SOVEREIGN

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SOVEREIGN REPORT 48

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

Only here for the beard – tribute chin-wear was specially cultivated by colleagues in honour of Nigel Anteney-Hoare (seated centre, wearing permanent beard) for display at a surprise lunch to mark his retirement as Managing Director of Sovereign's Portugal operation.

Brexit – UK referendum vote

There has a lot been written about this. The result was surprising but it seems like there will be no change until 2019 at the earliest. And even then the most likely scenario is virtually no change. The UK and Europe need to do a trade deal. A trade deal with full access to the EU market is unlikely without Britain agreeing to free movement of people and probably continuing to contribute to EU coffers. Controlling immigration seemed to the main reason that voters in the UK voted to leave but how that can be achieved is not easy to envisage. Strange.

One of the less reported stories was from Gibraltar, where there was a near 100% turnout and a near 100% vote to Remain. The Gibraltarians feared that if they left the EU, Spain would get more aggressive about trying to reclaim sovereignty. Sure enough, the day after the vote Spain put out a statement saying it wished to re-examine this longstanding dispute. The primary concern for Gibraltar's working population is that Spain may again close the border to put pressure on Britain. A large number of those who work in international companies in Gibraltar actually live in Spain and cross the border every day. This could be a big problem in the years to come so we will be keeping a close eye on it. Contingency plans will have to be made anticipating the worst case scenario.

Sovereign signs new partnership with government of Dubai

Our Dubai office has signed a strategic partnership with Dubai FDI, which is the government department dedicated to attracting foreign investment. We are delighted to have our expertise in assisting companies to set up in Dubai officially recognised in this way.

It has taken many years to gain this recognition and means that clients can be assured of quality service and a fast track service if they use Sovereign to help establish themselves in the region. In particular, we have some unique solutions to the potentially problematical requirement that any local business must be majority-owned by Emirati shareholders.

On the 23rd of September we will be co-hosting an event with Dubai FDI at the Royal Automobile Club in London. We will be presenting to UK companies that wish to explore the possibilities of doing business in one of the fastest growing economic areas in the world. Please contact us if this is of interest and we will provide suitable invitations.

Sovereign named as International Retirement Provider Of The Year

I am also delighted that Sovereign Group was named "International Retirement Provider of the Year – Product" at the inaugural International Adviser Product and Service Awards 2016. We were selected for our Calpe and Centaurus retirement benefit schemes, two Qualifying Recognised Overseas Pension Schemes (QROPS) established and regulated in Gibraltar and Malta respectively. The judges recognised them as "products that are differentiated from competitors as innovative and backed by consistent service and support."

We continue to invest heavily in product development, staff and systems across the globe to ensure that we can provide relevant, cost effective products for the market and continue to deliver first-class administration services.

To this end we have just acquired UK-based MW Pensions, which will enable us to offer new Self Invested Personal Pensions (SIPPs). Sovereign has over 10,000 existing QROPS members and adding a SIPP operation in the UK makes sense because it means we can now offer a one-stop-shop for the retirement planning needs of expatriates. We offer free transfers within our range of QROPS products and this is being immediately extended to our new SIPP offering.

Our very first retiree

We used to think of Sovereign as a very young company. I suppose we are all getting maturer but this month we had our first executive officially retire from the Group. Nigel Anteney-Hoare has been with us since inception in 1987 but is now heading off into the sunset with our best wishes. He will remain on the Board of our Portuguese company and will be staying in touch with us and his longstanding clients. Nigel, who for many years has sported the Group's only beard (see picture above), says he is looking forward to spending time on what he does best – doing not very much at all. We wish him every success.

Howard Bilton
Chairman of the Sovereign Group

EUROPE

Cyprus to begin accepting online betting applications

President of the Cyprus National Betting Authority (CNBA) Ioanna Fiakkou announced, on 28 July 2016, that the NBA would begin accepting online betting applications on 3 October. Gambling sites that fail to submit an application within a one-month window – closing on 3 November – will have their domains added to the online blacklist.

The CNBA was established under the Betting Law of 2012, which revised the regulation of traditional and newer forms of betting in Cyprus. Article 12 of the Law sets out the two classes of authorised betting services; Class A covers physical premises, while Class B encompasses all forms of electronic betting. The new measure to regulate online betting will not expand the list of approved online options but it will increase the number of companies approved to offer online betting and therefore expand the market.

Cypriot finance minister, Harris Georgiades said that opening up the online betting market was part of the government's strategy to bolster tax revenue via gambling expansion. This strategy includes the ongoing process to award one physical casino licence, the licensing of video lottery terminals at sub-venues and privatising the operation of the state lottery.

"By opening and regulating online betting and the rest of the steps undertaken (by the government) in the betting industry, we create new significant prospects for the economy," he said. "Licensing will create the conditions for new jobs and the opening of new firms with a physical presence to Cyprus, new jobs for specialised staff, as well as for more effective control."

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In the last few years the worldwide online gaming industry has grown into a multi-billion dollar business and it is good to see that Cyprus is following in the footsteps of other recognised jurisdictions by offering a regulatory framework for online gaming companies. Sovereign has extensive experience in providing support services to the gaming industry and we are very much looking forward to adding Cyprus to the list of jurisdictions where such services are available.

UK votes to leave the European Union

23 June 2016, the UK voted to leave the European Union by 52% to 48% in a referendum. Prime Minister David Cameron, unsuccessful leader of the Remain campaign, announced he would resign. Theresa May succeeded Cameron as Prime Minister and leader of the Conservative party on 13 July. She immediately appointed Philip Hammond to replace George Osborne as Chancellor.

May, a Remain supporter, said the government respects the decision of the voters and will resolve to negotiate Britain's exit (Brexit) from the EU. To do so, the UK must trigger Article 50 of the Lisbon Treaty, which stipulates a two-year time limit for a withdrawal agreement to be reached. May has indicated that Article 50 will not be triggered until next year. The UK will therefore remain a full member of the EU, with all its rights and obligations intact, until at least 2019.

Hammond said the initial response to any loss of confidence in the UK was in the hands of the Bank of England and there will be no emergency Budget. He promised to create a new fiscal framework to boost the confidence of companies and households, but declined to elaborate on the scale of any possible fiscal stimulus or whether there would be changes to deficit reduction plans.

Brexit will give the UK government more freedom over its tax system although it could be constrained by economic factors. The UK currently has one of the most competitive corporate tax regimes in the EU and this is set to fall from 20% to 17% by 2020 under existing proposals. Unless the UK joins the European Economic Area or European Free Trade Association, it will no longer be bound by EU State Aid rules, enabling it to offer tax incentives to a much wider range of taxpayers. It will also regain control over the setting of taxes within the framework of tax treaties.

It is likely that some key directives already approved at EU level will never be transposed into UK law, while existing directives will have to be specifically enacted by the UK if they are to continue in effect. In terms of current EU initiatives, the UK would not have to adopt the latest anti-avoidance package and would not participate in proposed corporate tax harmonisation projects, notably the common consolidated corporate tax base.

If the UK leaves the EU VAT regime, UK businesses will be no longer be bound by the EU VAT Directive. This may create many new VAT compliance obligations and complexities, particularly for companies trading from and into the UK. Likewise there may be more unfavourable withholding tax outcomes on intra-group payments in the EU if the UK is no longer bound by the Parent/Subsidiary and Interest and Royalties directives.

Brexit will allow the UK to pursue bilateral trade deals with economies not currently included in free trade agreements (FTAs) negotiated by the EU, but these are complex instruments and it may prove difficult to build up a network of FTAs swiftly.

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The referendum was only advisory in nature. It is uncertain whether the result will have to be endorsed by a parliamentary vote. However May has said the government respects the decision of the voters and will resolve to negotiate a Brexit. It must therefore be assumed that the UK will, at some point, have a different legal and trading relationship with the EU. The past two years have seen the EU adopt several controversial directives, including the Fourth Anti-Money Laundering Directive (4ML). Some aspects of this directive, such as the mandatory register of trusts, were accepted by the UK only after much debate. The 4ML directive has not yet been transposed into UK law and may now be re-examined.

UK Budget tax changes heralds a further clampdown on avoidance

The 2016 Budget, announced on 16 March, contained reductions to capital gains tax, changes to Stamp duty land tax (SDLT), some clarification on the new "non-dom" regime and a further clampdown on tax avoidance.

The applicable rate of CGT for all gains realised as of 6 April 2016 will be reduced from 28% to 20% for higher rate taxpayers and from 18% to 10% for basic rate taxpayers. The lower rates will not apply to gains on residential property and carried interest.

The additional 3% SDLT charge for the purchase of second homes, first announced in the 2015 Autumn Statement, was confirmed. The government also brought the SDLT regime for non-residential and mixed-use property into line with that for residential property by changing from flat rate charge to a system based on value – 2% from £150,000 to £250,000, and 5% above – with immediate effect.

Legislation in respect of reforming the non-dom regime, and associated transitional measures, are to be introduced in Finance Bill 2017. However it was clarified that there will be automatic rebasing of offshore assets on 6 April 2017 for those non-domiciled taxpayers who are to be treated as deemed domiciled for income and capital gains, as well as inheritance tax purposes. There was also reference to a "transitional provision with regards to offshore funds to provide certainty on how amounts remitted to the UK will be taxed".

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London-based Group Tax Counsel Laurence Lancaster welcomed the clarification in certain areas. However UK taxation remains highly complex for both corporate and personal taxpayers. Whilst this was a feature of the Osborne budgets, it remains to be seen if new Chancellor Philip Hammond will change direction during the rest of the parliament given early indications that the austerity-led deficit reductions may be somewhat relaxed following the EU referendum.

Swiss parliament approves corporate tax reform bill

The Swiss Parliament approved, on 17 June 2016, the final bill on Corporate Tax Reform III, which is designed to align the Swiss corporate tax system with the latest international standards by removing certain preferential tax regimes and introducing competitive replacement measures.

The reform will phase out all special corporate tax regimes, such as the mixed, domiciliary, holding and principal company regimes, as well as the Swiss finance branch regime. Federal and cantonal tax holidays will not be affected by the reform and will continue to be granted.

A number of measures are included to compensate for the phase out, which include:

- Introduction of a patent box regime that is fully compliant with the modified nexus approach of the OECD. The patent box will only be available at the cantonal level and the maximum level of permissible tax relief for income related to the patent box has been set at 90%;
- Introduction, at the discretion of the individual cantons, of an increased tax deduction for research and development (R&D) expenses up to a maximum percentage of 150% of qualifying expenses incurred in Switzerland;
- Introduction of a notional interest deduction (NID) regime (mandatory at the federal level and optional at the cantonal level) on surplus equity. At the cantonal level, at least 60% of dividend income derived from qualifying participations held by individuals as private assets must be subject to personal income tax.
- Reduction of the cantonal/communal annual net wealth tax in relation to the holding of participations and of patented intellectual property, at the discretion of the individual cantons.

To boost the attractiveness of Switzerland as a business location and to compensate for the abolition of the cantonal tax regimes, most cantons are expected to lower their ordinary corporate tax rates. The cantons' share in the direct federal tax revenue will be increased from 17% to 21.2% to compensate. The final Bill is subject to an optional referendum. The target date for the entry into force of the reform package is currently 1 January 2019.

The Swiss Federal Council set 1 July 2016 as the date for the entry into force of the Foreign Illicit Assets Act and related ordinances, which strengthens its legislative framework for the freezing, confiscation and restitution of illicitly acquired assets in cases which cannot be solved on the basis of the Act on Mutual Assistance in Criminal Matters. The Act was approved by Parliament in December 2015.

The Act aims to address situations where foreign leaders have enriched themselves by misappropriating assets through corrupt or criminal means and have then transferred those assets to financial centres in other countries.

France opens Register of Trusts to public access – then suspends it

France's National Register of Trusts was made publicly accessible as of 30 June 2016 by a Decree of 10 May. Online access opened on 5 July but a judge of the Conseil d'Etat, France's highest administrative court, ordered a provisional suspension of the Decree on 22 July pending a full hearing by the Conseil Constitutionnel.

The Register was established in 2013 by a law requiring trustees to make annual or event-triggered reports to the tax authorities if either the trustee, the settlor or one of the beneficiaries are French tax residents, or if any of the trust assets are located in France. Currently, 16,000 entities have been identified as trusts and are registered with the French tax administration.

It contains the names, dates of birth and place of birth of settlors, trustees and beneficiaries. Details of beneficiaries who are minors are also given. Under the Decree, it was open to inspection by any individual with a French tax number.

A legal challenge was brought by an 89-year-old American woman, resident in France, who is a beneficiary of one of the listed trusts. The judge considered that the personal nature of the information being in the public domain could lead to the disclosure of the applicant's intentions in respect of her estate.

If the Decree is ruled constitutional, the Conseil d'Etat will judge whether or not it disproportionately infringes on the obligation to protect the applicant's private life. Unless the French courts restrict access to the tax office, the case may go the European Court of Human Rights.

UK government targets foreign owners of UK property

The UK government announced, on 12 May 2016, that foreign companies that own or wish to purchase property in the UK, or bid for central government contracts, will be required to join a new public register of beneficial ownership. Foreign companies currently own around 100,000 properties in England and Wales, including more than 44,000 in London alone. The Scottish government included similar proposals in its recent land reform bill.

Designed to prevent corrupt individuals and countries being able to move, launder or hide illicit funds through the property market, the announcement did not explain how the measure would be implemented or whether there would be penalties for non-compliance.

On 15 June, the UK government published legislation to amend the tax treaties between the UK and the Crown Dependencies of Guernsey, Jersey and the Isle of Man. The treaty protocols will introduce modern OECD provisions allocating the primary taxing right over income, profits and gains from land to the jurisdiction in which that land is situated. Legislation will also be enacted to tax trading profits derived from land in the UK.

These rules will apply equally to resident and non-resident businesses, and will not depend on the existence of a "permanent establishment" in the UK. This is designed to remove a loophole that enabled property development companies located in the Crown Dependencies to argue that the treaties prevent the UK from taxing them on the full amount of their profits from developing UK land.

SOVEREIGN COMMENT

This further demonstrates the UK government's aim to reduce potential revenue losses from the holding of UK property in overseas structures. Alternative compliant structures for UK property holding are available, particularly for non–UK domiciled investors. Interested readers should contact our UK office for details.

New EASA rules come into force

The new EASA European regulations, came into force on 25 August 2016. Designed to raise the standards of private aviation closer to those required for commercial air transport, the Part-NCC (Non-Commercial Complex) rule will place obligations on all non-commercial operators of "complex motor-powered" aircraft.

The regulations apply where aircraft are either registered in an EASA state – the 28 EU member states, plus Iceland, Norway, Switzerland and Liechtenstein – or where the operator is established or resides in an EASA state. It will also affect "third country" operators from outside EASA that operate aircraft into Europe.

The Part-NCC rule is designed to oblige non-commercial operators – those without an Air Operator Certificate (AOC) – to demonstrate that they have systems in place to implement and monitor regulatory safety and operational standards. These systems will be subject to audit and regular inspection. Failure to comply with the regulations will be a criminal offence and could lead to withdrawal of insurance cover and grounding of the aircraft.

Gibraltar's new Limited Liability Partnerships Act comes into force

The Gibraltar Limited Liability Partnerships (LLP) Act was brought into force on 24 March 2016 with the gazetting of the Limited Liability Partnerships (Application of Companies Act 2014 and Insolvency Act 2011) Regulations 2016, which will regulate the management and winding-up of LLPs.

An LLP is not legally a partnership. Like a company, it is a corporate body with a continuing legal existence independent of its members. Primarily designed for use by professional service providers, whose partners may be at risk from the careless or accidental negligence of a colleague, it is also available in respect of any type of trade, profession and occupation.

Any agreement that may be in place between the members remains confidential between the members and the LLP, and no disclosure or registration requirements apply. An LLP is also regarded as fiscally tax transparent and members can undertake management functions without forfeiting their limited liability protection.

Gibraltar Justice Minister Gilbert Licudi said: "I am delighted that we have been able to complete the framework so as to enable this legislation to come into operation as it adds to the significant work that this government has carried out in recent years to ensure our legislation is current, up to date and fit for purpose in a changing world environment."

SOVEREIGN COMMENT

We have highlighted other Gibraltar initiatives in recent issues, covering corporate legislation and retirement planning options in particular. The jurisdiction continues to push forward in several keys areas in order to enhance its competitive advantage.

EC proceeds with common property regime for international couples

The European Commission adopted, on 2 March 2016, proposals to clarify the rules applicable to property regimes for international married couples or registered partnerships.

The Commission is proceeding with only 17 Member States through a so-called "enhanced cooperation" because it was not possible to reach unanimity. Other Member States will continue to apply their national law while retaining the right to opt in.

The proposals, originally brought forward in 2011, will establish clear rules in cases of divorce, separation or death and bring an end to parallel and possibly conflicting proceedings in various Member States on property or bank accounts.

EU Justice Commissioner Vera Jourová said: "The new proposed rules will bring legal clarity and ease the complicated process of dividing up joint assets no matter where they are located."

There are currently around 16 million international couples in the EU. Out of the 2.4 million new marriages in 2007, 13% (310,000) had an international element. Similarly, 41,000 of the 211,000 registered partnerships in the EU in 2007 had an international dimension. Parallel legal proceedings in different countries, complex cases and the resulting legal fees cost an estimated €1.1 billion a year.

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AMERICAS & THE CARIBBEAN

US Treasury rules to increase financial transparency

The US Treasury Department announced, on 5 May 2016, a Customer Due Diligence (CDD) Final Rule, proposed beneficial ownership legislation and proposed regulations for foreign-owned, single-member Limited Liability Companies (LLCs). The actions are designed to strengthen financial transparency and combat the misuse of companies for illicit activities.

The CDD Final Rule adds a new requirement that financial institutions – including banks, brokers or dealers in securities, mutual funds, futures commission merchants, and introducing brokers in commodities – must collect and verify the personal information of the real people (beneficial owners) who own, control and profit from companies when those companies open accounts.

Financial institutions will have to identify and verify the identity of any individual who owns 25% or more of a legal entity, and an individual who controls the legal entity. It also extends the proposed implementation period from one year to two years, expands the list of exemptions, and makes use of a standardised beneficial ownership form optional as long as a financial institution collects the required information.

Financial institutions must further ensure that they understand the nature and purpose of customer relationships in order to develop customer risk profiles, as well as conduct ongoing monitoring to identify and report suspicious transactions and, on a risk basis, to maintain and update customer information.

The proposed legislation will require companies to know and report adequate and accurate beneficial ownership information at the time of a company's creation, so that the information can be made available to law enforcement. As part of the legislation, companies formed within the US would be required to file beneficial ownership information with the Treasury Department or face penalties for failure to comply.

For foreign-owned "disregarded entities", including foreign-owned single-member LLCs, financial institutions will require them to obtain an employer identification number (EIN) with the IRS. This will enable the IRS to determine whether there is any tax liability and to share information with other tax authorities.

A Treasury release said: "Together, these efforts target key points of access to the international financial system – when companies open accounts at financial institutions, when companies are formed or when company ownership is transferred, and when foreign-owned US companies seek to evade their taxes."

Treasury Secretary Jack Lew also highlighted the new proposed measures in a letter to the US Congress, urging it to act. "The Treasury Department has long focused on countering money laundering and corruption, cracking down on tax evasion, and hindering those looking to circumvent our sanctions," he said. "The actions we are finalising today mark a significant step forward to increase transparency and to prevent abusive conduct within the financial system."

Noting that the full Senate has not approved any income tax treaty or protocol since 2010, Lew also called for the Senate to approve eight pending tax treaties. Finally, he told Congress that it should enact proposed legislation to give the US full reciprocity on foreign tax reporting.

SOVEREIGN COMMENT

These rules are becoming the norm, which is why Sovereign asks for full disclosure of ultimate beneficial ownership for all new business – and why we also continue to monitor and request updated information from our existing clients. Oddly, given the rules it has imposed on foreign financial institutions under the Foreign Account Tax Compliance Act (FATCA), the US has lagged behind in respect of its domestic standards of transparency. It is now catching up. The OECD Common Reporting Standard, as discussed in previous editions, is now a reality and customers seeking to do business internationally must be prepared to provide full details at the outset of any new relationship with service providers, professional advisers and banks.

Cayman to repeal Confidential Relationships (Preservation) Law

The Cayman Islands' Government published, on 11 May 2016, a Bill to repeal the Confidential Relationships (Preservation) Law. Although it was originally enacted in the 1970s, no one has ever been prosecuted under the legislation which criminalises the disclosure of confidential information except: when it is disclosable in the ordinary course of business; when requested by certain enforcement or regulatory authorities or by a court order; or with the consent of the person to whom it belongs.

It will be replaced by the Confidential Information Disclosure Bill 2016, which continues to recognise when it is lawful to disclose otherwise confidential information whilst removing criminal sanctions for disclosure. It includes the ability to seek court directions, if required, to disclose confidential information in proceedings where otherwise unable to rely on an exception.

The Cayman Islands will further introduce a new Data Protection Law, which will regulate the processing of data and further underpin the principles arising from the duties of confidentiality and the right to privacy.

The Companies (Amendment) Law 2016 was brought into force on 13 May. It removes the power of Cayman Islands exempted companies to issue bearer shares and other forms

of negotiable shares. It provided that existing bearer shares had to be converted into registered shares before 13 July 2016 or they will be void.

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The Cayman Islands is adjusting to new international standards but Premier Alden McLaughlin said, on 17 May, that the islands would not adopt a mechanism for the exchange of beneficial ownership information until the US agreed to do so. He called for a level playing field in terms of financial transparency and stated that a standard without US participation would not be "a global standard". He emphasised that Cayman has not agreed to a specific method for exchanging any information but had agreed to participate in a global discussion to develop such a mechanism. His comments followed the Anti-Corruption Summit in London on 12 May attended by 40 countries. The US, represented by Secretary of State John Kerry, advised that it was not in a position to even sign the summit communiqué, which outlined the steps needed to combat corruption as agreed by attendees.

Julius Baer signs deferred prosecution agreement with the US

Swiss bank Julius Baer was charged on 4 February 2016 with conspiring with many of its US taxpayer-clients and others to help US taxpayers hide billions of dollars in offshore accounts from the IRS and to evade US taxes on the income earned in those accounts. The US Department of Justice (DoJ) announced simultaneously that it had agreed a deferred prosecution agreement.

The agreement, under which the bank admitted that it had knowingly assisted many of its US taxpayer-clients in evading their tax obligations under US law, required Julius Baer to pay a total of $547 million. If the bank abides by all of the terms of the agreement, the DoJ will defer prosecution on the Information for three years and then seek to dismiss the charges.

The statement of facts to the agreement said that from at least the 1990s through to 2009, Julius Baer helped many of its US taxpayer-clients evade their US tax obligations by opening and maintaining undeclared accounts for US taxpayers and by allowing third-party asset managers to open undeclared accounts for US taxpayers.

At various times client advisers at Julius Baer advised US taxpayer-clients that their accounts at Julius Baer would not be disclosed to the IRS because Julius Baer had a long tradition of bank secrecy and no longer had offices in the US, making it less vulnerable to pressure from US law enforcement authorities.

The DoJ said that by at least 2008, Julius Baer began to implement institutional policy changes to cease providing assistance to US taxpayers in violating their US legal obligations. In November 2008, the bank began an "exit" plan for US client accounts that lacked evidence of US tax compliance and imposed a prohibition on opening accounts for any non-compliant US clients.

In November 2009, before Julius Baer became aware of any US investigation into its conduct, it had decided to self-report to the DoJ and notified its regulator, the Swiss Financial Market Supervisory Authority (FINMA), of its intention to do so. FINMA requested that it did not contact US law enforcement authorities in order that it would not prejudice the Swiss government in any bilateral negotiations with the US on tax-related matters.

Since engaging with US authorities, the DoJ said Julius Baer had taken exemplary actions to demonstrate acceptance and acknowledgement of responsibility for its conduct, which included advocating in favour of a decision provided by the Swiss Federal Council in April 2012 to allow banks under investigation by the DoJ to produce employee and third-party information. It also encouraged certain employees to accept responsibility for their participation in the conduct at issue and cooperate with the ongoing investigation.

Julius Baer chief executive Boris Collardi said the agreement was an important milestone for the bank and "ends a long period of uncertainty for us".

Canada to tax Florida and Delaware LLPs and LLLPs as corporations

Canada Revenue Agency (CRA) announced, on 26 May 2016, that limited liability partnerships (LLPs) and limited liability limited partnerships (LLLPs) governed by the laws of Florida and Delaware were to be treated as corporations for Canadian income tax purposes.

In the CRA's view, the separate legal personality and the extensive limited liability of Florida and Delaware LLPs and LLLPs were of "overwhelming significance" in determining that such entities should be treated as corporations for Canadian income tax purposes.

The CRA also stated that, absent any tax avoidance, such entities could be converted into some other recognised form of partnership by 2018 without triggering any adverse Canadian tax implications provided that:

- The entity was formed and carried on business prior to July 2016;
- The members formed the entity in order to carry on business as a partnership;
- The members intended the entity to be treated as a partnership, from its formation, for Canadian tax purposes; and
- Neither the entity nor any of its members have taken the position that the entity is not a partnership.

US court dismisses FATCA challenges

The US District Court for the Southern District of Ohio dismissed, on 26 April 2016, a challenge by US Senator Rand Paul and several other plaintiffs seeking declaratory and injunctive relief against enforcement of the US Foreign Account Tax Compliance Act (FATCA). The court held the plaintiffs lacked standing to sue.

Under FATCA, which went into full effect last year, US taxpayers must self-report more than $50,000 in foreign assets and foreign financial institutions (FFIs) must disclose information on US taxpayer accounts to the IRS through intergovernmental agreements (IGAs). The plaintiffs filed suit against the Treasury Department, the US Internal Revenue Service (IRS), and Financial Crimes Enforcement Network (FinCEN). They brought eight claims before the court.

The court held that all the plaintiffs lacked standing because they had failed to establish the concrete, particular harm that was a prerequisite to standing. As a result, the court granted the defendants' motion to dismiss the case.

MIDDLE EAST & ASIA

India to tax Mauritius and Cyprus investments from April 2017

A protocol to amend the provisions of the 1983 India-Mauritius double tax treaty was signed by both countries at Port Louis, Mauritius, on 10 May 2016. The Indian government had been trying to renegotiate the treaty since 1996 to combat issues of treaty abuse and round-tripping of funds.

Under the current treaty, capital gains arising from the disposal of shares in an Indian company are taxable only in the country of residence of the selling shareholder (and not in India). Accordingly a company resident in Mauritius that does not have a permanent establishment in India and which disposes of its shares in an Indian company is liable to CGT only in Mauritius. As Mauritius does not levy CGT, no tax is levied either in India or in Mauritius.

The full version of the protocol has not yet been published, but key changes include amendments to the taxing rights on capital gains and limitation of benefits. Article 13 of the current treaty will be amended such that, from 1 April 2017, capital gains arising from disposal of shares of a company resident in India will be taxable in India.

The protocol contains a "grandfathering" provision such that investments acquired before 1 April 2017 will be unaffected by the protocol and will remain taxable in Mauritius. There will also be a transition period, from 1 April 2017 to 31 March 2019, during which any capital gain generated on the sales of investments acquired after 1 April 2017, will be taxed in India at a reduced rate of 50% of the domestic tax rate (currently 15% for listed equities and 40% for unlisted ones) provided it fulfils the conditions of the Limitation of Benefits (LOB) article. The full domestic Indian tax rate will apply from 1 April 2019.

Under the LOB article, a Mauritian resident will benefit from the reduced CGT rate provided that it satisfies the main purpose and bona fide business test, and is not a shell or conduit company. A Mauritian company will be deemed to have substance provided it meets an annual expenditure threshold of Mauritian Rs 1.5 million (approx. US$43,000) in Mauritius in the period of 12 months immediately preceding the date on which the gains arise.

Other changes include an amendment to Article 26 of the current treaty on exchange of information to bring it into line with international standards. The Protocol also introduces provisions for assistance in collection of taxes and source-based taxation of other income.

The current treaty was a major reason for a large number of foreign portfolio investors and foreign entities to route their investments in India through Mauritius. Between April 2000 and December 2015, Mauritius accounted for US$93.66 billion — or 33.7% — of the total foreign direct investment of US$278 billion. However, due to the uncertainty concerning the Mauritius treaty over the last few years, Singapore has emerged as the preferred destination. Cyprus and the Netherlands also enjoy treaties that offer a capital gains tax exemption to investors.

It is expected that the amended tax regime for Mauritius will also be applicable to capital gains for Singapore tax residents. Article 6 of the protocol dated 18 July 2005 to the Singapore tax treaty sets out that the CGT exemption under the Singapore treaty will remain in force only while the CGT exemption under the Mauritius treaty remains in force

The Cyprus Ministry of Finance also announced, on 29 June 2016, that it had completed negotiations for a new tax treaty with India that allows for source-based taxation of capital gains from the alienation of shares. Under the deal, Cyprus will be removed from India's blacklist of "notified jurisdictional areas".

As with the Mauritius protocol, India and Cyprus have agreed to generous grandfathering provisions. For investments undertaken prior to 1 April 2017, the right to tax the disposal of such shares at any future date remains with the contracting state of residence of the vendor.

SOVEREIGN COMMENT

The India-Mauritius treaty is arguably one of the best-known treaties in force today. The proposed changes are wide ranging and it is vitally important that affected businesses take advice as soon as possible in order to ensure compliance and to mitigate any negative consequences. Regular readers will know of the growing importance of our Mauritius office headed by Bernadette Fulton. Several Sovereign staff are also regular visitors to India, so we are well placed to advise on these matters. We are also delighted that Cyprus is no longer a notified jurisdiction. Under Indian law, the designation resulted in enhanced reporting requirements and reduced tax deductions for transactions with Cyprus, as well as increased Indian withholding taxes on Cypriot residents.

New Hong Kong tax concessions for corporate treasury centres

The Inland Revenue (Amendment) (No.2) Ordinance 2016, which introduces a concessionary profits tax rate of 8.25% – 50% of the current corporate tax rate – for qualifying corporate treasury centres (CTCs) and more generous rules for interest deductibility of intragroup financing, was gazetted on 3 June 2016.

Passed by the Legislative Council on 26 May, the new law also modifies the profits tax and stamp duty treatment in respect of regulatory capital securities issued by banks to comply with the Basel III capital adequacy requirement.

Secretary for Financial Services and the Treasury, Professor K C Chan, said the new CTC scheme, which applies as of 1 April, would provide "a conducive environment for attracting multinational and Mainland corporations to centralise their treasury functions in Hong Kong, thereby enhancing the competitiveness of our financial markets and contributing to the development of a headquarters economy."

The changes to the rules on intragroup financing, also effective as of 1 April, remove current restrictions that limit interest deductions to cases where the interest income of the lender is chargeable to Hong Kong profits tax. The government said it would be issuing further guidance on the operation of the new rules and on anti-avoidance provisions.

SOVEREIGN COMMENT

The Ordinance reflects Hong Kong's increasing use of tax incentives to encourage the development of strategic sectors and to improve its position in respect of regional competitors, particularly Singapore. Between 2005 and 2015, the number of headquarters of global companies in Singapore increased from 3,600 to 12,600, according to Monetary Authority of Singapore and industry survey figures.
The incentive regime for CTCs is designed to complement Hong Kong's geographic and cultural advantages as the traditional gateway to China and to capitalise on its broad pool of financial and entrepreneurial talent and expanding network of double taxation agreements. To date, 33 such agreements have been signed.

South Africa revises Special Voluntary Disclosure Programme

The Treasury released, on 19 July 2016, revisions in respect of the Special Voluntary Disclosure Programme (SVDP) that was announced in the Budget on 24 February. Designed to enable individuals and companies to regularise both their tax and exchange control affairs ahead of the introduction of the new global standard for the automatic exchange of information, the SVDP will operate for a limited period of six months from 1 October 2016 to 31 March 2017.

The SVDP will be open to individuals and companies provided that no audit or investigation in respect of foreign assets or foreign taxes is underway or pending. Amounts in respect of which SARS has obtained information under the terms of any international exchange of information procedure will also be ineligible.

Taxpayers who disposed of any foreign-held assets prior to 1 March 2010 may also apply for relief under the SVDP. Special deeming provisions will apply. Trusts will not qualify but settlors, donors, deceased estates and beneficiaries of foreign discretionary trusts may participate if they elect to have the trust's offshore assets and income deemed to be held by them.

To simplify the SVDP, the amendments now include the calculation of only one amount to be included in taxable income and subject to tax in South Africa. This will equate to 50% of the highest value of the aggregate of all assets held by a taxpayer outside South Africa between 1 March 2010 and 28 February 2015.

The undeclared income that originally gave rise to those assets will be exempt from income tax, donations tax and estate duty liabilities that should have arisen in the past. However, future income will be fully taxed, and declared assets will remain liable for donations tax and estate duty in the future, should the applicant donate these assets or die while holding them.
The SDVP will also apply to exchange control contraventions that occurred before 29 February 2016 provided they are not currently under investigation by the Financial Surveillance Department (FinSurv).

A levy of 5% on assets repatriated to South Africa will be payable by successful applications; 10% if the applicant chooses to keep the assets offshore. A levy of 12% will be payable on foreign assets where the 10% levy is not paid from foreign-sourced funds. Individuals will not be allowed to deduct their R10 million foreign capital allowance (or any remaining portion) from any leviable amount.

SOVEREIGN COMMENT

The tax and exchange control processes will run simultaneously, although separately. Any readers concerned about these issues should contact either of our South Africa offices – in Cape Town or Johannesburg – for assistance and advice on the best way to proceed.

China's Unified Business Certificate

The introduction of the new "Unified Business Certificate" is a very welcome step in China's attempts to lessen the administrative burdens on companies. The reform took effect on 1 September 2015 in Guangzhou and 29 September 2015 in Beijing. It was then rolled out nationwide as of 1 October 2015.

Under this reform, the old business licence, organisation code certificate and tax registration certificate have been combined into one certificate – the new "Unified Business Licence" – which can be obtained from the local Administration of Industry and Commerce (AIC). This is a significant improvement. Previously, companies were obliged to apply for a business licence from the AIC, a tax registration certificate from the tax authorities, and an organisation code certificate from the technical supervision authority.

Any new entities established after 1 October 2015 are required to apply only for the new "3 in 1" or "Unified Business Licence". Companies existing prior to October 2015 have been granted a transition period during which to update their licence according to the new requirements. Shanghai and Beijing have set 31 December 2017 and 31 December 2020 as their respective deadlines for transition; the old licences will become invalid from these dates. We await further notifications on transition periods from the relevant AICs in other localities.

SOVEREIGN COMMENT

To apply for the new licence, companies must surrender their old licences and submit the application documents for a "Unified Business Certificate" at the relevant AIC; there is no fee for this. It should be noted that regional differences in terms of implementation of the reform might exist, so it is best to seek professional guidance regarding your particular situation. Sovereign has been assisting foreign companies with their operations in China for a number of years and can help you to navigate these new rules and procedures.

LEGAL NEWS

UBS agrees to US tax authority's Singapore disclosure request

The US Justice Department announced, on 22 June 2016, that it had voluntarily dismissed its summons enforcement action against UBS because the Swiss bank had fully complied with an Internal Revenue Service (IRS) summons for bank records held in its Singapore office.

The IRS served an administrative summons on UBS for records pertaining to accounts held by Ching-Ye "Henry" Hsiaw. According to the petition, the IRS needed the records in order to determine Hsiaw's federal income tax liabilities for the years 2006 through 2011. Hsiaw transferred funds from a Switzerland-based account with UBS to the UBS Singapore branch in 2002, according to the declaration of a revenue agent.

UBS resisted the summons when it was first issued in February this year, leading the US authorities to seek a court order to enforce it. However, after some negotiation, UBS agreed to comply without the need for court enforcement. It delivered up the relevant documents in two batches, on 31 May and 10 June.

UBS indicated that it handed over the data only with the permission of both the client and Singaporean authorities. "UBS confirms that it complied with the summons based on client consent in accordance with Singapore law," the bank said in a statement.

SOVEREIGN COMMENT

The US has gathered a huge trove of data from more than 80 Swiss banks and 50,000 US taxpayers who have disclosed their accounts to avoid prosecution. Acting Assistant Attorney General Caroline Ciraolo said recently: "No jurisdiction is off limits. Our investigations of both individuals and entities are well beyond Switzerland at this point."

Swiss bank in serious breach of money laundering regulations

The Swiss Financial Market Supervisory Authority (FINMA) found, on 24 May 2016, that Swiss bank BSI was in serious breach of the requirements for proper business conduct in respect of the Malaysian sovereign wealth fund 1MDB. It found serious breaches of the statutory due diligence requirements in relation to money laundering and serious violations of the principles of adequate risk management and appropriate organisation.

FINMA launched enforcement proceedings against BSI in 2015 after indications that the bank had breached money-laundering regulations. In the period from 2011 to April 2015, it found serious shortcomings in identifying transactions involving increased risk. These failures related in particular to business relationships with politically exposed persons (PEPs), the origin of whose assets was not sufficiently clarified, and whose dubious transactions involving hundreds of millions of US dollars were not satisfactorily scrutinised.

BSI was penalised by FINMA last year for misconduct in the Petrobras scandal concerning corruption at the Brazilian state oil company. FINMA announced its approval of the takeover of BSI by EFG International with the condition that BSI is integrated and then dissolved. It also ordered the disgorgement of profits amounting to CHF95 million and launched enforcement proceedings against two of the bank's former top managers.

The Monetary Authority of Singapore (MAS) further announced that it had served the bank a "notice of intention to withdraw its status as a merchant bank in Singapore". The two authorities cooperated intensively.

SOVEREIGN COMMENT

This case demonstrates all too clearly the necessity to follow compliance procedures from the outset – and indeed during the lifetime of any business relationship. As is made clear from this story, failure to do so can result in catastrophic consequences for the financial institution concerned, and of course its clients.

Spanish and French tax authorities raid Google's offices

Spanish tax inspectors raided the Madrid offices of US multinational Google on 30 June 2016 looking for "possible evidence of taxation in Spain that is less than what is appropriate given [Google's] real activity in the country". The previous month French tax inspectors searched the firm's offices in Paris, saying the company was under investigation for aggravated financial fraud and organised money laundering.

Google says it complies with the tax laws in every country in which it operates. It contends that its offices in Paris, Madrid and other European capitals are not permanent establishments, but operate as satellites of its international headquarters in Dublin, providing back-office services such as marketing. It routes most of its non-US revenue from activities such as advertising through Ireland, where the corporation tax rate is 12.5%, allowing it to avoid both European and US taxes on the income.

Former model secures £75 million divorce settlement in UK Court

The UK High Court awarded, on 8 July 2016, former model Christina Estrada a lump sum of £53.33 million to meet her future needs "as she moves into an independent life outside her marriage". The total settlement, which includes assets worth a further £22 million, still represents less than half of the £196.5 million that she had sought.

Estrada had rejected a total offer from Walid Juffali, chairman of one of Saudi Arabia's biggest conglomerates, worth £37 million. The case was brought under a section of the Matrimonial and Family Proceedings Act 1984, which enabled Estrada to apply for financial relief in England because she could not bring a

case in Saudi Arabia after Juffali divorced her by talaq under Sharia law in 2013.

Juffali had gone to what Estrada's lawyers called "extraordinary lengths" to avoid the case, even securing legal immunity in the UK by becoming a diplomat representing the Caribbean island of St Lucia. Last year he appeared on the London Diplomatic List as St Lucia's "Permanent Representative" to the International Maritime Organisation (IMO). In February, the High Court ruled that Juffali had acquired a "spurious" diplomatic status with the "sole intention" of thwarting Estrada's financial claim.

When Mrs Justice Roberts handed down her judgment, counsel for Juffali asked the judge to allow his client, who was terminally ill, until the end of this year to pay. She gave him three weeks. Juffali died on 20 July.

High Court dismisses claim over division of Liechtenstein assets

The UK High Court dismissed, on 13 May 2016, a claim brought by a brother against his sister for a half share of the assets placed in a Liechtenstein foundation by their father. The central issue was whether the assets formed part of their father's UK estate, or whether the foundation was void as a result of alleged tax evasion.

In *Hamilton v Hamilton & Anor* [2016] EWHC 1132 (Ch), David Hamilton was a non-domiciled UK resident who set up the Rainbow Foundation in Liechtenstein in the 1990s. During his lifetime, he was entitled to the assets and income; upon his death the foundation's assets were to be split between his children, Alan and Carolyn. He arranged for Carolyn to receive more, but did not disclose this to Alan. This was in contrast to his UK estate, which passed under his will and was split equally between the siblings.

On David's death, each sibling received a sealed envelope detailing their personal entitlements to assets in the foundation, which was administered by the Swiss bank UBS so that the assets could be passed on without notifying HMRC of their existence. Alan withdrew around £1.05 million and Carolyn around £2.2 million. Carolyn, who was UK resident, did not disclose the amount she received to her brother and did not declare the assets to HM Revenue & Customs.

Carolyn later made a disclosure under the UK's Liechtenstein Disclosure Facility (LDF). As her father's executor, she also had to declare income tax that should have been paid on UK-source income from investments held in the foundation in the last few years of her father's life. Her legal advisor contacted her brother to propose that his inherited assets should also be disclosed under the LDF. It was at this time that Alan, a US-based tax accountant, learned that he had inherited less from the foundation than his sister.

He sued his sister, claiming that the foundation's assets formed part of their late father's estate and passed to them equally under his will. He alleged that the Rainbow arrangement was either a "bare nomineeship for [his father] David, or a sham apparently designed to deceive the UK tax authorities and possibly others into believing that David had transferred his legal and beneficial interest in assets to the foundation".

The High Court dismissed the action, holding that Rainbow Foundation was valid under Liechtenstein law, because its founder had the necessary intent to establish it as an independent entity. David Hamilton had not retained beneficial ownership of the assets, either because Rainbow held them as his bare nominee or pursuant to a resulting trust.

The court also rejected Alan Hamilton's claim that Rainbow was a sham. "In the light of my findings of fact, it is impossible to contend that David and Rainbow shared a common intention to create legal rights and obligations different from those which they ostensibly created," said Henderson J. Alan Hamilton was refused permission to appeal the decision and was further ordered to pay his sister's legal costs.

SOVEREIGN COMMENT

The end result of this legal action was that the court followed David Hamilton's wishes. Once again however, the case clearly demonstrates the difficulties that may be encountered when dealing with estates where the treatment of beneficiaries differs, for whatever reason. In order to avoid future litigation, the noting of concise instructions reflecting a client's wishes – followed by accurate drafting – should always be paramount from the outset.

Guernsey court refuses to set aside "mistake" over £500,000 tax charge

26 February 2016, Guernsey's Royal Court declined an application that sought to invoke the equitable jurisdiction of the court to set aside the distribution of funds on the grounds of a mistake.

In the matter of *Abacus Global Approved Managed Pension Trust - Emanuel Gresh v RBC Trust Company (Guernsey) Limited and The Commissioners for Her Majesty's Revenue and Customs* (7/2016), trust beneficiary Emanuel Gresh obtained professional tax advice that a distribution to him from his RBC Guernsey pension fund would be tax-free provided that the distribution was not remitted to the UK. Gresh requested a withdrawal of £1.4 million from the fund. It later transpired that the advice was incorrect and the distribution was subject to a 40% income tax liability in the UK.

The case was originally brought by Gresh under the rule in *Hastings Bass*. HMRC's attempt to intervene for the first time ever in a *Hastings Bass* case was rejected by the Royal Court in May 2009, but allowed on appeal in September 2009. The case was then effectively stayed whilst *Futter v Futter* and *Pitt v Holt* progressed to the Supreme Court in England. Following the outcome of those cases Gresh recast his application as one based on equitable mistake.

It was agreed that under the law of Guernsey, there is jurisdiction to set aside a voluntary transaction as a result of a mistake and that the principles established by the English Supreme Court in *Pitt v Holt*, although not binding, would be highly persuasive in Guernsey. It was further agreed that a voluntary disposition made as a result of a mistake was not void, but might be set aside by the Court in the exercise of its discretion.

The Pitt and Futter rulings restricted the scope of Hastings Bass to cases where allowing the trustee's mistake to stand would be "unconscionable" – that is clearly unjust or unfair. The Court therefore considered the injustice or unfairness of setting aside, or not setting aside, the disposition.

The Court found that Gresh was the only person to be affected by the mistake, in that he alone would have a tax liability if the mistake were not corrected. In other cases where relief of this nature had been granted by the courts there had been multiple beneficiaries whose interests were also affected. It held that, although the impact on Gresh was undoubtedly severe, it was not "unconscionable" that he should have to retain the proceeds of the distribution made by the trustee to him. It would therefore not be an appropriate exercise of the Court's jurisdiction to set aside the distribution.

FISCAL NEWS

Singapore and Hong Kong sign up to OECD BEPS project

The governments of Singapore and Hong Kong announced their decision, on 16 and 20 June 2016 respectively, to participate in the OECD/G20 Base Erosion and Profit Shifting (BEPS) Project. Both join BEPS as associates having committed to the comprehensive BEPS Package, including its four minimum standards on harmful tax practices, tax treaty abuse, country-by-country reporting and improvements in cross-border tax dispute resolution.

In February, the OECD agreed a new framework to broaden participation in the BEPS Project. A new BEPS Implementation Forum will provide for all interested countries and jurisdictions to participate as BEPS associates on an equal footing with the OECD and G20 members on the remaining standard setting under the BEPS Project, as well as the review and monitoring of the implementation of the BEPS package.

Representatives of more than 80 countries and jurisdictions met in Kyoto, Japan, on 30 June for the inaugural meeting of the new Forum, which operates on an equal footing with the OECD's Committee on Fiscal Affairs. The OECD said the other 21 countries and jurisdictions that attended were likely to join in the coming months.

"Today we launch a new era in international tax," said Pascal Saint-Amans, director of the OECD Centre for Tax Policy and Administration. "Through their participation in the decision-making as well as the technical working groups of the OECD's Committee on Fiscal Affairs, the members of the inclusive framework will now have a direct influence in shaping international tax rules to tackle BEPS and ensuring a level playing field."

SOVEREIGN COMMENT

As two of the world's premier international finance jurisdictions, these announcements are critical to the OECD's BEPS project as its future credibility relies on the widest possible implementation across the world. Hong Kong and Singapore's participation should benefit the project hugely and we shall report in future editions on further announcements by other countries in the coming months.

European Council agrees draft rules on corporate tax avoidance

The European Council approved, on 21 June 2016, a draft directive addressing tax avoidance practices commonly used by large companies. The directive is part of a January 2016 package of Commission proposals to combat corporate tax avoidance and builds on the OECD's recommendations on base erosion and profit shifting (BEPS).

The directive addresses situations where corporate groups take advantage of disparities between national tax systems in order to reduce their overall tax liability. Corporate taxpayers may benefit from low tax rates or double tax deductions. Or they can ensure that categories of income remain untaxed by making it deductible in one jurisdiction whilst in the other it is not included in the tax base.

The draft directive covers all taxpayers that are subject to corporate tax in a member state, including subsidiaries of companies based in third countries. It lays down anti-tax-avoidance rules in five specific fields: interest limitation; exit taxation; the General Anti-Abuse Rule (GAAR); controlled foreign company (CFC); and hybrid mismatches.

The directive will ensure that the OECD anti-BEPS measures are implemented in a coordinated manner in the EU, including the seven member states that are not OECD members. Furthermore, pending a revised proposal from the Commission for a common consolidated corporate tax base (CCCTB), it takes account of discussions since 2011 on an existing CCCTB proposal within the Council.

Member states have until 31 December 2018 to transpose the directive into their national laws and regulations, except for the exit taxation rules, which are due by 31 December 2019. Member states that have targeted rules that are equally effective to the interest limitation rules may apply them until the OECD reaches agreement on a minimum standard or until 1 January 2024 at the latest.

EU Tax Commissioner Pierre Moscovici said: "For too long, some companies have been able to take advantage of the mismatches between different Member States tax systems to avoid billions of euros in tax. I congratulate our member states who are now fighting back and working together to make the changes needed to ensure that these companies pay their fair share of tax."

UAE signs tax treaty with UK and protocol with Singapore

The UAE and UK governments signed a double tax treaty at the Ministry of Finance in Dubai on 12 April 2016. The agreement aims to enhance the economic and trade relations between the two countries, and protect companies and individuals from direct or indirect double taxation.

Commercial Secretary to the UK Treasury Lord O'Neill said: "This will fill an important gap in the framework for commercial cooperation between the UK and UAE. It will remove one area of possible uncertainty for the thousands of UK businesses operating in the UAE, and for the 100,000+ British nationals living and working in the UAE."

The UAE signed an agreement on the promotion and protection of investments with the UK, under a Federal Decree No. 26 in 1999. Both countries are also linked through the Joint Economic Committee, which held its fourth session in February 2013. UAE companies have invested in a number of key sectors in UK.

A Second Protocol amending the tax treaty between Singapore and the UAE entered into force on 16 March. The revised terms include increasing the threshold periods for a permanent establishment from nine months to 12 months and lower withholding tax rates on dividends and interest.

Withholding tax on dividends is reduced to 0% from the current 5% if the recipient is the beneficial owner of the dividends. Currently, no withholding tax is levied on dividends paid by companies resident in Singapore, so the 5% withholding tax rate on dividends under the treaty would not apply in Singapore.

Withholding tax on interest is also reduced to 0% from the current 7% if the recipient is the beneficial owner of the interest. Previously a zero withholding tax only applied to interest received by the government of the other contracting state. The Protocol further removes payments for "the use of, or the right to use, industrial, commercial or scientific equipment" from the definition of royalties.

SOVEREIGN COMMENT

These are very important developments and are to be welcomed. Sovereign's London-based team is well placed to provide advice on the wide range of corporate services available, including market entry, for British companies seeking to expand or establish new operations in UAE and Asia including Singapore together with inward investment opportunities. Interested readers should contact the London office for an initial, no obligation, discussion.

Five more nations agree to automatic exchange of information

The OECD Global Forum on Transparency and Exchange of Information for Tax Purposes announced, on 11 May 2016, that Bahrain, Lebanon, Nauru, Panama and Vanuatu had committed to share financial account information automatically with other countries under the Common Reporting Standard. They are expected to begin exchanging information in September 2018.

"These political commitments to join the fight against tax evasion must be turned into practical reality, through implementation of the standards and actual exchange of information," said OECD Secretary-General Angel Gurría. "I urge those countries that have not yet done so to sign the Multilateral Convention on Mutual Administrative Assistance in Tax Matters and the Multilateral Competent Authority Agreement we have developed to enable as many countries as possible to benefit from this new more transparent environment."

A total of 101 jurisdictions worldwide have now committed to implement information sharing developed by the OECD and G20 countries. The Global Forum is monitoring the implementation of tax transparency standards to ensure the effective and timely delivery of the commitments made, the confidentiality of information exchanged and to identify areas where support is needed. Lebanon has just joined the Global Forum, bringing membership to 133 jurisdictions.

G5 agree to automatic exchange of beneficial ownership information

The G5 countries of UK, Germany, France, Italy and Spain announced, on 14 April 2016, a pilot scheme to exchange information on company beneficial ownership registers and planned new registers of trusts on an automatic basis.

According to a letter to their G20 counterparts, the G5 finance ministers said beneficial ownership information relating to "companies, trusts, foundations, shell companies and other relevant entities and arrangements" will be exchanged "in a fully searchable format" and will include "information on entities and arrangements closed during the relevant year".

The exchange will initially operate as a pilot, during which participating economies will explore the best way to exchange this information with a view to developing a "truly global common standard". Ultimately, the system should develop into one of "interlinked registries containing full beneficial ownership information," according to the letter.

UK companies and limited partnerships have been obliged, since 6 April, to keep a register of "people with significant control" (PSCs) – individuals who hold more than 25% of a company's shares or voting rights, have the right to appoint a majority of directors or have the right to exercise, or actually exercise, significant influence or control over the company.

Other major economies have committed to introducing similar registers that will be accessible to "competent authorities" and other limited categories of people with a legitimate interest in accessing the information.

The British Crown Dependencies and Overseas Territories (CDOT) have also agreed to deliver information on company beneficial ownership to the UK authorities electronically within 24 hours, or within one hour in "urgent" cases. After months of negotiation, CDOT leaders have all now signed an exchange of letters with the UK government confirming their commitment although none has agreed to make the registry publicly available as the UK government originally requested.

China completes transition to VAT

China completed the transition to a new nationwide value-added tax (VAT) regime on 1 May 2016. It replaces the previous Business Tax (BT), which was charged at every stage of the supply chain on the gross amount rather than the net value added. The move to VAT will help to eliminate double tax issues and remove distortions to supply chains. It represents one of the biggest reforms to China's tax system in more than two decades.

First introduced as a pilot scheme in Shanghai in 2012, the programme has been expanded to several other municipalities and provinces and applied to various sectors, including railways, postal services, telecommunications and certain service industries. VAT has now been fully implemented nationwide and extended to the construction, real estate, financial and consumer services sectors.

Premier Li Keqiang is adamant that taxpayers should not face additional burdens under the new system. Although the headline VAT tax rates are higher than the BT rates – construction services, for example, will be subject to an 11% tax rate under the VAT system, compared to the previous BT rate of 3% – the VAT tax rate is only applied to the value added component rather than the gross amount.

SOVEREIGN COMMENT

For companies across all business sectors, key considerations of the switch to VAT will be how to claim input VAT credit effectively and pass on output VAT to customers, as well as maintaining the continuity of existing tax reductions and exemptions that applied under the BT system. In addition, a key challenge faced by business operators will be to upgrade their accounting and IT systems to accommodate the change. Sovereign China and our licensed accountants and tax professionals can assist you to understand the changes and ensure that your business is ready for this new era in China's tax system.

IN THE PRESS

CHINA INSIGHTS

A version of this article by Michael Diliberto first appeared in the June issue of Sovereign's *China Focus* newsletter. Diliberto has spent more than ten years travelling to or living in China, most recently as the Founder and General Manager of Jiaxing Lynx Displays Ltd., a part of New Zealand-based Lynx Innovation, a global provider of brand marketing and retail merchandising solutions. These days Diliberto divides his time between supporting manufacturing on the ground in China and servicing clients in Asia, North America and Europe.

Why is achieving product quality in China so difficult?

"Why are Chinese products of such low quality?" people say. "If Apple can make the iPhone in China, why do we still struggle?" As a sourcing professional in China, I can safely say that if I had a nickel for every western manager that pulled out an iPhone during a discussion about product design or quality control in China, I could have retired a few years back.

This oft-made comparison is inappropriate because the iPhone is not made in China. The iPhone is *assembled* in China. I could just as easily ship all the parts, assembly and testing jigs and production instructions to Vietnam, Italy, Mexico, or even the US, and I could churn out identical iPhones to ones that are assembled here in China.

The important distinction is that, while the iPhone is made from parts manufactured all over the world, it is designed by a top team of engineers at Apple's headquarters. Those engineers designed not just the iPhone, but also the methods of manufacture. They created tight tolerances between parts and sourced suppliers that could build to that tolerance level; in some cases, those suppliers are in South Korea or the US.

That same engineering team made test jigs for the iPhone such that at each assembly station on the production line, a worker can simply insert their sub-assembly into a jig and get a simple green light (send phone to the next station) or red light (remove phone and send to the re-work line).

In other words, that engineering team did not just design and engineer the iPhone; it also designed and engineered the entire production process. The processes of *designing for manufacture* and *process engineering* are not nearly as simple or easy as they sound when I describe them in ten sentences.

The next question I inevitably get asked is, what it takes to "build our products like Apple builds the iPhone?" OK, no problem – but first let's look at some numbers.

According to Apple's earnings report, it spent just over a billion dollars in R&D costs. The iPhone makes up about half of Apple's revenue; so it would be reasonable to guess that they allocated US$500 million of R&D spend towards the development of the iPhone 5S (and 5C). Even if we could further divide the cost (we probably cannot, but let's suspend disbelief) between the two phone models, that is still allocating US$250 million towards the research and development of a single phone. If you divide the costs again between product development and manufacturing, then Apple may have spent US$125 million just to design the best way to make a phone (and that is, I believe, a conservative figure).

Ok, now that we have the iPhone question out of the way, let's get to the meat of this question, which is: "*Why are Chinese products of such low quality?*" This can be stated simply but is in fact a massive question. Most firms spend way too much time thinking about WHAT they are making and not nearly enough time thinking about HOW they will make it.

A little background on Chinese manufacturing (in general)

Let's assume for a minute that you are asking why Chinese firms turn out poor quality products. Not all factories do. Some factories, especially those that have exported products on their own account or worked as contract manufacturers for western firms, will consistently and without excessive guidance turn out high quality product. There is an equal number of factories, however, that will turn out anything you ask them to produce, defaulting to minimum cost and minimum quality unless otherwise specified. There are a number of factors here that are worth exploring.

First, and foremost, Chinese domestic market consumers generally (it's changing, but holds for now) are not looking for quality. They either go for the best product or the cheapest product. So if you are not making the best, then you are racing to the bottom to make the cheapest. Chinese manufacturers are not rewarded for making incrementally better products.

Since production costs are very cheap and few people typically complain about cheap products, those customers that do complain are generally just given new product by the supplier. China is one of the few places where consumers will tolerate a supplier having to replace a defective product several times and, in the eyes of many suppliers, this is not an issue.

Lastly, with historically lax enforcement of product safety requirements, many Chinese domestic suppliers have become accustomed to cutting corners where possible. Plastic too expensive? Chuck some regrind material back into the hopper. Solder too hard to work with? Use one with lead in it, because it will flow better. Price of copper rising? Get thinner printed circuit boards. You get the idea.

Chinese products that are imported into another country

Here is an example. Meet Joe Bloggs, American Entrepreneur. Joe is attending a consumer electronics show armed with his idea for an awesome mp3-o-tron. Knowing that he needs to get his product made in China because his start-up is lean on cash, Joe heads straight over to the Asia pavilion and meets with some of the more polished Chinese suppliers – probably from the Pearl River Delta region. They show him some examples of other products they have made and Joe chooses a supplier that he believes can deliver his mp3-o-tron. Its prices are also much more reasonable than some of the other vendors he has met at the show.

After reviewing Joe's engineering drawings and documentation, the supplier explains that it would be much cheaper to modify their existing cassette-tape-o-tron into his mp3-o-tron. The supplier explains that they have produced millions of cassette-tape-o-trons and have ironed out any manufacturing issues, so this is the safest route to take. Since Joe has not had any design-for-manufacture work done, nor has he done any process engineering (let's assume Joe is a few million shy of the millions Apple would have spent in manufacturing process development), he agrees to go along with their suggestions.

Unfortunately, the cassette-tape-o-tron is a Chinese domestic market product. This means it has not been subjected to the rigorous testing that would apply to an exported product. Federal Communications Commission approval? UL Listing? Lead in the solder? Have any of these tests been done? The biggest problem here is that Joe doesn't know enough to ask and his supplier doesn't know that this may be an issue.

A few prototypes later and the mp3-o-tron is not looking all that great. There are performance issues with audio playback and, on top of that, three of the ten prototypes that Joe brought back from his last trip have stopped working – one right in front of a customer. Joe calls the supplier to complain and the supplier says: "No problem. We'll give you three new ones when you come back". Joe is not pleased. When Joe's customers ask about FCC approval, Joe just nods and makes a mental note to ask his supplier. After all, surely they must know that his product needs FCC approval to be sold in the US?

The costs keep mounting. As Joe demands approvals, testing and certification, the supplier keeps raising the price. Finally Joe balks. "Lower the price or we are not buying mp3-o-trons from you!" The supplier agrees – but how will it save the cost? Fake chips? Thinner than specified printed circuit boards? Tin screws instead of stainless steel? Unless Joe is testing for each of these possibilities, he is at serious risk of unapproved component substitutions.

The first containers of mp3-o-trons finally arrive in the US. The costs are higher than planned, the product barely scraped through all the certifications required for sale in the US market and they are of dubious quality. Joe, not having budgeted for his own QC team to be on site at the factory during production, has had to rely on the supplier to confirm the quality of his goods.

Soon word gets out about Joe's mp3-o-tron; just another low quality Chinese product. But how did we get here? The journey, as you can see, is not that simple.

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SOVEREIGN NEWS

Volunteering in Dubai

By Nicholas Cully, Managing Director – Middle East

A team of six from Sovereign's Dubai office took "Dress Down Thursday" to a whole new level when they volunteered at the Senses Residential and Day Care Centre for Special Needs in Umm Suqeim, Dubai.

Senses is one of the many facilities to receive funding from Dubai-based charity, START, which runs over 60 art therapy sessions per week, reaching more than 2,000 children and young adults. These workshops give the children an opportunity to express themselves, engage with others and learn in a safe environment.

On arrival at the venue, we were given a short briefing about the centre and about the class in which we would be participating. We entered the classroom with some trepidation but were warmly greeted by the teacher, Mahbouba, who then gave us an opportunity to introduce ourselves to the children. Then the selection process began. Each child selected their own assistant to help them through the session. Ibrahim chose me.

Ibrahim is Emirati and in his late teens. He finds it hard to walk and his special needs are compounded by his inability to speak. However, he more than makes up for this through his art. My job was to guide Ibrahim through the stages of the class and to help him to follow Mahbouba's instructions, which she was putting up on her white board.

Whilst Ibrahim found the class hard, anyone could see that he and the other children – not to mention the volunteers – were enjoying the session and were completely engaged in what they were doing. Although we had never met previously and came from very different cultures, Ibrahim and I were able to build up a bond through the art that we created – punctuated by numerous "high fives"!

The class was extremely well run by Mahbouba and I enjoyed the fact that we, as volunteers, were also expected to create a picture and to display it at the end alongside the children's pieces. This meant it was very much a joint effort.

So many thanks to START for organising this opportunity for us and to Senses for hosting us. The second group of Sovereign volunteers is now signed up and is looking forward to joining a class soon.

The 2016 Sovereign Asian Art Prize

The Sovereign Art Foundation announced Indian artist Baptist Coelho as the winner of the 2016 Sovereign Asian Art Prize and recipient of the US$30,000 cheque. The announcement was made at SAF's 12th annual gala dinner on 3 June in the Grand Ballroom of the Four Seasons Hotel Hong Kong.

Baptist, a Mumbai-based artist, impressed the panel of judges with his artwork titled *Attempts to contain*, 2015 – a piece consisting of eight photographs on archival paper, which explores how the body responds to the physical and psychological need to protect itself by forming a mesh of interlocking body parts.

The Schoeni Prize of US$1,000, which is voted for solely by the public, was awarded to Philippines-based artist duo Alfredo and Isabel Aquilizan, for their piece *Left Wing*. As the artists were busy installing an exhibition at the newly opened National Gallery Singapore, *Asia Art Archive's* Head of Development Alexandra Seno kindly stepped up to receive it on their behalf.

The Grand Ballroom at the Four Seasons was decked out in dramatic style for the event. Huge paper planes soared over a room lit in sky blue in keeping with the evening's theme of 'Hope Takes Flight', while large balloons floated on ribbons twinkling with tiny lights at the centre of each table.

Chairman of Christie's Asia Pacific, Francois Curiel, led the auction of finalist works in his own inimitable style; and a dynamic performance by *Asia's Got Talent* finalists Junior New System had guests leaping out of their seats – and breaking out some impressive moves on stage!

Our thanks go to all SAF sponsors – Pictet Wealth Management, Christie's, Hong Kong Land, G4Si, Links Concept, Ovolo Hotels, *Hong Kong Tatler, The Financial Times, Time Out Hong Kong*, Aesop and Easiway – for helping us stage the 2016 Prize Edition, and to all of those who attended the gala dinner, bid on artwork or made a pledge. We couldn't do what we do without you.

To check out more pictures from the event please go to the SAF Facebook page.

Make It Better Graduation

It was smiles all round at the Ovolo Southside Hotel on Saturday, 18 June, when participants in the *Make It Better* programme gathered to celebrate their graduation. On display was an exhibition of the beautiful artworks that had been created during the workshops.

The ceremony opened with a performance by the Umpqua Singers, a vocal jazz ensemble from Oregon, who delighted the kids with a rendition of a popular TV theme tune in Cantonese.

A total of 46 children from centres across Sham Shui Po, Tseung Kwan O and Kowloon City then took to the stage to receive graduation certificates and colouring sets to take home. The afternoon concluded with a delicious spread of goodies generously provided by Ovolo Hotels.

A big thank you to Ovolo Hotels and Umpqua Singers for helping to make this event such a success! More pictures of the ceremony can be viewed on the new SAF Makes It Better Facebook page.

SIMON GARVEEN IS...

SOVEREIGN MAN

A pretty reasonable trade off (trusts)

So, I had the promised lunch with Larry Largefees, my lawyer, at the Golf Club to discuss making a will. As usual I ended up paying. I suppose that was fair enough as I was picking his brain and getting his initial thoughts for free. But sometimes I wish he would get his own wallet out. After all, I pay him a hefty whack over a typical year.

Anyway, after we had moved on to a rather cheeky Graham's 1983 port, the conversation turned to the serious matter of death and bequests. Cheery stuff. I explained to him what I wanted to achieve and that I thought I needed to write a will. He explained to me that I already had a will but it dated from the time when I was still with my first wife.

Imagine what would have happened if I had "bought the farm" with that still in place! Now I actually get on pretty well with the first wife but she has now remarried and the guy is loaded – so she certainly doesn't need my cash. This will had left all the income to her for her lifetime and thereafter for our three kids in equal shares. The current Mrs G and our joint progeny would have been left bereft. Whoops!

So I certainly need to rewrite my will but Largefees suggested it would probably be better to put everything into trust. I would still need a will to tidy up the remnants but, he explained, assets held in trust would be "outside" my estate, so would not be subject to estate duty or inheritance tax. And I could organise everything properly while I'm still around to do it, which would be much more simple and straightforward than when I'm not. After all, I know where all the assets are so can easily arrange a transfer into trust.

If I left it to my executors to go and find everything, it could take them several years and cost as much as 6% of the total assets to get it all done. And while all that was going on, the assets would be frozen, which might cause tremendous difficulties for my loved ones. The trust idea sounded much jollier. The problem is my domicile. If I'm still domiciled in the UK the transfer into trust will cost me 20% of the value of the assets. There's no way I am going for that. Largefees thought that I was probably no longer UK-domiciled because I'd lived abroad for so long but we would need to get certainty on that.

The bit I'm not entirely comfortable with is that (by setting up a trust) I would lose control of my assets – and that includes all my shares in my own company. I have since had discussions with the proposed trustees who explained they could insert clauses in the trust deed such that they wouldn't interfere in the running of the company and would not be liable for any losses at the corporate level. This would mean that I would be left to get on with it even though, technically speaking, I would no longer be a shareholder.

That seemed a pretty reasonable trade off, but I also don't want to have to ring the trustees up every time I need some cash. No problem, they said, we could restructure the capital of my company to create three classes of shares: A shares, which only have rights to dividends; B shares, which only have rights to capital; and C shares, which only have votes. Usually shares have all three characteristics but they can, it seems, be split.

I have checked on this and I like it. The trustees can certainly have the capital (B) shares. This means they get to hold most of the value. I get to hang on to the A class shares, which means I can take the dividends. The value of the A shares should be minimal compared to the B class capital shares. And I will also hold the C class shares so I can continue to manage the company without the need to involve the trustees continually. My will would then state that any B or C shares I still own upon death should be transferred to the trustees.

This seems like an excellent solution to me, so I told them to go ahead. The terms of the trust will dictate that, when I'm no longer around (perish the thought), the trustees will have to make the decision as to whether to sell the company or keep it together. I have indicated that I would like it to continue for as long as the existing senior management is capable of running it. This all now ties with the long-term incentive plan (LTIP) that I've set up. If they've done well they will own a decent slice of the company themselves by then.

Either way the trust can be designed to look after Mrs G in some style during her lifetime. After that, the kids will get some minor bequests and any grandchildren will get their school fees paid, while the capital will be retained with the income being distributed to the charity I've set up. That seems to tick every box. Sweet.

CASE STUDY

UAE CORPORATE SHAREHOLDER MODEL

The United Arab Emirates (UAE) has a global reputation as a wealth generator and investment stronghold. With its world-class infrastructure, business-friendly environment and strategic location for the high growth markets in the Middle East, Africa and South Asia, Dubai is a natural choice for business expansion and new initiatives. However international companies face major challenges when entering foreign markets and the UAE is no exception.

The UAE has almost 40 Free Zones in which 100% foreign ownership is permitted. In addition, companies based in a Free Zone can enjoy 100% import and export tax exemptions, 100% repatriation of capital and profits, corporate tax exemptions for up to 50 years, no personal income taxes and assistance with labour recruitment, as well as additional support services such as sponsorship.

If however your business requires you to trade on the UAE mainland, you will need a company that is established in Dubai under the UAE Commercial Companies Law (CCL) and is licensed by the Department of Economic Development (DED). Such companies are also far less restricted in their choice of premises and are not required to pay the standard 5% customs duty on imported goods. However you will require a local majority owner, often referred to as local partner. UAE nationals or their wholly owned companies must hold a minimum of 51% of the shares of all companies established under the CCL in the UAE.

Many investors are concerned by the foreign ownership restrictions and are uncomfortable at the prospect of having to relinquish control of their company to a local partner. To allay these concerns, Sovereign has created a "corporate shareholder" model, which is designed specifically to allow clients to maintain 100% effective ownership control of their business.

THE PROBLEM

JLFB is a Scandinavian multinational group that designs and sells ready-to-assemble furniture, appliances and home accessories. It wishes to establish a substantial retail presence in Dubai due to the large number of western expats living there. However it is a PLC group and the board wishes to maintain full control of its management, finances and intellectual property, without the need for a local partner.

Setting up in a Free Zone would not work for JLFB because it needs to be able to trade with other companies in Dubai without any restrictions. Moreover it doesn't want to be limited on the number of visas that it can obtain for employees or be restricted on its choice of office and retail locations in the UAE.

THE SOLUTION

Dubai-based Sovereign Corporate Services has created a number of 100% Emirati-owned LLCs – in this case Sovereign Partners Investment LLC (SPI) – that it fully manages and controls through Powers of Attorney and other legal agreements. These companies can act as the 51% local partner for JLFB and, through a suite of risk mitigation documentation, will pass all management control, financial control, as well as the day-to-day running of the business, back to the 49% shareholder (JLFB) in return for a "Fixed Annual Sponsorship Fee".

Sovereign will not take any commercial role in the new company and its annual fee will be fixed such that there will be no variation depending on increased turnover or profitability of the business. This solution will satisfy both the requirements of the CCL/DED as well as the requirements of the JLFB board, which has expressed serious reservations about handing 51% of a subsidiary to an Emirati individual.

THE BENEFITS

The key benefits of Sovereign's Corporate Shareholder Model to JLFB are:

- **Maintains 100% control of the UAE business** – the JLFB board is satisfied and can focus on its UAE business plan;
- **Sovereign provides multiple signatories who are available all year round** – Emirati individual partners may leave the region, particularity in the summer months;
- **Absence of potential succession issues** – As a company, SPI offers perpetual succession. JLFB therefore knows that its business will not be affected by the ill-health or death of an Emirati individual partner;
- **No emotional connection** – By employing a corporate shareholder like SPI, JLFB will not be dealing with an individual person as a shareholder but rather with an international, fully licensed and regulated company that has no emotional ties to the business and no local vested interests;
- **Sovereign's fee is fixed** – JLFB can be confident that there will be no sudden changes to its costs, so it can forecast and plan accordingly;
- **Sovereign has a 60-day exit strategy** – Should JLFB decide to leave the UAE market or transfer its business to another local sponsor (either corporate or individual), Sovereign will not impose exit penalties or barriers;
- **Sovereign is in partnership with the Dubai Government** - Sovereign Corporate Services LLC has entered into a formal, strategic partnership with Dubai FDI, the dedicated investment development agency within the DED. JLFB's board can therefore be assured that Sovereign's corporate shareholder model is in full compliance with UAE companies law;
- **Sovereign has a global office network and can assist clients with market entry on a worldwide basis** – JLFB would benefit from partnering with a global market entry specialist such as Sovereign rather than one with a solely UAE perspective.

The vehicle you drive is a reflection of your lifestyle, outlook and taste. A corporate vehicle also implies more about your life than you might think – and many owners are unaware of the impression they are creating.

A simple offshore structure will rarely achieve any tax benefits, let alone more complex commercial or personal objectives; in fact it may lead to increased tax and restrictions.

Sovereign provides fully compliant international vehicles and structures that will deliver legitimate advantages to you, your family and your business. They offer genuine performance and don't have to be hidden away, allowing you to drive anywhere with confidence.

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