SOVEREIGN™

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SOVEREIGN REPORT

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INTRODUCTION

The Sovereign Art Foundation collaborated with Thai-based artist studio StudiOK, led by artist Ravin Rawanwhcaikul, to create an interactive booth at Art Central full of activities for adults and children alike.

The "Panama Papers"

The release of the so-called "Panama Papers" – all 11 million of them – has once again turned the press spotlight on to the offshore finance industry and many politicians (at least those not mentioned in the "Papers") have rushed to comment and criticise. But most of the commentary has been off the mark and fundamentally misunderstands how things work.

Whilst it appears that the firm in question was not applying the international standards of transparency and due diligence, the exposure of its clients has simply been brought forward by a year. Just a few weeks ago, the OECD told G20 Finance Ministers that Panama was back-tracking on its commitment to automatic exchange of financial account information and described it as "the last major holdout that continues to allow funds to be hidden offshore from tax and law enforcement authorities."

By the end of next year, the OECD's Common Reporting Standard (CRS) will have been introduced – 96 jurisdictions (and counting) will introduce automatic exchange of financial account information within the next two years. This will require all financial institutions – banks and offshore service providers – to exchange information about anybody and everybody that does business with them who is not resident in their own jurisdiction.

CRS does not mean that offshore structures will no longer be effective or useful. But we have been telling clients for years that if they cannot afford to have the details of their arrangements revealed to their home tax authority, they should not be doing it. A tax offence only occurs if the taxpayer signs an incorrect tax form. See the full article on Page 14 of this issue.

Sovereign acquires UK-based SIPPs specialist

I am delighted to announce that Sovereign has acquired MW Pensions Ltd (MWP) a UK-based and regulated business that provides a range of well-regarded Self-Invested Personal Pension (SIPP) and Small Self Administered Scheme (SSAS) products. MWP will change its name to Sovereign and continue to service its existing client and introducer base from its offices in the North West of England. MWP's sister operation in the Isle of Man, SIPP Specialists Ltd., will also be acquired as part of the deal.

Sovereign has developed into a market leader in the transfer and provision of pension schemes and retirement planning is now one of our core product offerings. Adding a SIPP operation in the UK makes sense for our Group. While most UK non-residents say they won't return to the UK, the reality is that many do. Sovereign can now offer a one-stop-shop for their retirement planning needs. We offer free transfers within our range of QROPS products and that will now be extended to our SIPP offering.

SAF collaborates with StudiOK at Art Central

The Sovereign Art Foundation (SAF) has focused on developing its *Make It Better* programme in 2016 so as to reach more underprivileged communities in Hong Kong than ever before.

SAF is now working with the University of Hong Kong's expressive arts therapy students, together with experienced charity partners and a diverse group of professionals and practitioners who are intent on creating the pre-eminent "healing through art" programme in Hong Kong, alongside our own newly expanded team of art teachers.

In a very exciting first time collaboration with internationally-renowned Thai artist Navin Rawanchaikul and Chiang Mai-based StudiOK, SAF recently offered Art Central Hong Kong visitors the chance to hang out in its art-inspired activity booth. Activities included the decorating of postcards, which were then sent to children attending the Ta-luk Elementary School in Chiang Mai, as well as the chance to be painted into a live wall mural, tale part in a curated art treasure hunt, and a host of other activities inspired by having fun with fabric.

Sovereign News

As some readers may already be aware, our Head of Group Sales John Hanafin, has departed Sovereign to join one of our very good customers, Arton Capital. For John this was an opportunity too good to miss and, although he will leave a big gap, we hope and expect this move will benefit both us and Arton Capital in the future. We are very grateful to John for all his work over the last 10 years.

Also, congratulations go to Johannesburg-based Richard Neal on his appointment as Director of Sovereign Trust (South Africa) Ltd. We wish Richard well in this new role.

Howard Bilton
Chairman of the Sovereign Group

EUROPE

UK targets second-home owners in Autumn Statement

UK Chancellor George Osborne, delivering his Autumn Statement to Parliament on 25 November 2015, announced that higher rates of stamp duty land tax (SDLT) will be charged from 1 April 2016 on purchases of "additional" residential properties above £40,000 such as buy-to-lets and second homes.

The higher rate will be 3% above current rates, at every band, taking the top rate band to 15% for properties above £1.5 million. By providing a disincentive for investors purchasing additional properties, the measure is intended to assist first-time buyers. The surcharge will not apply to corporates and funds owning more than 15 residential properties.

The government also confirmed in December that the 3% surcharge would be applied to foreign buyers and non-UK domiciliaries (non-doms), as well as to UK residents. Responding to a question in parliament, Treasury Minister David Gauke said: "Foreign investors and people not domiciled in the UK will be treated in exactly the same way as UK residents under these new rates. If purchasers own another property anywhere else in the world and are purchasing an additional property in England, Wales or Northern Ireland they will be charged under the new rates."

In addition, from April 2019, payment on account of capital gains tax (CGT) for residential property will be required within 30 days of completion, instead of by 31 January in the tax year following the date of sale. This is in line with the payment deadline for non-resident investors. The principal private residence exemption from CGT remains unaltered.

HMRC is to be given a further £800m to tackle non-compliance through tax evasion and non-compliance in the tax system by 2020-21. Disguised remuneration schemes and stamp duty avoidance were highlighted as key targets. Other measures would be used to close the "tax gap" and punish those involved in failed tax avoidance schemes and those who commit tax evasion.

In the summer 2015 Budget, the Chancellor announced reforms to the taxation of non-doms. The test for deemed domicile is to be changed and the concept of deemed domicile will further be extended from inheritance tax (IHT) to cover income tax and CGT. These changes are to apply from April 2017.

The period an individual can be resident in the UK before they become deemed domiciled for all personal taxes will be 15 out of the 20 tax years before the tax year under consideration. Previously, for IHT purposes, it was 17 out of 20 tax years ending with the tax year under consideration. An individual will therefore become deemed-domiciled for IHT at the start of their sixteenth consecutive year of UK residence, rather than at the start of their seventeenth year of residence.

The government also proposes to double the amount of time it takes for an individual to be classed as non-domiciled after leaving the UK, increasing the three-year inheritance tax tail to at least six years. This means a UK-domiciled individual would be liable to pay IHT on their worldwide assets up to six years after leaving the UK.

The Finance Bill 2016 draft clause 43, introducing the IHT changes, was published on 9 December 2015. In addition to the shortened period for deemed domicile, a new rule is introduced whereby a person born in the UK with a UK domicile who has since acquired a domicile of choice elsewhere will be treated as UK-domiciled for IHT purposes if they are resident in the UK in at least one out of the two previous tax years.

Draft legislation extending the deemed domicile rules for income tax and CGT was published on 2 February 2016. Under the legislation non-doms will likewise be deemed UK-domiciled for income tax and CGT if they have been resident in the UK for 15 out of the previous 20 years. As a result, from 6 April 2017, the £90,000 remittance basis charge (first applied last April) to non-doms who have been resident in the UK for 17 out of 20 years will cease to operate.

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When the measures were announced in the summer 2015 Budget it was made clear that for most purposes a deemed UK-domiciled individual would be treated exactly as a UK-domiciled individual. However, exceptions were promised relating to offshore trusts settled by a long-term UK resident before becoming deemed domiciled; such individuals were not be taxed on trust income and gains that are retained in the trust. This would be a significant change to the way that the income and gains arising in offshore trusts and their underlying entities are taxed and means there would be no need for trustees to have to recreate the history of the income and gains in the trust for tax purposes once an individual becomes deemed-UK domiciled. Disappointingly, these exceptions were not included in the draft Finance Bill 2016 legislation. However they are proposed for Finance Bill 2017.

Sovereign Malta pensions to offer "flexi-access" drawdown

The Malta Financial Services Authority has now confirmed the transition of Sovereign Pension Services – together with the Centaurus and Centaurus Lite retirement benefit schemes – from licensing and regulation under the Special Funds (Regulation) Act. They will now be licensed and regulated under the Retirement Pensions Act, which came into force on the 1 January 2015.

As a result, we are now in a position to offer "flexi-access drawdown" (FAD) under our Malta schemes, with immediate effect, enabling any transfers of UK relevant funds to be subject to the UK's new FAD rules. This means 100% of a member's fund may be available from the above schemes from age 55.

Members are strongly advised to take independent tax advice on the implications of how they take benefit from their pension and also to consider any early redemption charges that they may apply on their investments. Please contact your regional Sovereign consultant for full details.

Cyprus plans to amend Intellectual Property tax regime

The Ministry of Finance announced, on 30 December 2016, that the Intellectual Property (IP) tax regime would be amended to incorporate the recommendations of the OECD Action Plan against Base Erosion and Profit Shifting (BEPS), which was issued on 5 October 2015, as well as the conclusions of the ECOFIN Council adopted on 8 December 2015.

The approach of the OECD's Action 5 requires the existence of material activity (the so-called nexus approach), which includes the clear interconnection between the rights that create the income and the activity that contributes to that income.

The Cypriot authorities intend to amend the IP legal framework in line with the provisions of Action 5 by 1 July 2016. The amendment will provide for the maximum transitional arrangements that are included within the revised framework.

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Our Cyprus office has been working with clients on IP routing structures for many years and these developments are being closed watched. Managing Director Baiba Saldovere said: "There is a global drive towards compliance and I am very pleased to see Cyprus at the forefront of these changes. In the next few months we are expecting further announcements on the implementation of the new regime but in the meantime there is still a limited opportunity to explore the advantages offered by the existing IP Box regime."

Guernsey introduces flexibility of retirement benefits

The Guernsey States (parliament) approved, on 29 September 2015, a Billet d'Etat to provide for the introduction of flexible retirement benefits in Guernsey. The Income Tax (Pension Amendments) (Guernsey) Ordinance 2015 was brought into force on 2 October.

The amendments will allow inward transfers to a Guernsey personal pension scheme the same flexibility of benefits as allowed by the legislation of the jurisdiction from where the funds or benefits entitlement originate. The availability of flexible benefits will depend on whether the pension provider amends a scheme's rules to permit the new freedoms.

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Under current UK legislation, a Guernsey pension scheme's ability to meet the UK's Qualifying Non-UK Pension Scheme (QNUPS) conditions will be impeded by offering flexible pension benefits. This could lead to an UK Inheritance Tax (IHT) exposure for the scheme's underlying members. As a result, Sovereign will not be introducing flexible benefits for members of its former QROPS schemes at this time. However, with QROPS and QNUPS offerings available from a number of alternative jurisdictions, those members seeking to access their benefits "flexibly" should contact their local Sovereign representative to discuss their individual position and the options available to them.

Guernsey aircraft register to open up for commercial operations

Guernsey's parliament unanimously approved, on 17 December 2015, a proposal to permit the Channel Islands Aircraft Register (2-REG) to issue Air Operator Certificates (AOCs), The move, which will enable Guernsey-registered aircraft to operate commercially, will differentiate Guernsey from competitor registries such as the Isle of Man, which cover only aircraft operated for private or corporate use.

2-REG Aircraft Registry started operations in December 2013 and accommodates all aircraft types from larger airliners through to general aviation, based anywhere in the world. Although 2-REG has enjoyed only limited success in the registration of private jets in the face of stiff competition from other jurisdictions, it has generated considerable business in the temporary registration of commercial airliners that are dormant between operational leases.

The proposal, published in Billet D'état XXIII, noted that the aircraft registrar has worked with the operator (SGI Aviation) to "retarget the Aviation Registry to appeal to business rather than private clients". New legislation to accommodate the AOC operations is now being drafted and is expected to pass for final government approval.

Guernsey Director of Civil Aviation Gus Paterson said: "Our business-to-business approach has won over major lessors and this is the logical next step in the development of our portfolio."

SOVEREIGN COMMENT

Brian T. Richards, director of Sovereign's aviation division RegisterAnAircraft.com (RANA), said: "This change represents an exciting opportunity for this currently private aircraft register to tap into a valuable sector of the corporate aviation market. It certainly lays down a challenge to competing jurisdictions."

Swiss Senate votes for automatic exchange of tax information

The Swiss Senate followed the House of Representatives by approving, on 2 December 2015, a legal framework for the automatic exchange of tax information. Only four senators, all from the conservative right Swiss People's Party, voted against the measure, which paves the way for an end to bank secrecy.

Currently, Switzerland sends data about account holders to foreign governments and institutions upon request only. However, the new legal framework will enable such information to flow automatically to certain countries – including Australia and the 28 European Union nations – with which Switzerland has concluded automatic exchange agreements. Switzerland has also signed a similar automatic information exchange deal with the US through a bilateral Intergovernmental Agreement under the Foreign Account Tax Compliance Act (FATCA).

Those agreements make up part of Switzerland's commitment to share foreign clients' account data with other countries by 2018 as part of a new global Common Reporting Standard designed by the OECD. Agreements with individual countries will have to be ratified separately by parliament, but the Swiss Senate's decision creates the legal framework for their acceptance.

AMERICAS & THE CARIBBEAN

St. Lucia opens new Citizenship-by-Investment scheme

Saint Lucia began accepting applications for its new citizenship by investment programme on 1 January 2016. The programme was introduced by the Citizenship by Investment Act (No. 14 of 2015), which came into force on 24 August 2015. A Saint Lucia passport allows visa-free travel to 105 countries.

Under the regulations published on 2 October, the number of successful applications per year will initially be capped at 500 and applicants will be subject to a higher qualifying criteria. This includes a requirement to prove a minimum net worth of US$3 million in addition to making a qualifying minimum investment in either of:

- The Saint Lucia National Economic Fund (US$200,000);
- An approved real estate project (US$300,000);
- An approved enterprise project (US$3.5 million and no less than three permanent jobs);
- A purchase of government bonds (US$500,000 in five-year holding bond).

Dr Ernest Hilaire, chairman of the Citizenship by Investment Unit, said: "We are confident the new programme will provide a platform for strategic developmental reasons whilst attracting individuals who are best placed to invest in Saint Lucia."

SOVEREIGN COMMENT

Saint Lucia is now the fifth Caribbean island to offer a "Citizenship-by-Investment" programme. It joins Antigua and Barbuda, Dominica, Grenada and St. Kitts and Nevis in granting citizenship to high net worth individuals. Citizenship-by-Investment allows high net worth individuals to access several benefits, such as visa free international travel to a large number of countries, increased security and flexibility while travelling, and it will act as an insurance in times of political or economic disorder elsewhere.

Overseas Territories resist demands for beneficial ownership registers

The British Overseas Territories (OTs) – including the British Virgin Islands, Cayman Islands, Turks and Caicos Islands and Bermuda – will not be required to implement central registers of the beneficial ownership of companies registered there, provided that they put "similarly effective" systems in place.

The political leaders and representatives of the UK and its OTs met as the Joint Ministerial Council (JMC) in London on 2 December 2015. The UK plans to introduce a central, publicly accessible register of "persons with significant control" of UK companies in June 2016, in line with a commitment made by members of the G8 leading global economies in June 2013.

It further called for similar registers to be introduced in all the OTs, as well as the Crown Dependencies of Jersey, Guernsey and the Isle of Man. Ahead of the JMC, Foreign Office minister James Duddridge stated the UK's explicit requirements as follows:

- UK law enforcement and tax authorities must be able to access company beneficial ownership information without restriction, subject to relevant safeguards;
- These competent authorities should be able to quickly identify all companies that a particular beneficial owner has a stake in without needing to submit multiple and repeated requests; and
- Companies or their beneficial owners must not be alerted to the fact that an investigation is under way.

Non-compliant US accountholders at Swiss banks that have settled must pay a 50% penalty to the IRS if they wish to enter the IRS Offshore Voluntary Disclosure Programme.

Most OTs and the Crown Dependencies had previously indicated that they would not do so on grounds that they were already in compliance with international standards and it would place them at a competitive disadvantage with other jurisdictions. At the JMC, they rejected both the UK's request to create public registers of beneficial ownership and to permit unrestricted access to information to UK and domestic law enforcement and tax authorities.

According to the JMC communiqué, however, there was agreement to hold beneficial ownership information in their respective jurisdictions via central registers or "similarly effective systems". OTs also agreed to give the "highest priority" to implementation, which included developing timely, safe and secure information exchange processes through technical dialogue with UK law enforcement authorities. Progress on implementation will be kept under "continuous and close review".

Cayman islands to introduce Limited Liability Companies

The Cayman Islands government tabled a bill, on 18 December 2015, to provide for the establishment of a Cayman limited liability company (LLC). Largely based on the Delaware LLC model, but with modifications required to fit with existing Cayman Islands law, it is anticipated that the LLC Bill will be approved during the first quarter of 2016.

A Cayman LLC will offer separate legal personality and limited liability for its members. The internal operations of a Cayman LLC can be tailored in the operating agreement to the exact needs of the LLC members in respect of capital accounting and commitments, allocation of profits and losses, distributions, voting rights and classes of interest.

The Bill makes provision for the applicability of other Cayman Islands laws to an LLC such that an LLC can automatically be structured under the Mutual Funds Law, the Exempted Limited Partnership Law or the Securities Investment Business Law.

A Companies (Amendment) Law 2015 was also gazetted last September and brought into force on 2 November. Its purpose is to extend the deadline for filing entries or changes to the register of directors and officers of a company and to establish maximum penalties for a breach of the new requirements. It therefore has potential application for all Cayman Islands companies.

Previously, under sections 55 and 56 of the Companies Law (2013 Revision), first appointments of directors and officers to a Cayman Islands company had to be notified to the Registrar of Companies within 90 days of the incorporation. Any subsequent changes to directors and officers then had to be notified to the Registrar within 30 days.

The new legislation amends these time periods such that a company must now notify the Registrar within 60 days of incorporation of the first appointment of any director or officer. Any change in the information contained in the Register must be notified within 60 days of the date of the change.

BVI introduces requirement to file a Register of Directors

The BVI House of Assembly enacted the BVI Business Companies (Amendment) Act on 21 December 2015, which introduces a compulsory requirement for all BVI business companies to privately file a "register of directors" at the Registry of Corporate Affairs. The Act was brought into force on 1 January 2016.

The Act also creates an option of filing the company's register of members. The information on both registers will only be made available to "competent authorities in the execution of their duties" – regulators, tax administrators or law enforcement agencies. Other persons will only have access by getting a court order.

BVI premier Orlando Smith said this would reassure practitioners and clients that the BVI's business sector will be safeguarded and its competitive advantage maintained. The changes, he said, would provide mechanisms to ensure timely access by law enforcement and tax authorities, equivalent to those provided by a "central register" as requested by the UK. The BVI Financial Services Commission (FSC) anticipates that the transition period for existing companies to file a register of directors will run from 1 April 2016 to 31 March 2017. A Register of Directors may be filed without attracting a filing fee up to 30 September 2016.

The BVI also passed, on 29 December 2015, amendments to the Mutual Legal Assistance (Tax Matters) Act 2003 to implement the OECD's Common Reporting Standard for the exchange of tax information (CRS). These entered into force on 1 January 2016.

The CRS imposes similar reporting and other obligations as are required under the US Foreign Account Tax Compliance Act (FATCA) regime, but reporting under the CRS relates to tax residency rather than citizenship. BVI Financial Institutions (FIs) will need to report information on the holders of "Reportable Accounts" that are tax resident in "Reportable Jurisdictions" to the BVI International Tax Authority (ITA). This information will then be reported to the home jurisdiction.

The scope of exemptions available under the CRS is also much narrower. FIs that are not currently reporting under FATCA may be classed as Reporting FIs for the purposes of the CRS and will therefore need to implement a suitable compliance programme.

There is no sponsoring entity regime under the CRS. The first annual reports to the ITA are due by 31 May 2017 in respect of new accounts opened during the 2016 calendar year.

Reporting FIs are further required to complete due diligence on high value pre-existing accounts held by individuals (balance or value exceeding US$1 million as of 31 December 2015) to determine if they are Reportable Accounts by 31 December 2016. Due diligence on lower value pre-existing accounts held by individuals is to be completed by 31 December 2017.

The UK is expected to phase out "UK FACTA" under its Intergovernmental Agreement with the BVI government. During 2016, Reporting FIs will need to file returns under the CRS, with supplementary information on pre-existing low-value individual accounts and pre-existing entity accounts to satisfy UK FATCA. The US is not a "participating jurisdiction" and US FATCA will continue to operate as normal.

SOVEREIGN COMMENT

The BVI remains committed to achieving transparency in the financial services sector internationally. Although the UK government has opted for a public central register that will make the ownership of companies available centrally to the public, this approach has not been widely adopted internationally. The UK government has acknowledged that similarly effective systems can be utilised. The BVI will continue to monitor global standards and best practices to ensure that it remains a competitive financial jurisdiction for global business.

US collects US$1.36 billion under Swiss Bank Programme

27 January 2016, the US Department of Justice announced that it reached its final non-prosecution agreement under Category 2 of the Swiss Bank Programme. The department has executed agreements with 80 banks since 30 March 2015 and imposed a total of US$1.36 billion in penalties. Every bank in the programme is also required to cooperate in any related criminal or civil proceedings through 2016 and beyond.

The DoJ said completion of the agreements under Category 2 of the Swiss Bank Programme represented a substantial milestone in its efforts to combat offshore tax evasion and it remained committed to holding financial institutions, professionals and individual taxpayers accountable for their respective roles in concealing foreign accounts and assets, and evading US tax obligations.

The Swiss Bank Programme, which was announced on 29 August 2013, was designed to provide a path for Swiss banks to resolve potential criminal liabilities in the US. Swiss banks eligible to enter the programme were required to advise the department by 31 December 2013, that they had reason to believe that they had committed tax-related criminal offences in connection with undeclared US-related accounts. Banks already under criminal investigation related to their Swiss-banking activities – Category 1 banks – and all individuals were expressly excluded from the programme.

US Attorney General Loretta Lynch said: "Through this initiative, we have uncovered those who help facilitate evasion schemes and those who hide funds in secret offshore accounts. We have improved our ability to return tax dollars to the United States. And we have pursued investigations into banks and individuals. I would like to thank the Swiss government for their cooperation in this effort, and I look forward to continuing our work together."

MIDDLE EAST & ASIA

Hong Kong government gazettes tax information exchange bill

8 January 2016, the Inland Revenue (Amendment) Bill 2016, which seeks to provide a legal framework for Hong Kong to implement the new international standard for automatic exchange of financial account information in tax matters (AEOI), was gazetted.

In September 2014, Hong Kong committed that, subject to the passage of local legislation, AEOI would be implemented on a reciprocal basis with appropriate partners which could meet relevant standards on protection of privacy and confidentiality of information exchanged and ensuring proper use of the data exchanged, with a view to commencing the first information exchanges by the end of 2018.

Under the AEOI standard, a financial institution (FI) is required to identify financial accounts held by tax residents in the jurisdictions with which Hong Kong has entered into an AEOI arrangement. FIs are required to collect the reportable information of these financial accounts, and furnish such information to the Inland Revenue Department (IRD). The IRD will exchange it with the tax authorities of AEOI partner jurisdictions on an annual basis.

"We intend to conduct AEOI only with our partners with which Hong Kong has signed comprehensive avoidance of double taxation agreements (CDTAs) or tax information exchange agreements (TIEAs), on a bilateral basis. The safeguards for exchange of information under the respective CDTAs and TIEAs will be applicable to information exchanged under the AEOI mode, alongside safeguards under the AEOI Standard," said a Hong Kong government spokesman.

The bill was tabled at the LegCo on 20 January. The government has committed to secure its early passage.

China and Singapore to enhance Free Trade Agreement

President of the People's Republic of China Xi Jinping, during a visit to Singapore on 6 November 2015, reached agreement with Singapore President Tony Tan to launch negotiations to upgrade to the China-Singapore Free Trade Agreement (CSFTA). The negotiations are scheduled for conclusion next year.

The CSFTA was signed in September 2008 after two years of negotiations and went into effect on 1 January 2009. It was the first comprehensive bilateral FTA signed by China with another Asian country.

Under the present CSFTA, Singapore has eliminated tariffs on all its imported goods from China, while China cancelled 97.1% of its duties on Singaporean exports. China is Singapore's largest trading partner, while Singapore has been China's largest foreign investor since 2013. Singapore also became China's largest overseas direct investment destination in ASEAN in 2014.

The Singapore Ministry of Trade and Industry (MTI) said the upgraded CSFTA would provide Singapore businesses with enhanced trade facilitation and greater investment protection in China, as well as address investment barriers.

"Both sides will also explore greater cooperation in areas such as legal services and financial services. To keep abreast of global developments, the CSFTA will also be enhanced with new generation elements such as E-commerce and environment," an MTI spokesperson said.

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Corporate benefits under the FTA include reduction on withholding taxes for a variety of services, including chargeable royalties. This, coupled with Singapore's low corporate and individual income tax rates, is one of the reasons Singapore has become a corporate regional hub for investments into China and Asia, as well as receiving increasing amounts of Chinese outbound investment. Foreign investors automatically qualify as Singaporean companies when setting up a subsidiary here, so they can also access Singapore's impressive array of international tax treaties – which include numerous FTAs, as well as over 80 bilateral double tax treaties.

Sovereign Management Services in Singapore specialises in setting up Singapore companies and also provides an array of ancillary services covering immigration assistance, accountancy, payroll and intellectual property. Managing director Andrew Galway said: "Our team is highly skilled and experienced, as well as offering such services in both English and Mandarin. We also assist Singapore firms entering China by liaising with our China office, which is dedicated to market entry and growth strategy and implementation."

Hong Kong again ranked as world's freest economy

Hong Kong has retained its position as the world's freest economy for the 22nd consecutive year in the Heritage Foundation's Index of Economic Freedom, which ranks the degree of economic freedom in 178 economies around the world.

The 2016 Index assessed 10 factors: business freedom, trade freedom, fiscal freedom, government spending, monetary freedom, investment freedom, financial freedom, property rights, freedom from corruption, and labour freedom.

Hong Kong achieved an overall score of 88.6 (on a scale from 0 to 100), a decline of one point compared with 2015 but still above Singapore's second place score of 87.8, which was down 1.6 points from last year. The gap between Hong Kong and Singapore actually widened slightly, after narrowing for five consecutive years.

Hong Kong retained top position in business freedom, trade freedom, and financial freedom. The Foundation praised Hong Kong's low and simple tax regime, zero tariff rates and its reputation as one of the most open economies in the world for trade and investment.

It said: "The implementation of prudent economic policy within a stable and transparent legal environment has been the cornerstone of Hong Kong's continuing achievement in maintaining the world's freest economy. Well-secured property rights ensure vibrant commercial interactions and entrepreneurial growth. With a high level of market openness and fiscal discipline, Hong Kong continues to be a leading global business and financial hub." The financial sector remains highly competitive and well-capitalised, serving as a leading global hub."

A Hong Kong government spokesperson said that the slight dip in Hong Kong's overall score was: "A timely reminder that, with other regional economies progressing forward, we must keep up with the pace of global economic development closely and strive to enhance our global competitiveness ... the government will continue to uphold the free market principles by providing a favourable business environment, ensuring fair competition and free trade, maintaining a simple tax regime with low tax rates, and keeping an efficient public sector."

The scores of Hong Kong and Singapore were significantly ahead of third-placed New Zealand (81.6), Switzerland (81.0), Australia (80.3), and Canada (78.0). The US scored 75.4, a fall of 0.8 points, and was ranked only eleventh on the 2016 Index, one place below the UK, which improved by 0.6 points to 76.4.

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Director of Sovereign Trust (Hong Kong) Julia Connolly said: "It is no surprise that investors continue to flock to Hong Kong, the freest economy in the world, to establish new companies. As part the 2016-2017 Budget in late February 2016, Financial Secretary John Tsang announced HK$500 million for a new Innovation and Technology Fund for Better Living, HK$2 billion to set up an Innovation and Technology Venture Fund, as well as HK$8.2 billion for promotion of smart production and research by Science Park, all of which will enhance the competitiveness of SMEs in Hong Kong. Sovereign has had a presence in Hong Kong since 1995 and we look forward to a bumper 2016!"

Invest HK assists record number of foreign companies

Invest Hong Kong, the territory's inward investment agency, announced that it assisted a record number of businesses to set up or expand in Hong Kong in 2015. The agency assisted 375 overseas and Mainland companies to set up or expand in Hong Kong in 2015. This number represents an all-time high and a year-on-year increase of 5.6%.

InvestHK's Director-General of Investment Promotion, Simon Galpin, said: "2015 was another record year for InvestHK in terms of the number of companies assisted. Despite ongoing challenges in the global economy, Hong Kong continues to attract overseas and Mainland investors because of its enduring advantages and emerging business opportunities."

The 375 companies came from 36 economies. Mainland China continued to lead with a total of 78 companies, followed by the US with 49 companies, the UK (36), Japan (31), and France (20). For the first time, InvestHK helped two companies from Latvia and Seychelles to set up in Hong Kong.

InvestHK set up a dedicated team to assist start-ups in 2014. It assisted 69 start-ups in 2015, which represented 18.4% of the total number of companies assisted last year. They were mainly from France, the US, and the UK (10 from each). The agency confirmed that it would continue to promote Hong Kong as one of the fastest growing start-up ecosystems in the world.

China confirms drive to replace Business Tax with VAT

China's State Council announced, at a meeting on 22 January 2016, that China would complete the implementation of its new value-added tax (VAT) regime, in place of business tax, across all industries in 2016. The change is seen as "a crucially important part for deepening fiscal and tax reforms."

Transportation, postal and telecom services were added to the VAT base in 2014. This year China will extend VAT to financial services, construction, real estate and consumer services.

Business tax is a levy on the gross revenue of a business while VAT is levied on the difference between a commodity's price before taxes and its cost of production. A pilot scheme on business tax-to-VAT was tested in 2012 and gradually been expanded to industries including transportation, telecommunication and postal service.

A primary objective of VAT reform is to alleviate the corporate tax burden. From 2012 to the first half of 2015, the measure resulted in tax savings of over CNY484.8 billion (US$75 billion), accounting for 0.2% of GDP in the period, according to a report by China International Capital Corp (CICC), the country's first joint venture investment bank.

Once all industries shift to VAT in 2016, the overall tax saving will be more than CNY900 billion, or 0.4% of GDP, CICC predicted. VAT can encourage firms to outsource more services rather than adopting a do-it-all business model, promoting the development of the service sector and the upgrading of manufacturing industries, the report added.

SOVEREIGN COMMENT

The existing business tax, which VAT is replacing, is charged at every stage of the supply chain on the gross amount, rather than the net value added. VAT will therefore eliminate the double tax issues encountered by businesses and remove distortions to supply chains.

Mauritius to begin automatic exchange in September 2018

The Mauritius Revenue Authority (MRA) announced, on 15 January 2016, that the first exchange of information under the OECD's new Common Reporting Standard (CRS) would take place in September 2018 – a year later than originally planned.

Mauritius was among the first 51 jurisdictions – known as the "early adopters" – that signed a multilateral competent authority agreement in October 2014 to automatically exchange on financial account information. These countries committed to start exchanging automatically in 2017.

In a recent communiqué to stakeholders, the MRA said that the requirement to apply due diligence procedures to record tax residence of clients opening new accounts would now take effect as from 1 January 2017 rather than 1 January 16. A technical committee will finalise the guidance notes for the implementation of CRS.

FISCAL NEWS

G20 leaders endorse OECD's plan to combat BEPS

The leaders of the world's 20 largest economies endorsed, at the G20 summit in Antalya, Turkey, on 16 November 2015, the OECD's proposed package of measures to tackle corporate tax evasion by multinational companies that is categorised as "base erosion and profit shifting" (BEPS).

BEPS refers to the shifting of profits of multinational groups to low tax jurisdictions and the exploitation of mismatches between different tax systems so that little or no tax is paid. The OECD estimates that the resulting revenue losses to national treasuries have risen from $100 billion to $240 billion, or 4 to 10% of global tax revenues, every year.

Following international recognition that the international tax system needed to be reformed to prevent BEPS, the G20 asked the OECD to recommend possible solutions. In July 2013, the OECD published a 15-point Action Plan, which seeks to oblige multinationals to pay tax in the country where their main business activity is based. Its final recommendations were published in October 2015.

In a joint statement delivered after the two-day summit, G20 leaders declared that they "strongly urge the timely implementation of the project and encourage all countries and jurisdictions, including developing ones, to participate." They asked the OECD to monitor progress on BEPS and to develop a framework to allow developing countries to join the project.

An important milestone towards implementation of the OECD/G20 BEPS Project was achieved on 27 January 2016, when 31 countries signed the OECD's Multilateral Competent Authority Agreement (MCAA) for the automatic exchange of country-by-country reports (CbC). The signing ceremony marked and a significant increase in cross-border cooperation on tax matters.

The MCAA is intended to enable consistent and swift implementation of new transfer pricing reporting standards developed under Action 13 of the BEPS Action Plan by ensuring that tax administrations obtain a complete understanding of the way multinational enterprises (MNEs) structure their operations.

The CbC Reporting Implementation Package consists of: model legislation that can be used by countries to require the ultimate parent entity of an MNE group to file the CbC Report in its jurisdiction of residence; and three model Competent Authority Agreements to facilitate implementation of the exchange of CbC Reports, based on:

- Multilateral Convention on Administrative Assistance in Tax Matters;
- Bilateral double tax treaties; and
- Tax Information Exchange Agreements (TIEAs).

The CbC MCAA sets out the rules and procedures for the competent authorities of jurisdictions implementing BEPS Action 13 to automatically exchange CbC Reports prepared by the reporting entity of an MNE Group and filed on an annual basis with the tax authorities of the jurisdiction of tax residence of that entity with the tax authorities of all jurisdictions in which the MNE Group operates.

The tax administrations where a company operates will get aggregate information annually, starting with 2016 accounts, relating to the global allocation of income and taxes paid, together with other indicators of the location of economic activity within the MNE group. It will also cover information about which entities do business in a particular jurisdiction and the business activities each entity engages in. First exchanges will start in 2017-2018 on 2016 information.

"CbC Reporting will have an immediate impact in boosting international co-operation on tax issues, by enhancing the transparency of multinational enterprises' operations," said OECD Secretary-General Angel Gurría. "Under this multilateral agreement, information will be exchanged between tax administrations, giving them a single, global picture on the key indicators of multinational businesses. This is a much-needed tool towards the goal of ensuring that companies pay their fair share of tax, and would not have been possible without the BEPS Project."

The 31 countries to sign the CbC MCAA were: Australia, Austria, Belgium, Chile, Costa Rica, the Czech Republic, Denmark, Estonia, Finland, France, Germany, Greece, Ireland, Italy, Japan, Liechtenstein, Luxembourg, Malaysia, Mexico, the Netherlands, Nigeria, Norway, Poland, Portugal, Slovak Republic, Slovenia, South Africa, Spain, Sweden, Switzerland and the UK.

European Council adopts Directive for exchange of advance tax rulings and pricing arrangements

The European Council adopted, on 8 December 2015, a new directive that will require EU member states to exchange information automatically on advance cross-border tax rulings and advance pricing arrangements (APAs) as from 1 January 2017. Member states receiving the information will be able to request further information where appropriate.

The European Commission will be empowered to develop a secure central directory, where the information exchanged would be stored. This directory will be accessible to all member states and, to the extent that it is required for monitoring the correct implementation of the directive, to the Commission.

The text amends directive 2011/16/EU on administrative co-operation in the field of taxation, which sets out practical arrangements for exchanging information. Member states will be required to transpose the new rules into national law before the end of 2016.

The following rules will apply in respect of rulings issued before 1 January 2017:

- If advance cross-border rulings and advance pricing arrangements are issued, amended or renewed between 1 January 2012 and 31 December 2013, such communication shall take place under the condition that they are still valid on 1 January 2014;

- If advance cross-border rulings and advance pricing arrangements are issued, amended or renewed between 1 January 2014 and 31 December 2016, such communication shall take place irrespectively of whether they are still valid or not;
- Member states will have the possibility (not an obligation) to exclude from information exchange advance tax rulings and pricing arrangements issued to companies with an annual net turnover of less than €40 million at a group level, if such advance cross-border rulings and advance pricing arrangements were issued, amended or renewed before 1 April 2016. However, this exemption will not apply to companies conducting mainly financial or investment activities.

The directive is in line with developments within the OECD and its work on base erosion and profit shifting (BEPS). The Commission proposed the directive as part of a package of measures in March 2015. The Council reached political agreement on the directive on 6 October 2015. The European Parliament gave its opinion on 27 October 2015.

European Commission finds Belgian "excess profit" tax scheme is illegal

The European Commission ruled, on 11 January 2016, that the Belgian "excess profit" tax scheme, which gave tax reductions of around €700 million to at least 35 multinational companies, was illegal under EU state aid rules. Belgium now has to recover the unpaid tax from the companies concerned.

Belgian law requires both stand-alone companies, and companies that are part of a group, to pay taxes on the profits they actually record in Belgium. However the "excess profit" scheme allowed the Belgian tax authorities to issue tax rulings to specific multinationals which deemed certain profits to be derived from synergies and economies of scale.

Under the rulings, this "excess profit" was not taxed in Belgium and the company's tax liability was reduced accordingly. In practice, this meant that the companies concerned did not pay taxes on more than 50% of their actual profits, and in some cases up to 90%.

The Commission ruled against the scheme under state aid rules because it gave qualifying multinationals a preferential, selective subsidy compared with their competitors liable to pay taxes in Belgium under the normal Belgian company tax rules. It also discounted the alleged "excess profit" unilaterally from the tax base of a single group company rather than following the "arm's length principle" on allocating profits between a group of companies at market terms.

Finally, contrary to what Belgium claimed, the Commission ruled that the scheme could not be justified by the need to prevent double taxation. The discounted profits were not taxed elsewhere and the scheme did not even require companies to demonstrate any evidence or even risk of double taxation. Instead of preventing double taxation, in reality the scheme gave a "carte blanche" to double non-taxation.

Margrethe Vestager, European Commissioner for Competition, said: "There are many ways for EU countries to subsidise investment in line with EU state aid rules. However, national tax authorities cannot give any company, however large or powerful, an unfair competitive advantage compared to others. This means that national tax authorities cannot establish tax schemes that only benefit a select group of companies, in this case, multinationals.

"According to the information Belgium submitted, at least 35 multinationals benefitted from the scheme. We cannot name the companies at this stage because the Commission assessed and found the scheme itself illegal. We did not have to investigate the specific tax rulings to each company that are based on the scheme. They are automatically illegal. It is now for the Belgian authorities to confirm which companies actually benefitted from the scheme and implement recovery."

Belgian Finance Minister Johan Van Overtveldt said he had expected the decision and therefore had suspended the scheme for new companies as soon as the EU investigation began. Reports said multinational beneficiaries of the scheme included brewer AB InBev, BP, BASF, Proximus, Atlas Copco, Wabco Holdings and Celio France.

The Commission said it was continuing its inquiries into tax rulings practices in all EU Member States to identify and address distortions of competition, in addition to in-depth investigations into tax rulings in Ireland and Luxembourg.

EC presents new measures against corporate tax avoidance

The European Commission published, on 28 January 2016, new proposals to tackle corporate tax avoidance. The "Anti-Tax Avoidance Package" calls on Member States to take a stronger and more coordinated stance against companies that seek to avoid paying their fair share of tax and to implement the international standards against base erosion and profit shifting (BEPS).

The key features of the new proposals, which are intended to combat aggressive tax planning, boost transparency between Member States and ensure fairer competition for all businesses in the Single Market, include:

- Legally-binding measures to block the most common methods used by companies to avoid paying tax;
- A recommendation to Member States on how to prevent tax treaty abuse;
- A proposal for Member States to share tax-related information on multinationals operating in the EU;
- Actions to promote tax good governance internationally;
- A new EU process for listing third countries that refuse to play fair.

The two legislative proposals in the Package will be submitted to the European Parliament for consultation and to the Council for adoption.

Switzerland agrees AEOI with British Crown Dependencies

20 January 2016, Switzerland signed joint declarations on the introduction of the automatic exchange of information (AEOI) in tax matters on a reciprocal basis with the British Crown Dependencies of Jersey, Guernsey and the Isle of Man, as well as with Iceland and Norway.

The AEOI will be implemented based on the OECD Multilateral Competent Authority Agreement on the Automatic Exchange of Financial Account Information (MCAA). Switzerland and these countries intend to start collecting data in accordance with the global AEOI standard in 2017 and to start transmitting data in 2018, after the necessary legal basis has been created.

The joint declarations meet the criteria set by the Swiss Federal Council in the negotiation mandates of 8 October 2014. Aside from the EU and the US, the negotiations initially concern countries with which there are close economic ties. Switzerland has already signed a similar joint declaration with Australia as well as concluding an agreement on AEOI with the EU. It further signed a joint declaration with Japan on 29 January.

LEGAL NEWS

European Commission opens formal investigation into McDonald's tax deal with Luxembourg

The European Commission opened, on 3 December 2015, a formal probe into Luxembourg's tax treatment of US food chain McDonald's on grounds that an advantageous tax ruling may have been in breach of EU State aid rules.

Commissioner Margrethe Vestager, in charge of competition policy, said: "A tax ruling that agrees to McDonald's paying no tax on their European royalties either in Luxembourg or in the US has to be looked at very carefully under EU state aid rules. The purpose of Double Taxation treaties between countries is to avoid double taxation – not to justify double non-taxation."

The Commission requested information on the tax rulings in summer 2014. Based on two tax rulings given by the Luxembourg authorities in 2009, the Commission found that McDonald's Europe Franchising had subsequently paid no corporate tax in Luxembourg despite recording large profits – more than €250 million in 2013 – from royalties paid by franchisees operating restaurants in Europe and Russia for the right to use the McDonald's brand and associated services.

The company's head office in Luxembourg was designated as responsible for the company's strategic decision-making, but the company also had two branches – a Swiss branch that had limited activities related to the franchising rights, and a US branch that had no real activities. The royalties received by the company were transferred internally to the US branch of the company.

A first tax ruling given by the Luxembourg authorities in March 2009 confirmed that McDonald's Europe Franchising was not due to pay corporate tax in Luxembourg on the grounds that the profits were to be subject to taxation in the US under the Luxembourg-US double tax treaty. Under the ruling, McDonald's was required to submit proof every year that the royalties transferred to the US via Switzerland were declared and subject to taxation in the US and Switzerland.

However McDonald's Europe Franchising did not have any taxable presence in the US under US law and therefore McDonald's could not provide any proof that the profits were subject to tax in the US, as required by the first ruling. McDonald's clarified this in a submission requesting a second ruling, insisting that Luxembourg should nevertheless exempt the profits not taxed in the US from taxation in Luxembourg.

The Luxembourg authorities then issued a second tax ruling in September 2009 according to which McDonald's was no longer required to prove that the income was subject to taxation in the US. McDonald's argued that the US branch of McDonald's Europe Franchising constituted a "permanent establishment" under Luxembourg law, because it had sufficient activities to constitute a real US presence.

Simultaneously, McDonald's argued that its US-based branch was not a "permanent establishment" under US law because, from the perspective of the US tax authorities, its US branch did not undertake sufficient business or trade in the US.

The Luxembourg authorities recognised the McDonald's Europe Franchising's US branch as the place where most of their profits should be taxed, whilst US tax authorities did not recognise it. The Luxembourg authorities had therefore exempted the profits from taxation in Luxembourg despite knowing that they were not subject to tax in the US.

The Commission will now investigate further to see if its concerns are justified that the second tax ruling in particular provided McDonald's Europe Franchising with a favourable tax treatment in breach of EU state aid rules. It will assess whether the Luxembourg authorities selectively derogated from the provisions of their national tax law and the Luxembourg-US double tax treaty and whether the Luxembourg authorities therefore gave McDonald's an advantage not available to other companies in a comparable factual and legal situation.

SOVEREIGN COMMENT

Since June 2013, the Commission has been investigating the tax ruling practices of Member States. It extended this information inquiry to all Member States in December 2014. In October 2015, the Commission found that tax rulings for Fiat in Luxembourg and Starbucks in the Netherlands granted illegal selective tax advantages to the companies in breach of EU state aid rules. The Commission also has ongoing in-depth state aid investigations into tax rulings concerning Apple in Ireland, Amazon in Luxembourg and Belgium's "excess profit" ruling system.

Spanish soprano receives suspended jail sentence for tax fraud

15 December 2015, Spanish opera singer Montserrat Caballé was given a six-month suspended jail sentence for tax fraud. The sentence was the result of an agreement with prosecutors that avoided the need for a trial. All first convictions resulting in sentences of less than two years are suspended in Spain. She was also fined €326,000.

Prosecutors claimed that she had earned more than €2 million from a number of recordings and concerts in countries that included Spain, Germany, Switzerland, Italy and Russia in 2010. The singer claimed she was a resident in neighbouring Andorra at the time but, it was alleged, she was actually living in Spain "with the sole objective of not paying taxes to the Spanish state".

According to court documents, Caballé allegedly signed all her concert contracts through a company registered in Andorra and deposited the income in an Andorran bank account with the aim of "ensuring the treasury did not have knowledge of her income and her true residency in Spain".

In a brief hearing, the singer ratified an out-of-court agreement in which she admitted that she had avoided paying €508,000 in taxes related to her earnings from 2010. Caballé, who is 82 years old and has avoided public engagements since a stroke in 2012, appeared at the hearing via videolink from her home.

The singer said that she had been unaware of how her income was being handled for tax purposes, and that she had become confused after a previous adviser had passed away. The governments of Spain and Andorra signed a bilateral Tax Information Exchange Agreement (TIEA) in 2010.

Florida appeal court upholds award to Robert Rauschenberg estate trustees

6 January 2016, the District Court of Appeal of Florida held that a USD24.6 million award granted to three trustees who administered the estate of the late US artist Robert Rauschenberg had been properly calculated by a lower court.

Rauschenberg's estate was structured such that the Rauschenberg Foundation was the primary beneficiary of the Robert Rauschenberg Revocable Trust. The trustees – Darryl Pottorf, Bennet Grutman and Bill Goldston, respectively Rauschenberg's executor, business partner and accountant – oversaw the trust for several years after Rauschenberg's death in 2008 while its assets were being transferred to the foundation. During that time, it was claimed that the value of the trust's assets rose from about $600 million to $2.18 billion.

The trust documents did not include any indication as to trustee remuneration and the dispute arose as to the method to be used to calculate their fees. The trustees claimed they were owed $51 million to $55 million because of the nature of their work and the vast increase in the value of the assets. Representatives of the Foundation, however, argued that, based on an hourly rate, the three were only entitled to $375,000.

Judge Rosman, in the Circuit Court for Lee County in August 2014, chose to follow the principles regarding reasonable compensation set out in *West Coast Hospital Ass'n v. Florida National Bank* (1958). These include (among others): considering the amount of capital and income received and disbursed by the trustee; the success or failure of the administration of the trustee; unusual skills or experience which the trustee in question may have brought to their work; the fidelity or disloyalty displayed by the trustee; and the amount of risk and responsibility assumed.

Judge Rosman found that the trustees' accomplishments on behalf of the trust had been substantial and that they had made "very good decisions and rendered very good service". As the trustees had already split USD8 million in fees among themselves, he ordered that they were entitled to another USD16.4 million, totalling USD24.6 million.

The Second District Court of Appeal unanimously agreed. "The court's findings regarding those factors and the reasonable fee amount are supported by the evidence presented at trial," wrote Judge Morris Silberman.

Widow's claim for further financial provision rejected

The Central London County Court dismissed, on 12 February 2016, a claim brought by a widow under the Inheritance (Provision for Family and Dependants) Act 1975 without any further financial provision being awarded out of the estate.

In *Wooldridge v Wooldridge*, Thandi Wooldridge sought to claim an additional £3.75 million from her late husband's estate. Ian Wooldridge, who died in a helicopter crash in Northern Ireland in 2010, ran a construction business and a commercial polo facility with his brother. He left an estimated £10 million, which included the £4.25 million family home in Surrey and various other assets.

Wooldridge's will left the family home to his widow, who he had married in 1999, together with the benefit of several life assurance policies valued at £1.6 million. He left his interests in the two businesses to their son Rhett, aged six, as well as his son Charlie, aged 22, by a previous relationship.

Following his death, Mrs Wooldridge, Charlie and Rhett had received £1.985 million, £315,000 and £200,000 respectively under a fatal accidents claim in Northern Ireland in relation to the helicopter crash to compensate for their financial dependency on Wooldridge.

In August 2012, Mrs Wooldridge commenced a claim under the 1975 Act for further financial provision from Wooldridge's estate. She sought a further £3.75 million from his husband's estate on the basis that that her existing assets and entitlement under the will were insufficient to meet the standard of living that she and Wooldridge had enjoyed prior to his death, which she admitted was lavish.

She said that the life policy sums left to her had been eaten into by past debts and that although the matrimonial home had increased in value, she did not have sufficient liquid capital. She claimed she needed £372,000 a year to maintain her lifestyle, including £178,000 for personal expenditure on social events, clothes, jewellery, personal care and entertainment.

Her stepson, Charlie, disputed her claim and argued that the future of the family business would be profoundly jeopardised by such a pay-out.

Judge Karen Walden-Smith found that Mrs Wooldridge had assets of some £10.5 million to her name, including assets of nearly £5.3 million that could be invested to produce an income for her. Contrary to the case made by her at trial, Mrs Wooldridge also had significant earning potential as a skilled businesswoman.

The court held that even though the deceased's business interests were worth in the region of £40 million, Mrs Wooldridge's claim could not be satisfied from liquidity within the estate and that any increase in her provision would likely result in the sale of business assets. The court held that this would be contrary to the best interests of Charlie and Rhett. The court concluded she already had sufficient to satisfy her reasonable financial needs.

SOVEREIGN COMMENT

The case confirms the importance of the word "reasonable" when assessing the merit of claims for "reasonable financial provision" under the 1975 Act. Spouses are not bound to receive further provision from an estate to enable them to maintain the standard of living to which they had become accustomed, especially if the assets already available to them are capable of supporting a high standard of living. The Court must have regard to the competing needs of other family members or dependants when assessing a spousal claim.

THE PANAMA PAPERS

A version of this article by Sovereign Group chairman Howard Bilton originally appeared in *Be Beyond* magazine.

This one is set to run and run. The reputation of Mossack & Fonseca (M&F) and Panama may be irreparably damaged. The reputation of the offshore industry generally may also suffer but most of the commentary has been off the mark and informed by moralistic hubris. The so-called "Panama Papers" – all 11 million of them – were obtained by hacking. In most countries that is illegal, and so is using or receiving stolen information. Nobody seems to be commenting on that.

It is clear that some of the structures set up by M&F were beneficially owned and set up by persons with high-level political connections. Such persons are known as Political Exposed Persons or PEPs. Financial institutions who deal with such persons are required to undertake the highest levels of due diligence and be particularly inquisitive about source of funds to ensure that monies received by the structures are legitimately earned rather than the proceeds of corruption. It seems little or no care was taken. Other structures were used for blatant tax evasion.

But the exposure of such persons has simply been brought forward by a year. Just a few weeks ago, the OECD told G20 Finance Ministers that Panama was back-tracking on its commitment to automatic exchange of financial account information and described It as "the last major holdout that continues to allow funds to be hidden offshore from tax and law enforcement authorities."

By the end of next year, the OECD's Common Reporting Standard (CRS) will have been introduced – 96 jurisdictions (and counting) will introduce automatic exchange of financial account information within the next two years. This will require all financial institutions, so that includes banks and offshore service providers, to exchange information about anybody and everybody that does business with them who is not resident in their own jurisdiction. The mechanism for the exchange is yet to be worked out entirely but for sure every tax authority anywhere in the world will be able to get this information and use it to ensure that it is no longer possible for persons within their jurisdiction to illegally evade tax by failing to declare taxable income.

CRS does not mean that offshore structures will no longer be effective or useful. Responsible advisors should be telling clients that if they cannot afford to have details of the structures they are setting up revealed to their home tax authority, they should not be setting them up. In some countries, simple offshore structures can still be used very effectively to reduce taxes. Or the structure may not be tax-led and might set up for many other purposes.

Many countries attribute income earned by offshore companies and trusts to the owners (if there is such a thing as an owner of an offshore trust). These so-called attribution or Controlled Foreign Company (CFC) rules mean that offshore structures will not be effective in reducing taxes for many unless they illegally "forget" to declare the underlying income on their tax form.

A tax offence occurs when the taxpayer signs an incorrect tax form. There is still nothing illegal or wrong for a taxpayer to set up an offshore structure or for M&F to assist them to do this. In fact M&F rarely deals with the end user client. It is a wholesaler that habitually provides companies to other financial intermediaries, particularly Swiss banks. However the Swiss banks have many clients whom they knew or suspected were not declaring the income from their Swiss bank accounts correctly.

This became a major problem with the advent of the EU Savings Directive, which required Swiss banks to automatically reveal details of any EU tax resident who had accounts in Switzerland. But, the Directive only covered individual accounts. The solution – or "suggestion" – of the Swiss banks was to avoid having to make a report by transferring the account from an individual name into a corporate name.

Later this Directive was expanded to catch accounts beneficially owned by EU residents even if the account was held in the name of a trust or company. The suggested solution to that problem was to transfer the accounts to Singapore. M&F knew why Swiss banks were ordering large numbers of companies for their clients. But it was not advising these clients directly, now was it was encouraging them to sign an incorrect tax form.

It might also be argued that the Swiss banks were complicit in tax evasion but ultimately every taxpayer is responsible for their own tax affairs and neither M&F nor the Swiss banks have any duty to check that the client is signing their tax form correctly. They are not agents for foreign tax authorities. If they asked a taxpayer to show their tax forms, they would probably refuse. And in any event, it is by no means certain that they could tell whether the income earned on the Swiss bank account had been included in total income or not.

Of course the case coukld be made that both M&F and the Swiss banks were complicit in a conspiracy to defraud foreign revenue authorities. That is undoubtedly arguable and different levels of guilt could be attributed to both. No doubt we will find this out in the fullness of time.

What seems to me to be of greater concern is that the argument has now moved on to whether it is appropriate for any taxpayer to attempt to reduce the amount of tax they pay. The media is clearly taking a stance that any arrangement that saves tax is morally reprehensible even if it is totally legal. For them, it is not sufficient to rely on the law. Any tax saving arrangement is surely wrong and should be outlawed.

And nobody it seems should be entitled to keep their financial affairs private. There is even talk of moving to a Scandinavian-type system where the tax returns of every individual are a matter of public record. The right to privacy has already been largely eroded and many are arguing it should disappear completely – which is like saying, "if you're not doing anything wrong, why would you mind taking your pants down in public". Shades of 1984, I think.

In the UK press, Prime Minister David Cameron is now being criticised because he received a gift from his mother. UK inheritance tax rules mean that, if his mother left the money to him in her will, it would be subject to tax at 40%. If she gives it to him during her lifetime and survives for seven years, no tax is payable. In other words, Mrs Cameron used a perfectly legal way of potentially avoiding 40% tax on a capital sum by making a lieftime gift to her son. Yet they are being castigated.

This is surely taking the argument too far. If the UK government wished to tax such gifts, it is perfectly able to do so. It has chosen not to. Should everyone be forced to hang on to all their wealth until they die, just so that the tax take can be maximised? The press seem to believe so. The dictum of Lord Tomlin in the *Duke of Westminster* case – "Every man is entitled, if he can, to order his affairs so that the tax attaching under the appropriate Acts is less than it otherwise would be" – seems to have been long forgotten. Rather it now seems that every taxpayer is expected arrange their affairs to maximise the amount of tax payable – or face heavy press criticism.

It could be pointed out to anybody who regards tax efficiency as fundamentally wrong that any good advisor will also be able to arrange their affairs in such a way that the amount of tax they pay is maximised. I doubt there would be a rush of takers for that service – even from journalists, commentators or members of Her Majesty's Most Loyal Opposition.

SIMON GARVEEN IS...

SOVEREIGN MAN

All the pies (long-term incentive plans)

I started my software company way back in 1990 and we have done quite well. The beauty of this business is that it's adhesive. Every year we get a royalty from every customer, which means that since we started – barring some bad years when people were either cutting back or claimed they were unable to pay – the annually recurring revenues have been going upwards. Many years ago we reached the point where the annual fees cover our overheads, so any more software we sell is essentially pure profit. Not bad for an idea that started on the back of a cigarette pack.

The fact that banks are currently paying virtually nothing for cash on deposit makes this type of business even more attractive. I get frequent approaches from investment funds, private equity firms and trade buyers asking if we are for sale – and there are some big numbers being bandied about. Big to me at least. It seems the highest multiple I might expect is about nine times our profits.

A sale at that price would generate a nice lump of cash. I certainly wouldn't have to work again. But what would I do with it? If I gave it to a private bank and told them to invest conservatively, they indicate that the best return I could currently expect is between 5% and 10%. I assume that really means 5%! In fact that level of return, which includes both income and capital gains, seems to be pretty much the average expectation over a prolonged period in any market.

So why would I take money out of a business that I understand and control myself and which gives me an 11% return on its perceived capital value, and put it in something over which I have no control and is likely to pay only half that return? Added to which, my business is increasing in value so I'm pretty sure that I should achieve a capital gain on top of the dividend income. Finally, my business is set up to work very tax efficiently but, if I were to retire, many of these benefits would cease and that would make my net return even lower.

If selling doesn't sound like a good idea, what is the alternative? I don't want to keep working as hard as I am forever, so I'm going to need a good succession plan. And that means employees who are committed to the business over the long term.

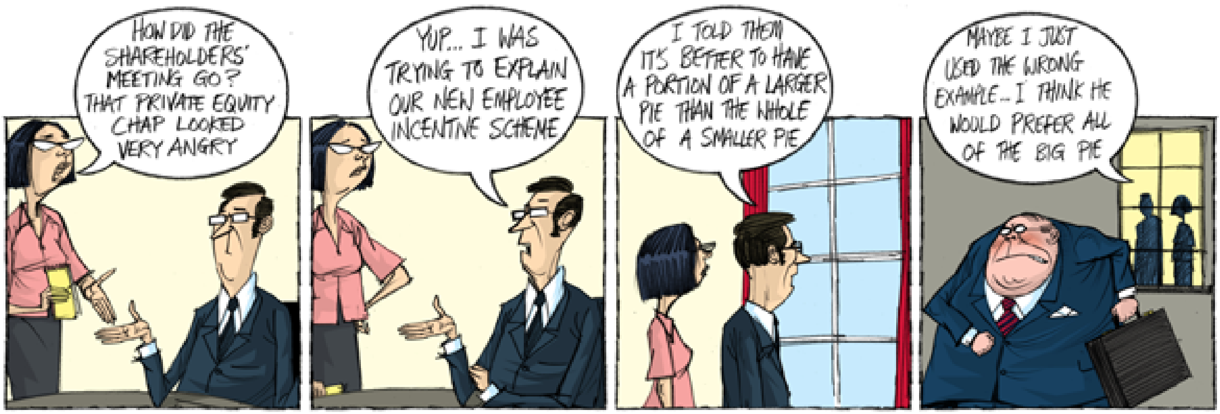
> *"It is better to have a portion of a larger pie, than the whole of a smaller pie."*

Over the years I've tried different ways to keep the staff incentivised. When I started the business, we simply paid a salary that was reviewed periodically according to performance. That seemed to work well for a time and when we looked at bonus schemes we could see as many disadvantages as advantages. Staff might be tempted to sell customers the wrong product just to boost their bonus and, besides, bonuses don't always account for the costs of a sale. They also create a culture where everyone is competing rather than cooperating.

In the end however, it became clear that we could not attract or retain good staff without a bonus scheme, so key staff were given share options. Unfortunately this corresponded with the downturn, so very few were exercised and it didn't seem to spur anybody to greater effort. Later we were put under pressure to revise the option targets to match the actual results. That seemed pointless, so we declined and the whole scheme became a damp squib.

Now Sovereign has helped us devise a long-term incentive plan. It works by giving key staff an interest in the capital and income of the company for as long as the company's results improve. The employees' interests are held by the trustees, so we don't have to deal with multiple shareholders; and we can take the "shares" back if an employee leaves or stops performing.

In this way it should work equally well for employees, by giving them a stake in the ongoing success of the company, and shareholders, because it is better to have a portion of a larger pie, than the whole of a smaller pie. I'm pleased with the results and we'll find out soon if the employees like it. I hope so because that back seat is looking mighty comfortable from where I'm sitting.



CONSERVO CASE STUDY
SOUTH AFRICAN SPORTSMAN

By Coreen van der Merwe, Managing Director of Sovereign Trust (SA) Limited

Sports professionals face a unique challenge when it comes to planning for their financial future. With an average retirement age of 33 years, making the right financial decisions early in a sports career, preferably before the peak-earnings period, will have a profound bearing on lifestyle later in life.

When planning for their financial future, sports professionals need to consider carefully what their life may look like when they have retired from their sport:

- Will they begin a second career in a related or separate area?
- Do they have, or intend to have, a family to support?
- Are current purchases, such as real estate, aligned to their wider financial goals?

A robust pension plan that adequately caters for the needs of the principal and any dependants will always be a vital element in a good financial plan. Pension plans should be flexible and tax efficient, as well as having a transparent cost structure and excellent administration.

Sovereign has created an International Retirement Plan, called the Conservo, which is a low cost and highly flexible vehicle for retirement savings. The Conservo is structured as a Guernsey-based, multi-member retirement trust. The trustee of the plan is Sovereign Trust (Guernsey) Limited, a trust company licensed and regulated by the Guernsey Financial Services Commission.

The Conservo is an ideal plan for South African tax residents who wish to consolidate offshore assets and utilise their annual foreign investment allowance – which was increased from ZAR4 million (approx. US$320,000) to ZAR10 million as of 1 April 2015.

FACTS

Francois is a 31-year-old South African professional rugby player now based in France. Having played for a South African provincial team in both the Currie Cup and Super Rugby competitions, he has signed a two-year contract to play for a French Top 14 side.

Francois also plays for the South African national team. Excepting injuries, he would have won more than the 40-plus international caps currently to his name. He does not have a Springbok national contract but, under his French contract, is available for the Boks for certain parts of the year.

As a senior Bok in South Africa, Francois earned upwards of ZAR4 million a year, including his provincial contract, win bonuses and commercial work. He opted to contribute 12.5% of his fixed remuneration towards the South African Rugby Players Association (SARPA) Retirement Fund. Under his new Top 14 contract in France, Francois has increased his potential earnings by a further ZAR3 million a year.

Francois has currently saved ZAR1.2 million in an interest bearing account with Absa Bank and a further ZAR6 million in unit trusts. He has invested in real estate worth a total ZAR14 million in South Africa and has business interests in a gym and a winery in South Africa.

Francois is married and currently has two children under the age of five. They have now joined him in France, where he has just acquired a property that is valued at €900,000 (approx. ZAR12.8 million). Since the start of his new contract, Francois has become tax resident in France.

Having the bulk of his assets in South Africa, Francois has concerns about South Africa's political stability, the Rand's volatility, inflation, as well as the high tax regime. Francois is also concerned about his ability to support a family in the longer term given the brevity of a sports career and the ever-present risk of a career-ending injury.

ACTIONS

The SARPA Retirement Fund is specifically designed for professional rugby players and confers favourable tax treatment on receipt of retirement savings from age 32 rather than from age 55. Francois and his advisor therefore decide to leave these investments in place but instruct a currency expert to transfer both the ZAR1.2 million in his Absa account and the ZAR6 million from his South African unit trusts to his Conservo account.

In addition to future savings, Francois can also make ad hoc transfers to the Conservo account, as and when he receives sums from signing fees, bonuses, sponsorships or endorsements. The plan is very flexible and accepts most assets. Funding is uncapped. Funds transferred to the Conservo are generally globally invested and would be expected to generate annualised returns of at least 3% to 5% over a full market cycle.

ZAR1.2 million
in his Absa account →

ZAR6 million
(the proceeds from selling his South Afrian unit trusts) →

Conservo Bank account & Investment Account
(Guernsey)

BENEFITS

- **Investment Diversification:** Francois is reducing his investment risk by investing in the international market;
- **Rand hedge:** Francois is reducing his exposure to the Rand by investing in hard currency as well;
- **Tax Efficient Structure:** Retirement trusts are not liable for tax on income or gains in Guernsey, ensuring maximum growth. The capital contributed by Francois may be returned to him without triggering tax. Payments from growth will be taxed as follows: 33% of growth will be taxed at Francois's marginal rate at the time of receiving the benefit;
- **Estate and Succession Planning:** Francois's heirs can benefit from the assets owned by the Conservo without unnecessary delays or restrictions due to the probate process. The assets will fall outside his estate and therefore no estate duty (20%) or executors fees (up to 3.99%) will be applicable;
- **Flexible drawdown options:** Francois may have access to the funds held by the Conservo at the age of 50 or later in life. He may also receive loans from the Conservo (up to a maximum of 50% of the total asset value) before he turns 50;
- **Peace of mind:** Francois has funds in a strong currency in a safe environment which he can access at short notice should he have to relocate for whatsoever reason;
- **Asset protection:** Trust assets are protected from future claims against Francois's estate.

COSTS

The trustee of the plan is Sovereign Trust (Guernsey) Ltd, which is licensed and regulated by the Guernsey Financial Services Commission. The plan starts at £750 to establish and £900 p.a. to administer. Charges may vary according to the plan investments.

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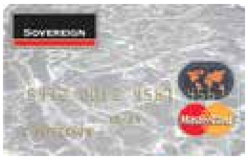

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