking sector in 2013 as part of a European Union agreement for a €10 billion euro international bailout, which forced major depositors at the two biggest banks in Cyprus to pay part of the cost of the rescue.

Italy opens voluntary disclosure programme for foreign assets

The Italian parliament approved legislation, on 4 December 2014, to introduce a voluntary disclosure programme under which Italian citizens can regularise undeclared capital held abroad. Taxpayers will be obliged to pay all the taxes due but will be subject to reduced administrative penalties and immunity from some criminal penalties.

Under the final Decree, effective as of 1 January 2015, voluntary "self-declarations" of undeclared assets have to be made by 30 September 2015, but persons who are already subject to a tax audit or investigation will not be eligible.

An application for inclusion in the programme will need to contain details of all investments or financial assets held – directly or indirectly – abroad for all the tax periods for which the statutes of limitation have yet to expire up to 30 September 2014. Applicants must be identified by name and will have to provide all relevant bank and other financial intermediary details, so that the history of, and all income from investments can be reconstructed.

The tax rates applied are the statutory rates but it is possible to benefit from a 27% flat tax rate, provided that the average financial assets value is less than €2 million in each tax year. The taxable income will be calculated as 5% of the value of the financial assets at the end of each tax year.

A reduction of 50% of the penalties will apply if the undisclosed financial assets were held in, or are transferred to Italy, another EU Member State or to an EEA Member State that is a "cooperative country". However, if undisclosed financial assets were held in a currently black-listed non-cooperative state, the related penalties are doubled, unless the non-cooperative state signs an agreement on exchange of information within 60 days of the law entering into force.

Participants in the programme will have to remit all taxes that would have been payable on undeclared investments, in one lump sum or three monthly instalments, but with much reduced administrative and criminal penalties. They will also be free from criminal prosecution, including a new criminal offence of money laundering, which was introduced under the Decree.

SOVEREIGN COMMENT

It is interesting to note that Switzerland signed a Protocol to its double tax treaty with Italy on 23 February, which makes provision for the OECD standard for the exchange of information upon request. This was within the 60-day window set by Italy for "blacklisted" states and will therefore enable the regularisation of untaxed assets held by Italians in Switzerland at the reduced rates.

Russia introduces "de-offshorisation" Law

Russian President Vladimir Putin signed a new Law (No. 376-FZ) on 24 November 2014 that makes wholesale changes to the taxation of foreign entities. The Law introduces: the concept of "beneficial ownership"; a new definition of corporate residence, a controlled foreign company (CFC) regime; new rules on the indirect disposal of shares of Russian real estate-rich companies; and requirements that Russian legal entities and individuals disclose information on their interests in foreign companies. The Law came into effect on 1 January 2015.

The new law incorporates a statutory definition of the concept of beneficial ownership into the Russian tax code. To apply the provisions of a tax treaty to the payment of income to a foreign company, the Russian payer will have to first obtain a tax residence certificate from the non-resident that is the beneficial owner of the income. The Russian payer is entitled to request a confirmation that the recipient is the beneficial owner of the income.

The new law amends the definition of tax residence for companies to be based on the place of effective management of the company rather than the place of incorporation. Legal entities incorporated abroad but meeting the place of effective management test will be subject to unlimited tax liability in Russia.

Under the new CFC regime, foreign companies managed and controlled from Russia will pay the same profits tax as Russian companies where certain conditions are met. According to the government, the new CFC legislation will prevent companies from using low tax jurisdictions to obtain unjustified tax benefits and allow for the taxation of the undistributed profits of CFCs.

A "controlled foreign company" is a foreign company – including corporate entities or structures without legal identity established under the laws of a foreign country – that is managed and controlled by a Russian tax resident.

A "controlling person" of a foreign entity is any natural or legal person whose participation in the foreign entity exceeds 25%, or individuals, together with a spouse and dependents, whose participation exceeds 10%, and the share of participation of all residents exceeds 50%. The participation threshold will be reduced to 25% from 2016, rather than the 2017 date suggested during the first reading of the Bill.

A foreign company is not subject to the CFC legislation if it is situated in a country with which Russia has signed a double tax treaty, providing that the partner country also exchanges tax information on request and has an effective corporate tax rate that is at least 75% of the weighted average Russian tax rate, which now factors in dividend tax rates as well as Russia's 20% corporate income tax rate.

Foreign companies whose passive income accounts for less than 20% of their profits will also be exempt, as will foreign companies undertaking crude oil activities outside Russia on certain conditions.

The new regime sets out specific notification requirements concerning companies deemed to be CFCs, with reporting to begin from as soon as early 2015. A new penalty regime has also been put in place.

The minimum amount of profit that must be declared will decrease from 50 million roubles ($1.065 million) in 2015, to 30 million roubles in 2016 and 10 million roubles ($213,190) after 2017. Russians must notify the tax service of the ownership of more than 10% of authorised capital of a CFC before April 2015.

SOVEREIGN COMMENT

This is a wide ranging series of changes; the new rules governing CFC legislation will be of particular interest to advisers and their clients. Anyone who may be affected by the new law should not delay in ensuring they remain fully compliant. Russian government efforts are likely to be stepped up given the sharp decline in the country's economy due to US and EU sanctions and the near halving of the oil price.

AMERICAS & THE CARIBBEAN

Obama proposes tax on overseas profits of US firms

US President Barack Obama proposed, on 2 February 2015, a one-off 14% tax on the profits of US corporations held overseas, as well as a 19% tax on future overseas profits as they are earned. The move, part of the 2016 budget proposals, is linked to boosting infrastructure spending.

No tax is currently imposed on the foreign profits of US corporations provided that they are not brought into the US. Research firm Audit Analytics calculated last April that US corporations were holding $2.1 trillion of profits abroad. General Electric reported US$110 billion in undistributed overseas earnings in 2013, while the figure for Apple Inc. was US$54.4 billion.

The Obama administration said its plans for an immediate 14% tax would raise $238 billion, which would be used to fund a wider $478 billion public works programme of road, bridge and public transport upgrades.

"This transition tax would mean that companies have to pay US tax right now on the $2 trillion they already have overseas, rather than being able to delay paying any US tax indefinitely," said a White House official, while the 19% permanent tax on overseas profits "would level the playing field, and encourage firms to create jobs here at home." Companies could reinvest those funds in the US without paying additional tax.

Canada launches immigration pilot programme for HNWIs

The Canadian government opened a new Immigrant Investor Venture Capital (IIVC) Pilot Programme on 28 January 2015, but only for a limited period to 11 February. The Pilot Programme, which was announced on 16 December, will offer 50 high-net-worth individuals (HNWIs) and their families with a pathway to permanent residence.

Under the programme, applicants must make a CAD2 million non-guaranteed investment into the IIVC fund for 15 years. They will also have to demonstrate that they can integrate into Canada's economy and society. The selection criteria includes: proficiency in one of Canada's official languages; education credentials; and a net worth of at least CAD10 million (obtained legally).

"Through the launch of this pilot programme, we are attracting investors who can make a significant investment and who have the education and proven business or investment experience necessary to achieve success in Canada," said Citizen and Immigration Minister Chris Alexander. "The funds will be invested in innovative Canadian-based start-ups with high growth potential."

The IIVC pilot programme comes after the government scrapped both the immigrant investor programme and the entrepreneur programme last year. Launched in 1986, the immigrant investor programme offered visas to business people with a net worth of at least CAD1.6 million who were willing to lend CAD800,000 to the Canadian government for a term of five years.

It was been put on hold in 2012 due to a huge backlog of applications and was then cancelled because, the government said, it had been riddled with fraud. Thousands of applicants who had been waiting for permanent residency under the programme sued the federal government but a Federal Court judge ruled against them in June last year.

SOVEREIGN COMMENT

The cancellation of the previous IIP programme last year was met with considerable disappointment by both practitioners and potential applicants alike because Canada remains one of the most popular IIP jurisdictions. The opening up of this pilot programe, albeit very limited in scope, is hugely welcome because it should lead to a full relaunch of the IIP in the future. Sovereign and its trusted partners are well placed to assist applicants for IIPs both in Canada and elsewhere in the world. For further information about global residency and citizenship programmes, contact your local Sovereign office.

IRS opens FATCA data exchange service

The US Internal Revenue Service introduced, on 12 January 2015, an International Data Exchange Service for foreign financial institutions (FFIs) and their host country tax authorities to send information reports on financial accounts held by US persons under the Foreign Account Tax Compliance Act (FATCA) or under the terms of an intergovernmental agreement (IGA).

FATCA requires foreign financial institutions (FFIs) to report on the holdings of US taxpayers to the IRS or withhold up to 30% in tax on their US-source income. More than 145,000 FFIs have registered through the IRS FATCA Registration System. The US has also signed, or agreed in substance, more than 110 IGAs with other jurisdictions.

"The opening of the International Data Exchange Service is a milestone in the implementation of FATCA," said IRS commissioner John Koskinen in a statement. "With it, comes the start of a secure system of automated, standardised information exchanges among government tax authorities. This will enhance our ability to detect hidden accounts and help ensure fairness in the tax system."

Where a jurisdiction has a reciprocal IGA and the jurisdiction has the necessary safeguards and infrastructure in place, the IRS will also use IDES to provide similar information to the host country's tax authority on accounts in US financial institutions held by the jurisdiction's residents. IDES is an online application that features encryption at both the file and transmission level in order to safeguard sensitive tax information.

The IRS has also announced that its current Offshore Voluntary Disclosure Programme (OVDP), which opened in 2012, will remain "open for an indefinite period until otherwise announced". It said that since the first OVDP opened in 2009, there had been more than 50,000 disclosures and it had collected more than $7 billion from the initiative.

SOVEREIGN COMMENT

As reported in previous editions, the Sovereign Group is totally compliant with the US FATCA rules worldwide and our offices have registered accordingly. As a result, we continue to welcome US resident clients or US expatriate citizens but of course this is on the basis that any US taxpayers' holdings will be reported to the IRS in compliance with our FATCA obligations. The second part of the news item above concerning the indefinite extension of the OVDP is also noteworthy; readers concerned about their own situation in this regard should contact professional advisers as soon as possible.

Cayman stands firm on beneficial ownership regime

The Cayman Islands government followed Bermuda in rejecting, on 30 December 2014, the UK's request that its Crown Dependencies and Overseas Territories should create public access central registers of the beneficial owners of companies. Minister of Financial Services and Commerce, Wayne Panton, said that Cayman has been adhering to the global standard for more than a decade by providing this information to law enforcement, tax and regulatory authorities from data collected, verified and maintained by licensed and regulated corporate service providers.

The Cayman government, in a report based in part upon the responses given during a recent public consultation, determined that no change was necessary to Cayman's already effective beneficial ownership system. Some 80% of those who responded did not believe Cayman needs a central register with public access.

In the report, the government noted that the Financial Action Task Force (FATF) Recommendations outlined three options for countries to comply with the global availability of information standard. The UK, it said, was now taking steps to adhere with the standard via one of these options, by consolidating information into a central register, but the Cayman's CSP regime was another option that adhered to current global standards.

Furthermore, Cayman's CSP regime also complied with the core set of principles in the G20's High-Level Principles on Beneficial Ownership Transparency, which was issued last November. As a result, the Cayman government stated: "Until such time as there is global agreement on appropriate exemptions and safeguards, and this becomes the internationally practiced standard, the Cayman Islands will continue to follow its CSP regime."

Jude Scott, chief executive of Cayman Finance, said: "The changes that were being insisted upon were unreasonable and went far beyond globally accepted practices which would only serve to create unfair and unnecessary disadvantage and damage for Cayman's financial services industry."

SOVEREIGN COMMENT

This fascinating debate will no doubt intensify due the leadership role that the UK has taken at both the G20 and the EU level. The Cayman government is not alone in arguing that it already complies with the international standards set by OECD and FATF amongst others. Most of the UK overseas territories are in the same, strong, position. It will be interesting to see how this develops but, as we continue to stress, structures held by Sovereign clients should be fully reportable so any concerns should simply not apply.

The report also outlines steps that the government will take to further strengthen Cayman's framework through enhanced accuracy, access, availability, and monitoring and enforcement of ownership information.

Cayman Grand Court (Amendment) Law comes into force

The Cayman Islands government gazetted, on 20 October 2014, the Grand Court (Amendment) Law (Law 15 of 2014) to facilitate grant of interim relief in aid of foreign proceedings. This inserts a new Section 11A, which empowers the Grand Court to make an order appointing a receiver, or orders for any other interim relief that it would have the power to grant in proceedings within its jurisdiction, in respect of proceedings which have been or will be commenced in an overseas court and which are capable of giving rise to a judgment that may be enforced in the Cayman Islands under any statute, or at common law.

Section 11A(4) empowers the Grand Court to make such orders for interim relief even if the cause of action which is being litigated in the foreign proceedings is not a cause of action which could be litigated in the Cayman Islands. It also provides that the order need not be ancillary or incidental to any proceedings in the Cayman Islands.

Section 11A(5) entitles the court to refuse an application for interim relief if, in its opinion, it would be unjust or inconvenient to make an order. Further, Section 11A(6) requires the court to have regard to the fact that the power is ancillary to proceedings outside the Cayman Islands, and that the purpose of the power is to facilitate the process of the foreign court that has primary jurisdiction over the dispute.

The changes necessary to make to the Grand Court Rules to provide for service out of the jurisdiction of this new form of relief have not yet been implemented.

BVI brings Arbitration Act 2013 into force

The British Virgin Islands Arbitration Act 2013, which is intended to facilitate alternative dispute resolution in the BVI, was brought into force on 1 October 2014. The Act is modelled on the United Nations Commission on International Trade Law (UNCITRAL) Model Law on International Commercial Arbitration, which provides rules on arbitration proceedings and is recognised internationally by many countries. This ensures that BVI arbitration will be conducted according to international standards and that BVI arbitrations will also be internationally recognised.

The BVI became a signatory to the UN Convention on Recognition and Enforcement of Foreign Arbitral Awards (the New York Convention) on 25 May 2014, which will ensure that BVI arbitration awards are enforceable in all countries that have signed up to the Convention.

The Act also makes provision for the establishment of a corporate body known as the BVI International Arbitration Centre (IAC) to promote and facilitate arbitration in the BVI. The IAC will be tasked with, among other things, providing all the facilities and services necessary for the conduct of arbitral proceedings and mediation in the BVI.

The definition of a valid arbitration agreement has been significantly widened. The Act provides that an arbitration agreement is an agreement by the parties – whether signed or not – to submit to arbitration all or certain disputes that have arisen between them in respect of a defined legal relationship whether contractual or not. The agreement must be in writing. An agreement is in writing if its content is recorded in any form, whether or not the arbitration agreement has been concluded orally, by conduct, or by other means.

INVESTMENT NEWS

SOVEREIGN ASSET MANAGEMENT

- A SOLUTION FOR ALTERNATIVE INVESTMENT FUNDS

By Marion Frings, Investment Consultant – Sovereign Asset Management

The Alternative Investment Fund Management Directive (AIFMD), which came into force on 22 July 2013, establishes a harmonised regulatory framework for firms that manage and/or market alternative investment funds (AIFs) in the European Union. It is the most radical reshaping of fund management and marketing regulation in the EU since the UCITS directive changed the landscape for European retail investment funds.

AIFMD applies to Alternative Investment Fund Managers (AIFMs) domiciled in the EU that manage EU or non-EU domiciled AIFs, as well as to non-EU domiciled AIFMs that manage non-EU domiciled AIFs and market them in the EU. AIFMD introduces a common EU approach to bringing alternative funds and their managers within the scope of regulatory supervision, and creates transparency and stability to the way these funds operate.

Under the new directive, AIFMs who manage AIFs with assets under management of at least €100 million (leveraged) or €500 million (close-end, unleveraged) are required to be authorised and thereby comply with obligations such as capital requirements, operational requirements, depository requirements, remuneration, conflicts of interest, risk and liquidity management, transparency, disclosure and regulatory reporting. Further obligations target private equity firms and funds that are substantially leveraged.

Achieving AIFM authorisation involves significant time and cost. There are onerous on-going requirements that will require additional resources including compliance, regulatory and risk management expertise, as well as IT resource to implement processes.

The Sovereign Group has therefore created its own AIFM – Sovereign Fund Management (SFM) – to serve as an AIFM platform in Europe. SFM is a fully owned subsidiary of the Sovereign Group, which has a global office network and assets under administration in excess of US$5 billion. SFM is incorporated and regulated in Gibraltar, which is part of the EU, and is therefore able to leverage the AIFMD passport opportunities for cross-border European distribution.

SFM will become the AIFM to a fund, appoint the manager to undertake delegated portfolio management and assume responsibility for all of the other duties under the AIFMD, such as risk management, compliance monitoring, regulatory reporting and investor due diligence. It will also appoint a depositary as required. SFM is a straightforward and cost effective solution that allows the investment manager to focus on its core business of analysing investment opportunities. It will be of particular use to:

- Existing EU AIF funds that are looking to cross over the AIFMD authorisation threshold;
- Fund sponsors that consider their own AIFM conversion too complex or costly;
- Non-EU AIFMs or AIFs looking to enter the EU for marketing purposes;
- AIFMs looking to establish sub-funds under an umbrella structure to take advantage of the AIFMD passport.

The Sovereign Group's existing master fund structures are incorporated in Gibraltar. These umbrella funds are structured as Gibraltar Protected Cell Companies (PCCs), which provide for the segregation of assets and liabilities between cells. The PCC structure also allows a manager to create a single investment house within which there can be accommodated several bespoke sub-funds with different investment risk parameters.

Sovereign's PCCs are set up as Experienced Investor Funds (EIFs), which are similar to the professional or specialised investor fund categories in other jurisdictions such as Malta or Luxembourg. The sub-funds can also be listed on a recognised stock exchange. Establishing a Gibraltar fund as an EIF presents a number of key advantages:

- Speed to market;
- Competitive start-up costs;
- No investment or borrowing restrictions;
- Tax neutrality;
- AIFMD compliance;
- Benefit of other EU Directives, such as Parent Subsidiary Directive (PSD).

The Sovereign Group has the experience and necessary licences to set up and manage funds in a number of jurisdictions, plus a proven track record both inside and outside the EU. Depending on a fund's needs, particularly in respect of its prospective investors and the countries in which it is to be promoted, Sovereign will have the appropriate solution.

MIDDLE EAST & ASIA

Abu Dhabi financial free zone selects English common law

The proposed Abu Dhabi Global Market (ADGM) published, on 7 January 2015, draft legislation for consultation, which sets out that the new financial free zone will have its own administration, court system and tax incentives to attract banks and companies from around the world.

Under the proposals, the ADGM will follow the Dubai International Financial Centre (DIFC) in basing its legal framework on English common law. "English common law, as it stands from time to time, will therefore govern matters such as contracts, tort, trusts, equitable remedies, unjust enrichment, damages, conflicts of laws, security, and personal property," ADGM said in one of six consultation papers.

It will also seek to adopt the most effective legislation from around the world. "ADGM has the opportunity to take the best of the UK approach, while avoiding some of its historic peculiarities that have been removed or abandoned by the best practice of other jurisdictions," it said. For example, shares in ADGM companies will not have a par value, in line with the approach taken in jurisdictions such as Hong Kong, Singapore and Australia.

It will also introduce a new type of "restricted scope company" with lighter disclosure and compliance requirements which, it said, would be "holding vehicles for professional investors and limited instances of institutions for whom less regulation and a greater degree of confidentiality will be appropriate." The ADGM is further considering extending this regime to include entities owned entirely by an individual or close family members.

China announces new measures on FTZs and pilot reforms

China's State Council announced, on 12 December 2014, its intention to reduce further the number of items on the "negative list" that applies to foreign-invested entities engaging in business in the China (Shanghai) Pilot Free Trade Zone (FTZ). The negative list sets out the industries and activities for which foreign investment is restricted or prohibited. In particular, more restrictions will be lifted in the service and high-end manufacturing sectors.

The Shanghai FTZ is also being expanded to include the Lujiazui financial district, Jinqiao development zone and Zhangjiang hi-tech park, which are all in the Pudong district of Shanghai. Enterprises established in these areas will be able to take advantage of all the preferential policies implemented in the Shanghai FTZ. The expansion will allow Shanghai to give full play to the advantages of the Pudong New Area and to test foreign investment reform on a larger scale, said officials.

The State Council is also to establish three new FTZs in Guangdong, Tianjin and Fujian, based on the existing special zones in these areas. The FTZs in Guangdong and Fujian will be aimed at promoting economic cooperation between Mainland China and Hong Kong, Macau and Taiwan while the new FTZ in Tianjin will focus on key industries, such as high-end manufacturing, financial services and logistics and transportation.

The rules in the new FTZs are expected to be similar to those in the China (Shanghai) Pilot FTZ but may also contain some aspects that reflect the features of the specific region. The State Council said it would further roll out nationwide 28 pilot measures on investment, trading, finance and the opening up of service sectors, as well as six pilot measures applicable to customs and inspections/quarantines in special customs areas.

The new FTZs and the expansion of the Shanghai FTZ will be effective 1 March 2015.

Microsoft fined $137 million for "tax evasion" in China

It was reported on 23 November 2014 that the Chinese authorities have levied US$137 million in back taxes and interest against an unnamed US multinational – understood to be Microsoft Corporation – in the first major case concerning cross-border tax evasion in the country.

According to an article published by China's Xinhua official news agency, a US multinational identified only as "M" must pay the Chinese government 840 million yuan (US$137 million) in back taxes and interest, as well as more than 100 million yuan in additional taxes a year in the future.

The report said "M" had reported losses for six years in China of more than 2 billion yuan while its competitors had posted profits; the tax authorities concluded its behaviour was unreasonable. It said the US company had admitted tax avoidance and its mainland subsidiary had agreed to pay the levy.

The article said "M" was one of the world's biggest 500 firms and had established a wholly owned foreign subsidiary in Beijing in 1995. Microsoft is the only company that fits that description.

SOVEREIGN COMMENT

Sovereign welcomes the development of new FTZs together with the ongoing expansion of the existing facilities. Of particular interest is the further relaxation of part of the "negative list" as set out in the story above. We have reported in past editions on the development of Sovereign China and that part of our business continues to go from strength to strength. Readers interested in learning about our China entry services may contact Sovereign China direct or alternatively via any Sovereign global office, all of whom are well positioned to assist.

According to its fiscal 2014 annual report, Microsoft's overall effective tax rate was 21% – well below the 35% US corporate rate – primarily because it channels earnings through "foreign regional operations centres" in Ireland, Singapore and Puerto Rico.

Dubai proposes new succession rules for non-Muslims

The Dispute Resolution Authority (DRA) of the Dubai International Financial Centre (DIFC) issued for public consultation, on 16 November 2014, draft rules relating to succession and inheritance for non-Muslims. The intention is to provide certainty to non-Muslims in passing their assets in Dubai to their chosen heirs without the need for proceedings in the Dubai courts.

Existing UAE law provides that the law of a deceased non-Muslim's nationality should apply to their estate but in practice the Dubai Courts have tended to apply Shariah law at first instance. Executors and heirs who do not wish the Shariah rights of inheritance to apply are then obliged to appeal through the Dubai Courts.

This can be a complex, costly and uncertain process during which assets located in Dubai may be frozen. As a result, non-Muslim individuals have been more reluctant to invest in Dubai and generally seek to minimise assets in Dubai by keeping cash offshore and holding real estate through an offshore company.

Under the proposed DIFC Will and Probate Rules (WPR), non-Muslim individuals with assets in Dubai will be able to execute and register a will under the jurisdiction of the DIFC and its courts. Upon death, the deceased's executors must apply to the newly formed DIFC Wills and Probate Registry for a grant of probate, which will be issued by the DIFC Court and will be directly enforceable in Dubai. A testator – a person making a will – will also be able to appoint guardians in respect of any minor children within a DIFC will.

The testator must be non-Muslim and aged 21 or older. The will must only cover moveable and non-moveable assets in Dubai, and must be signed in front of, and witnessed by, the registrar or an authorised officer. The DIFC said it intended to accept appointments for the registration of wills from January 2015.

SOVEREIGN COMMENT

It is very encouraging to see this proactive step. The proposed rules demonstrate the commitment of Dubai to supporting expatriates and should result in increased capital retention, as well as growth in direct investment. Further details may be obtained from our Dubai office.

MEBA makes debut at Al Maktoum

The new exhibition centre at Al Maktoum International Airport in Jebel Ali, 37 kilometres south west of Dubai, played host for the first time to the biennial Middle East Business Aviation exhibition (MEBA) on 8 December 2014. As the centrepiece of the Dubai World Central free zone, the airport is known as "the world's first purpose-built aerotropolis", with a projected annual capacity of 12 million tonnes of freight and 160 million passengers, as well as being the future home of 900,000 people. Organised by F&E Aerospace on behalf of the Middle East Business Aviation Association (MEBAA), official figures confirmed that with 420 exhibitors, over 7,000 attendees and 36 aircraft in the static park, it had well exceeded the figures for 2012. The principal manufacturers all featured their designs in the static park – notably Gulfstream, which displayed its newly certified G650ER at a trade event for the first time. At the smaller end of the market, much attention was also focused on the Ukrainian-built Softex-Aero V-24-L four-seat light business aircraft, which is designed to compete with the Diamond DA40/42.

Sovereign's Aviation Division Director Brian T Richards was struck by apparent changes in emphasis. "The new venue appears more compact and the show is certainly more logically laid out," he said. "However there seemed to be a paucity of 'jurisdictional' exhibitors, with the exception of the San Marino Aircraft Registry (and by association, Aruba). This was in marked contrast to the MEBA of two years ago when both the Isle of Man and Malta had a large presence. The show remains however a showcase for the industry and is a vital networking forum for companies such as Sovereign, which has a significant presence in the region."

Singapore to adopt OECD information exchange standard by 2018

Finance Minister Tharman Shanmugaratnam said, on 4 November 2014, that Singapore would implement the OECD's new global standard on Automatic Exchange of Information (AEOI) by 2018, provided certain conditions were met.

"There must be a level playing field among all major financial centres, including Hong Kong, Dubai, Switzerland and Luxembourg, to minimise regulatory arbitrage," he said in a written response to a parliamentary question.

Tharman also said Singapore would only agree to exchange information with countries that can ensure the confidentiality of the data they provide and offer reciprocity. "These conditions are necessary to make sure that we continue to respect legitimate expectations for taxpayer confidentiality," he said.

In October, finance ministers and tax chiefs from 51 countries, including Luxembourg, signed up to be "early adopters" of the new OECD standard. Singapore, Hong Kong, Switzerland and the United Arab Emirates were not among the signatories, although they have all signalled their intent to adopt the pact.

Singapore, which had more than US$1.40 trillion in assets under management at the end of 2013, brought in new rules last year to make tax evasion a criminal offence under its money laundering rules and has signed up to previous OECD standards on tax transparency.

SOVEREIGN COMMENT

This positive development is to be welcomed given Singapore's ever-increasing importance as a global financial centre. The staggering level of AUM demonstrates the substance of the jurisdiction and these new rules relating to tax transparency, taken together with the rules making tax evasion an offence, show that Singapore is willing to assume all the international responsibilities that go with it.

FISCAL NEWS

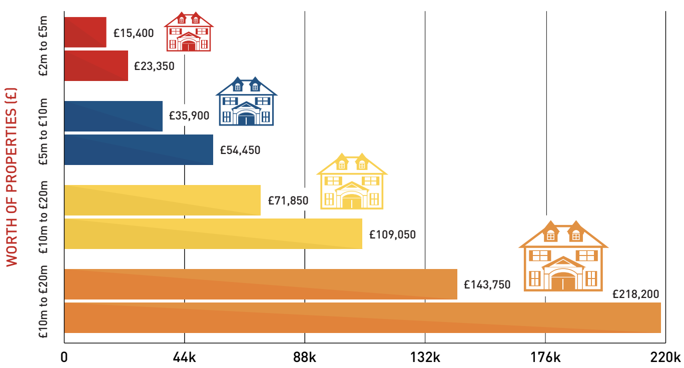
SOVEREIGN COMMENT

Readers with long memories may recall that the EU Savings Tax Directive originally came into force almost ten years ago, on 1 July 2005. These amendments to the Directive were proposed almost from the beginning and it is good to see that they have finally been agreed because a high degree of certainty is always preferred when dealing with European matters. It will take some time, as the item above concedes, for the legislation to be adopted across the EU. It will be interesting to see how long it is before yet further changes are demanded.

INCREASE IN ATED IN UK

"UK Chancellor George Osborne announced a raft of new measures to tackle tax evasion and aggressive tax planning in the Autumn Statement on 3 December 2014...The Annual Tax on Enveloped Dwellings (ATED) is to be increased."

-'UK ramps up tax measures in Autumn Statement', pg 13



EU signs off on enhanced parent-subsidiary directive

The Council of the European Union formally adopted, on 27 January 2015, a decision to add a binding anti-abuse clause to the EU Parent-Subsidiary Directive. An earlier amendment was adopted in July 2014 to tackle hybrid loan mismatch arrangements. Member states have until 31 December 2015 to transpose both changes into national law.

Revision of the Parent-Subsidiary Directive was part of the Action Plan for a more effective EU response to tax evasion and avoidance, which was presented by the European Commission in December 2012. It said the Directive, which was originally designed to prevent the double taxation of same-group companies based in different member states, was being exploited by certain companies to achieve double non-taxation.

The amendment to address loopholes related to hybrid loans involved the adoption of provisions to prevent corporate groups from using hybrid loan arrangements to achieve double non-taxation under the Directive.

The new "de minimis" (minimum standards) anti-abuse clause will enable member states to implement stricter or more specific domestic provisions or double tax treaty anti-abuse provisions. A common anti-abuse rule will allow member states to ignore artificial arrangements used for tax avoidance purposes and ensure that taxation takes place on the basis of real economic substance.

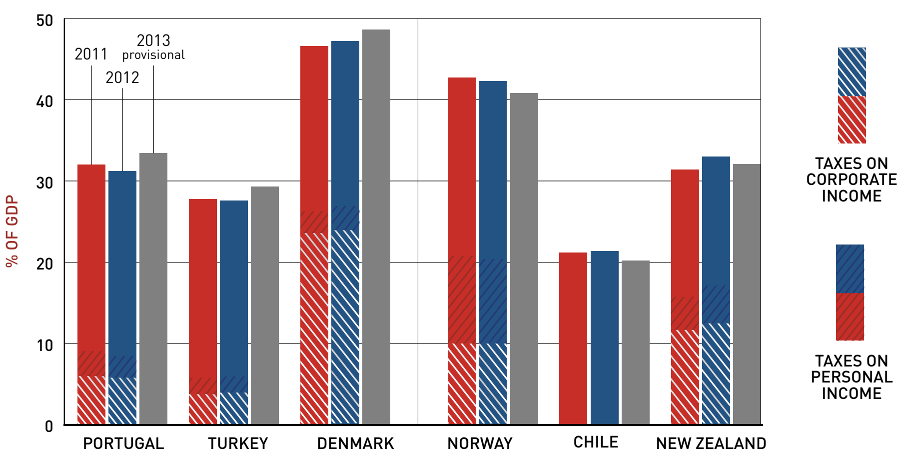
Pierre Moscovici, European Commissioner responsible for Economic and Financial Affairs, Taxation, and Customs, said: "With the Council's adoption of the anti-abuse clause of the Parent Subsidiary Directive today, the European Union is living up to its pledge of tackling tax evasion and aggressive tax planning. Today, we are building on the existing EU legislative framework to ensure a level-playing field for honest businesses in the EU's Single Market, and we are closing down loopholes that could be exploited for aggressive tax planning."

TAX INCOME AS % OF GDP (2011-13)

"In 2013, the tax burden rose in 21 of the 30 countries for which data is available, and fell in the remaining 9. The largest increases in 2013 occurred in Portugal, Turkey, the Slovak Republic, Denmark and Finland. The largest falls were in Norway, Chile and New Zealand."

-'OECD says tax revenues are rebounding from the financial crisis', pg 14

All figures from OECD.org



European Commission extends enquiry on tax rulings to all Member States

The European Commission broadened its enquiry into the tax ruling practice under EU state aid rules to cover all Member States on 17 December 2014. The Commission will ask Member States to provide information about their tax ruling practice, in particular to confirm whether they provide tax rulings and, if they do, to request a list of all companies that have received a tax ruling from 2010 to 2013.

Commissioner in charge of competition policy, Margrethe Vestager, said, "We need a full picture of the tax rulings practices in the EU to identify if and where competition in the Single Market is being distorted through selective tax advantages. We will use the information received in today's enquiry as well as the knowledge gained from our ongoing investigations to combat tax avoidance and fight for fair tax competition."

Since June 2013, the Commission has been investigating under state aid rules the tax ruling practice of seven Member States – Cyprus, Ireland, Luxembourg, Malta, the Netherlands, the UK and Belgium. It has also requested information about intellectual property taxation regimes, so-called "patent boxes", from ten Member States – Belgium, Cyprus, France, Hungary, Luxembourg, Malta, the Netherlands, Portugal, Spain and the UK.

In June 2014, the Commission opened formal investigations under state aid rules against Apple in Ireland, Starbucks in the Netherlands and Fiat Finance & Trade in Luxembourg. In October it opened another investigation regarding Amazon in Luxembourg. The investigations are examining whether Member States provide certain companies a selective advantage in the context of issuing a tax ruling.

UK ramps up tax measures in Autumn Statement

UK Chancellor George Osborne announced a raft of new measures to tackle tax evasion and aggressive tax planning in the Autumn Statement on 3 December 2014. These include increasing the amount and scope of civil penalties for tax evasion and a new "Google tax" on profits shifted abroad.

The existing offshore penalty regime imposes penalties of up to 200% of the "potential lost revenue" based on three categories of offshore territories, which broadly reflect the quality of the information exchange arrangements in place. The classification will be updated to reflect jurisdictions that have adopted the standard of automatic tax information exchange and the penalty regime will further be extended to include:

- Inheritance tax;
- Domestic offences where proceeds of non-compliance are hidden offshore;
- A new aggravated penalty of up to a further 50% where hidden funds are moved to circumvent international tax transparency agreements.

The Disclosure of Tax Avoidance Schemes (DOTAS) regime, first introduced in 2004 to enable allows HMRC to keep up to date with and respond to tax avoidance schemes, will be strengthened to prevent circumvention and there will also be greater public disclosure of DOTAS schemes and their promoters. A new taskforce to police the DOTAS regime will be introduced.

The government announced the introduction of a new Diverted Profits Tax – the so-called "Google Tax" – of 25% as of 1 April 2015, which will apply to multinational companies who seek to use artificial arrangements to divert profits overseas so as to avoid UK tax.

Osborne also announced the abolition of the "cliff edge" thresholds for Stamp Duty Land Tax (SDLT) in favour of a more graduated system. Under the new rules, there will be no tax payable for houses worth less than £125,000, 2% on the next portion up to £250,000, 5% up to £925,000, 10% up to £1.5m and 12% on any higher portion.

The Annual Tax on Enveloped Dwellings (ATED) is to be increased. From 1 April 2015, the ATED charge for residential properties owned through a company or other "enveloped" structure will be raised from £15,400 to £23,350 for properties worth £2m to £5m, from £35,900 to £54,450 for those worth £5m to £10m, from £71,850 to £109,050 for properties worth £10m to £20m and from £143,750 to at £218,200 for properties above £20m. Non-resident owners of UK residential property will also be subject to CGT at 28% on any gains realised on residential property after April 2015.

The annual charge for those who elect to be taxed on the remittance basis is set to increase for those who have been resident for at least 12 out of 14 years, from £50,000 to £60,000. A new level of charge will also be introduced for those who have been resident for 17 out of the last 20 years, which will be set at £90,000.

The government will also consult, in early 2015, on introducing further deterrents for serial avoiders and on penalties for tax avoidance cases where the General Anti-Abuse Rule applies.

The government said it would be proceeding with a proposal to introduce a single settlement nil-rate band of IHT to multiple trusts held by an individual. Instead it will introduce new rules to target avoidance through the use of multiple trusts and also simplify the calculation of trust rules in the Finance Bill 2015.

SOVEREIGN COMMENT

The seemingly constant and far reaching changes to UK tax legislation, particularly as they affect international clients with property interests in London and elsewhere can at times appear overwhelming. It is interesting to note that 90% of the £100 million raised by the ATED in 2013/14 came from properties in London, with Westminster and Kensington & Chelsea property owners contributing £52 million and £28 million respectively. A seminar covering a number of the most important areas was hosted by Sovereign's London office on 29 January to an audience of some 150 advisers. Complimentary copies of the presentation and a video recording of the seminar are available to interested advisers and their clients upon request. Contact the office at uk@SovereignGroup.com for further details.

Swiss voters retain "lump sum" tax regime for wealthy foreigners

Swiss voters rejected by referendum, on 30 November 2014, an initiative calling for an end to the so-called "lump sum" tax regime under which wealthy foreigners pay a fixed annual sum based upon their Swiss living expenses, disregarding their overseas earnings or accumulated wealth.

Some 59% of Swiss voters voted against the proposal, which was brought by left-wing Alternative List political grouping. Voters in cantons that are home to the highest number of foreign lump sum beneficiaries came out strongest in support of retaining the tax system.

Vaud, Valais, Geneva and Ticino are home to the majority of Switzerland's estimated 5,500 lump sum tax beneficiaries. Schaffhausen, one of five cantons that have currently prohibited lump sum taxation, was the only canton out of 26 actually to support the initiative.

Swiss Finance Minister Eveline Widmer-Schlumpf said: "This maintains the tradition of allowing cantons to decide their own fiscal regimes." She added that several other European countries currently offer competing special tax regimes for wealthy foreigners and also reiterated that new federal rules, due to come into force at the start of 2016, will both tighten up qualification for lump sum tax status and increase the levy.

Under the new federal rules, the minimum taxable basis (deemed income) will be CHF400,000. Living expenses will be assessed as at least seven times the annual rental cost or rental value of the taxpayer's dwelling in Switzerland, or at least three times the costs for a hotel. The new law also stipulates that worldwide living expenses must be taken into account to determine the tax base and requires cantons to introduce rules to determine the tax base for income and wealth tax purposes.

UK agrees to limit patent box regime

The UK decided, in an agreement brokered by Germany on 12 November 2014, to limit the scope of its patent box regime, which provides for a concessionary 10% tax rate of tax on income from intellectual property. All existing regimes will be closed to new entrants (products and patents) in June 2016 but IP within existing regimes will be able to retain the benefits of these until June 2021.

The regime, which came into operation in April 2013, was opposed by Germany – with the backing of a number of EU member states – which argued that it was encouraging companies to shift their profits to the UK artificially to the detriment of other states.

Under the agreement, preferential tax treatment will only be granted in cases where the patent is linked to research and development actually carried out in the UK. This would deter multinationals from moving their tax domicile to the UK because they would also need to relocate their R&D to take advantage of the patent box.

A statement by the UK government said the agreement "aims to resolve the concerns countries have expressed about some features of the Modified Nexus Approach, and identify what further work is required in order to enable agreement to be reached on this issue during 2015."

SOVEREIGN COMMENT

The result of the referendum is good news for any potential applicants and their advisers looking to benefit from the Swiss "lump sum" tax regime. A temporary re-establishment of the Canadian IIP is also featured on the Americas pages of this issue. Wealthy people around the world are increasingly looking to move to environments that offer political stability and fiscal certainty. Readers interested in the Swiss option are encouraged to contact our Geneva or London offices for further details.

OECD says tax revenues are rebounding from the financial crisis

Tax burdens and revenue collection in advanced economies are reaching record levels not seen since before the global financial crisis, according to new OECD research published on 10 December 2014. However the tax mix continues to vary widely between countries.

Revenue Statistics 2014 shows that the average tax burden in OECD countries increased by 0.4 percentage points in 2013, to 34.1%, compared with 33.7% in 2012 and 33.3% in 2011. The tax burden is the ratio of total tax revenues to GDP.

Historically, tax-to-GDP ratios rose through the 1990s, to a peak OECD average of 34.3% in 2000. They fell back slightly between 2001 and 2004, but then rose again between 2005 and 2007 before falling back following the crisis.

In 2013, the tax burden rose in 21 of the 30 countries for which data is available, and fell in the remaining 9. The largest increases in 2013 occurred in Portugal, Turkey, the Slovak Republic, Denmark and Finland. The largest falls were in Norway, Chile and New Zealand.

Denmark has the highest tax-to-GDP ratio among OECD countries (48.6%), followed by France (45%) and Belgium (44.6%). Mexico (19.7%) and Chile (20.2%) have the lowest tax-to-GDP ratios among OECD countries, followed by Korea (24.3%), and the United States (25.4%).

The OECD said a number of factors were behind the rise in tax ratios. About half of the increase is attributed to personal and corporate income taxes, which are typically designed so that revenues rise faster than GDP during periods of economic recovery. Discretionary tax changes have also played a role, as many countries raised tax rates and/or broadened tax bases.

LEGAL NEWS

UK Revenue loses CGT dispute over Reynolds painting

19 January 2015, the UK Revenue and Customs was refused leave to appeal to the Supreme Court against the decision of the Court of Appeal to disallow its attempt to charge capital gains tax (CGT) on the £9.4 million sale by the executors of the late Lord Howard of Henderskelfe of a Joshua Reynolds painting in 2001.

In *Executors of Lord Howard of Henderskelfe (Deceased) v HMRC*, the case concerned a Reynolds painting, Omai, which had belonged to the Howard estate since the late 18th century. From the 1950s the painting has been on display to the public at the family home, Castle Howard.

HMRC attempted to charge CGT on its disposal at auction in 2001, but the executors pointed out that the painting had been on long-term loan to the Howard family's stately home business, where it acted as plant and machinery. It was therefore a depreciating asset and exempt from CGT.

The executors' argument was rejected at the First-tier Tax Tribunal, but accepted at the Upper Tribunal. HMRC took the case to the Court of Appeal in March last year. The executors successfully argued that the painting was plant within the definition provided in an 1887 case *(Yarmouth v France)*. In addition and, most importantly for the wasting asset rules, the Court of Appeal confirmed that the painting was plant even though it was used by another entity, the operating company, which did not own the painting.

HMRC applied to the Supreme Court. The Supreme Court under Lord Neuberger considered whether the fact that the painting was not used as plant by the estate itself was an arguable point of law against the Appeal Court's decision. It refused leave to appeal.

SOVEREIGN COMMENT

It has long been a tradition in Britain that wealthy families can use gifts of art and other assets when negotiating with the tax authorities to reduce inheritance tax bills. This case is extremely interesting because it goes further by opening up a potential avenue for relief from Capital Gains Tax. One must assume that HMRC is considering its reaction to the outcome of the Howard case but the precedent is now in place and future cases will surely follow.

Dutch Tax Court confirms ECJ decision on incompatibility of fiscal unity regime

The Second Instance Tax Court of Amsterdam confirmed, on 11 December 2014, the decision made by the European Court of Justice (ECJ) in June that the fiscal unity regime in the Netherlands Corporate Income Tax Act is incompatible with the freedom of establishment principle in the EU Treaty. The case had been referred back to the Amsterdam court to issue a final decision.

Under the fiscal unity regime, two or more companies can be treated as a single taxpayer if certain requirements are met. In three cases – all involving group structures wherein some companies in each group were established in another EU member state – the issue was whether denial of a fiscal unity would infringe EU law.

In all cases, the fiscal unity requests were limited to the Dutch resident companies and the connecting EU companies and the non-resident parent companies were not included because they did not have a permanent establishment in the Netherlands. The Dutch tax authorities denied the requests.

Following the ECJ's 2008 decision in the Papillon case, which involved France's tax consolidation regime, the European Commission initiated an infringement procedure against the Netherlands on the grounds that the Dutch law disallowing a fiscal unity between two sister companies – without consolidation of the joint parent company that is a resident of another EU member state – infringed EU law. At the same time, a taxpayer brought another similar case before the Dutch lower tax courts.

German Court orders amendments to inheritance tax exemptions for family-owned firms

The Federal Constitutional Court, Germany's highest court, ruled on 17 December 2014 that the applicable Inheritance and Gift Tax law was partially – the exemption regulations for business assets – unconstitutional.

Family-owned companies account for 92% of German corporations, one of the highest levels in the world. The Mittelstand, the small to mid-size companies that make up the backbone of the German economy, generate more than half of the country's economic output and employ 60% of its workforce. While most family companies are small, more than 170 have revenue of at least €1 billion.

In 2012, German companies obtained nearly €40 billion in tax exemptions while tax authorities only collected €4.3 billion in inheritance tax revenue, the court said. An unidentified taxpayer who was taxed at 30% on a cash inheritance challenged the law. It was argued that it was unfair to be required to pay more than taxpayers who inherited a company.

At issue were changes to tax rules in 2009 that enable people who inherit ownership of companies to avoid 85% of inheritance taxes if they maintain employment for five years, and to pay no taxes at all if they maintain employment for at least seven years. However firms with 20 employees or fewer — a category that includes 90% of Germany's family-owned companies — are not required to preserve jobs to avoid the inheritance tax.

The eight-judge panel found that while the 2009 rule served a legitimate goal in seeking to protect jobs and "productive wealth", the legislation violated the constitutional principle of fair taxation because preferential treatment was extended to all companies, including large corporations, without case-by-case checks being performed as to whether an exemption was economically justified.

The court gave legislators until the end of June 2016 to tighten the law. To claim an exemption, the court said that big companies should, in future, have to prove that their existence would be threatened if fully subjected to inheritance tax. The court further ruled that heirs to small companies with fewer than 20 staff should in future no longer be automatically exempted from inheritance tax, calling instead for the exemption to be awarded only to businesses with "few" staff.

The ruling came after Germany's highest tax court said it was too easy for business owners to convert private assets into non-taxable business assets. The Constitutional Court also requested that the law should be amended to prevent company owners using the tax exemption to transfer assets not directly related to the running of their businesses.

Legislators have two options to respond to the ruling. First, they could abolish tax privileges and apply a lower, equal inheritance tax rate for all business and private assets. The second, most likely option, is to narrow the range of tax exemptions awarded to companies.

The German Finance Ministry said the ruling affected only some individual aspects of the existing law but not the fundamental goal of helping family-owned companies to preserve jobs. "The government sticks to its maxim: no higher overall economic burden and awarding constitutional preference to business assets that get passed on to heirs," the ministry said in a statement.

SOVEREIGN COMMENT

As this news item points out, Germany is in an almost unique position among developed nations due to its longstanding tradition of family owned businesses. It is interesting to compare other major EU partners where the percentages held in family hands are considerably less at around 60%. Therefore any changes to tax rules, particularly as they affect inheritance, will be greeted with some concern by German families, especially those where succession is likely to become an issue sooner rather than later. As the story points out, the German Finance Ministry has left open the possibility that future individual rulings may be challenged.

The UK's highest high-net-worth divorce settlement

The UK High Court made an award of £337 million to the American wife of a London financier on 27 November 2014. Hedge fund manager Sir Christopher Hohn and his US-born wife Jamie Cooper-Hohn, separating after 17 years of marriage, had disputed assets said to be worth more than £700 million.

Mrs Cooper-Hohn had sought half their assets but Sir Christopher offered a quarter, arguing that he had made a special contribution to their wealth throughout their marriage. The couple, who together set up the Children's Investment Fund Foundation, have reportedly given away around £1 billion.

Mrs Cooper-Hohn commenced divorce proceedings in 2012. While Sir Christopher argued that he had bought more wealth into the union, describing himself as an "unbelievable money maker", the court looked at the contribution made by his ex-wife to their charitable foundation and the influence she had in the marriage.

Details emerged after a draft ruling was given to the pair's legal teams. Mrs Justice Roberts, who made the award, said that although the hearing had been in private, what had been said could be reported. The judgment is not yet available.

Credit Suisse ordered to pay US$1.8 billion to finalise US guilty plea

A US court accepted, on 21 November 2014, Credit Suisse's guilty plea to end a criminal case accusing it of helping wealthy Americans avoid paying taxes, and ordered the Swiss bank to pay around US$1.8 billion in fines and restitution.

Credit Suisse agreed to the payout as part of a more than US$2.6 billion settlement with several government authorities. The payout includes a $1.14 billion criminal fine and a nearly $667 million payment to the Internal Revenue Service. An additional $100m will be paid to the Federal Reserve and $715m to the New York State Finance Department.

In May, Credit Suisse admitted to conspiring to aid and assist US taxpayers in filing false income tax returns and other documents with the IRS. For decades prior to 2009, the bank opened and maintained "secret accounts", concealing the offshore assets and income of US citizens from the Internal Revenue Service (IRS).

The bank had also destroyed account records sent to the US for client review, used its managers and employees as unregistered investment advisers on undeclared accounts, and provided offshore credit and debit cards to deport funds in the undeclared accounts.

A federal court in Norfolk, Virginia accepted the guilty plea. Chief Judge Rebecca Beach Smith said she wanted to see a stiff punishment and would accept the $1.14 billion fine, which was payable within one week, because it fell within recommended federal guidelines. "Deterrence is very important here," she said.

In addition to the payments in criminal fines and compensation, the bank has agreed to cooperate to fully disclose all of its cross-border activities, which includes providing account information and details about other banks that transferred funds into undeclared accounts.

A Credit Suisse spokesman said: "We have worked closely with the US Department of Justice to conclude this matter, and having it fully resolved is an important step forward for us." The verdict follows years of investigation by US law enforcement authorities, which have also charged seven Credit Suisse employees, of which two have pleaded guilty to date.

IN THE PRESS

SWISS BANKS - WHAT HAVE THEY BEEN GETTING UP TO?

Swiss banks, once a byword for secrecy and for so long the gold standard for wealth management, have been in the firing line from international organisations, governments and tax authorities for years. Even worse, their previously impenetrable defences have been completely undermined by employees stealing confidential information and selling it to foreign tax authorities. The light that this data has shed on Swiss banking practices has not been flattering.

As a result, certain Swiss banks have been indicted in the US, charged with conspiracy to defraud the IRS, obliged to pay massive fines and hand over client names. Bankers have been arrested and jailed – some have also been handsomely rewarded on release for shopping their customers. Outside the US, Switzerland has been obliged to enter into a number of bilateral agreements and treaties to "regularise" accounts of foreign nationals.

The most recent bank to be ushered into the spotlight is HSBC in Switzerland, which has been heavily criticised and much embarrassed by allegations that it assisted UK taxpayers to conceal assets and avoid (or evade) UK tax. A BBC documentary made reference in particular to "undeclared accounts" owned by British residents.

The reality is there is no such thing as an undeclared account. The UK tax system works on the basis of self-assessment. This means that anybody resident in the UK must file a return that details all income and capital taxes due and payable. A UK tax form does not ask for details of individual accounts, assets or sources of income. In other words UK taxpayers don't need to declare accounts.

Those who are resident but not domiciled in the UK are only taxable on UK-source income and foreign income that is actually remitted to the UK. If a "non-dom" has a bank account in Switzerland that generated income they would not be required to declare that income unless they remitted it to the UK.

It is up to each taxpayer to get such professional advice as they need in order to complete the tax form correctly. Failure to declare due to ignorance is no excuse. In most cases whether or not income or capital gains is taxable will be patently obvious.

All sources of income and capital gains are taxable irrespective of where they arise if you are UK resident and domiciled. Income belonging to non-UK companies and trusts is likely to be attributed to a UK beneficial owner or settlor under the anti-avoidance rules, so this is also declarable and taxable even though, technically, it does not belong to the taxpayer.

The implication on the TV programme and press articles was that these accounts were funded with capital on which the correct amount of (or any) tax had not been paid. That lump sum was then invested and generated income which also was not declared. It is not up to a bank to ensure that a taxpayer fills out their tax form correctly. Indeed even if they wanted to check whether a taxpayer has declared any income earned on an account, they would be unable to do so unless they had intimate knowledge of all that persons financial affairs.

If, for instance, a bank knows that a customer has received income from an account, it would have no way of knowing whether any income that the customer has declared for tax purposes was the income they had helped them to generate because the tax return does not identify the particular sources of income. Banks are not agents of the UK HMRC and can't be expected to interrogate a customer about their tax return.

There may be many legitimate reasons for opening accounts with a Swiss bank. First and foremost is that they have a level of international experience and expertise that is hard to find in the UK. Swiss banks have traditionally been focused on investment business and generally don't take risks by funding speculative ventures or making loans. Swiss banks are therefore safe and secure and generally have long track records of generating good returns. Are we seriously trying to suggest that UK taxpayers can only use banks situated in the UK and should be prevented from making investments abroad? Of course not. UK taxpayers should be free to put their money wherever they like. Exchange controls were, after all, abolished in the UK many years ago.

There are many expatriate UK taxpayers who can also benefit greatly from banking outside the UK. If they bank in the UK, tax is deducted on interest at source. If they are not UK taxpayers they would ordinarily not need to pay that tax so matters are much simplified if they bank outside the UK where tax is not withheld.

Switzerland has a reputation of being one of the most stable countries in the world. Swiss banks rarely go bust and there is seldom any government interference in the running of a bank, let alone any sequestration of assets by the Swiss government. You only need to look at what happened in Cyprus. When the Eurozone crisis struck, the government imposed a 30% haircut on accounts held in Cypriot banks to help pay off its national debt. In other countries banks simply go bust and everyone loses their money. These things don't happen in Switzerland. That is why people like Swiss banks.

The problem with HSBC is that it appears to have gone much further than simply allowing UK persons to open accounts. The allegation is that it knew that certain of these accounts were funded by money upon which tax should have been paid but had not. That could well be classed as money laundering because tax evasion is a criminal offence in the UK. Happily for the Swiss, tax evasion, unlike tax fraud, is not a criminal offence in Switzerland, so handling the proceeds of tax evasion is not classed as money laundering.

Internal memos would seem to suggest that HSBC knew that UK taxpayers were not making correct tax declarations for the income they were earning on their Swiss accounts and, further, it seems to have gone to great lengths to assist those taxpayers to receive the money in cash deliveries. Again, it is arguable that this is not their problem but assisting the taxpayer to conceal the account for the stated purpose of escaping tax is surely conspiracy to defraud HMRC. Advising the taxpayer that they should declare any income generated on their account and refusing to handle any monies on which it knew that tax had not been paid would have been both legal and ethically correct.

SIMON GARVEEN IS...

SOVEREIGN MAN

Simon Garveen is a typical Sovereign client. Now in his mid-40s, Simon is a successful entrepreneur who floated a software business on the AIM in 2005 and sold out his remaining stake the following year. He is now an investor in multiple private businesses worldwide, with a current focus on China, Africa and the Middle East. His business interests range widely, from software and manufacturing through to food and wine production, property, hotels and leisure. He also supports a number of charitable concerns. He calls Hong Kong home but travels widely and has houses in the UK and Portugal. He holds UK and St Kitts' citizenship, is divorced from his first wife, with whom he has three children aged 12 to 19 – all being expensively educated in the UK and US. He remarried in 2008 and has two further children under the age of six. He enjoys travel and sailing, and collects art, antiquities, wine and now classic cars. He supports his elderly parents and to some degree his other young relatives. Much of his wealth is tied up in physical assets or in long term or active investments so he doesn't generally have ready access to much cash. His life could be very complicated but, with expert help, he makes it look easy.

Not-so-dodgy motors

"One of my private equity investments came good the other day – which is nice because plenty don't. My rule is to invest in 10 – five will likely not come to much, three will wash their face and then I hope other two will make it all worthwhile. This one did really well so I've got a decent chunk of change in the bank account for the first time in a while and have been thinking about what to do with it.

"Stock markets stress me out. However long term the investment strategy, I find it impossible not to check the indexes regularly and it's no fun if they are falling. Besides, as they keep reminding me, highly paid (they say "adequately remunerated") investment managers are looking after my portfolio – so it's alternative asset classes that I should be focusing on. My wine cellar is full and I have plenty of art on my walls, so my thoughts have turned to classic cars.

"According to several recent surveys, classic cars have been the best performing asset class over the last 20 years. Genuine classics do fit the investment model: they don't make them any more; they didn't make many to start with; there is usually a significant attrition rate from accident, theft or neglect; and they enjoy a substantial fan base. And what could be better than having a 'boys' toy' that can be fully justified as an investment.

"After some fairly extensive research I have drawn up a hit list of relatively low priced vehicles that experts are tipping to increase dramatically in value. The market seems to be on fire and they are such beautiful things that, even if they don't increase in value, I get to enjoy them and drive them. The top end of the market is looking very frothy and anyway I can't afford the very rarest models so I've settled on trying to find a Ferrari 575 Marinello. These seem to have been priced at £60K for ages but now seem to be increasing in value so I'm hoping that will continue. Although I plan to keep my cars in the UK, I think a left hand drive model might be preferable. I don't find them difficult to drive and the market for LHD is so much bigger.

"The best option is to look for a low mileage example in mint condition with a full service history. The market seems quite imperfect. Import duties, VAT, tax, condition, mileage, the number originally manufactured and estimated numbers left all have a big bearing on price. As do the profit expectations of dealers. After some time I tracked down a few cars which fit my criteria in Dubai – where they don't seem to value classic cars as much as they do brand new flashy ones. On top of that the climate means no rust and they have rarely done many miles.

"Of course if you're buying at a distance it is absolutely crucial to have a local expert you can trust, who can vet the car and ensure that money is handed over only in return for legal title. Luckily I had someone recommended to me who was qualified to examine the car and documentation and then negotiate the price – but there are many scamsters in this business so great care is needed. More on that another time.

"It seems that to get it back to the UK, I'll have to stump up for shipping, 5% import duty and 20% VAT. Even after factoring in all these costs I think I have ended up with a bargain. Irrespective, there isn't too much wrong with having a beautiful Ferrari parked in my UK garage. I'm told it should be owned through a structure in order to avoid potential liability to 40% UK inheritance tax. I've also been recommended an insurance policy that treats my car like a work of art, which substantially cuts the usual cost. In fact, it should cost less to insure than my existing cars.

"Acquisitions can be addictive and I may already be turning into a 'petrol head'. I am now hunting for 1960s open top Italian sports cars by Alfa Romeo and Lancia. These are lovely things from a time when they made things properly and they didn't disintegrate after their first wet outing in the UK. After all, what is more enjoyable – a BP share certificate or a Ferrari ... let me think about that for just a millisecond."

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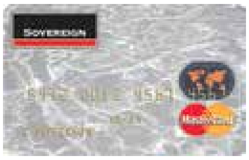

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