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I INTRODUCTION

At a macro level, the dominant trend affecting the private wealth arena in the last 12 months continues to be the impact of various supranational initiatives seeking greater transparency with respect to anti-money laundering regimes and tax information exchange. I propose to focus in this year’s introduction on the central importance of the concept of ‘beneficial ownership’ and the theme of convergence in the increasingly interconnected arenas of anti-money laundering policy and tax information exchange.

The clearest examples of this trend can be found in the introduction of centralised beneficial ownership registers, especially in the European Union and the Crown Dependencies and Overseas Territories of the United Kingdom (generally collectively referenced as CDOTs).1 There are two specific manifestations of this:

a corporate beneficial ownership registers; and

b trust beneficial ownership registers.

In parallel, 2017 has witnessed the first substantive reporting by the first wave ‘adopters’ of the Common Reporting Standard (CRS) in the context of the 2016 calendar year.

I would like to first reference the common definitions that connect CRS with beneficial ownership registers and then refer in detail to the UK domestic trust register that was introduced by Regulations adopted in June 20172 (2017 MLR) before noting some key developments in the CRS domain.

i Common use of beneficial ownership concept

The key ‘source document’ with respect to the concept of beneficial ownership is the Financial Action Task Force (FATF) 2012 Recommendations.3 These recommendations were introduced as part of the international anti-money laundering policy but have been adopted as an essential element of the international tax information exchange policy implemented by the CRS.

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1 These jurisdictions includes Jersey, Isle of Man, Guernsey, Cayman Islands, Bermuda and British Virgin Islands.
This is clearly confirmed in a CRS context by the CRS Commentary on the concept of controlling persons. Paragraph 132 of the interpretive notes to Recommendation 10 on Customer Due Diligence, states:

Subparagraph D(6) sets forth the definition of the term ‘Controlling Persons’. This term corresponds to the term ‘beneficial owner’ as described in Recommendation 10 and the Interpretative Note on Recommendation 10 of the Financial Action Task Force Recommendations (as adopted in February 2012), and must be interpreted in a manner consistent with such Recommendations, with the aim of protecting the international financial system from misuse including with respect to tax crimes.\(^4\)

The FATF recommendations lead to a position where one essentially moves away from a strict legal definition of who might be entitled to enjoyment of an asset as a beneficial owner to an expanded concept. Under these rules, if it is not possible to identify a beneficial owner based on ‘ownership interests’ it is necessary to identify a beneficial owner based on ‘control’ even though the person or persons who control a legal entity have no capacity to call for the assets of the entity for their own personal benefit. In addition, as a last resort, if no ‘ownership’ or ‘control’ test can be satisfied, the final step is to look to the ‘senior managing official’ of the entity at the top of the ownership chain. This three-level ordering of who is to be regarded as the ‘beneficial owner’ is taken from the interpretive notes to Recommendation 10 of the FATF 2012 Recommendations:\(^5\)

Identify the beneficial owners of the customer and take reasonable measures to verify the identity of such persons, through the following information:

(i) For legal persons:
(i.i) The identity of the natural persons (if any – as ownership interests can be so diversified that there are no natural persons (whether acting alone or together) exercising control of the legal person or arrangement through ownership) who ultimately have a controlling ownership interest in a legal person; and
(i.ii) to the extent that there is doubt under (i.i) as to whether the person(s) with the controlling ownership interest are the beneficial owner(s) or where no natural person exerts control through ownership interests, the identity of the natural persons (if any) exercising control of the legal person or arrangement through other means.
(i.iii) Where no natural person is identified under (i.i) or (i.ii) above, financial institutions should identify and take reasonable measures to verify the identity of the relevant natural person who holds the position of senior managing official.

The immediately following interpretive notes describe the steps to be taken to identify the beneficial ownership of a trust (or similar legal arrangement such as a foundation). In this case the approach is subtly different. They start with a composite list that blends together

\(^4\) Emphasis added.

those who might benefit personally with those who are perceived to have some ‘control’. They state:

For legal arrangements:

(ii.i) Trusts – the identity of the settlor, the trustee(s), the protector (if any), the beneficiaries or class of beneficiaries, and any other natural person exercising ultimate effective control over the trust (including through a chain of control/ownership);

(ii.ii) Other types of legal arrangements – the identity of persons in equivalent or similar positions.

What is notable here is the introduction of a ‘residual’ concept of:

Any other natural person exercising ultimate effective control over the trust

I will refer to this as the ‘NPEEC’ in the rest of this article.

Until recently, there has been a major problem with construing who might be regarded as an NPEEC in a trust context especially because there has been no guidance in a FATF or CRS context that sheds light on what is meant by ‘control’. This has created uncertainty as to when a person has ‘control’ over a trust, for example, will it include someone who has power to remove a trustee, someone who can only exercise powers jointly with someone else or someone who holds only powers of veto rather than positive powers to act.

In the Anti-Money Laundering context, the 2017 MLR includes a definition of ‘beneficial owner’ and ‘control’ for the purposes of the Regulations. At Regulation 6 it states:

6.—(1) In these Regulations, ‘beneficial owner’, in relation to a trust, means each of the following—

(a) the settlor;
(b) the trustees;
(c) the beneficiaries
(d) where the individuals (or some of the individuals) benefiting from the trust have not been determined, the class of persons in whose main interest the trust is set up, or operates;
(e) any individual who has control over the trust.

(2) In paragraph (1)(e), ‘control’ means a power (whether exercisable alone, jointly with another person or with the consent of another person) under the trust instrument or by law to—

(a) dispose of, advance, lend, invest, pay or apply trust property;
(b) vary or terminate the trust;
(c) add or remove a person as a beneficiary or to or from a class of beneficiaries;
(d) appoint or remove trustees or give another individual control over the trust;
(e) direct, withhold consent to or veto the exercise of a power mentioned in sub-paragraphs (a) to (d).

A critical point to note here is that the mere existence of one of the relevant powers with respect to a trust is sufficient to be regarded as control even in circumstances where that power is not actually exercised. This is substantially different from the idea of a person who exercises effective management of a trust or a company in many tax contexts. The more conventional concept is a facts and circumstances test that requires the actual exercise of powers rather than the mere capacity to exercise them for control to be attributed to a person.

What is striking here is that in Regulation 6(2), both the holding of joint powers and that the withholding of consent or ability to veto the exercise of key powers is to be equated
with ‘control’. I will return to the specific implications for CRS Reporting in the context of trusts later – for now, it is sufficient to note the expansive definition of beneficial ownership which sits behind the various regimes.

A final point to note is that the scope of powers that can be held with respect to a trust that come within this incredibly wide concept of control extend substantially beyond the power to appoint and remove trustees. Thus powers that relate to changing the class of beneficiaries, varying or terminating the trust and powers to invest or deal with trust property are also to be equated with control.

ii UK Trust Register

I now turn to the UK Trust Register in its own terms. The reason I wish to consider this piece of domestic UK legislation in detail is because, as far as I am aware, it represents the first instance where a major ‘onshore’ jurisdiction with a domestic trust law has introduced a centralised beneficial ownership register for trusts. The 2017 MLR effectively implements the UK’s obligations under the EU Fourth Money Laundering Directive ((EU) 2015/849 (4AMLD)) to introduce a UK trust register. The regulations have a wide context with respect to the combating of terrorist financing and the fight against organised crime more generally. It seems likely that they will be widely copied, especially by trusts administered in the CDOTs where the UK has substantial influence.

The Regulations require the UK tax authority (HMRC) to maintain a trust register. The trust register will principally apply to trusts with UK resident trustees. However, trusts with non-UK resident trustees are also within the scope of the register if they hold UK situate assets that generate the obligation to report to UK HMRC with respect to certain taxes, including income and capital gains tax, inheritance tax and stamp duty land tax. The scope of the register requires more extensive information to be reported and maintained than that required to be disclosed under CRS.

In addition to the information which would typically be disclosed for the purposes of CRS (see paragraph 11 above) it also necessary to provide HMRC with the following information:

a The trustees must provide information about certain professional advisers to the trust, namely those who provide ‘legal, financial or tax advice’6 to the trust.

b There is a requirement to provide ‘a statement of accounts for the trust, describing the trust assets and identifying the value of each category of the trust assets’. CRS, in contrast, only requires a composite value for the notional ‘account value’ of the trust fund of the trust without breaking this value down into categories.

c In considering who might be regarded as a beneficiary, Regulation 44(5)(b) states that trustees must report information ‘about any other individual referred to as a potential beneficiary in a document from the settlor relating to the trust such as a letter of wishes’. This means that reference has to be made to documents other than the trust deed itself which, in the longer term, is likely to create a significant degree of confusion and uncertainty over reporting given that there is no current requirement to undertake such an exercise that I am aware of in any CRS or other equivalent tax reporting context with regard to persons who are not named as current beneficiaries.

6 See regulation [   ] of 2017 MLR.
The UK Trust Register will (subject to the caveat noted below) only be accessible by law enforcement agencies in the UK and throughout the rest of the EU/EEA – the issue of what happens to this EU/EEA access post Brexit is presently unclear. The categories of persons with access to the UK Trust Register under 2017 MLR are arguably narrower than those described in Article 14 of 4AMLD. Article 14 states that:

persons who are able to demonstrate a legitimate interest with respect to money laundering, terrorist financing, and the associated predicate offences, such as corruption, tax crimes and fraud should also have access to beneficial ownership

It is, therefore, possible that NGOs and investigative journalists with an anti-corruption profile could seek access to the UK Trust Register on the basis that the UK (as a current EU member) has failed to implement 4AMLD in full.

### iii Trustee obligations under the UK Register

A trustee of a relevant trust is obliged to:

- maintain an up-to-date register of the 'beneficial owners' of and advisers to the trust;
- provide HMRC with detailed information about the beneficial owners on an annual basis and with respect to the assets of the trust and their capital value;
- inform relevant persons of:
  - its status as a trustee;
  - the beneficial owners of the trust; and
  - any change of beneficial owners (within 14 days of the change occurring).
- respond to any request for information from any law enforcement agency with respect to the trust within the reasonable period specified in the notice of request.

### iv Information about the trust under the UK Trust Register

With respect to the trust itself, it will be necessary to confirm:

- the name of the trust and its date of creation;
- a statement of accounts for the trust, describing the trust assets and identifying the value of each category of the trust assets;
- the place where the trust is administered;
- a contact address for the trustees; and
- the full names of any advisers who are being paid to provide legal, financial or tax advice in relation to the trust.

With respect to individuals identified as beneficiaries or NPEECs it will be necessary to provide:

- full name and date of birth;
- details of the individual's role or roles in relation to the trust; and
- unique tax reference number of the individual.

---

7 Essentially a trust within scope of reporting.
8 Essentially financial in institutions and other professional persons with reporting regulations under AML rules.
Where a corporate entity is involved in a trust, one is obliged to ‘look through’ that entity and identify the individual(s) who control it; they are subject to disclosure in their own right.

v  CRS developments
In a CRS context, I would like to consider two key areas. The first is the issue of local guidance and fragmentation, especially with respect to trust reporting. The second is the vexed issue of reporting protectors and its overlap with the NPEEC concept.

vi  Fragmentation
On fragmentation, it is notable that during 2017, many jurisdictions issued their own local guidance on certain issues. To take a few examples:

a Canada: as in the case of the Foreign Account Tax Compliance Act (FATCA), Canada takes the position that other than in certain instances where banks or similar entities are concerned, most trusts with professional trustees are to be regarded as passive non-financial entities (NFE) not reportable financial institutions (RFI).

b Singapore: Singapore has issued guidance that permits settlors who are excluded as beneficiaries to report a nil value in terms of the value of their equity interest in the notional account represented by the trust fund.

c Bermuda: a trust where the settlor reserves a right to direct investments is not to be regarded as an RFI even though its trustee is a financial institution.

d Cayman Islands: all financial institutions are required to file a nil report even though they are non-reporting FIs. This is contemplated in CRS but is likely to create a significant degree of extra reporting in large and complex trust structures.

The concern here is that there will be substantial confusion over what to report where local guidance generates positions that contradict OECD’s own commentary or the position taken in other jurisdictions generally. It is also likely that a pattern of jurisdictional arbitrage will emerge.

vii  Protectors
On the issue of reporting protectors, it is well known that there is an inconsistency in the class of persons who are to be identified as the controlling persons of a trust when compared with those who to be identified as holding an equity interest in a trust. The two lists of persons are substantially similar except that the latter makes no express reference to ‘protectors’. This has led to a great deal of confusion and divided opinion on when protectors are required to be reported. OECD in an FAQ issued in June 2016 takes the view that protectors must always be reported but a strict reading of the wording of the Model Treaty leads to the conclusion that they should only be disclosed as holders of an equity interest where they satisfy the test as a NPEEC.

What is interesting is that, in the context of the UK Trust Register, 2017 MLR do not make express reference to protectors either. Instead, as noted above, they refer to ‘any individual who has control over the trust’ and then refer to the powers over the trust that are to be equated with ‘control’.

viii  NPEECs and control
I would like to consider the question of who is to be regarded as ‘exercising control’ and who might be regarded as an NPEEC for CRS purposes if one follows the approach adopted in 2017 MLR.
It is interesting to note that, in commenting on the issue of control under the Controlling Persons heading in the CRS Handbook at paragraph 227, the OECD states:

The account held by a trust will also be reportable if it the trusts has one or more Controlling Persons that are Reportable Persons. The concept of Controlling Person used in the CRS is drawn from the 2012 FATF Recommendations on beneficial ownership. As such, the Controlling Persons of a trust are the settlor(s), trustee(s), beneficiary(ies), protector(s) and any other natural person exercising ultimate effective control over the trust. *This definition of Controlling Person excludes the need to inquire as to whether any of these persons can exercise practical control over the trust.*

It is reasonable to conclude that OECD’s intention was to follow the FATF expansive definition of beneficial ownership which is not based on a conventional legal analysis of matters such as control but, instead, to ensure that those persons reported under CRS include those with the capacity to exercise substantial influence over how a trust is run.

This approach is echoed in OECD’s comments at paragraph 214 of the Handbook with respect to those to be regarded as holding an equity interest in an RFI Trust. This states:

*The Equity Interests are held by any person treated as a settlor or beneficiary of all or a portion of the trust, or any other natural person exercising ultimate effective control over the trust. The reference to any other natural person exercising ultimate effective control over the trust, at a minimum, will include the trustee as an Equity Interest Holder.*

The fact OECD uses the phrase ‘at a minimum’ is confirmation of this expansive approach.

My view is that the definition of control from MLR 2017 could well be widely adopted in a CRS context to assist in defining NPEECs with respect to trusts. If this does indeed happen, it will mean that virtually all protectors with significant powers with respect to trusts will be reportable as NPEECs, thus rendering the debate about whether protectors of RFI trusts are reportable as such largely academic.

II CONCLUSION

The year 2017 has witnessed some important developments in beneficial ownership reporting. The convergence of the expanded concept of who is to be regarded as a beneficial owner or exercising control in the tax reporting and AML arena looks set to be a dominant trend in the years ahead. Advisers should be very conscious of this, not only in advice on existing wealth ownership structures but also in the design of new ownership structures.

John Riches
RMW Law LLP
London
September 2017

9 Emphasis added.
10 Emphasis added.
Chapter 1

EU DEVELOPMENTS

Richard Frimston

I INTRODUCTION

The European Union was a structure under stress, facing significant change. Its development from the European Coal and Steel Community into a European Economic Community and then to a European Community and now a European Union was one of incremental steps. Its competence, in relation to taxation, has in the past been limited to the European sales tax, value added tax. Although the recent problems with the single currency, the euro, may seem to have largely disappeared, with the exception of Greece’s place in it, its structural difficulties remain unchanged. The referenda in Denmark and the United Kingdom demonstrated a general unhappiness of EU citizens with the direction of travel. The trends in Austria and the Visegrad Group of Poland, Hungary, Slovakia and Czech Republic were seen to be away from the liberal social democratic model of the majority of Member States. However, the 2017 election results in the Netherlands and France, in which right wing anti-EU parties were defeated, and the improving economic outlook have given the European Union and its various institutions hope that a corner has been turned.

All Member States were focused on debt reduction and maximising tax collection particularly from corporations, while dealing with their citizens’ concern over immigration. The EU institutions are conscious of the overwhelming priority to maintain the euro as a single currency and to produce economic growth. The eurozone perspective and priorities continue to drive those Member States towards ever closer union. Relations with the United States are also under review. The US support of NATO can no longer be taken for granted and Angela Merkel’s statements as to the future of Europe separate from the US and the UK show that geopolitics may also push the eurozone states more firmly together. The US wish to renegotiate the Paris Climate Accord has given China an opening to be seen to stand with the EU on the issue.

Uncertainties in Ukraine and with Russia moved the Baltic States firmly into the euro, in contrast to the non-euro Member States such as the Czech Republic, Sweden and Poland who remain firmly outside. The two-tier euro/non-euro EU has already created significant tensions. The stark divisions within the United Kingdom exacerbated by its referendum would objectively call for some form of compromise. The EU is very frightened of contagion and other dominoes falling. Brave political leadership may be in short supply, but other differences are in any event producing a more complex and multi-layered EU.

While strictly not a federation, at many levels the EU behaves as if it were one. Since the Lisbon Treaty of 2009, the Treaty on European Union and the Treaty on the Functioning

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1 Richard Frimston is a partner at Russell-Cooke LLP.
of the European Union govern its constitution and legislative processes. The relationship between its civil service (the Commission), the Member States’ governments (the Council of Ministers) and the European Parliament (the EP) is still a work in progress. The results of the EP elections held in May 2014, although producing generally anti-EU results in the UK and France, had been taken as a vote for business as usual by the EP, which is flexing its muscles, particularly in the area of tax. In the field of anti-money laundering and tax evasion, the Commission appears to be siding with an increasingly vocal Parliament rather than with the Council of Ministers. However, there is no evidence that the EP (or the Commission) has taken on board the implications of the more complex EU forces at work.

The EU, even if reduced to 27 Member States, is a place of significant wealth. With a combined population of 500 million or 7 per cent of the world’s population, it has approximately 20 per cent of the world’s exports and imports. The European Economic Area (EEA) consists of the EU, Iceland, Liechtenstein and Norway (Switzerland being a member with Iceland, Norway and Liechtenstein of the European Free Trade Association (EFTA) but not in the EEA).

The economic prosperity of the EEA made it increasingly an attractive destination for those fleeing conflict and poverty to its south and east. If the UK exits the EU, even if it remains in the EEA, the strength and prosperity of both the UK and the EEA are likely to be diminished.

To the tensions of the multi-speed EU are added the problems of mass migration. Under the Treaty on European Union, the two-year timetable started once the UK served notice under Article 50. The 2016 referendum in the UK as to whether it should remain within the EU and subsequent serving of Article 50 notice to leave the EU in March 2017 has cast a shadow over the workings of the EU. The migration of both EU and non-EU nationals to the wealthier parts of the EU bring the fundamentals of the EU into sharp focus. The free movement of labour and capital is designed to produce economic growth for both Member States and business. The demographics of most Member States require immigration in order to feed economic growth and counter falling birthrates. However, mass migration is an issue for all front-line Member States, such as Italy, Malta and Greece, and is also one for indigenous citizens who perceive their own wages and standard of living as being reduced by the competitive market.

Similarly, France, Germany and the UK have all suffered from very public terrorist attacks in 2016 and 2017. Being seen to deal with such threats effectively while maintaining European traditions of tolerance and freedom gives EU governments common problems and reasons to work together.

Against a backdrop of continuing security threats, it is unlikely that the EU, its Member States and the EEA will be able easily to square the circle in relation to mass migration and economic growth.

II UNITED KINGDOM

The United Kingdom, which was in the middle of a constitutional crisis, is now in a political disaster. The referendum in September 2014 in Scotland as to whether it should be independent, focused much thought as to the continuing nature of the strange ragbag of arrangements between the UK government in Westminster and those in Scotland, Wales and Northern Ireland. Northern Ireland, a product of its history and geography, is also caught

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between numerous forces; its recent uneasy peace, having been sadly taken for granted. London, while having a larger population than each of those jurisdictions, has limited local government, while England as a whole has none.

The UK 2017 snap General Election result that produced no clear winner came as a surprise to many, but the rise of the Conservative Party in Scotland in protest at the Scottish Nationalist Party should not have done. In England the Labour Party ran a much more effective and optimistic campaign while the Conservative Party was, in general, blamed for calling an unnecessary election and asking voters to give it a blank cheque. They declined to do so. It would seem that many electors voted against a party rather than necessarily for one.

The timetable for Brexit, is ticking and the politicians are only now addressing the extremely difficult and complex fundamental questions that should have been considered before the EU Referendum rather than after Article 50 notice had been served.

The margin of 4 per cent on a 73 per cent turnout in the EU Referendum has left the UK completely divided and the 2017 general election has not healed the division. London and Scotland by a 20 per cent majority and Northern Ireland by a smaller one, voted to remain in the EU. The remainder of England and Wales with the exception of some cities such as Bristol, Liverpool and Oxford voted by a significant majority to leave. The campaigns are symptoms of the continuing struggle within the Conservative party, which is currently left with a lame duck leader, and no sign of a way out of the quagmire it has got itself into. The Labour Party, however, is now seen as being on the up.

The EU institutions had seen the referendum as a distraction that was unnecessary. The UK was seen as a pragmatic and effective major EU Member State, but that is no longer the case. Whether it will have a government able to follow through any negotiations and enact any necessary treaty arrangements is seen as questionable.

The downsides for the EU of the UK leaving have not been openly discussed. The necessary reductions in EU income are likely to be matched by increased taxation rather than reductions in spending. The loss of a major common-law state would leave a more homogeneous civil law EU, less open-market or outward looking. It would be the poorer for it.

The UK government and institutions will now have to expend all of its energy in negotiating its position with the EEA and the effects of any exit from the EU on its laws and structures, while being blown and buffeted by events. While the absence of a written constitution has enabled flexible and incremental change in the UK, all these tensions will create mounting pressure for the new relationships between the various existing UK structures. In the meantime, it is very likely that the UK and EEA economies will decline, while at the same time the proportion of UK government spending will inevitably increase.

III TAX

Generally, the EU has no competence over personal taxation for individuals, such matters being for individual Member States and outside its competence. However, with increasing frequency the European Court of Justice has held\(^3\) that the right to free movement of persons,\

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3 In for example Case C-364/01 Barbier [2003] ECR I–15013 (treatment of immovable property), Case C-513/03 van Hilten-van der Heijden [2006] ECR I–1957 (inheritance tax within 10 years of being resident was permissible), Case C-464/05 Geurts [2007] ECR I–9325 (exemption for Belgian businesses only), Case C-256/06 Jäger [2008] ECR I–123 (reduction for German agricultural property
goods, services and capital within the EU applies to limit the taxation rights of Member States. Inheritance was found to be a movement of capital and many Member State governments have been forced to amend existing tax rules. In the case of Austria, this led directly to the abolition of gift and inheritance tax.

As a result, the EU Commission looked at two separate initiatives:

1. the effects of inheritance taxes on the rights of free movement; and
2. double non-taxation.

The limited competence of the EU in these areas has, however, meant that the recommendations were advisory only.

Over the years, the EU has developed various cross-border structures such as the European Company (SE) and the now lapsed proposal for a European Foundation (FE). However, the tax treatment of these structures is not uniform. There has as yet been no proposal for an EU-wide tax transparent vehicle such as an LLC, LLP or SCI.

By contrast, the EU has concentrated much firepower on corporate taxation. There is broad consensus on the part of EU institutions, Member States and the Organisation for Economic Co-operation and Development (OECD) on tackling aggressive tax planning by corporations. Tax justice and a level playing field are seen as a priority. The EU Commission has presented its Action Plans for Fair and Efficient Corporate Taxation in the EU and has relaunched the Common Consolidated Corporate Tax Base (CCTB).

The proposed EU/US Transatlantic Trade and Investment Partnership (TTIP), the main goal of which was to remove regulatory ‘barriers’ that restrict the potential profits to be made by transnational corporations on both sides of the Atlantic, is now seen as a dead duck. The EU/Canadian agreement (CETA), however, was finalised in the EU Parliament in February 2017 subject to ratification by national legislatures. The EU appears to be making good progress with a free trade agreement with Japan. Further legislation continues to be made. The Regulation on Mutual Recognition of Protection Measures in Civil Matters came into force in January 2015 and binds the United Kingdom and Ireland but not Denmark. The Brussels I Regulation was reviewed and amended: Brussels I-bis came into force in January 2015. The Brussels II-bis Regulation is still under review. The EU (and Mexico and Singapore) has ratified Hague 37 on choice of court agreements that entered into force on 1 October 2015. It applies in Ireland (and the UK) but not Denmark.

Rome IVa, (EU) 2016/1103, dealing with matrimonial property and Rome IVb, (EU) 2016/1004, dealing with the property effects of registered partnerships came into force on
29 July 2016 but will not become fully effective until 29 January 2019, but were Regulations subject to enhanced co-operation and will only apply in 18 Member States. This is dealt with more fully below.

The Regulation (EU) 2016/1191 of 6 July 2016 on promoting the free movement of citizens by simplifying the requirements for presenting certain public documents in the European Union was not subject to any opt-out by the UK or Ireland and will become fully effective on 16 February 2019.

How the UK is to extract itself from the EU acquis built up over 40 years, will not be straightforward. The proposed transitional arrangements on judicial cooperation in civil and commercial matters, suggested by the EU Commission Task Force, are very sensible but highlight the practical difficulties and complexities of disengagement in whatever form.

IV  TAX COLLABORATION, ENFORCEMENT AND REGULATION

Although the European Union is not a fully functioning federal state, its role in world organisations such as the OECD and the Financial Action Task Force (FATF) over money laundering and fraud or the Hague Conference over private international law, and in negotiating with world powers such as the United States in relation to matters such as the Foreign Account Tax Compliance Act (FATCA), should not be underestimated.

The European Union data protection laws appear to be what forced the United States into its FATCA Model 1 agreements with Member States. The European Commission played a significant role in those negotiations. However, while the Commission hoped to introduce a European FATCA, this was not politically acceptable in all Member States. The former Savings Tax Directive is now dead and is likely to be repealed.

In parallel, however, the OECD developed its Common Reporting Standard (CRS), which seems to have been accepted by the EU as the model for automatic tax information exchange and brought to an end further changes to the Savings Tax Directive. There seems, however, to be no realistic prospect of the US abandoning FATCA in favour of the CRS at the moment.

The EU revised its Directive on Administrative Co-operation (DAC). Council Directive 2011/16/EU established procedures for better cooperation between tax administrations in the EU – such as exchanges of information on request – in 2014 by Council Directive 2014/107/EU, which extended the cooperation between tax authorities to automatic exchange of financial account information and, in effect, incorporates CRS in the EU. In June 2017 the EU Commission controversially produced further amendments proposing a Directive regulating financial intermediaries such as banks, lawyers and accountants in cross-border structures that may avoid tax.

Money Laundering Directives were originally introduced to counter terrorist activity. Tax evasion and ‘abusive’ tax avoidance are now increasingly being targeted. The proposals for registers of beneficial interests in companies inevitably led to strong calls from the EP for registers for trusts and beneficial interests. However, the fourth Money Laundering Directive EU 2015/849, came into force on 26 June 2015 and was due to be implemented in each

10 The starting point for all US FATCA Model 1 Agreements.
EU Developments

Member State by 26 June 2017. Article 30 imposes different obligations on the trustees of express trusts to the obligations imposed in relation to beneficial ownership information required for legal entities under Article 29.

The Panama Papers and other calls from NGOs have resulted in the Commission and the EP revisiting the effectiveness of the fourth Money Laundering Directive EU 2015/849. There is ever increasing demand for public registers of beneficial ownership in relation to all structures in all jurisdictions. It is unclear where these demands will lead. As at July 2017, the EU Commission and Parliament are demanding public registers of all trusts, which the Council of Ministers is opposed to. Since the UK is unlikely to take any meaningful part in these EU negotiations, further widening of the effects of EU 2015/849 are almost inevitable. The EU Parliament Report from the Committee on the Panama Papers will also inevitably call for full open registers and focus on financial intermediaries.

Since Henry VIII’s Statue of Uses, equity has been successful in adapting and evolving to meet the demands modern society placed on it. Equity’s success is perhaps now under attack particularly from the civil law world and civil society that sees it as a hindrance against corruption and tax fairness. It will be interesting to see how equity develops in response. Whether if the UK leaves the EU, it will pull back from some EU developments is yet to be seen.

Practitioners therefore face continuing change, multiple registration and compliance and public pressure for transparency, all of which will push up the costs of practice.

V SUCCESSION AND MATRIMONIAL PROPERTY

It is in the area of succession law that the EU demonstrates its particular complexities. The substantive laws in Member States vary considerably in all areas. Individual forms of wills and succession agreements vary, as do the rules on forced heirship and reserved portions. Clawback or obligations to restore in states such as Italy last for the full lifetime of a donor and are enforceable rights in rem, while in Germany they are monetary claims and diminish by 10 per cent per annum and disappear after 10 years. Sweden and Austria have models of administration, while in France and Spain assets vest directly in the family heirs who can then be personally liable for the deceased’s debts even if greater than the value of the deceased’s assets. In addition, the private international law or conflicts of law rules (PIL) also varied considerably. Some Member States used connecting factors of habitual residence, while others used those of domicile. The majority used that of nationality.

While the EU has not sought to affect Member States’ internal substantive law, it has for many years been seeking to harmonise Member State PIL in this area. The Succession Regulation (EU) No. 650/2012 has finally entered into force. It became effective in all Member States (other than Denmark, Ireland and the United Kingdom) (the SR Zone) on 17 August 2015. In the SR Zone, the universal connecting factor is now that of habitual residence and the SR Zone Member State of habitual residence has universal jurisdiction. Renvoi has been abolished unless it is sending back into the SR Zone. A choice of national law (with no renvoi) is also permitted and a choice made prior to 2015 is still effective. Wills and succession agreements are now accepted throughout the SR Zone. The Succession Regulation also created the European certificate of succession (ECS) for use throughout the SR Zone. Recognition of the ECS, decisions of the Member State with jurisdiction and of clawback or

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obligations to restore throughout the SR Zone has changed the landscape for estate planning worldwide not only in relation to SR Zone nationals and residents, but also in relation to SR Zone situated assets for all individuals. There continues to be uncertainty as to whether Denmark, Ireland and the UK were included within the definition of a Member State for the purposes of the Succession Regulation. Winkler v Shamoon [2016] EWHC 217 (Ch) is an example of the effect that the Succession Regulation has had on other areas of law. For the purposes of Brussels I, ‘Succession’ has been interpreted extremely widely and included oral proprietary estoppel as a matter for the Succession Regulation and therefore outside the scope of other Regulations. If the UK leaves the EU, its relationship with the Succession Regulation will remain unchanged and it will continue to apply the Succession Regulation in accordance with its own private international law rules.

Similar issues also affect matrimonial property and matrimonial property regimes. The EU has an even more complex patchwork quilt of substantive laws and of PIL. Regimes vary from full community in the Netherlands, to limited community in other Member States and to marital gains in Germany. PIL is governed by the 1978 Hague Convention in France, Luxembourg and the Netherlands. In other Member States connecting factors can vary from that of nationality or residence and changes in these during a marriage sometimes do and sometimes do not produce a change, whether retroactive or not. France and Germany have agreed a new form of matrimonial regime that can be used in both countries. Again the EU did not propose to amend Member States’ substantive law but wished to legislate in order to harmonise Member States’ PIL. Rome IVa dealt with the property effects of marriage and Rome IVb with the property regimes for registered partnerships. Due to the significant differences in the recognition of same sex relationships throughout the EU, there was strong political opposition. The Visegrad Four of Hungary, Poland, Slovakia and Czech Republic have become increasingly more vocal and some of its members vetoed (as a family matter it required unanimous support) both Rome IVa and Rome IVb. In record time, the EU put in their place both the Regulations under the enhanced co-operation mechanism so that they have been adopted by all EU Member States (other than Croatia, Cyprus, Denmark, Estonia, Hungary, Ireland, Latvia, Lithuania, Poland, Slovakia or the UK) and will be fully effective from 2019. Rome IVa deals with the property rights of all married couples, whether mixed sex or same sex and similarly Rome IVb deals with the property effects of all registered partnerships whether mixed sex or same sex.

Although many practitioners consider that the issues involved in matrimonial property regimes do not concern them if the domestic law of their particular state does not use the concept, the England and Wales case of Slutsker v. Haron Investments Ltd13 is an example of PIL bringing such matters into play. They will continue to be of vital importance for international couples.

While the International Commission on Civil Status14 (ICCS/CIEC) has made proposals for a convention dealing with the recognition of registered partnerships, this has met with little support in the EU and the future of the ICCS seems less assured. The diversity of arrangements for the registration of marriage for same-sex couples, and for registered partnerships for same-sex and mixed-sex couples and for the recognition of such marriages and registered partnerships, cause considerable conflict. In many Member States such as Sweden, the Netherlands, Belgium, France, Spain and Portugal, marriage is available to both

mixed-sex and same-sex couples. The Marriage (Same Sex Couples) Act 2013 in England and Wales and the Marriage and Civil Partnership (Scotland) Act 2014 in Scotland recognised same-sex marriage from 2014. Ireland is also to introduce such legislation. The ability to convert a registered partnership to a marriage does create its own PIL problems. There appears to be no indication of any change in the law in Northern Ireland. In many states, one party must be a national or habitually resident in the particular Member State in order to register a marriage. In other Member States, such as Romania, Latvia and Lithuania, there are protection of marriage laws that make it unlawful for marriage to be other than between a man and a woman. In yet others such as Austria, the Czech Republic, Finland, Germany, Hungary, Ireland, Italy, Slovenia and Northern Ireland, registered partnerships are permitted. The Netherlands permits both marriages and registered partnerships for either same-sex or mixed-sex couples. The French PACS is a form of registered contract that is available to both same-sex and mixed-sex couples. The changes to the law in Scotland and in England and Wales do not permit mixed-sex registered partnerships. Thus, while Northern Ireland will recognise a same-sex marriage from another jurisdiction as a registered partnership and Scotland and England and Wales as a marriage, the United Kingdom will not recognise a mixed-sex Dutch registered partnership or French PACS as either a marriage or a civil partnership. Whether a Scottish, English or Welsh same-sex marriage between a couple, one of whom is domiciled in a state that does not recognise same-sex marriage, would be valid in the United Kingdom is uncertain. Adoption and recognition of surrogacy for same-sex couples is not available or recognised in many MS. It may be another generation before Member States substantive laws begin to converge sufficiently to permit some measure of harmonisation. However, Italy has now introduced the concept of a registered partnership. The impact of the United States Supreme Court decision in Obergefell v. Hodges\(^\text{15}\) of 26 June 2015 continues to reverberate in the US and around the world.

**VI MENTAL IMPAIRMENT**

As populations live longer, the problems for individuals with diminished mental capacity across borders are also growing. The Hague Convention 35 of 13 January 2000 on the International Protection of Adults (Hague 35) deals with the PIL issues of the recognition and enforcement and the applicable law of protective measures and the applicable law for private mandates. Hague 35 has already been ratified by Austria, the Czech Republic, Estonia, Finland, France, Germany, Monaco, Scotland and Switzerland.

Cyprus, Greece, Ireland, Italy, Latvia, Luxembourg, the Netherlands and Poland have all signed but not yet ratified. It is anticipated that Latvia may ratify during 2017 and Ireland in 2018. Portugal and Belgium are likely to accede shortly and Spain, Sweden and Italy are also now working towards ratification. Northern Ireland may also do so, using a similar model to Schedule 3 of MCA 2005 in Schedule 9 to the Mental Capacity Act (Northern Ireland) 2016. The changes to the internal law in Ireland and Northern Ireland will be significant.

For England and Wales there is considerable confusion since the Mental Capacity Act 2005 came fully into force on 1 October 2007 and gives full effect to the Convention notwithstanding the fact that England and Wales has not yet ratified.

The EU Parliament passed a further Resolution 2015/20185(INL), P8_TA(2017)0235 on 1 June 2017\(^\text{16}\) and this issue is likely to be on the EU programme during the next five years. Member States will be encouraged to ratify and further EU legislation is possible. Hague 35 is, however, not without its own problems and further developments are likely. The inherent conflicts in the UN Convention on the Rights of Persons with Disabilities (UN CRPD) between the protection of rights under Article 12 and the protection from abuse under Article 16 are probably impossible to square. It is argued that Hague 35 and the legislation of many states bound by UN CRPD are not compatible with it. The debate is one that will continue.

**VII WEALTH STRUCTURING AND REGULATION**

As a result of the lack of EU competence in the area of personal taxation, there are no vehicles to provide structures that are comprehended throughout the EU. Trusts, while recognised in Cyprus, Ireland, Italy (now increasingly less novel), Malta and the United Kingdom, are not recognised in many other Member States. The changes to French tax law in 2011 and the EU AML Directives have been a partial acceptance of trusts, but have not been welcomed. Belgium and Spain have followed France with similar moves. In many Member States, life insurance is given beneficial tax status, while structures such as usufructs or partnerships are also often used.

As mentioned above, Article 30 of the fourth Money Laundering Directive EU 2015/849 imposes obligations on trustees of express trusts. Pressure for public registers will continue. While seen as problematic, logically this should lead to further acceptance and enforcement of trusts in the long term.

**VIII CONCLUSIONS AND OUTLOOK**

Harmonisation of PIL in the EU is likely to continue. Free movement of EU nationals, goods, services and capital is still seen as an engine for growth, even though the EU is under pressure to legislate less. The role of the European Court of Justice will also continue to increase although in response to political trends, it may tend towards protecting national sovereignty against EU encroachment.

All Member States were focused on debt reduction and maximising tax collection. The EU institutions are conscious of the overwhelming priority to maintain the euro as a single currency and to concentrate on economic growth. As a result, the EU institutions are likely to be proactive in encouraging any OECD and FATF initiatives that might be perceived to increase revenue share. The eurozone perspective and priorities are likely to drive those Member States in the eurozone towards ever closer union. Some Member States still consider Anglo-Saxon light-touch regulation as principally to blame for the economic and banking crises developing particularly since 2008. Pressure for increased regulation is likely to continue.

Whether the process of the UK negotiating its exit from the EU will encourage some Member States to review the previous direction of travel for the EU and whether some Member States may themselves be encouraged to hold referenda or attempt to become more detached is not yet clear. It is perhaps more likely that the EU will become more homogenous, civil law focused and perhaps more protectionist, but the tensions between those Member States inside and outside the eurozone may well deepen.

Chapter 2

THE FOREIGN ACCOUNT TAX COMPLIANCE ACT

Henry Christensen III and Toni Ann Kruse

The Foreign Account Tax Compliance Act (FATCA), contained in Sections 1471 to 1474 of the US Internal Revenue Code (the Code), was enacted as part of the Hiring Incentives to Restore Employment Act in 2010. Final regulations under FATCA were adopted by the US Treasury on 17 January 2013, effective as of 28 January 2013 (the Regulations). On 12 July 2013 the Treasury postponed the effective date of FATCA’s withholding provisions by six months, from 1 January 2014 to 1 July 2014, as it continued to work with foreign governments in an effort to meet their requests for changes in the implementation rules. Withholding provisions became effective as planned on 1 July 2014. Reporting by certain financial institutions began on 31 March 2015 for the 2014 year.

FATCA was adopted with the principal purpose of preventing US persons from using foreign accounts and foreign entities to evade US tax on their assets deposited abroad. FATCA requires US payers, including US banks, brokers and companies, to withhold 30 per cent of certain ‘withholdable’ payments made to a foreign entity unless the entity qualifies for an exemption or is itself compliant with FATCA. The 30 per cent withholding rate is that which has historically been imposed on payments of interest, dividends, and other passive income by US payors to foreign persons, but until FATCA there were no withholding requirements on payments to foreign accounts of US persons. Payments made to foreign banks, brokers, investment advisers and other foreign financial institutions (FFIs) will have withholding imposed upon the full payments made to the FFI, even if most of the payment is allocable to foreign account holders, unless the FFI itself is exempt from withholding or, if not exempt, enters into an agreement with the Internal Revenue Service (IRS) to report on all US account holders. Payments made to non-financial foreign entities (NFFEs) with US owners are also subject to FATCA, with different reporting requirements than those imposed on FFIs. Essentially, FFIs report directly to the United States Treasury or to their own government, while NFFEs report to financial institutions. This chapter provides a general overview of FATCA as it relates to individuals and related entities (i.e., foreign trusts and foreign corporations owned by foreign trusts) that are deemed to be FFIs.

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1 Henry Christensen III and Toni Ann Kruse are partners at McDermott Will & Emery LLP. They acknowledge with thanks the assistance of their associate, Michael D Shapiro, in collecting 2017 developments regarding FATCA, so as to update this chapter.

OVERVIEW

Withholdable payments for purposes of FATCA generally include: (1) payments of US-sourced ‘fixed or determinable annual or periodic’ income, such as dividends and interest; (2) payments of the gross proceeds from a sale or disposition of property occurring after 31 December 2018 that can generate US-sourced interest or dividends; and (3) ‘foreign passthru payments’ made by certain FFIs. The withholding under FATCA can be draconian; in some cases, a foreign entity may not be entitled to a refund or credit of taxes withheld in excess of the entity’s actual liability for the tax. In order to avoid this, clients must take steps to qualify for an exemption or otherwise comply with the reporting requirements.

The requirements with which a foreign entity must comply to avoid FATCA withholding differ depending on whether the entity is classified for FATCA purposes as an FFI or an NFFE; and whether the entity is resident in or organised under the laws of a jurisdiction with which the United States has entered into an intergovernmental agreement (IGA). FFIs are generally subject to a higher compliance burden than NFFEs, and compliance obligations under the Regulations may be different from those under an IGA.

Under the Regulations, an FFI is any ‘financial institution’ that is a foreign entity. There are five types of ‘financial institutions,’ but the most relevant to this chapter is an ‘investment entity’. An investment entity includes an entity the gross income of which is primarily attributable to investing, reinvesting or trading in financial assets and which is managed by another entity that primarily conducts as a business on behalf of customers the activities of individual or collective portfolio management or otherwise investing, administering, or managing funds, money or financial assets on behalf of other persons. Generally, foreign trusts will be treated as FFIs.

The United States is offering foreign jurisdictions the opportunity to enter into one of two types of IGA that alter the compliance burdens under FATCA. In general, if the United States enters into an IGA with another country, the United States undertakes to give that country full financial disclosure concerning US accounts maintained by residents of that country in the United States, and, in certain cases, reciprocity for the financial institutions in that country giving financial disclosure to the United States Treasury on accounts maintained there by US account holders. The countries that enter into Model 1 IGAs (the Model 1 Countries) undertake to the United States to adopt internal reporting rules that replicate

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3 Treas. Reg. Section 1.1473-1. The Regulations do not define ‘foreign passthru payments’; further guidance will likely define the term to include foreign-sourced payments that are treated as derived from payments described in clauses (1) and (2) above. Deductions and withholding on foreign passthru payments made by a participating FFI to an account held by a recalcitrant account holder or to a nonparticipating FFI will not begin before the later of the publication of the Regulations of a definition of ‘foreign passthru payments’ and 1 January 2019. Treas. Reg. Section 1.1471-4(b)(4).
4 Treas. Reg. Section 1.1471-5(d).
5 See Treas. Reg. Section 1.1471-5(e).
FATCA, and to require FFIs in the jurisdiction to report information on US accounts and account holders to the tax authorities of the partner jurisdiction, which then agrees to automatically share all of the reported data with the United States Treasury on an annual basis. FFIs located in or organised under the laws of a jurisdiction that has adopted a Model 1 IGA are subject to the provisions of the IGA, rather than to the Regulations. The countries that enter into Model 2 IGAs (the Model 2 Countries) agree to amend their laws in order to require FFIs in their jurisdiction to report directly to the United States Treasury information on accounts maintained by US persons within the jurisdiction.

To avoid FATCA withholding on all payments of income made to it on all accounts it maintains which are made to it by US payers, an FFI generally needs to be treated as a ‘participating FFI’ (PFFI) or a ‘deemed-compliant FFI’ under the Regulations. There are a number of options available to FFIs to qualify for either type of category, including: (1) if subject to the Regulations or a Model 2 IGA, they can enter into an agreement with the IRS regarding reporting and withholding (known as an FFI Agreement) so as to qualify as a PFFI or, if subject to a Model 1 IGA, they can comply with local law so as to qualify as a ‘reporting Model 1 FFI’ (treated as an RDC FFI under the Regulations); (2) they can fulfil the requirements to be an ‘owner documented’ FFI and thus qualify as a deemed-compliant FFI under the Regulations; or (3) they can enter into an agreement with a ‘sponsoring

8 See Treas. Reg. Sections 1.1471-2(a)(1), 1.1471-2(a)(4). ‘Deemed-compliant FFIs’ include registered deemed-compliant FFIs (RDC FFIs), certified deemed-compliant FFIs (CDC FFIs), non-reporting IGA FFIs, and owner-documented FFIs. FFIs that satisfy the requirements for one of these categories are considered ‘deemed-compliant’ because they comply with FATCA without entering into an FFI agreement with the IRS. The overarching difference between RDC FFIs and CDC FFIs is that RDC FFIs must register with the IRS, whereas CDC FFIs need only certify their FATCA compliance to each withholding agent. See Treas. Reg. Sections 1.1471-5(f)(1), 1.1471-5(f)(1)(ii)(A), 1.1471-5(f)(2).

There has been some question as to whether foreign grantor trusts that are FFIs need to become PFFIs or deemed-compliant FFIs or whether the payer can look through the grantor trust to its owner. Under Treas. Reg. Section 1.1471-3(a)(3)(ii)(B), it appears that a grantor trust (as a ‘flow-through entity’) that does not become a PFFI or deemed-compliant FFI will be treated as a ‘payee’ by withholding agents and will thus be subject to withholding under FATCA. More clarity on this subject has been requested from Treasury by practitioners.


10 See Treas. Reg. Sections 1.1471-1(b)(91), 1.1471-1(b)(114). If an FFI is a member of an affiliated group of entities (such as a chain or corporations and trusts connected through greater than 50 per cent ownership), the FFI generally cannot qualify as a PFFI or RDC FFI unless each other FFI in the group is a PFFI or RDC FFI. See also Treas. Reg. Sections 1.1471-1(b)(92), 1.1471-4(e)(1). There are limited exceptions to this rule, however, many of these exceptions became unavailable after 31 December 2016. See Treas. Reg. Sections 1.1471-4(e)(2); 1.1471-4(e)(3). On the other hand, if a member of an affiliated group is a holding company, it may be excluded entirely from the definition of an FFI and therefore may not need to comply with the requirements described herein to avoid FATCA withholding. See Treas. Reg. Section 1.1471-5(e)(5)(iv). For a holding company to be so excluded, it generally cannot maintain any financial accounts or receive payments from a withholding agent other than a member of its affiliated group. The IRS FATCA registration form (Form 8957) seems to contemplate that an affiliated group of FFIs will designate a ‘lead’ entity and that the registration of all entities in the affiliated group will be linked through this lead.

11 Treas. Reg. Sections 1.1471-2(a)(4)(iv), 1.1471-3(d)(4), (6). This option is available to an FFI subject to the Regulations. While not entirely clear, it may also be available to an FFI subject to a Model IGA.
The Foreign Account Tax Compliance Act

entity’ for the latter to comply on behalf of the FFI and other FFIs (for example, for all of a family’s foreign trusts) and thus qualify either as an RDC FFI or a CDC FFI under the Regulations.¹²

II TRUSTS AS FOREIGN FINANCIAL INSTITUTIONS AND TRUST BENEFICIARIES AS US REPORTABLE ACCOUNT HOLDERS

There are significant arguments that a foreign trust should be treated as an NFFE, not an FFI, and the author argued for this position with Ellen Harrison on behalf of the American College of Trust and Estate Counsel (ACTEC), with the draftsmen of the Regulations at the Treasury Department. Under the Code, a ‘foreign financial institution’ is a foreign entity that: (1) accepts deposits in the ordinary course of a banking or similar business; (2) as a substantial portion of its business, holds financial assets for the account of others (that is, acts as a custodian); or (3) is engaged primarily in the business of investing, reinvesting, or trading in securities, partnership interests, commodities or any interest in the same. ACTEC argued that in all events an individual trustee wasn’t an ‘entity’, that no trustee could meet the definitions of (1) or (2), and that as to (3), trustees were investing their own money, not that of others. Treasury tried to meet these reasoned objections, and to a considerable extent did so, but most large foreign trusts will be treated as FFIs under the Regulations, because all foreign trusts with corporate trustees acting for different customers will be FFIs,¹⁴ as will individual trustees or private trust companies (PTCs) that retain any outside investment advisers.¹⁵ In the authors’ experience foreign trusts are usually better advised to treat themselves as FFIs, and do their own reporting, rather than as NFFEs (see discussion of alternative reporting methods below), where the depository financial institutions will determine the scope of reporting. The Regulations are not clear as to their treatment of PTCs which do all their own investing and retain no professional advisers, but we think such PTCs are rare.

To be compliant with FATCA, a foreign trust that is treated as an FFI must undertake to perform due diligence so as to obtain all requisite information on its ‘account holders’ (beneficiaries), including ‘Chapter 4 status’ of the account holder (that is, is the account holder a US person for tax purposes or a non-US person), name, address, taxpayer identification number, account balance, and distributions made to any US person during the preceding tax year. Under the Regulations, a person is deemed to hold an interest in a foreign trust if he or she has mandatory interest in the trust,¹⁶ or received a distribution in the preceding year.¹⁷ Guidance notes and draft guidance notes in some partner jurisdictions provide clarification on whether a trust beneficiary is a US Reportable Account holder.

Under the FATCA Regulations, a US discretionary beneficiary of a US trust that is a financial institution is only a reportable account holder in the trust if the beneficiary actually receives distributions in a given year (referred to in the Regulations as holding an ‘equity

¹² Treas. Reg. Sections 1.1471-2(a)(4)(iv), 1.1471-3(d)(4), (5). This option is available to an FFI subject to the Regulations or an IGA.
¹³ Code Sections 1471(d)(4)-(5).
¹⁴ See Treas. Reg. Section 1.1471-5(e).
¹⁵ Id.
interest’). ACTEC urged this position on US Treasury, and it was adopted in the Regulations. Yet as discussed above in Section I, FFIs subject to IGAs may be subject not to compliance methods as stated in US Treasury Regulations, but rather to those stated in the relevant IGA. In the Cayman Islands, guidance notes released in December 2014 and last updated 1 July 2015 state that the definition of ‘equity interest’ used in the Treasury Regulations may also be used under the Cayman-US IGA. The British Virgin Islands released guidance notes in March 2015 with a similar distribution requirement for an ‘equity interest’. Guernsey’s draft guidance notes use the same definition, as do Jersey’s, the Isle of Man’s, Ireland’s and Singapore’s. South Africa’s guidance notes take a broader approach, noting in the definition of ‘equity interest’ that a Specified US Person will only be treated as a beneficiary of a foreign trust if the person has the right to receive, directly or indirectly, a mandatory distribution, or may receive, directly or indirectly, a discretionary distribution. Mauritius and India’s Guidance Notes use the same definition as South Africa’s. It is important that each trust and financial institution determines which IGA controls it, and what definitions apply under that IGA.

III PARTICIPATING FOREIGN FINANCIAL INSTITUTIONS AND REPORTING MODEL 1 FOREIGN FINANCIAL INSTITUTIONS

Generally, FFIs that choose to comply with FATCA as a PFFI (if covered by the Regulations because the country in which the FFI is located has a Type 2 IGA with the United States or has no IGA) or a reporting Model 1 FFI (if covered by a Model 1 IGA) should register their

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28 Gov’t of India Ministry of Fin. Dep’t of Rev., ‘Guidance Note on FATCA and CRS’, released May 2016, Paragraph 3.5.1.
status as such with the IRS. An FFI will be able to register with the IRS through the FATCA registration portal, a secure website. In addition to registering, this portal will allow an FFI to manage its registration information and, as necessary, agree to perform the due diligence, reporting and withholding requirements described herein (in other words, enter into an FFI Agreement). Upon registering, the FFI will receive a GIIN, which it will provide to withholding agents to identify itself as a PFFI (or reporting Model 1 FFI) and avoid FATCA withholding. In our view, all foreign trusts will want to have or report under a GIIN.

To be treated as a PFFI, an FFI covered by the Regulations will be required to enter into an FFI Agreement pursuant to which it must agree to take steps to identify its ‘US accounts’, report certain information to the IRS with respect to its US accounts and withhold 30 per cent of certain payments made to individuals or entities that fail to comply with FATCA (so called ‘recalcitrant account holders’).

Under its FFI Agreement, an FFI will be required to obtain information necessary to identify its ‘US accounts’. A US account is a financial account maintained by an FFI that is held by one or more specified US persons or US-owned foreign entities. An equity interest in an FFI is generally treated as a financial account maintained by that FFI. The PFFI will then make annual reports to Treasury on amounts distributed to US account holders.

See the preamble to the Regulations. Although it is not entirely clear whether a reporting Model 1 FFI is required to register with the IRS to comply with FATCA, we advise such FFIs to register in order to obtain a global intermediary identification number (a GIIN) and to safely avoid being the subject of certain due diligence and reporting requirements and being subject to FATCA withholding. See Treas. Reg. Sections 1.1471-2(a)(4)(iv), 1.1471-3(d)(4)(i); Model 1 IGA, Annex 1, Paragraph IV(D)(2)(b), V(B)(1). Form 8957, which may be used by an FFI to register with the IRS, also suggests that a Model 1 FFI should register. Additionally, the IRS FATCA Online Registration User Guide states that ‘FIIs that are treated as reporting FIs under a Model 1 IGA ... should register as RDCFIs’. Publication 5118 (Rev. 06-2017), Section 2.4: Special Rules for Registration, available at http://www.irs.gov/pub/irs-pdf/p5118.pdf. A reporting Model 1 FFI will not enter into an FFI Agreement but will instead be required to comply with certain requirements pursuant to local law.

See Treas. Reg. Section 1.1471-1(b)(57). A specified US person is generally, any US person other than a publicly traded corporation, a tax exempt charity, the United States government or an agency thereof, or a bank. Treas. Reg. Section 1.1473-1(c). For the definition of a US-owned foreign entity, see the discussion below.

An equity interest in an FFI that is not an ‘investment entity’, however, is treated as a financial account only in certain circumstances. See Treas. Reg. Section 1.1471-5(b)(1)(iii). An investment entity generally (1) is in the business of investing, administering, or managing funds on behalf of others; or (2) generates 50 per cent or more of its income from investing, reinvesting or trading its financial assets and is professionally managed. See Treas. Reg. Section 1.1471-5(e)(4)(i). Most professionally managed trusts will be investment entities.

A PFFI will be required to annually report to the IRS using Form 8966: FATCA Report. Generally, such report should include (1) the name, address and tax identification number of each US account holder; (2) the account number (if relevant); (3) the account balance or value of the account; (4) the payments made with respect to the account during the calendar year; and (5) any other information required pursuant to the instructions of Form 8966.
Under the Regulations, a PFFI must deduct and withhold 30 per cent from certain payments it makes to a ‘non-participating FFI’ or to a ‘recalcitrant account holder’.  

i  Foreign financial institutions covered by a Model 1 IGA
An FFI resident in or organised under the laws of a Model 1 Country will generally be covered by a Model 1 IGA. Similar to the Regulations, an FFI covered by a Model 1 IGA will be subject to specific due diligence and reporting requirements based on whether it maintains accounts held directly by US persons (e.g., a foreign trust with US beneficiaries or, in the case of a grantor trust, a US deemed owner) or maintains accounts held by other foreign entities owned by US persons (e.g., a foreign holding company owned by a foreign trust with US beneficiaries or a US owner).

ii  Foreign financial institutions covered by a Model 2 IGA
To be treated as a PFFI, an FFI covered by a Model 2 IGA will be required to comply with the due diligence and reporting requirements of an FFI agreement, except to the extent modified by the terms of the Model 2 IGA.

The terms of the Model 2 IGA do not modify the due diligence and reporting requirements described in the Regulations as they apply to an FFI that is a foreign trust. The trust will be required to compile and report to the IRS information about its US owner (if it is a foreign grantor trust deemed owned by a US person), and about its US beneficiaries only to the extent that the beneficiaries are entitled to mandatory distributions or actually receive discretionary distributions.

IV  OWNER-DOCUMENTED FOREIGN FINANCIAL INSTITUTIONS
An FFI may be able to comply with FATCA by becoming an ‘owner-documented FFI’ (ODF). An ODF does not need to register with the IRS. Rather, the burden of providing information about the US owners and beneficiaries of an ODF is shifted to institutions with which the ODF has accounts and entities in which the ODF owns interests. The ODF approach may be of limited application to foreign trusts.

38 Treas. Reg. Section 1.1471-4(b)(1). A non-participating FFI is generally an FFI that is not a PFFI or a deemed-compliant FFI (including a registered deemed-compliant FFI). Treas. Reg. Section 1.1471-1(b)(82). A recalcitrant account holder is a holder of an account maintained by an FFI who is not himself or herself an FFI and who fails to comply with requests by the FFI for documentation or information the FFI is required to obtain pursuant to FATCA Treas. Reg. Section 1.1471-5(g)(2). Withholding on ‘pass-through payments’ (i.e., any withholdable payment or other payment to the extent attributable to a withholdable payment) will begin no earlier than 1 January 2019. Treas. Reg. Section 1.1471-4(b)(4).

39 See Model 1 IGA, Article 1, Paragraph 1(b).

40 See Model 2 IGA, Article 1, Paragraph 1(v), Article 2, Paragraph 1(a); Treas. Reg. Section 1.1471-4(a). Similar to an FFI covered by a Model 1 IGA, an FFI covered by a Model 2 IGA that is a trust is treated as complying with the terms of the IGA if the trustee of the trust is itself a PFFI under the Regulations or an FFI in compliance with the requirements of an IGA. See Model 2 IGA, Annex II, Paragraph IV(A).

41 See Model 2 IGA, Article 2, Paragraph 1(t), (v), Annex 1.

42 See Model 2 IGA, Article 1, Paragraph 1(s), (ee); Treas. Reg. Sections 1.1473-1(b)(3). Under the Model 2 IGA, the trust will also be required to obtain consent from the beneficiaries to report their information to the IRS. See Model 2 IGA, Article 2, Paragraph 1(b), (d).

43 See generally Treas. Reg. Section 1.1471-5(f)(3).
i Owner-documented foreign financial institutions under the Regulations

The ODF option is available only with respect to payments an FFI receives from and accounts held with a US financial institution, a PFFI or a reporting Model 1 FFI that agrees to undertake due diligence and reporting requirements on behalf of the ODF (a designated withholding agent).44

To qualify as an ODF, an FFI will be required to provide the designated withholding agent with information about its foreign and US owners, which in the case of an FFI that is a trust, includes information about its foreign and US beneficiaries, to the extent that its beneficiaries are entitled to mandatory distributions or may receive, and actually do receive, discretionary distributions.45 This option may be unattractive in view of the extent of information about owners and beneficiaries that an ODF will generally be required to disclose and, perhaps more troublesome to some trustees, the information will be disclosed to institutions and other designated withholding agents, rather than to the IRS.

As an alternative to providing designated withholding agents with information about its US and foreign owners, an ODF may provide a letter (an auditor’s letter) from an accounting or law firm in the United States. The auditor’s letter will generally be required to certify that the firm or a representative of the firm has reviewed the ODF’s documentation with respect to all of its owners or beneficiaries.46 In addition to the auditor’s letter, the ODF must continue to provide the designated withholding agents with information regarding its US owners or beneficiaries.47

ii Owner-documented foreign financial institutions under the Model IGAs

It is unclear whether FFIs covered by the Model IGAs can comply with FATCA by meeting the requirements of an ODF. While the Model IGAs make no specific provision for ODFs, they suggest that a foreign entity that meets the requirements of a deemed-compliant FFI under the Regulations will be treated as complying with FATCA notwithstanding that the entity is subject to a Model IGA rather than the Regulations.48

V SPONSORED FOREIGN FINANCIAL INSTITUTIONS

The sponsored entity categories allow an FFI that meets certain requirements to enter into an agreement with another entity (the sponsoring entity) under which the sponsoring entity will

47 Id. This alternative may be useful to an FFI that prefers to provide information about its foreign owners or beneficiaries to a trusted accounting or law firm rather than the institutions in which it invests. Its usefulness is limited by the requirement that the FFI continue to provide information about its U.S. owners or beneficiaries to such institutions.
48 See Article 4, Paragraph 4 of the Model 1 IGA, which requires the United States to treat Non-Reporting [FATCA Partner] Financial Institution as complying with (or exempt from) FATCA. See also Article 1, Paragraph 1(q) of the Model 1 IGA, which defines a non-reporting [FATCA partner] financial institution to include an FFI covered by the Model 1 IGA ‘that otherwise qualifies as a deemed-compliant FFI… under relevant US Treasury Regulations…’ See identical provisions in the Model 2 IGA, Article 1, Paragraph 1(p) and Article 3, Paragraph 4.
fulfil the sponsored FFI’s due diligence, withholding and reporting obligations on its behalf. For many foreign trust groups, it may be attractive to select one sponsoring entity to report on behalf of all entities in the group.

i  Sponsored foreign financial institutions under the Regulations

The Regulations include provisions regarding sponsored FFIs within each of the broader RDC FFI and CDC FFI categories: the RDC FFI rules provide for ‘Sponsored Investment Entities’,49 whereas the CDC FFI rules allow for ‘Sponsored, Closely Held Investment Vehicles’.50 The rules regarding sponsored investment entities and sponsored, closely held investment vehicles are very similar. Only an investment entity that is not a qualified intermediary (QI), withholding partnership (WP) or withholding trust (WT) can be a sponsored entity.51

The sponsoring entity must be authorised to act on behalf of the FFI to fulfill all due diligence, withholding and reporting responsibilities that the FFI would have assumed if it were a PFFI.52 The sponsored entity provisions under the IGAs also require that the sponsoring entity be authorised to act on behalf of the FFI to fulfill its FATCA compliance obligations. Under the Regulations, the only potential sponsoring entity for a foreign trust that is covered by the Regulations is a trustee that is a private trust company or an institutional trustee, such that a trustee of a group of related trusts could sponsor all of them.

The sponsored and sponsoring entity must have an agreement that the sponsoring entity will undertake FATCA obligations on behalf of the sponsored entity. Under the provisions for sponsored investment entities and sponsored closely held investment vehicles, the sponsoring entity must ‘agree’ to undertake these obligations.53 The sponsoring entity must be registered with the IRS as a sponsoring entity.54

ii  Sponsored entities under the IGAs

Both the Model 1 and Model 2 IGAs create sponsored entity mechanisms very similar to those under the Regulations. Under the Model 1 IGA, a sponsoring entity reports to the FATCA partner country on behalf of the sponsored entity, rather than to the IRS. Apart from some differences in the terminology,55 the provisions under the Model 1 and 2 IGAs regarding sponsored entities are nearly identical.

51 Treas. Reg. Sections 1.1471-5(f)(1)(i)(F)(1)(i), 1.1471-5(f)(2)(iii)(A). The definitions of QIs, WPs and WTs under the Regulations (see Treas. Reg. Section 1.1471-1(b)(107), (149) and (151), respectively) direct the reader to the definitions of such persons/entities as set forth in the regulations for Code Section 1441. See Treas. Reg. Sections 1.1441-1(c)(5)(ii), 1.1441-5(c)(2)(ii) and 1.1441-5(e)(5)(v). Generally, QIs, WPs and WTs are defined as such by virtue of having entered into a withholding agreement with the IRS.
55 Because the Model 2 IGA generally makes use of the terms used in the Regulations, and the Model 1 IGA creates many of its own terms, certain of the terms in the rules in each IGA are different, though they generally have similar meanings.
**Sponsored entities under the Model 1 IGA**

Under the Model 1 IGA, the United States agrees to treat each 'non-reporting [FATCA partner] financial institution as a deemed-compliant FFI or as an exempt beneficial owner' and such entities will be exempt from withholding.56 Annex II of the Model 1 IGA includes three categories of ‘deemed-compliant FFIs’57 among the entities identified as non-reporting FATCA partner financial institutions that are of interest. First, Annex II creates an entirely new category entitled ‘Trustee-Documented Trust’,58 under which a trustee that is a FATCA-compliant entity can comply on behalf of a trust. Annex II additionally contains a ‘Sponsored Entity and Controlled Foreign Corporation’ category and a ‘Sponsored, Closely Held Investment Vehicle’ category, each of which is very similar to the parallel category in the Regulations.59

For a trust to qualify as a deemed-compliant FFI (and therefore a non-reporting financial institution) under this category, the following requirements must be met: (1) the trust must have been established under the laws of the FATCA partner jurisdiction at issue; (2) the trustee of the trust must be a reporting US financial institution,60 a reporting Model 1 FFI or a PFFI; and (3) the trustee of the trust must report all information required to be reported pursuant to the IGA with respect to all US reportable accounts61 of the trust.

As is the case under the Regulations, only an investment entity established in the FATCA partner jurisdiction that is not a QI, WP or WT can be a sponsored entity.62 The sponsored entity must have an agreement with another entity that the latter will act as sponsoring entity for the sponsored entity.63

The sponsoring entity must be authorised to act on behalf of the sponsored entity to fulfil all registration requirements.64

The sponsoring entity must register as such pursuant to applicable registration requirements on the IRS website.65

The sponsoring entity must agree to perform, on behalf of the sponsored entity, all due diligence, withholding, reporting and other requirements that the sponsored entity would have been required to perform if it were a reporting financial institution.66

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56 Model 1 IGA, Article 4, Paragraph 4.
57 Note that the Model 1 IGA does not explicitly distinguish between ‘registered deemed-compliant FFIs’ and ‘certified deemed-compliant FFIs.’
58 See Model 1 IGA, Annex II, Paragraph IV(A).
59 See Model 1 IGA, Annex II, Paragraphs IV(B), IV(C).
60 A ‘Reporting U.S. Financial Institution’ is (1) any financial institution that is resident in the United States, but excluding any branch of such financial institution that is located outside the United States; and (2) any branch of a financial institution not resident in the United States, if such branch is located in the United States, provided that the financial institution or branch has control, receipt, or custody of income with respect to which information is required to be exchanged under subparagraph (2)(b) of Article 2 of the Model 1 IGA. See Model 1 IGA, Article 1, Paragraph 1(p).
61 A ‘U.S. Reportable Account’ is a financial account maintained by a reporting [FATCA partner] financial institution and held by one or more specified US persons or by a non-US entity with one or more controlling persons that is a specified US person. See Model 1 IGA, Article 1, Paragraph 1(cc).
62 See Model 1 IGA, Annex II, Paragraphs IV(B)(1), IV(C)(1).
63 See Model 1 IGA, Annex II, Paragraphs IV(B)(1), IV(C)(2).
64 See Model 1 IGA, Annex II, Paragraphs IV(B)(3)(a), IV(C)(2).
The sponsoring entity must identify the sponsored entity (including, in the case of a sponsored investment entity, the identifying number of the sponsored entity, obtained by following applicable registration requirements) in all reporting completed on the sponsored entity's behalf.67

The sponsoring entity must register the sponsored entity pursuant to applicable registration requirements, but only if the sponsoring entity identifies any US reportable accounts with respect to the sponsored entity.68 The sponsoring entity must be a reporting US financial institution, a reporting Model 1 FFI or a PFFI.69 The sponsored entity must not hold itself out as an investment vehicle for unrelated parties.70 Twenty or fewer individuals must own all of the debt and equity interests in the sponsored entity (disregarding certain interests).71

**Sponsored entities under the Model 2 IGA**

The provisions of the Model 2 IGA regarding deemed-compliant FFIs are virtually identical to those of the Model 1 IGA, though, of course, a sponsoring entity under the Model 2 IGA would report to the IRS on behalf of a sponsored entity rather than to the Model 2 jurisdiction government. The Model 2 IGA also specifically denotes which deemed-compliant entities are considered ‘registered deemed-compliant’ and which are considered ‘certified deemed-compliant’ (sponsored investment entities are considered the former, trustee-documented trusts and sponsored, closely held investment vehicles the latter).

**VI ELECTING FFI V. NFFE STATUS**

A number of US tax advisers have urged foreign trusts that seem to have a choice, as many do, to elect to be treated as NFFEs, rather than FFIs. This choice may be available, for example, to a private trust company in an offshore jurisdiction that acts as a trustee for a number of trusts for a single family, and manages all of the investments itself. Under the Regulations, it could claim status as an NFFE, not an FFI, on the basis that its investments are not professionally managed.72 While initially appealing, we have concluded that this position is ultimately not the most desirable, for two reasons. First, it requires taking the position that a family's PTC is not 'professional' in its investment management, a position that ultimately could prove disadvantageous in other contexts. Second, because the Regulations provide that US beneficiaries of foreign trusts that are FFIs only have to be disclosed to the extent they receive distributions, we believe status as an FFI is not intrusive, versus if the foreign trust is treated as an NFFE it must disclose whatever the US financial institution making distributions requires it to disclose.73

67 See Model 1 IGA, Annex II, Paragraphs IV(B)(3)(e), IV(C)(5)(c).
69 See Model 1 IGA, Annex II, Paragraph IV(C)(2).
70 See Model 1 IGA, Annex II, Paragraph IV(C)(3).
71 See Model 1 IGA, Annex II, Paragraph IV(C)(4).
73 See Treas. Reg. Section 1.1472-1(e).
VII IMPLEMENETATION

The FATCA registration portal opened in early 201474 and FATCA withholding and account due diligence requirements began on 1 July 2014. The deadline for sponsored entities to be registered by their relevant sponsoring entities was 1 January 2017.75 Since 31 March 2015, FFIs have been required to report to the IRS annually, via the IRS FATCA registration website, on certain US persons or entities that hold interests in or accounts with such FFIs.

Participating countries

As of July 2017, 97 countries have entered into IGAs with the United States and 16 additional countries have reached agreements but have not yet signed.76 The following jurisdictions have signed IGAs with the United States:

Model 1 IGA

Algeria, Angola, Anguilla, Antigua and Barbuda, Australia, Azerbaijan, Bahamas, Bahrain, Barbados, Belarus, Belgium, Brazil, British Virgin Islands, Bulgaria, Cambodia, Canada, Cayman Islands, Colombia, Costa Rica, Croatia, Curaçao, Cyprus, Czech Republic, Denmark, Dominican Republic, Estonia, Finland, France, Georgia, Germany, Gibraltar, Greece, Greenland, Grenada, Guernsey, Guyana, Holy See, Honduras, Hungary, Iceland, India, Ireland, Isle of Man, Israel, Italy, Jamaica, Jersey, Kosovo, Kuwait, Latvia, Liechtenstein, Lithuania, Luxembourg, Malta, Mauritius, Mexico, Montenegro, Montserrat, Netherlands, New Zealand, Norway, Panama, Philippines, Poland, Portugal, Qatar, Romania, Saudi Arabia, Singapore, Slovak Republic, Slovenia, South Africa, South Korea, Spain, St. Kitts and Nevis, St. Lucia, St. Vincent and the Grenadines, Sweden, Thailand, Trinidad and Tobago, Turkey, Turks and Caicos Islands, Ukraine, United Arab Emirates, United Kingdom, Uzbekistan and Vietnam.

Model 2 IGA

Austria, Bermuda, Chile, Hong Kong, Japan, Macao, Moldova, San Marino, Switzerland and Taiwan.77

Additionally, as of July 2017, the following jurisdictions have reached agreements in substance with the United States:

Model 1 IGA

Cabo Verde, China, Dominica, Haiti, Indonesia, Kazakhstan, Malaysia, Peru, Serbia, Seychelles, Tunisia and Turkmenistan.

Model 2 IGA

Armenia, Iraq, Nicaragua and Paraguay.

77 Consistent with the Taiwan Relations Act, the parties to the agreement are the American Institute in Taiwan and the Taipei Economic and Cultural Representative Office in the United States. Id.
ii ‘Nil reporting’

Some countries require FFIs with no ‘reportable US persons’ holding accounts to register and report the mere existence of the FFI with the partner government. This practice is referred to as ‘nil reporting’. As applied to a trust, a ‘nil report’ would include nominal information such as the trust’s name. ‘Nil reporting’ is required in Guernsey,78 Ireland,79 Malta,80 Mauritius,81 Malaysia,82 Singapore83 and South Africa84 at this time. Nil returns are definitively not required in the British Virgin Islands,85 Canada,86 the Cayman Islands,87 Isle of Man,88 Jersey,89 France,90 Australia91 and the United Kingdom.92 The US requires nil reporting by

80 ‘Guidelines for the implementation of the FATCA Agreement and the FATCA Regulations in Malta issued in terms of Article 96(2) of the Income Tax Act (Chapter 123 of the Laws of Malta)’, revised 29 July 2014, Section 2.18. Section 3.3 of the Malta Guidelines exempt a trust that does not have a US Reportable Account from nil reporting.
82 ‘Compliance Requirements for Malaysia-US Intergovernmental Agreement on Foreign Account Tax Compliance Act (FATCA)’, draft dated 11 September 2015, Sections 8.9.2, 9.2.4, 11.1.2.
87 ‘Guidance Notes on the International Tax Compliance Requirements of the Intergovernmental Agreements between the Cayman Islands and the United States of America and the United Kingdom’, revised 1 July 2015, Section 17.3.
direct reporting NFFEs and by sponsoring entities reporting on behalf of a sponsored direct reporting NFFE, which must file Form 8966 to declare that it has no substantial US owners for the calendar year.\textsuperscript{93}

iii Deadline fluctuation

FATCA reporting was initially scheduled to begin in 2015 and many jurisdictions began reporting in 2015, including Australia,\textsuperscript{94} British Virgin Islands,\textsuperscript{95} Ireland,\textsuperscript{96} Singapore,\textsuperscript{97} and South Africa.\textsuperscript{98} Many other countries, however, extended their FATCA reporting deadlines in order to accommodate logistical issues with reporting portals. In June 2015 alone, eight countries\textsuperscript{99} extended their FATCA reporting deadlines. To accommodate these logistical hurdles, in October 2015, the IRS extended the deadline for certain FFIs covered by an IGA as long as the ‘jurisdiction is making good faith efforts to exchange the information as soon as possible’.\textsuperscript{100} Belgium, for example, implemented FATCA reporting in 2016\textsuperscript{101} and Italy implemented it in 2017.\textsuperscript{102}

In October 2015, the IRS also extended several other dates and deadlines.\textsuperscript{103} Withholdings on payments of gross proceeds and passthru payments will not begin until the later of either the publication in the Regulations of a definition of ‘foreign passthru payments’ or 1 January 2019.\textsuperscript{104} The registration deadline for sponsored entities was extended until 1 January 2017 and finally, any limited FFI or limited branch status set to expire on 31 December 2015 did not expire until 31 December 2016.\textsuperscript{105}

In August 2016, the IRS announced that on 1 January 2017 it would begin treating jurisdictions that have not brought their IGA into force as not having an IGA in effect,

\textsuperscript{96} Revenue, ‘Guidance Notes on the Implementation of FATCA in Ireland,’ issued 30 June 2017, Chapter 4, Paragraph 10.
\textsuperscript{99} In June 2015 alone, the following countries extended their FATCA reporting deadlines: Ireland, Vietnam, the Cayman Islands, the Channel Islands, Malta, Luxembourg, British Virgin Islands and United Arab Emirates.
\textsuperscript{102} Italy: FATCA reporting deadline extended, KPMG (28 Mar., 2017).
\textsuperscript{104} Treas. Reg. Section 1.1471-4(b)(4).
unless the jurisdiction provided, by 31 December 2016, a detailed explanation of why the jurisdiction had not yet brought the IGA into force and a step-by-step plan that the jurisdiction intends to follow to bring the IGA into force.106

iv Reporting portals

The IRS opened the FATCA Online Registration System in 2014 and continues to update both the website and the registration process.107 Upon registration and receipt of a GIIN, FFIs are added to the IRS FFI list that includes all other registered financial institutions and entities. This list is available online in order to facilitate FATCA implementation.108 As reporting increases in subsequent years, FFIs and other entities will begin filing Forms 8966 through the International Data Exchange Service, a private service available through the IRS website.109 For additional guidance on how to populate the electronic form, the IRS published its revised FATCA XML v2.0 User Guide in April 2017.110

VIII COMMON REPORTING STANDARD

The implementation of FATCA in the United States has influenced other countries to implement similar legislation in their own jurisdictions. The United Kingdom was the first country to do so, enacting legislation that aimed to obtain information from the Crown Dependencies (i.e., the Isle of Man, Guernsey and Jersey) and the British Overseas Territories (i.e., the Cayman Islands, the British Virgin Islands, Bermuda, Anguilla, Turks and Caicos Islands, Montserrat and Gibraltar), commonly referred to as UK FATCA.111 In early 2014, the OECD announced an information exchange policy called the ‘Standard for Automatic Exchange of Financial Account Information: Common Reporting Standard’ (Common Reporting Standard).112 The United Kingdom worked closely with the OECD in developing

106 I.R.S. Announcement 2016-17, 2016-33 I.R.B. 238. The IRS maintains a list of jurisdictions that are treated as if they have an IGA in effect at https://www.treasury.gov/resource-center/tax-policy/treaties/Pages/FATCA.aspx.
the Common Reporting Standard, which will replace UK FATCA in 2018.\footnote{113} The Common Reporting Standard is in large part based upon FATCA, but has significant differences. It has been adopted by other nations, without the withholding tax hammer used in FATCA, as part of a worldwide effort to accomplish transparency of income earned by residents of one country in another country. This measure has been approved by the G20 and has 101 signatory jurisdictions as of June 2017 that desire to automatically exchange tax information.\footnote{114} The information exchange began in 2017 for 50 countries.\footnote{115}


NOTES ON THE TAXATION OF WORKS OF ART IN THE UNITED KINGDOM

Ruth Cornett

I INTRODUCTION

Ownership of works of art has long been a feature of the international private client. In the UK the art market services international clientele and attracts dealers and collectors from across the globe. A significant boom took place between 2010 and 2015 with a market correction in 2016 but in 2017 there is evidence that the market is recovering and that confidence in art remains resilient. From the start of the credit crisis in September 2008, the growth across this international asset class has been enormous and London especially has benefited from this surge of interest. Many collectors who may have initially acquired works of art purely for pleasure witnessed their acquisitions become a significant proportion of their net wealth and, with this in mind, other collectors entered the market seeking to spread their class of investments; whether this will continue cannot be certain, but for the moment, at least the fiscal policy has remained largely the same. Since the result of the June 2016 UK referendum on membership of the European Union there has been speculation about the impact on the art market, but no changes to the current rules or policies have been announced at the time of writing.

UK government policy generally is in favour of the arts and heritage. The importance of the art, culture and heritage industries for the UK economy is widely promoted and has been recognised in some favourable tax treatments (see below). Nevertheless, the importance of establishing the correct ownership structure must be the first consideration for collectors and it is useful to have in mind the ultimate destination for any collection when deciding how it should be owned, whether that is a legacy to the next generation, a bequest to a museum or, in due course, a sale.

1 Ruth Cornett is the director of the Heritage and Taxation Advisory Service at Christie’s.
3 See, for example, the reported drop in the sale results of both Sotheby’s and Christie’s in the first half of 2016, with results dropping by approximately 27 per cent.
4 Christie’s auction sales results for the first half of 2017 showed a 29 per cent increase over the same period in 2016, with sales overall of £2.35 billion.
5 The contemporary art 100 index for the period from September 2008 to June 2015 reported a 33.3 per cent rise in prices for paintings, but by June 2016 this had stabilised.
6 See, for example, the policy document ‘Heritage Means Business’ launched by the UK Historic Houses Association (HHA) in March 2014 and the HHA’s own survey of members in 2015. The HHA’s 2015 survey estimated that visits to historic houses and gardens in private ownership exceeded 24 million per annum.
The United Kingdom does not maintain a general register of chattels, although the UK’s tax collecting and administration agency, HM Revenue and Customs (HMRC), does keep a register of works of art that are conditionally exempt from inheritance tax (IHT); see below. Currently there is no wealth tax applicable to individuals or their chattels, consequently there are attractions in terms of privacy, personal enjoyment and deferred taxation to this class of investments for those who are willing to hold non-income producing assets as part of their overall portfolio. Many works of art in the United Kingdom have been held by the same families for generations and the UK tax legislation has beneficial rules to encourage the care and maintenance of heritage chattels in private ownership. Provided that public access to those objects is given. Since as far back as 1896 there has been a recognition that heritage assets require special protection and successive legislation has addressed this point.

The government acknowledges that to thrive the art market requires participation from, and access to, buyers and sellers across the world. Through its export licensing system, the government seeks to strike a balance between the protection and retention in the United Kingdom of those works of art and cultural objects that it considers are of outstanding national importance (and whose export would be a misfortune), and the needs of the UK art market. This is a particularly specialised area and separate advice should always be sought from recognised experts should an export licence for any cultural object or work of art be required.

Finally, the United Kingdom is a signatory to the Convention on the International Trade of Endangered Species (CITES) and any work of art containing material from endangered species may be subject to import or export restrictions. VAT and excise duty are also applicable in certain circumstances, but both are outside the scope of these notes.

II RELEVANT TAX CONSIDERATIONS

The general rules for the taxation of works of art follow the United Kingdom’s tax legislation for the relevant ownership structure. Consequently, UK-resident and domiciled individuals are taxed on gains arising on disposal of chattels worldwide, at their prevailing rate of capital gains tax (CGT) (usually at 20 per cent). On death chattels are valued and IHT at 40 per cent is paid above the relevant threshold. There are some useful exemptions from both taxes (see below). Income tax is payable by self-employed art dealers and agents, and corporation

7 See, for example, the conditional exemption rules (Sections 30–35A Inheritance Tax Act 1984 and Section 258 Taxation of Chargeable Gains Act 1992).
8 Section 20 Finance Act 1896.
9 See, for example, Section 63 Finance Act 1910, Section 40 Finance Act 1930 and Section 39 Finance Act 1969.
10 The Reviewing Committee on the Export of Works of Art and Objects of Cultural Interest (RCEWA) was set up in 1952 following the Waverley Report issued in the same year. The Waverley Report was commissioned in response to the perceived loss of works of art through sales from the United Kingdom in the immediate post-war period. The most recent annual report of the RCEWA was published in April 2016 and it, together with more details about the rules for the export of works of art, can be read online at: www.artscouncil.org.uk/export-controls/reviewing-committee.
11 From 6 April 2016 the rate of CGT was reduced from 28 per cent and 18 per cent for higher and basic rate taxpayers respectively, to 20 per cent and 10 per cent for most disposals.
12 Open market value must be used for this purpose (Section 160 Inheritance Tax Act 1984).
13 The first £325,000 of a chargeable estate is taxed at zero per cent.
Notes on the Taxation of Works of Art in the United Kingdom

Notes on the Taxation of Works of Art in the United Kingdom

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Tax by companies dealing in art. UK trustees holding works of art are subject to the rules applicable to trusts and, for relevant property trusts, this means that an IHT charge at around 6 per cent is applicable every 10 years to the value of the chattels owned at that date. Likewise, IHT and potentially CGT charges apply on the creation of trusts and appointments from them.

i Capital gains tax

For CGT purposes particular reliefs apply to any gains arising on the disposal of chattels. Those chattels disposed of for proceeds (deemed or actual) of £6,000 or less are exempt from CGT, irrespective of any gain arising on that disposal, or the number of chattels disposed of and qualifying for this relief, in any year.\(^{14}\) Likewise losses arising on a disposal for £6,000 or less will be restricted. One of the advantages of the ‘chattels’ relief’ is that the taxpayer is still able to use the annual exemption for CGT purposes against any remaining chargeable gains.

In addition to the general chattels’ relief applying to proceeds, certain types of chattels are exempt from CGT altogether, for example no CGT is due on the disposal of private passenger vehicles, wasting assets and chattels held to be plant or machinery.\(^{15}\) In this context machinery includes other motor vehicles not normally used as private passenger vehicles. Specific rules apply to the treatment of sets of chattels, a good example of which would be the sale of a set of dining room chairs on a chair-by-chair basis, and any attempt to manipulate the sale proceeds of chattels by dividing a set in this way would be ineffective for CGT purposes.\(^{16}\)

Non-UK resident individuals may sell works of art in the United Kingdom without incurring a liability to CGT in the year of disposal, although care should be taken that a gain is not deemed to arise on returning to the United Kingdom should residency be resumed within five tax years of departure from it.\(^{17}\) In addition, foreign-resident trustees do not pay CGT on the sales of chattels in the United Kingdom, but both individuals and trustees in these circumstances must be careful not to be deemed to be trading in the United Kingdom. There are also special rules concerning the benefit of enjoyment of a work of art in the UK where the chattels are owned by a company or trust and in this specialist area, advice should be sought at the earliest opportunity. General anti-avoidance legislation does not impinge on this area of practice at the moment, but the position may well be reviewed again.

Where a UK resident is claiming the remittance basis of taxation, bringing a work of art into the United Kingdom will be treated as a remittance of the underlying income or gains used to purchase it, if the lifetime exemption for temporary importation to the United Kingdom (currently 275 days) is exceeded.\(^{18}\) The rule was brought into force following the Finance Act 2008 and there are some exemptions. No remittance will be triggered if the

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\(^{14}\) Section 262 Taxation of Chargeable Gains Act 1992 contains the details of the exemption and the restrictions that may be applicable on its use in certain circumstances.

\(^{15}\) The law in this area changed following the decision in Revenue and Customs Commissioners v. Executors of Lord Howard of Henderskelfe (deceased) [2014] All ER (D) 176 (Mar). The Finance Act 2015 introduced restrictions on the ability to claim this relief, limiting it to those owners who are also carrying on the trade in which the plant or machinery are used. A further restriction is that the relief is not available if capital allowances have, or could have been, claimed on the chattels.

\(^{16}\) HMRC sets out its specific views on this in the CGT manual (at CG76631), which is published online at www.hmrc.gov.uk/manuals/cgmanual/CG76631.htm.

\(^{17}\) Section 10A Taxation of Chargeable Gains Act 1992.

chattel was purchased out of ‘clean’ capital\textsuperscript{19} (i.e., the capital used did not carry an inherent tax liability derived from its original source) or if the chattels are for personal use, such as jewellery and clothing or for public exhibition, repair or conservation.\textsuperscript{20} Since 6 April 2012 there has been an exemption for the remittance of works of art that are brought into the United Kingdom specifically for the purposes of sale provided that the proceeds of sale are taken outside the United Kingdom within 45 days of receipt.\textsuperscript{21}

\section*{Inheritance tax}

The United Kingdom provides for the conditional exemption (a form of deferral) from IHT for chattels and works of art that qualify as being of ‘pre-eminent\textsuperscript{22}’ importance. The exemption from IHT is granted on the condition that the owner abides by certain undertakings negotiated with HMRC. In return for the grant of conditional exemption, an owner must sign undertakings to make the relevant objects available for the public to see on at least 28 days per year, commonly known as ‘the access requirements’;\textsuperscript{23} furthermore, works of art must not be removed from the UK without HMRC’s consent and are subject to a duty of care. Since the Finance Act 1998 came into force, the access requirements have become more stringent and access must be advertised (on websites, in guides and relevant publications) and be given without an appointment. A reasonable charge may be imposed to defray some, but not necessarily all, of the owner’s costs of fulfilling the obligations and the owner may ask visitors to provide evidence of identity. Pre-1998, the undertakings permitted owners to limit public access to a ‘by-appointment’ basis and the merit test for qualifying objects was that of ‘museum-quality’, rather than pre-eminence. HMRC is advised by a panel of experts as to whether an object meets the pre-eminence test.\textsuperscript{24} Once an object has been accepted for conditional exemption, details of its description, but not value or ownership, are published online by HMRC.

Central to the arrangement between the owner and HMRC is the requirement that the owner will care for the conditionally exempted works of art; should the owner breach the undertakings, the exemption ends. On a breach of the undertakings HMRC will assess the deferred IHT by reference to current rates and thresholds. This can be an unwelcome surprise to owners. In a climate of rising values for works of art, this has the potential drawback of increasing the amount of tax payable. Should the owner dispose of the work of art, there is, in addition to the IHT, a potential charge to CGT. Any CGT due is deducted from the proceeds of disposal and IHT is charged on the net amount.

\begin{thebibliography}{9}
\bibitem{19} Section 832 Income Tax (Trading and Other Income) Act 2005.
\bibitem{20} Section 809X Income Tax Act 2007.
\bibitem{21} Section 809YA Income Tax Act 2007.
\bibitem{22} Land and buildings have been capable of being accepted in lieu of IHT (initially Estate Duty, the forerunner of IHT) since 1910 and chattels since 1956. The full details of the exemption are provided in Sections 30–31 Inheritance Tax Act 1984. Chattels may also be offered in lieu if they are historically associated with buildings that are pre-eminent, (i.e., listed for their historical or architectural importance as grade I or II*).
\bibitem{23} The requirement is 28 days per annum for England. In Scotland, Wales and Northern Ireland the requirement is only 25 days per annum.
\bibitem{24} The experts also opine on the acceptance in lieu scheme (see below) and the procedure is administered by Arts Council England (ACE), which works closely with HMRC Heritage and the professional advisers to those taxpayers involved.
\end{thebibliography}
A unique feature of the IHT regime is that a taxpayer may be able to settle an IHT liability by offering a chattel or work of art to the nation in lieu of that liability. The scheme known as the acceptance in lieu scheme (AIL) has become increasingly popular as a method of settling an IHT bill. The government allows an annual budget of £40 million for tax to be met in this way, although that budget must be shared with the Cultural Gifts Scheme (CGS, see below). As an incentive to use the scheme, the government provides an inducement for using the AIL scheme, in the form of a douceur (literally, a sweetener). The douceur is a fiscal incentive of 25 per cent of the total tax otherwise due on the object or objects being offered, so that their tax settlement value is increased. The AIL scheme can be used whenever an IHT liability arises, in lifetime or on death and the offeror can express a wish or condition as to the ultimate destination in the United Kingdom for the work of art. To that extent the scheme acknowledges the appropriateness of certain works of art for particular institutions (a good example is material relating to Captain Robert Scott RN, allocated to the Scott Polar Research Institute), but in expressing a wish or condition, the offerors must be mindful that the nominated institution must qualify for this purpose.

The mechanics of making an offer are comparatively straightforward and are designed to ensure the United Kingdom only accepts objects for which the offeror has good title and that the agreed value is fair. The offeror must provide a statement of pre-eminence, a justification of the gross value of the object, a calculation of the ‘special price’, a condition report and due diligence statements in support of ownership and entitlement to make the offer. Together with high-quality photographs of the object, the offer documents are submitted to HMRC who advise whether the offer is competent, that is a tax liability has arisen, however, HMRC delegate the practical consideration of the chattels to Arts Council England (ACE). A panel of experts at ACE advises HMRC whether the pre-eminence tests have been satisfied and that the value is fair. Some negotiation over the agreed value may ensue. An essential point when considering whether to make an offer is the question of timing since to obtain the grant of probate any IHT due on the death must be paid first. It is not possible for the personal representatives of the deceased to anticipate the success of an offer and thereby pay a reduced amount of IHT to obtain probate. This point is often a surprise to those making an offer and inevitably impinges on the cash flow of the estate.

### iii Private treaty sales

For some owners of works of art, there is the possibility of negotiating a private treaty sale of their objects to public institutions. A private treaty sale provides vendors with the opportunity to enjoy the same tax incentives as an offer in lieu, but without the restriction of having to use the proceeds to settle an IHT liability. The work of art is bought for a tax-remitted sum by the acquiring institution, having taken any applicable CGT and IHT into account. The

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25 Section 230 Inheritance Tax Act 1984. Note that only a liability to IHT or its forerunner, Estate Duty, can be settled; the scheme does not extend to any other tax liability, though no CGT is charged on a disposal of an object as an AIL, a notional CGT liability can affect the AIL special price calculations in some circumstances.

26 The increased use of the scheme is reflected in the tax settled through its use, which has risen from £4.9 million in 2010/11 to £26.6 million (including cultural gifts settling tax of £319,000) in 2015/16, the last year for which statistics are available.

27 The annual budget for tax settled via the scheme until 31 March 2014 was £30 million.

28 The definition of a qualifying institution is given in Schedule 3 Inheritance Tax Act 1984.

29 The special price is the tax-reduced amount that the offeror will receive for the object.
key difference between a private treaty sale and an AIL is that the vendor receives cash for the work of art rather than having a tax liability settled. The likelihood of private treaty sales taking place in the current financial climate is comparatively limited, although institutions will make special efforts for works of art that are especially appropriate to their institution (good examples of which would be the sale of a watercolour to a gallery in the location depicted or the sale of a portrait to a gallery that already owns the pendant to it). From the vendor’s perspective, the private treaty sale has much to recommend it, as cash is paid for the acquisition, net of all tax, and, as the negotiations are conducted simply between the parties concerned, this can allow the process to conclude comparatively quickly. Private treaty sales have no bearing on the annual budget for other tax reliefs and HMRC is involved only to confirm the tax computations but otherwise is not party to the negotiations. The difficulty for many owners and indeed the acquiring institutions, is that while both parties may be willing to transact, the inevitable fundraising required to complete the sale can be difficult and time-consuming; institutions are, therefore, wary of conducting private treaty sales negotiations unless they are confident of success.

iv  The Cultural Gifts Scheme

In the Finance Act 2012, the government introduced a new tax incentive for the gift of works of art and cultural objects to the nation, which is commonly known as the ‘Cultural Gifts Scheme’ (CGS). With the introduction of this scheme, for the first time the government enacted fiscal support to the donation of pre-eminent objects to the nation. The incentive takes the form of a reduction against income tax or CGT for individuals and corporation tax for companies. The tax reduction is set at 30 per cent of the gross value (for an individual) or 20 per cent (for a company). The CGS permits the donor to spread the tax reduction over five consecutive years starting with the year of donation, as the donor wishes. Crucially the scheme does not allow the reduction against liabilities from earlier years, so there is no repayment of tax already paid, despite lobbying from interested parties in the consultation period. The scheme is not open to trustees or joint owners of objects, which limits its application further. The budget available for tax reduction under the CGS is shared with the AIL scheme. While a very welcome reward for those who are philanthropically minded, the level of relief means that 70 per cent of the value of the object is foregone and to that extent a donation made under the CGS should perhaps be seen as primarily an act of philanthropy. As a comparatively new tax reduction scheme in the United Kingdom, it will be some time before an assessment of its success can be made.

III  CONCLUSIONS

The art market and heritage industries in the United Kingdom are important sectors of economic activity and tourism. The importance to the United Kingdom, especially London, of maintaining its position as the leading art market is a consideration for successive governments and to this end fiscal policy is comparatively benign; where possible the government seeks to encourage private retention of works of art, thus reducing the public costs associated with keeping them in the United Kingdom. The government seeks a pragmatic solution to the competing needs of the market, the need to raise tax and the wish to retain outstanding works
of art in the United Kingdom. More recently, philanthropy using cultural objects has been recognised and rewarded. It remains to be seen how much the changes in the relationship with European countries will affect the art market or if successive governments will continue in this comparatively benign approach. Nevertheless, while the art market prospers, the United Kingdom will continue to attract buyers and sellers from across the world to its art dealers, auction houses and experts.
Chapter 4

OECD DEVELOPMENTS

George Hodgson and Emily Deane

I INTRODUCTION

i OECD developments
The OECD has become the central body charged with delivering the international agenda for greater transparency regarding asset holdings. There have traditionally been two main strands to its work in this area, both aimed at establishing internationally consistent standards. One strand focuses on information exchange for tax purposes and is led by the Global Forum on Transparency and Exchange of Information for Tax Purposes (the Global Forum). The other strand is focused upon international standards for anti-money laundering (AML) regulations. The work here is led by the Financial Action Task Force (FATF). While the Global Forum and the FATF remain distinct bodies within the OECD, they nevertheless work closely with each other. A third major work stream, known as base erosion and profit shifting (BEPS), led by the OECD Committee on Fiscal Affairs, has come to the fore. This work stream is focused on tackling corporate tax planning strategies that artificially shift profits to low or no-tax locations where there is little or no economic activity. All three initiatives have now gained considerable momentum thanks to the strong support of most of the world’s major economies.

ii The FATF
The FATF published revised recommendations for minimum national AML standards (generally referred to as the FATF’s 40 Recommendations) in February 2012. The 40 Recommendations were the result of long and at times heated negotiations and their publication has prompted a period of very intensive implementation work in many of the major economies. As a result, a variety of jurisdictions are now working on significant new legislative proposals in the AML area.

It was clear at an early stage that many of the most fundamental changes flowing from the FATF’s Recommendations would result from new requirements intended to improve the transparency of beneficial ownership. While the proposed new regime for trusts (outlined in FATF Recommendation 25) contains only relatively limited changes in this area, the changes for companies (outlined in Recommendation 24) are much more fundamental.

1 George Hodgson is chief executive of STEP and Emily Deane is STEP technical counsel.
The FATF now requires that countries should ensure that companies either obtain and make available information on their beneficial ownership or ensure that there are alternative mechanisms, such as registries, in place so that beneficial ownership of a company can be determined in a timely manner by competent authorities. Countries are also required to ensure that one or more natural persons, or DNFBPs, are authorised by the company and accountable to competent authorities for the provision of beneficial ownership information to competent authorities and for giving assistance to competent authorities.

The UK’s response to this new global standard has been to enact reform of procedures for the collection and holding of information on people with significant control (PSCs) via the Small Business, Enterprise and Employment Act. It is notable that this legislation is not just aimed at meeting the requirements of FATF Recommendation 24, but goes significantly further. Not only does it establish a statutory register of beneficial owners of companies (in the form of PSCs) but it also gives a right of public access to the beneficial ownership information rather than confining access to competent authorities. Thus the Regulations require companies to hold information on their own beneficial ownership and respond to any reasonable public request for information from the register as well as file beneficial ownership information with the national registrar of companies.

The UK focus on ensuring public access to corporate beneficial ownership information raises the issue of what information should be shown on the corporate register where the beneficial owner of a corporate entity is a trust. The initial suggestion was that the corporate register should show the name of the trust, the trustees and the beneficial owners of the trust. Ultimately, however, the argument that in practice many trusts are established to protect vulnerable beneficiaries and that publication of the names of such beneficiaries would potentially leave them at risk was accepted. The Regulations therefore call for the corporate register, where the beneficial owner is a trust, to show simply the names of the trustees and anyone who has the ‘right to exercise, or actually exercises, significant influence or control over the activities’ of the trust or company. The Regulations apply to all UK-incorporated companies, including limited liability partnerships, as well as to individuals who hold a UK company through an overseas holding company, and they will be obliged to register unless they hold a minority interest – in which case they will be exempted.

The UK approach to implementing the FATF Recommendations is particularly notable since the UK has indicated that it would like the UK, the Crown Dependencies and Overseas Territories (CDOTs) to ‘move forward together (with the UK) in raising standards of transparency globally’ and that ‘making company beneficial ownership information open to the public is by far the best approach’. Most CDOTs have now created or are in the process of creating registers of beneficial ownership, although there may be differences with regard to whether they are centralised or publicly available.

Publicly accessible registers of beneficial ownership are also a key feature of the Fourth EU AML Directive, which entered into force and appeared in the Official Journal in June 2015.

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3 Designated Non-Financial Business and Professions.
5 Schedule 1A, Part 1, paragraph 6.
The Directive, which was implemented by Member States on 26 June 2017, goes well beyond FATF requirements. For corporates and other legal entities Article 30 requires that Member States ensure that beneficial ownership information is held in a central register and that the information held on the register is available to competent authorities, obliged entities and ‘any person or organisation that can demonstrate a “legitimate interest”. A “legitimate interest” is to be interpreted by each Member State but the general expectation is that they will allow public access, in line with the UK’s PSC register approach.

Article 31 takes a different approach for trusts. Trustees must hold beneficial ownership information and this will be held in a central registry ‘when the trust generates tax consequences’. Law enforcement and competent authorities will have full access to the central registry and a Member State may opt to allow public access to the register.

In the wake of French terrorist attacks and the Panama Papers leak last year, the EU decided to revise the Fourth AML Directive (4AMLD) even before it had been implemented.\(^8\) The proposed revisions for Article 31 state that beneficial ownership information on companies and business-related trusts will be publicly available and all other trusts will be included in the national registers and available to parties that can show a legitimate interest. Beneficiaries of private trusts need only be disclosed to parties ‘holding a legitimate interest’, which could include non-governmental organisation groups and journalists. The European Parliament, Commission and Council are currently engaged in tripartite negotiations under The Estonian Presidency with regard to finalising the Directive; however, views towards the varying levels of access differ. The European Data Protection Supervisor’s Opinion\(^9\) on proposed amends to the 4AMLD, published on 2 February 2017, raises questions as to whether or not the proposed collection of personal data is proportionate to the fight against money laundering and terrorism financing. It scrutinises the access to beneficial ownership information and the significant and unnecessary risks that this might cause an individual who has a right to privacy and data protection. Some Member States have concerns about publishing details of beneficiaries, particularly vulnerable beneficiaries, which would leave them seriously exposed to potential abuse, given the risk of such information falling into the wrong hands and being disseminated for illegitimate purposes.

The Regulations leave it to each Member State to decide the level of transparency to be applied and the UK has confirmed that access to this register will be limited to law enforcement agencies on the grounds of privacy.

The Directive additionally requires the Commission to identify third-country jurisdictions which have strategic deficiencies in their national AML regimes (‘high-risk third countries’). It gives the Commission a wide degree of discretion on how to define such high-risk countries and it has been suggested that this will be used to pressure near neighbours of the EU and significant financial centres to adopt similar AML procedures to those laid out in the Directive.

The UK’s decision to leave the EU creates uncertainty as to the future force of EU Directives in the UK. It is likely that it will be excluded from negotiations regarding the EU regulation but it may nevertheless be pressured into implementing EU legislation to preserve access to EU markets. It appears that Europe has moved decisively towards publicly accessible registers to meet its obligations under the revised FATF Recommendation.

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The US seems to be taking a different approach. It is now a FATF requirement for governments to conduct an AML national risk assessment and the US has now published its first such assessment since 2005. The assessment acknowledges that ‘the United States has a large, complex and open financial system – making it a destination for legitimate trade and investment but also a target for illicit activity and actors’. Rather than registers, however, the US approach rests on the twin pillars of extensive regulation of financial institutions alongside well-equipped enforcement and supervisory bodies. The assessment concludes that in the case of the US, ‘law enforcement generally has access to the information it needs to investigate money laundering cases in the United States, but cooperation and transparency are not always present in other countries’. The Trump administration is also being pressured to review the US tax reform, which could result in the repatriation of millions of corporate profits currently being held in offshore jurisdictions. However, the Trump policy agenda remains uncertain.

The FATF is currently conducting mutual evaluations of national implementation of the FATF Recommendations. A mutual evaluation report provides detailed analysis of a country’s system in place designed for preventing criminal abuse of the financial system.

The UK’s Mutual Evaluation is due to take place in 2018.

II OECD GLOBAL FORUM ON TRANSPARENCY AND EXCHANGE OF INFORMATION FOR TAX PURPOSES

The Global Forum is the major international body for ensuring the implementation of the internationally agreed standards of transparency and exchange of information in the tax area. The Global Forum was originally established in the early 2000s but was significantly restructured in 2009 and now has a much wider membership comprised of 126 jurisdictions (plus the European Union).

The restructuring of the Global Forum resulted in a major expansion of the Global Forum’s work programme, with the main objective being the establishment of a comprehensive network of bilateral tax information exchange agreements (TIEAs). TIEAs are based on the principle of tax information exchange on request, reinforced by a peer review process to examine both the availability of the necessary information for tax information exchange and the effectiveness of the processing of requests for information exchange.

The arrival from the US of the Foreign Account Tax Compliance Act (FATCA), based on automatic information exchange, nevertheless changed the basis of the international debate on tax information exchange. In spring 2013, the G20 Finance Ministers and Central Bank Governors endorsed automatic exchange, as opposed to information exchange on request, as the new global standard for tax information exchange and requested the OECD, working with the G20, to develop a new standard based upon automatic exchange of information.

The OECD’s model, generally known as the Common Reporting Standard (CRS), is based heavily on the Model 1 Intergovernmental Agreements (IGAs) many jurisdictions have concluded with the US. The CRS model was first published in outline in February 2014, with further details being published in July 2014. The OECD’s approach has now been endorsed by all 34 members of the OECD and in total over 101 jurisdictions have committed

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to first exchanges by 2017 and 2018.\footnote{12} The only major outlier is therefore the US, which
remains committed to FATCA and declines to implement the CRS on the basis that FATCA
is adequate for its needs.

The legal basis for the CRS highlighted by the OECD is the Multilateral Convention on
Mutual Administrative Assistance in Tax Matters,\footnote{13} which currently has over 111 signatories,
including all members of the G20. The Convention requires separate agreements between
the competent authorities of the various parties, with automatic exchange of information
then taking place on a bilateral basis between the relevant parties. This is seen as providing
an important protection since jurisdictions will be able to decline to enter into agreements
with any party where there are significant concerns about ensuring the confidentiality of data
exchange or the uses that will be made of information exchanged for tax purposes. There is,
however, a proposal currently being worked upon to provide a standardised assessment of
each participating jurisdiction’s ability to ensure appropriate use of any tax data received as
part of a peer review type process.

Certainly in this context the OECD itself is keen to stress the safeguards inherent in
both the Convention and the CRS and make it clear that where the required standards ‘are
not met (whether in law or in practice), countries will not exchange information’.\footnote{14} It is
notable, however, these protections, plus the presumption of reciprocity, are coming under
criticism from those campaigning on behalf of developing countries on the grounds that they
may in reality mean that many poorer developing countries are denied access to the CRS. The
OECD acknowledges the ‘developing countries may face particular capacity issues as regards
automatic exchange of information’\footnote{15} and notes that the Global Forum has been asked to
work with the OECD Task Force on Tax and Development and others to assist with capacity
building in developing countries.

Alongside capacity building in developing countries, the Global Forum will now be
responsible for monitoring and reviewing the implementation of the CRS. There are global
concerns that the information being exchanged under CRS might be leaked; therefore,
the monitoring of the robustness of each jurisdiction’s system will be essential. The precise
methodology by which implementation will be monitored has yet to be decided, but it seems
likely that the peer review process established for the previous global standard, tax information
exchange on request (via TIEAs) will now be extended to the new global standard, automatic
exchange of tax information.

The arrival of the CRS as the new global standard for exchange of tax information
has implications for some of the other tax information exchange initiatives that have been
developed. It is envisaged, for example, that the arrival of CRS reporting in 2017 will
effectively replace the FATCA-style Intergovernmental Agreements the UK has with the
CDOTs.

It is anticipated, however, that the CRS will exist alongside the current OECD TIEA
process, with the limited information exchange automatically via the CRS prompting more
detailed inquiries via information exchange. The CRS came into effect in the UK this year so

\footnote{12} See: www.oecd.org/tax/transparency/AEOI-commitments.pdf.
\footnote{14} See: www.oecd.org/ctp/exchange-of-tax-information/Automatic-Exchange-Financial-
Account-Information-Brief.pdf.
\footnote{15} See: www.oecd.org/ctp/exchange-of-tax-information/standard-for-automatic-exchange-of-
all UK-based financial institutions (FI) (including banks, funds and insurance companies as well as UK branches and subsidiaries of overseas FIs) will have to review the tax residency of their customers and report them to HMRC.

Industry has broadly welcomed the convergence on a single standard of information exchange. Despite the OECD’s attempts to create a global standard for the automatic exchange of information, a significant number of jurisdictions have introduced local variations to reporting requirements. This inconsistency has hindered financial institutions in preparing for CRS. Several jurisdictions had threatened to develop their own versions of FATCA and a common approach clearly simplifies implementation. The major question mark, however, remains how the US will approach the OECD’s CRS initiative. The US is unlikely to move away from FATCA and adopt the CRS process. The US’s position, however, is that the Model I IGAs entered into under FATCA ‘acknowledge the need for the United States to achieve equivalent levels of reciprocal automatic information exchange with partner jurisdictions’.16

In spite of political commitment from the US to ‘advocate and support’ legislation to give effect to reciprocal information exchange, there is yet little prospect of any real progress here at the political level, although at the same time several non-US tax authorities are indicating that they are now receiving useful tax information from the US even if this is not yet as comprehensive as it would be under the CRS.

III  BEPS – BASE EROSION AND PROFIT SHIFTING

The other significant project that the OECD is working on is the BEPS programme. This is the umbrella term used for the OECD’s work on measures to inhibit the shifting of corporate profits to low-tax or no-tax jurisdictions where there is little or no economic activity. The OECD is currently in the process of developing a series of action plans covering various aspects of what is acknowledged to be a contentious and complex issue.17 Sufficient progress has been made, however, and the Treasury Department and the Inland Revenue Service have finalised a rule requiring US parent companies of multinational public and private companies to provide their financial data to the IRS on a country-by-country basis with other OECD countries.18 Tax authorities around the world are hoping that the intergovernmental exchange mechanisms will identify companies that are shifting their profits into tax havens, which will instigate further investigation.

The primary focus of BEPS is clearly on the corporate sector, but many private client structures will have a corporate component. The intention is clearly that corporate structures will now also be transparent and not used as tools of aggressive tax planning strategies to move income from one jurisdiction to another. The OECD and G20 have welcomed all interested countries and jurisdictions that are ready to commit to the BEPS programme and by June 2017 76 countries and jurisdictions had signed up to express their willingness to prevent BEPS by multinational enterprises. The OECD celebrated the signing ceremony saying that: ‘The signing of this multilateral convention marks a turning point in tax treaty history.’19

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19 OECD Secretary-General Angel Gurria.
IV OUTLOOK

The G5 launched an initiative for the automatic exchange of information on beneficial ownership in April 2016, following the Panama Papers leaks, to take decisive action against the ‘scourge of tax evasion’. Of course as with the CRS, to be fully effective such exchange should be on a global basis. We therefore hope that you will support this initiative and that we can collectively call on the OECD, in cooperation with FATF, to draw up a new single global standard for such exchange. This should cover the robust identification of beneficial ownership, the range of entities and arrangements which should be covered by such exchange, timing of exchange and wider exchange procedures.

At the G20 meeting in April 2016, discussions were also focused on the G20 tax agenda and the need to enhance transparency in tax matters and disclosure of beneficial ownership following the publication of the Panama Papers. The OECD issued a statement shortly thereafter:

The OECD and the Global Forum, in partnership with the Financial Action Task Force (FATF), have been mandated by the G20 and Anti-Corruption Summit to work on improving the availability of beneficial ownership to ensure effective implementation of the standard that will enable tax authorities to identify the true owners behind shell companies and other legal arrangements.

As of February 2017, the FATF has reviewed over 80 countries and publicly identified 61 of them. Of these 61, 49 have since made the necessary reforms to address their AML/CFT weaknesses and have been removed from the process. In addition, the anti-BEPS measures that have been implemented by the G20 and OECD have furthered the objective of retaining taxation in the appropriate jurisdictions where the profits have been generated.

The near-simultaneous implementation of major new processes for the collection of beneficial ownership information, the automatic exchange of tax information and improved transparency in the corporate sector, is likely to have significant consequences, both intended and unintended. The concept of ‘beneficial ownership’, always a problematic one in the trust context, is beginning to shift from AML to tax, with both FATCA and CRS using beneficial ownership, rather than tax liability, as the basis for the collection of tax information. Automatic exchange will also see information on wealth, rather than income, being reported, in many cases for the first time.

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21 Idem.
At the very least, this seems likely to generate many more queries regarding unexplained sources of wealth. In the long run, however, greater transparency as to both income flows and wealth holdings may also begin to influence how tax authorities structure the tax system to maximise tax yields. As intelligence improves on international tax-planning strategies, it seems inevitable that tax authorities will take action to block those they deem to be overly aggressive or otherwise unacceptable. The OECD has positively affirmed that ‘tax matters and transparency are finally front and centre in public discussions about fairness, good governance and responsible business (and individual) conduct’.  

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I  INTRODUCTION

Designing a trust entails understanding a settlor's aspirations, wishes and objectives and melding them into an organisational regime that may last many generations. The design process requires an understanding of trust law – an area of law that is continuously evolving – as well as tax law and ancillary legal matters. Those too continue to evolve. For the international private client, an array of US and non-US jurisdictions thankfully provide options, offering progressive trust laws.

Trust design involves many facets. This chapter explores several key aspects of modern trust design. Specifically, it considers the following questions:

a  What is the optimal governance structure for the trust?
b  How can a family-controlled entity play a role in the governance structure?
c  How can we preserve settlor intent?
d  What are the appropriate dispositive terms?
e  What is the appropriate duration for the trust?
f  How can we mitigate litigation risks?

Each of those questions focuses on an essential part of a trust. Addressing each question involves thoughtful drafting, as well as thoughtful situs selection. A clear, well-drafted trust deed is vital to any trust. Likewise, the selection of an appropriate situs is vital to ensuring that the trust has the right legal environment in which to grow.

II  TRUST GOVERNANCE MODELS

The design of a trust’s internal governance is one of the most important aspects of trust design. The governance structure determines who is responsible for each aspect of administering a trust. For trusts, there are four governance models:

a  unitary trustee;
b  directed trust;
c  divided trust; and
d  hybrid model.

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1  Todd D Mayo is a principal and general counsel of Perspecta Trust, and he is an attorney with Vanderwal Martens.

These models represent an evolutionary progression. This evolution began with the unitary trustee model, which was the original governance model. The directed trust subsequently emerged in an effort to improve upon the unitary trustee model. Likewise, the divided trust evolved from the directed trust, again in an effort to improve upon its predecessor. Although it can potentially be a sensible design in some cases, the hybrid model tends to be an evolutionary anomaly. This evolutionary progression has been more pronounced in the leading US jurisdictions.

i Unitary trustee
In the unitary trustee model, the trustee is vested with all of the trustee powers. The unitary trustee model is the traditional model. The trustee has the power to make distributions, the power to invest the trust property, and the power to administer the trust. In its simplest form, one trustee is vested with all of those powers. A trust, however, may have two or more cotrustees. If there is more than one trustee, the trustees share the trustee powers and collectively must decide how to exercise those powers.

A trustee may delegate certain powers to a co-trustee or an agent. For example, a trustee may delegate investment powers to a professional investment manager. The delegation must be prudent. The trustee must monitor the delegate, ensuring that the delegatee is acting within the scope of the delegation and ensuring that the delegatee is acting prudently. Thus, a trustee who delegates powers does not fully absolve himself of liability arising from the exercise (or non-exercise) of the delegated power. To the extent that the delegation may have been imprudent or the trustee fails to monitor adequately the delegatee, the trustee is potentially liable for any harm that the delegatee causes.

Certain powers, however, are non-delegable. Notably, a trustee generally cannot delegate the power to make discretionary distributions. In some instances, a power is non-delegable, because its delegation contravenes the settlor’s intent. For example, a settlor may have appointed a person as trustee based on the person’s particular experience or expertise – such as in managing a business – expecting that the person would personally exercise the related powers. In such instances, the trustee cannot delegate the powers that the settlor intended the trustee to exercise personally. The trustees are always responsible for participating in the exercise of non-delegable powers.

Advantages
The principal advantage of a unitary trustee model is its simplicity. In many cases, a single trustee or a small number of cotrustees can efficiently administer a trust. As a rule, those trusts involve uncomplicated family situations and uncomplicated trust holdings. For those trusts, a more complex governance structure – in which trustee powers are assigned to two or more persons – may be unwarranted.

Disadvantages
The unitary trustee model’s simplicity is its weakness in more complex issues. The unitary trustee model tends not to be well suited for trusts involving complicated family situations or complicated trust holdings. For those trusts, the ability to divide trustee powers among two or more persons – and partially or fully insulate each of those persons from liability for another person’s misfeasance or malfeasance – can promote more efficient trust administration and
more efficacious fulfilment of the settlor’s intent. Unlike other trust governance models, the unitary trustee model does not allow the assignment of a defined set of trustee powers to a specific person.

ii Directed trusts

In a directed trust, the trustee is vested with all of the trustee powers, but, with respect to certain powers, the trustee only acts in accordance with another person’s direction. For example, a person other than the trustee may have the power to direct the investment of the trust property. The person who has the power to direct the trustee may be the settlor, a beneficiary or another person.

Advantages

A directed trust offers the potential benefit of assigning trust powers to two or more persons in a manner that better achieves the trust’s purposes. At least in theory if not always in practice, a directed trust allows a settlor to assemble a team of persons who are collectively better able to achieve the trust’s purposes than a single trustee. A settlor may wish to appoint an institutional trustee to make decisions concerning discretionary distributions and handle administrative matters, such as record-keeping, reporting and tax compliance. The settlor, however, may prefer to have someone else – perhaps an investment management firm with which he or she has a long relationship – manage the trust property. A directed trust allows the settlor to create that structure for governing the trust’s internal affairs.

A directed trust avoids the limitations associated with delegation. A trustee generally cannot delegate its discretionary distribution power, because the power is generally viewed as a non-delegable trustee power. With a directed trust, a person other than the trustee can have the power to direct the trustee to make distributions. A directed trust mitigates the risks associated with delegation. If the trustee does not have any duty to monitor the powerholder, then the trustee in fact may avoid those risks altogether. A trustee can delegate only to the extent that the delegation is prudent, and the trustee has an ongoing duty to monitor the delegatee. Thus, for example, a trustee may be reluctant to delegate investment powers to a beneficiary who lacks investment management skill or experience. With a directed trust, the trustee is not selecting the person exercising a specific power and thus is not liable for an imprudent selection. For example, the trust deed may specify that a beneficiary has the power to direct the trustee concerning the investment of the trust property.

Disadvantages

A directed trust poses some administrative inefficiencies, and it may not eliminate the trustee’s liability with respect to the powerholder’s exercise or non-exercise of the powers that he or she holds. With a directed trust, the trustee is in the middle of the action. A powerholder directs the trustee to take a certain action – say, make an investment – and the trustee generally must act in accordance with the direction. This two-step process – direction and action – is administratively less efficient than an arrangement in which the decision-maker is also the person taking the action. Since the trustee is in the middle of each action, the trustee remains an attractive target when something goes wrong. A disgruntled beneficiary is likely to argue that the trustee should have taken steps to prevent the alleged harm caused by the powerholder’s action or failure to act, or at least taken steps to warn the beneficiary. A
trustee, in fact, may be tempted to communicate to the powerholder its concerns about the powerholder’s actions; as illustrated by the Mennen case, succumbing to that temptation may invite questions about whether the trustee assumed certain duties to the beneficiaries.3

Some critics assert that directed trusts (and divided trusts) eviscerate the concept of a trust. By shifting the decision-making about distributions or investments from a trustee to a person who may or may not be a fiduciary or who may or may not have any liability exposure under the terms of the trust, there may be no one who can be held accountable if something goes awry. This criticism is more properly directed towards the design of specific trusts, rather than a broadside against the governance model. Directed trusts (and divided trusts) are not immune from poor design and poor implementation.

Some critics also complain that directed trusts (and divided trusts) create confusion, because two or more persons are involved in administering the trust and sometimes it can be unclear who is responsible for what. Here again, the criticism is more properly directed toward the design of specific trusts, rather than a broadside against the governance model. In some circumstances, a unitary trustee governance model is optimal. For example, the unitary trustee model is often perfectly adequate for a trust that only holds a modest portfolio of publicly traded securities. As the complexity of the trust’s objectives and the value of the trust property increases, however, a more sophisticated governance model usually is warranted.

**Non-US jurisdictions**

In non-US jurisdictions, the reserved powers trust is an example of a directed trust. The Bahamas, the British Virgin Islands, the Cayman Islands, Guernsey and Jersey recognise reserved powers trusts. Under the statutes recognising reserved powers trusts, the settlor generally may reserve certain enumerated powers. In contrast to the leading US jurisdictions, it can be unclear whether, during the settlor’s life, a person other than the settlor may have one or more of the powers and whether, upon the settlor’s incapacity or death, another person can succeed the settlor in possessing and exercising a power that the settlor had reserved to himself or herself.

**Leading US jurisdictions**

The leading US jurisdictions recognise directed trusts. Delaware, New Hampshire and South Dakota have comprehensive statutes governing directed trusts.4 Notably, each of those states ring-fences the trustee’s and the powerholder’s respective powers and duties. In those states, a trustee does not have any duty to monitor a powerholder’s conduct, advise the powerholder, or warn a beneficiary concerning any matter in which the trustee might exercise a power in a different manner from the powerholder. To the extent that the terms of the trust provide that a trustee must follow another person’s direction, the trustee is not liable for acting in accordance with that direction. A trustee is not liable for the powerholder’s acts or omissions.

Delaware, New Hampshire and South Dakota notably recognise trust advisers and trust protectors. A trust adviser or trust protector is a person who is not a trustee and who has one or more trust powers. In a directed trust (or a divided trust), a trust adviser or trust

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3 Mennen v. Wilmington Trust Co, No. 8432-ML (Del. Ch. Apr. 24, 2015). The administrative trustee settled with the beneficiary before trial, so the court did not address whether the administrative trustee had assumed any investment-related duties.

4 Del. Code tit. 12, Section 3313; NH RSA 564-B:8-808 and NH RSA 564-B:12-1201 to NH RSA 564-B:12-1210; and SD Codified Laws Sections 55-1B-1 to 55-1B-11.
protector has the power to direct the trustee to take (or refrain from taking) certain actions. For example, a trust adviser may have the power to direct the trustee to make an investment, or a trust protector may have the power to veto a distribution.

**Other US jurisdictions**

Many other US jurisdictions recognise the power to direct, but the statutory authority fails to address many critical issues. The Uniform Trust Code, which a majority of states has adopted in some form, recognises the power to direct, unless the direction is manifestly contrary to the terms of the trust or the direction is a serious breach of a fiduciary duty that the powerholder owes to the trust’s beneficiaries. Thus, a trustee has a duty to monitor the powerholder’s exercise of the power to direct and make an independent assessment of whether the exercise is proper. The trustee likely also has a duty to warn the beneficiaries if it determines that the exercise or non-exercise of the power to direct may be improper or otherwise may be detrimental to their interests. For many trustees, the imposition of those ongoing duties are unattractive because the directed trust does not lessen the trustee’s potential liability.

Most US jurisdictions do not statutorily recognise trust advisers and trust protectors, and there is a dearth of common law concerning those roles. In the absence of developed law in those jurisdictions, there is considerable uncertainty concerning the nature and scope of the duties and powers that a person designated as a trust adviser or trust protector may have. Depending upon the nature and scope of the powers with which a trust adviser or trust protector is vested under the terms of a trust, a court could potentially conclude that the trust adviser or trust protector is a *de facto* trustee. Florida does not statutorily recognise trust advisers or trust protectors. In 2015, a Florida appellate court recently recognised the role of a trust protector. California and New York do not statutorily recognise trust advisers or trust protectors.

In the US, the Uniform Law Commission recently approved a uniform act governing directed trusts. The Uniform Law Commission is an association of academics and practitioners who work to develop model laws that US states can adopt. US jurisdictions likely will begin considering the adoption the Uniform Directed Trust Act in 2018. As states adopt that act, the use of directed trusts will likely become even more widespread.

**US tax considerations**

The settlor’s retention of powers can have US income, gift and estate tax implications. The settlor’s retention of certain powers may cause the trust to be classified as a grantor trust for US income tax purposes. With a grantor trust, the settlor is the deemed owner of the trust property and is taxable on the income and capital gains derived from that property. The settlor’s retention of certain powers may also cause the trust property to be includable in the settlor’s gross estate for US estate tax purposes. Although there is more flexibility in designing a trust in which a beneficiary has the power to direct, potential income, gift and estate tax issues lurk there too. If a non-US person possesses a power to direct, the trust may be classified as a non-US trust for US income tax purposes. For US income tax purposes, a

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5 Minassian v. Rachins, 152 So. 3d 719 (Fla. 4th DCA 2014).
8 26 C.F.R. Section 301.7701-7.
trust that is classified as a non-US trust is taxable only on certain US-source income. In light of the various tax issues, the settlor and his or her advisers must take care in structuring a directed trust in a manner that avoids undesirable tax consequences.

### iii Divided trusts

The divided trust is an increasingly popular governance model. The divided trust entails the division of trustee duties and powers among one or more trustees and other persons. Like a directed trust, a divided trust is a multiparty governance structure. The design of a divided trust requires consideration of the division of the powers and duties among those parties, the points at which those parties’ duties intersect and how the trust’s administration should function at those points, and the manner and extent to which the parties are insulated from the other parties’ acts and omissions.

A divided trust empowers each person who is a part of the trust’s governance to take direct action. In contrast, in a directed trust, a powerholder acts indirectly, directing the trustee to take a specific act. In a divided trust, each powerholder acts independently and acts directly. For example, in a directed trust, the settlor may have the power to direct the trustee on matters concerning the investment of the trust property. When the settlor wishes to buy an asset, the settlor must direct the trustee to buy the asset, and the trustee subsequently will take the necessary action to buy the asset. The trustee will execute the requisite documents, deliver the funds to the seller, and accept receipt of the newly acquired asset.

### Advantages

Divided trusts share the advantages of directed trusts, but generally are more efficient to administer, because each person involved in the trust’s governance can act directly. In addition, a divided trust potentially better insulates a trustee from liability, because the trustee is not involved in another person’s exercise of a distribution power, investment power or other trustee power.

### Disadvantages

Divided trusts generally share the disadvantages of directed trusts, except that divided trusts generally avoid the administrative inefficiencies inherent in directed trusts. Divided trusts can be more challenging to draft than directed trusts. In a directed trust, the trustee is vested with all of the trust powers, so the trustee unilaterally can exercise any power to the extent that another person does not have the power to direct the trustee with respect to that power. In a divided trust, there is a risk that the drafting attorney will fail to assign a trust power to a person.

### Non-US jurisdictions

Non-US jurisdictions have yet to embrace the concept of the divided trust. The leading US jurisdictions are on the vanguard of this evolutionary development of trust law.

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9 In practice, some people bypass the trustee of a directed trust. Under the theory that the powerholder is acting as the trustee’s agent or in some cases with less forethought, an accommodating trustee sometimes allows a powerholder to take the action directly (for example, taking the actions necessary to buy the asset). That approach is not without risk. The trustee may be breaching its fiduciary duties depending upon the terms of the trust and the applicable law.
Leading US jurisdictions
The leading US jurisdictions recognise divided trusts. Delaware, New Hampshire and South Dakota have comprehensive statutes governing divided trusts.\textsuperscript{10} Notably, each of those states generally ring-fences the powers, duties and liabilities of the trustees, trust advisers and trust protectors.

New Hampshire’s highest court was the first US court that expressly upheld divided trusts. In the \textit{Tamposi} case decided in 2013, the New Hampshire Supreme Court affirmed the division of investment and distribution powers between two classes of trustee, which, under the terms of the trust, were called ‘investment directors’ and ‘trustees’.\textsuperscript{11} Under the terms of the trust, the trustee had the power to make distributions, and the investment directors had the exclusive power to invest and manage the trust property. One of the settlor’s daughters sued both the trustee and investment directors for breach of trust, alleging in part that the investment directors had improperly managed the trust property. In construing the terms of the trust, the court concluded that the trustee did not have any duty with respect to investment matters, because the investment directors were exclusively vested with the investment powers. The court similarly concluded that the investment directors did not have any duties with respect to distributions, because the trustee was exclusively vested with the discretionary distribution powers.

Other US jurisdictions
Nevada, Tennessee and Wyoming recognise divided trusts. In many other US jurisdictions, the statutes do not provide clear authority for divided trusts. California, Florida and New York are among the states that lack clear authority for divided trusts.

The Uniform Law Commission has approved the Uniform Directed Trust Act, a model act governing directed and divided trusts. US jurisdictions likely will begin considering the adoption the act in 2018. Accordingly, the use of divided trusts will likely become more commonplace throughout the US.

US tax considerations
The division of trust powers can affect the trust’s status for US income tax purposes, and it can affect whether the person vested with certain powers may be subject to US income, gift and estate taxes. Accordingly, the settlor and his or her advisers must take care in structuring a divided trust in a manner that avoids undesirable tax consequences.

iv Hybrid governance model
A hybrid governance model incorporates elements of a directed trust and a divided trust. For example, a trust instrument may grant to a person the power to direct the trustee to make distributions, while granting to another person the exclusive power to manage the trust property. Too often, a hybrid governance model arises by accident, as the product of inartful drafting. A drafting attorney may attempt to create a divided trust using a trust deed for a directed trust as a precedent, but fail to address fully the division of the trust powers.

\textsuperscript{10} Del. Code tit. 12, Section 3313; NH RSA 564-B:8-808 and NH RSA 564-B:12-1201 to NH RSA 564-B:12-1210; and SD Codified Laws Sections 55-1B-1 to 55-1B-11.

\textsuperscript{11} Shelton v. Tamposi, 164 N.H. 490 (2013).
III USE OF FAMILY-CONTROLLED ENTITIES IN TRUST GOVERNANCE

Some families seek to include family-controlled entities in the governance structure of the family's trusts. Those entities include a family-controlled holding company under the trust, non-bank trust advisers and trust protectors, and private trust companies.

i Holding companies

In both US and non-US jurisdictions, a common technique for enabling the settlor or other family members to control investments is the use of a holding company. The trust generally holds an operating cash account and the interest in the holding company. The trustee uses the operating cash account to pay trust expenses and make distributions. The holding company holds the investments, either directly or indirectly through one or more subsidiary companies. The settlor or one or more family members serve as the directors or managers of the holdings company and any subsidiary companies. In their capacity as directors or managers, the settlor and the family members control the investments.

The use of a holding company minimises the trustee's involvement in any investment activity, because the investment activity is occurring one or more levels below the trust. At the trust level, a key consideration is the waiver of the duty to diversify, so that holding an undiversified portfolio (an operating cash account and an interest in a holding company that may or may not hold a diversified portfolio) is not a breach of any fiduciary duties. In the case of a directed trust or divided trust, a person other than the trustee may be vested with the investment powers and thus would make any determination whether to retain the interest in the holding company.

ii Non-bank advisers and protectors

New Hampshire and South Dakota expressly allow a non-bank company to act as a trust adviser or trust protector (i.e., possess certain trust powers). Those states have statutory safe harbours that, subject to certain conditions, permit a company to act as a trust adviser or trust protector without obtaining a charter as a bank or trust company. Coupled with a divided trust, a non-bank trust adviser or trust protector enables a family to create a structure that generally emulates a private trust company, while avoiding the regulatory and compliance issues involved in forming and operating a private trust company.

New Hampshire has two safe harbours. The newer safe harbour, which was enacted in 2017, generally allows a corporation, limited liability company, or foundation to act as a trust adviser or trust protector, so long as the company does not provide services to the general public. This safe harbour also allows a company to act as a private trust company. The older safe harbour is more restrictive. The older safe harbour applies only if the company's trust powers are limited (e.g., only discretionary distribution powers). Neither safe harbour requires the company to register with the state's banking commission.

South Dakota's safe harbour allows the company to have a broad array of trust powers, but requires the trustee to be a South Dakota-chartered bank or trust company or

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12 NH RSA 293-A:3.05 (relating to corporations), NH RSA 304-C:22-a (relating to limited liability companies), NH RSA 564-F:8-802 (relating to foundations), and NH RSA 383-C:12-1201 to NH RSA 383-C:12-1202; and S.D. Codified Laws Section 51A-6A-66.

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US-chartered bank with trust powers. In addition, South Dakota imposes a notice filing requirement. The entity acting as a trust advisor or trust protector must register with the state’s banking commission and file an annual report with the banking commission.

Unlike New Hampshire and South Dakota, Delaware does not have a statutory safe harbour for non-bank companies that act as trust advisers or trust protectors. Nonetheless, some practitioners form Delaware companies that act in those capacities.

iii Private trust companies

A private trust company is a company that is qualified to exercise trust powers for the members of a family and their related trusts, companies and charities. A private trust company can be attractive because it enables a family to have a family-controlled institutional trustee for their trusts, develop governance and succession plans within a single entity (rather than across many trusts) and potentially develop a more professional system for administering the family’s trusts and managing its wealth.

Non-US jurisdictions

The Bahamas, the British Virgin Islands, the Cayman Islands, Guernsey and Jersey allow private trust companies.

Leading US jurisdictions

New Hampshire and South Dakota allow the formation of private trust companies. New Hampshire allows the formation of regulated and unregulated private trust companies. South Dakota allows only the formation of regulated private trust companies.

A regulated private trust company is chartered and supervised by the state’s banking commission. An unregulated private trust company is not subject to the supervision of the state’s banking commission. An unregulated private trust company must register as an investment adviser with the US Securities and Exchange Commission, unless it qualifies for the family office exemption. The choice between a regulated private trust company and an unregulated private trust company often turns on whether the family values the discipline that a state banking commission generally demands and the supervision that it imposes.

New Hampshire does not require a private trust company to maintain an office within the state or have a resident director. Although maintaining an office in the state is unnecessary under New Hampshire law, it often is advisable for purposes of mitigating the risk that the private trust company is treated as a resident in another jurisdiction under a mind and management test or another legal standard. Notably, New Hampshire also allows a private trust company formed in another jurisdiction, including a non-US jurisdiction, to operate within the state.

13 For a general discussion of private trust companies, see Miles C. Padgett, ‘Private Trust Companies: A Practical Introduction to a Bespoke Solution’, Investments & Wealth Monitor, January/February 2016, pp. 37-41.

Modern Trust Design

In New Hampshire, a private trust company may be formed as a corporation or limited liability company. Beginning 1 October 2017, New Hampshire will allow a foundation to act a private trust company.\(^{15}\) Delaware does not allow the formation of private trust companies.

**Other US jurisdictions**

Florida, Ohio, Nevada, Tennessee and Wyoming allow the formation of private trust companies. Nevada and Wyoming allow the formation of unregulated private trust companies. California and New York do not allow the formation of private trust companies.

**IV SETTLOR INTENT**

For some settlors, the preservation of his or her intent is critically important. Other settlors are less concerned with whether his or her specific wishes and mandates will be strictly applied to future generations, who will largely comprise individuals the settlors will have never met or known. Even for a settlor who counts himself or herself in that latter group – and in some ways more importantly, the trustees and other persons charged with administering a trust – the preservation of settlor intent is important, because it may affect the efficacy of the settlor’s modification or waiver of certain duties, such as the duty to diversify or the duty to inform.

i **Non-US jurisdictions**

Compared to the leading US jurisdictions, non-US jurisdictions generally are less rigorous in protecting settlor intent. For example, many non-US jurisdictions allow the beneficiaries to terminate a trust. Subject to some variation, the *Saunders* rule is generally applicable in non-US jurisdictions.\(^{16}\) Under that rule, the beneficiaries of a trust can terminate the trust by unanimous agreement. Generally, all of the beneficiaries must be adults and must be competent.

ii **Leading US jurisdictions**

New Hampshire and South Dakota protect settlor intent. Within the US, New Hampshire may offer the strongest protection of settlor intent. New Hampshire’s tradition of respecting settlor intent is long-standing, and it infuses the state’s statutory regime. In *Burtman*, the state’s highest court wrote, ‘probably no jurisdiction has stood more steadfastly for giving effect to the intention of the [settlor] rather than to arbitrary rules of law than New Hampshire’. In *Lowy*, the court stated that, ‘when we construe a trust, the intention of a settlor is paramount’.\(^{17}\) New Hampshire has incorporated this paradigm into its statutes. In interpreting or construing the terms of a trust, New Hampshire’s statutes provide that, ‘the settlor’s intent shall be sovereign to the extent that the settlor’s intent is lawful, not contrary to public policy, and possible to achieve’.\(^{18}\) Similarly, in applying and construing the New

\(^{15}\) NH RSA 383-D:5-501A(a)(3) (as added by the Laws of 2017, ch. 257, Section 41).

\(^{16}\) *Saunders v. Vautier*, EWHC Ch J82 (1868).

\(^{17}\) Although the *Burtman* case involved the construction of a will, New Hampshire’s courts take the same approach for settlor intent as they do for testator intent. *Katz v. Katz*, 104 N.H. 478, 481-482 (1963).


\(^{8}\) NH RSA 564-B:1-112.
Hampshire Trust Code, New Hampshire’s statutes provide that a court must give ‘primary consideration […] to the preservation of the settlor’s intent as expressed in the terms of the trust’.19

iii Other US jurisdictions

US jurisdictions have historically rejected the Saunders rule. Instead, US jurisdictions have generally applied the material purpose test that was articulated in Claflin.20 Under that test, the beneficiaries could not terminate a trust so long as the trust’s continuation was necessary to achieve a material purpose of the trust. More recently, many US jurisdictions have adopted a variation of the Saunders rule, allowing the modification or termination of a trust even if the modification or termination would violate a material purpose of the trust. In some states, the settlor’s agreement is necessary to modify or terminate a trust in violation of a material purpose of the trust. Many US jurisdictions have also adopted (or at least have not expressly rejected) the benefit-of-the-beneficiary rule, which elevates the beneficiaries’ interests over settlor intent.

V DISPOSITIVE TERMS

i Discretionary distributions

Discretionary distributions provide flexibility to address changing circumstances. With discretionary distributions, the trustee can make distributions – and, importantly, refrain from making distributions – as appropriate based on the beneficiaries’ circumstances at the time. So long as property remains in a (properly designed) trust and distributions are discretionary, the property is generally outside the reach of a beneficiary’s creditors and, in the case of a person subject to US estate taxes, potentially excluded from his or her gross estate for US estate tax purposes. In addition, with discretionary distributions, a trustee is able to refrain from making distributions that may support a beneficiary’s addictive behaviours (e.g., gambling or substance abuse). In the context of a divorce, for example, a beneficiary’s right to receive a mandatory income distribution may be treated as marital property and, thus, subject to division.

Mandatory income distributions also can restrain the trustee’s investment of the trust property. A fully discretionary trust enables the trustee to invest for total return. A trust that contains mandatory income distributions generally forces the trustee (or whoever has investment powers) to invest the trust property in a manner that generates reasonable income, which, especially in the current interest rate environment, may be less than the income generated by a portfolio invested for total return.

In the trust deed, the settlor ideally would include a statement of intent or some precatory clauses, so that the trustee has some guidance concerning the purposes, timing and amounts of distributions that the trustee should make. Alternatively, the settlor would provide a letter of wishes, again for the purpose of guiding the trustee in its exercise of its power to make discretionary distributions.

19 NH RSA 564-B:11-1101.
20 Claflin v. Claflin, 149 Mass. 19 (1889).
ii Power to add beneficiaries

The power to add beneficiaries can provide additional flexibility. The use of the power is more common in trusts that have situs in non-US jurisdictions. The less frequent use of the power to add beneficiaries in a US-situs trust likely stems from the attitudes of settlors and their advisers towards control. There is also a potential tax implication. The trustee’s power to add beneficiaries will cause the trust to be classified as a grantor trust for US income tax purposes (subject to additional conditions if the settlor is not a US person). Thus, the settlor would be taxable on the trust’s income and gains. That result is often desirable, because it can yield more tax-efficient wealth transfer after taking into account US gift and estate taxes.

VI TRUST DURATION

In many jurisdictions, a settlor can create a perpetual or quasi-perpetual trust. The practical effect of perpetual trusts is the elimination of an arbitrary limit on the duration of trusts. Without any limit on a trust’s duration, a settlor can allow the trustee to determine the proper time to terminate a trust, taking into account the beneficiaries’ circumstances and the costs of administering the trust. For example, the trustee can refrain from making a terminating distribution at a time when a beneficiary is emotionally or financially immature, is suffering injurious addictive behaviours, such as gambling or substance abuse, or faces the likely loss of the distributed property to spousal claims, creditor claims or taxes. By its nature, a multigenerational trust will likely reach practical limitations on its efficient administration. As the beneficiary class expands from generation to generation, the trust may become too unwieldy to administer, or it may divide into many subtrusts that are economically inefficient to administer. In either case, the lack of any limitation on the trust’s duration enables the trustee to assess the administrative costs and complexities and terminate the trust when those costs and complexities outweigh the advantages that the trust offers.

i Non-US jurisdictions

The Bahamas, Guernsey and Jersey allow trusts of unlimited duration. The British Virgin Islands limits the duration of trusts to 360 years. The Cayman Islands allows a STAR trust (its form of purposes trusts) of unlimited duration, but otherwise limits the duration of non-charitable trusts to 150 years.

ii Leading US jurisdictions

New Hampshire and South Dakota allow trusts of unlimited duration. Delaware allows a trust of unlimited duration, except to the extent that the trust directly holds real property. Delaware limits the duration of a trust that directly holds real property to 110 years. Through proper planning, Delaware’s durational limitation on trusts holding real property is avoidable. The limitation does not apply to a trust to the extent that the trust indirectly holds real property, such as through a limited liability company or partnership.

iii Other US jurisdictions

Nevada limits the duration of trusts to 365 years, Tennessee limits their duration to 360 years and Wyoming limits their duration to 1,000 years. A recent scholarly article, however,

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21 26 U.S.C. Section 674.
questions the validity of those states’ statutes allowing for quasi-perpetual trusts.22 In each of those states, the state constitution expressly prohibit perpetuities. The article’s authors assert that the statutes purportedly allowing quasi-perpetual trusts violate those constitutional prohibitions, because the statutes deviate too substantially from the traditional limits on the deferred vesting of property interests. If their analysis is correct, trusts created under those statutes may be limited in duration by the rule against perpetuities or may possibly be invalid.

In Bullion Monarch Mining Inc, Nevada’s highest court held that the rule against perpetuities does not apply to a royalty provision in a commercial contract.23 In the opinion, the court mentions the 365-year period applicable to trusts, and it recognised the legislature’s role in articulating current public policy. The ruling may give some people comfort. The court, however, did not expressly address whether, as it applies to trusts, the statutory 365-year rule is valid under the state’s constitution.

California and Massachusetts continue to apply the rule against perpetuities, but have adopted wait-and-see statutes that mitigate the rule’s harsh effects. New York applies the rule against perpetuities.

VII DISPUTE MITIGATION AND RESOLUTION
i Governance structure
The design and implementation of the governance structure plays a critical role in mitigating disputes. The trust deed should specify the qualifications of trustees, trust advisers and trust protectors. An inexperienced trust adviser can wreak havoc with a trust. A governance structure that includes appropriate checks and balances helps to keep the trustees, trust advisers and the trust protectors accountable. A trust’s governance structure should include procedures for removing and appointing trustees, trust advisers and the trust protectors. In some trusts, term limits and age limits are beneficial.

ii No-contest provisions (forfeiture provision)
A no-contest provision is a provision that terminates a beneficiary’s interest in a trust if the beneficiary contests the trust or the trustee’s actions. A no-contest provision – also called an in terrem clause or forfeiture provision – can serve as a deterrent to litigation.

A no-contest provision changes the economic calculus. This may be especially true in the US, where, in the absence of a no-contest provision, a beneficiary’s downside cost of contesting a trust may be limited to the beneficiary’s own legal fees. In some US jurisdictions, that cost may be nearly nil, because some attorneys are willing to pursue trust contests on a contingency fee basis, collecting a fee only if the attorney succeeds in obtaining some financial benefit for the beneficiary. With a no-contest provision, the beneficiary’s economic analysis changes. The beneficiary’s downside cost is the loss of his, her or its interest in the trust. Thus, a rational beneficiary must have a higher degree of confidence in his, her or

its claim. Of course, not all beneficiaries are rational, and a beneficiary who unsuccessfully challenges a trust that contains a no-contest provision and consequently loses his or her interest in the trust may turn on his or her advisers.24

**Non-US jurisdictions**

In non-US jurisdictions, there is limited case law on the enforceability of no-contest provisions. In *AB Jnr & Another v. MB & Others* (18 December 2012), the Cayman court enforced a no-contest provision. The case followed *AN v. Barclays Private Bank & Trust (Cayman) Ltd* [2006] CILR 365, in which the Cayman court likewise enforced a no-contest provision.

**Leading US jurisdictions**

Within the US, the leading trust jurisdictions enforce a no-contest provision. Delaware, New Hampshire and South Dakota enforce no-contest provisions.25 Delaware and New Hampshire enforce a no-contest provision, even if the beneficiary acts in good faith or with probable cause in contesting the trust. In contrast, South Dakota will not enforce a no-contest provision against a beneficiary who acts in good faith or with probable cause in contesting the trust. In addition to its statutory enforcement of no-contest provisions, New Hampshire expressly authorises a trustee to suspend distributions to a beneficiary who may have violated a no-contest provision.

**Other US jurisdictions**

California enforces no-contest provisions, unless the beneficiary acts in good faith or with probable cause in contesting the trust.26 California courts, however, seem reticent to enforce no-contest provisions. New York enforces no-contest provisions, although the enforceability is based on common law and not statute.27 In New York, the courts disfavour no-contest provision and thus narrowly construe them,28 and a no-contest provision likely is unenforceable to the extent that the beneficiary acts with probable cause in contesting the trust.29 Notably, Florida does not enforce no-contest provisions.30 Florida views a no-contest provision as contrary to public policy, because it limits a beneficiary’s right to challenge a trustee’s actions. Florida has codified its prohibition against the enforcement of no-contest provisions.

### iii Non-judicial dispute resolution

Many wealthy families value privacy. Even families whose business or philanthropic interests expose them to significant public attention often wish to preserve the privacy surrounding

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25 Del. Code tit. 12, Section 3329; NH RSA 564-B:10-1014; and S.D. Codified Laws Section 55-1-46 to 55-1-51.
28 Id.
29 See N.Y. EPTL Section 3-3.5(b).
30 Fla. Stat. Section 736.1108(1). See also *Dinkins v. Dinkins*, 120 So.3d 601 (Fla. 5th DCA 2013).
their wealth and the manner in which they structure the disposition of that wealth. Thus, for many wealthy families, the private resolution of any trust disputes is an important aspect of trust design. In addition to avoiding the publicity that a judicial proceeding may entail, they wish to ensure that they have greater say in the qualifications of the individuals who decide any matters affecting the family's wealth.

The leading US trust jurisdictions expressly recognise non-judicial dispute resolution provisions in trust deeds. New Hampshire recognises non-judicial dispute resolution procedures.\(^{31}\) The procedures must be reasonable, and they may govern any matter except the determination of a trust's validity or the determination of a trust's material purposes. Delaware and South Dakota also recognise non-judicial dispute resolution procedures.\(^{32}\)

Other US jurisdictions generally do not expressly recognise non-judicial dispute resolution provisions in trust deeds; for example, California, Florida, New York and Wyoming.

**iv Lifetime approval of trusts**

A settlor who anticipates the possibility of a dispute concerning the validity of his or her trust may value the ability to obtain a declaratory ruling affirming the trust's validity. For the settlor as well as the court, a key benefit of the settlor seeking the determination is the settlor's availability as a witness. In many instances, a challenge to a trust's validity arises after the settlor's death, at which point the best witness is unavailable. In the US, Delaware and New Hampshire statutorily allows a settlor to seek a court’s determination of a trust’s validity.\(^{33}\)

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\(^{31}\) NH RSA 564-B:1-111A.

\(^{32}\) S.D. Codified Laws Section 55-1-54.

\(^{33}\) Del. Code tit. 12, Section 1311; and NH RSA 564-B:4-406(d).
I INTRODUCTION

Argentina is home to many wealthy individuals and families. Only a small group of these have received sophisticated technical advice in matters of tax planning and estate succession. Consequently there is an important group of wealthy people, mainly concentrated in the interior provinces of the country, lacking an adequate tax, financial and succession plan for their estates.

II TAX

i Introduction

Income tax is a national tax applied on the worldwide income obtained by individuals and legal entities domiciled in Argentina and Argentine branches of foreign entities. Foreign resident individuals are taxed only on their Argentinean income source through a withholding system and based on their presumed income.

Domestic individuals are taxed upon a sliding scale ranging from 5 per cent to 35 per cent depending on the income subject to taxation. Foreign individuals are taxed at a flat 35 per cent rate. The sale of shares, equity interests, bonds and other similar securities are subject to a 15 per cent rate, for both domestic and foreign individuals.

In the case of foreign or domestic individuals, income (trading or interest) derived from securities and shares that are listed in Argentina is generally exempt from income tax.

However, pursuant to Income Tax Regulatory Decree 1344/1998, securities listed in foreign markets would not be exempted in the case of domestic individuals. This is controversial given that income tax expressly exempts capital gains derived from the sale of shares, equity interest and securities that are either listed in stock markets or authorised to be publicly offered. The scope of this exemption was controversially limited by the tax's regulatory decree to securities traded through markets regulated by the Argentine National Securities Commission (CNV). Given that in Argentina, the principle of legality (no taxation without representation) is established in the constitution and that it is also applicable to exemptions, this limitation could be constitutionally challenged because it was not created by a law.

1 Miguel María Silveyra is a partner and Valeria Kemerer and Enrique López Rivarola are associates at Estudio Beccar Varela. Tadeo I. Fernandez and Gustavo Papeschi also collaborated with the preparation of this chapter.
Specifically, the sale of shares is exempt from income tax if they are listed in stock markets authorised by the CNV (according to the regulatory decree), solely in the case of domestic individuals. Foreign individuals cannot claim this exemption.

If the sale of shares is not exempt, a 15 per cent rate is applicable on the net gain from the operation. Foreign individuals can choose to pay the tax at a 13.5 per cent rate on the gross amount paid, rather than 15 per cent on the net gain (several double taxation treaties signed by Argentina limit this rate to 10 per cent).

In the case of Argentine privately listed bonds and trusts' debt and equity securities, interest and capital gains are exempt from income tax, if the securities are authorised to be offered by the National Securities Commission (CNV) and certain requirements are met by the issuer (dividends paid by trusts to holders of equity securities are not subject to tax either). Securities that are traded though local stock markets in Argentina typically comply with these requirements. These exemptions are applicable even in the case of foreign individuals.

In the case of Argentine sovereign bonds, interest and capital gains are also exempt from income tax, for both foreign and domestic individuals.

With regard to taxes on property, all Argentinean residents are subject to personal assets tax on their worldwide assets. The taxable base is, in principle, the value of such assets (except for few exceptions, debts are not deductible). Foreign residents are subject to this tax only upon their assets located in Argentina.

Personal assets tax applies when the assets owned by the taxpayer as of 31 December of each fiscal year exceeds the amount of 950,000 pesos for 2017 and 1,050,000 pesos for 2018 and onwards. The applicable tax rate for Argentinean residents is 0.5 per cent for 2017 and 0.25 per cent for 2018 onwards.

As a consequence of an amendment made to the Personal Assets Tax Law in 2016, the tax rate has been progressively reduced from the original maximum rate of 1.25 per cent and the threshold has also been raised.

In the case of individuals, deposits in Argentine banks and Argentine sovereign bonds are exempt from tax. However, other securities are usually taxed. In the case of ownership of shares of Argentine companies, the tax is paid by the company.

ii Gift and succession taxes

In Argentina only the provinces of Entre Ríos and Buenos Aires have gift and inheritance taxes. Nationally and in the remaining provinces there is currently no such tax.

In the provinces where this tax exists, it is levied on any asset received free of charge, such as gifts, donations, inheritances and legacies, if received by residents of such provinces or, alternatively, if they involve assets deemed to be located in them.

In the case of shares and equity interests, these assets are deemed to be located in such provinces (and, therefore, taxed regardless of the residence of the beneficiary) if the company is incorporated in such jurisdictions, if the shares are physically located there or, controversially, if the companies own assets within the province (and in such proportion). For tax assessment purposes, the shares will be valued by the net asset value of the latest closed financial statements.

The applicable rates vary between 4 per cent and 21.925 per cent depending on the relationship between the beneficiary and the contributor and on the value of the assets. Each province has established its own threshold, which also varies depending on this relationship and is usually adjusted on an annual basis.
iii  Issues relating to cross-border structuring

Local residents can register for foreign tax credits, taxes paid abroad that are deemed equivalent to income tax and personal assets tax, up to the amount of the tax payable in Argentina for the income or assets located or obtained abroad.

In the case of Argentine residents that are stockholders of foreign entities, tax credits for taxes paid abroad for direct or indirect investments in foreign companies can be offset against the payable income tax in Argentina on dividends paid by such entities. In the case of direct stockholders, the local taxpayer must be able to prove ownership of at least 25 per cent of the foreign company’s equity. In the case of indirect shareholders, a minimum 15 per cent ownership must be proved. Foreign taxes paid can be used as a tax credit up to a second-tier subsidiary. In this case, the subsidiary cannot be located in a country deemed to be a tax haven pursuant to Argentine regulation.

In the case of investments involving derivatives, there is some controversy regarding the potential use of income taxes paid abroad as credits. Income deriving from derivatives is deemed to be an Argentine income if its recipient is an Argentine resident. Domestic rules regarding foreign tax credits establish they can only be used by a local resident if they are linked with foreign source income. Therefore, although debatable, these credits could not be offset against income tax derived from this type of operation, unless a specific double taxation treaty states otherwise.

Argentina has double taxation treaties in force with Germany, Australia, Belgium, Bolivia, Brazil, Canada, Chile, Denmark, Spain, Finland, France, the UK, Italy, Norway, Netherlands, Russia, Sweden, Switzerland and Uruguay. These treaties may set forth limitations to the country’s tax jurisdiction in relation to income or personal asset tax and special rules regarding foreign tax credits. Except for the treaty with Bolivia, Argentine double taxation treaties are based on the OECD and UN tax models.

iv  Issues impacting entrepreneurs as holders of active business interests

Argentine corporations and limited liability companies are not pass-through entities pursuant to Argentine legislation and, therefore, must report their income and pay the resulting income tax at a 35 per cent rate. These two types of entities comprise the vast majority of Argentine companies.

Payment of dividends and utilities by those entities is not subject to income tax in Argentina, unless equalisation tax is applicable. Equalisation tax is applicable only on profits being distributed that have not been taxed at corporate level (in which case a 35 per cent withholding on this difference is due).

However, dividends paid by foreign companies are subject to income tax in the case of domestic individuals, at a 5 per cent to 35 per cent rate (unless an applicable double taxation treaty establishes otherwise). The disbursement of dividends by the foreign company to a domestic individual is not subject to income tax if the beneficiary can prove that the profits that are paid out derive from dividends or utilities originally paid from Argentina to such foreign company (that have been taxed in Argentina from the same individual or a local company).
III SUCCESSION

i Applicable jurisdiction and law

On 1 August 2015 a new Civil and Commercial Code (CCCN) entered into force and replaced both the former Civil Code and the Commercial Code. As a consequence, the inheritance, matrimonial and the private international law rules have been significantly amended, and there is still no sufficient case law on the issues addressed herein to fully foresee the final interpretation that the new provisions may entail.

According to the CCCN, succession to the estate of a deceased person is governed by the law of the country where the decedent was domiciled at the time of his or her death, regardless of the decedent’s or his or her inheritors’ nationality. However, and regardless of the above general rule, Argentine law will mandatorily govern all issues concerning real estate located in Argentina and precludes the application of any foreign law. The CCCN further provides that the same law governs the content and validity of wills.

Regarding jurisdiction, the general rule is that the judge sitting where the deceased was last domiciled shall have jurisdiction to hear the case. There is an exception to this rule when real estate is located in Argentina; in that case the judges sitting at the place where the real estate is located have jurisdiction to hear the case.

It is worth pointing out that pursuant to the Constitution, international treaties pre-empt domestic law. However, only two treaties are relevant for our analysis (i.e., the Treaties on International Civil Law (Montevideo) of 1889 and 1940), and given their limited territorial application, we will just point out that they set forth that the applicable law will be the law where the deceased person’s assets were located at the time of the death and that wills granted through a public deed in any member countries of the treaty will be valid in all other country members.

Although Argentina signed the 1989 Hague Convention on the Law Applicable to Succession of the Estates of Deceased Persons, this convention is not yet effective, and has had a low rate of acceptance.

Argentina has not signed the 1961 Hague Convention on the Conflicts of Laws relating to the Form of Testamentary Dispositions.

ii Outline of Argentine succession system

Forced heirship system

Argentina has a forced heirship system that limits the individual’s ability to freely dispose of his or her property by gifts inter vivos or wills. In this regard, according to the law individuals are able to dispose of their property by any of these means as long as a minimum share of their estate (reserved share) is reserved for their spouses, descendants and ascendants (forced heirs).

Descendants have the right to a reserved share of two-thirds of the decedent’s estate, whereas ascendants and spouses have the right to reserved shares of half of the estate of the deceased. If there are heirs entitled to share the state with different reserved shares (e.g., spouse and descendants), the highest reserved portion applies globally.

2 CCCN, Article 2,644.
3 Montevideo Treaty of 1889, ratified by Argentina, Bolivia, Colombia, Paraguay, Peru and Uruguay, while Montevideo Treaty of 1940, only by Argentina, Paraguay and Uruguay.
4 CCCN, Article 2,445.
The general rules described above are, however, significantly different when there are disabled heirs. In that case the law allows the individuals to improve such disabled heirs’ portion by reducing the reserved share of the other heirs by up to one-third.\(^5\)

The reserved shares are estimated using the aggregate value of the estate at the time of the decedent’s death and the computable gifts provided for each of the forced heirs.\(^6\) In the case of the spouse, the value of the marital assets belonging to the surviving spouse shall be subtracted from the base of calculation.

Beyond the reserved shares, individuals may freely dispose of their property, either by gift during their lifetime, or by means of a will. This disposable portion of the individual estate is called the ‘available share’.

Notwithstanding all of the above, in limited and serious cases listed by the CCCN,\(^7\) forced heirs may be deemed unworthy of inheriting and, therefore, can be excluded from the succession (e.g., when any forced heir is judged to be the author, accomplice or participant in an intentional crime offence against the deceased, his or her honour, sexual integrity, liberty or property).

**Order of vesting**

The law also determines how heirs are vested over the deceased’s estate: \(^8\)

a Descendants: they exclude the ascendants and concur with the spouse. Concurrence among descendants and the spouse is limited to the decedent’s non-marital property. Spouses do not concur as heirs with regard to marital property because they receive their half of such property as a result of the dissolution and liquidation of the marital property community. The decedent’s own property is distributed in equal portions among all of the descendants and the spouse. Among themselves, descendants equally inherit the deceased’s estate.\(^9\) Grandchildren inherit by representing the predeceased offspring.\(^10\)

b Ascendants: if there are no descendants, ascendants concur with the spouse over the non-marital property in halves.\(^11\) Among themselves, ascendants equally inherit the deceased’s estate.\(^12\) Closer generations exclude further ascendants.

c Spouse: the spouse may concur with descendants or ascendants.

d Collateral relatives: if no descendants, ascendants or spouse exist, collateral relatives, until the fourth degree of relationship, are equally entitled to the estate.

**Legal actions to protect the inheritance rights**

Rightful heirs have two options to protect and demand compliance with their inheritance rights.

First, there is an equalisation action that seeks to protect equality among heirs within the same rank of concurrence. This action entitles any rightful heir to claim that certain kinds of gifts received by any other heir during the decedent’s lifetime should be deemed

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5 CCCN, Article 2,448.
6 CCCN, Article 2,445.
7 CCCN, Article 2,281.
8 CCCN, Articles 2,424 through to 2,443.
9 CCCN, Article 2,446.
10 CCCN, Article 2,448.
11 CCCN, Article 2,434.
12 CCCN, Article 2,431.
as an ‘inheritance advance’ and therefore as part of the rightful portion of the inheritance corresponding to this heir. The result of this equalisation action would only be a credit arising out of the acknowledgement that another rightful heir has received from the decedent and during his or her lifetime certain assets that shall be deemed an ‘inheritance advance’ to such heirs.

Second, there is a reduction action that seeks to protect the reserved share and is meant to reduce any devise or bequest made in the will or as a gift *inter vivos* by the decedent\(^{13}\) to the extent that it prevents a forced heir’s right to his or her reserved share. This action entitles any forced heirs to file a claim against those heirs, legatees and grantees that have received gifts and legacies in excess of their rightful portion or in excess of the available share, in order to have their legacies reduced or their gifts returned. Reduction affects wills dispositions first, and in case their reduction were not enough to recompose the reserved share of the claimant, affects gifts, beginning by those more recent in time.

It may be reasonably construed that the reduction action regarding gifts is subject to a 10-year statute of limitation counted from when the heir, legatee or grantee took possession of the gifted asset.\(^{14}\) With regard to the reduction action against bequests or devises made in a will, no specific statute of limitations is provided for. It may be argued that the generic statute of limitation (i.e., five years) applies.\(^{15}\) However, it could also be construed that the applicable statute of limitation is 10 years (the term for accepting an inheritance), or even 20 years (the adverse possession term for real property).

### Agreements on future inheritances

Any general agreement entered into by and between future heirs during the deceased’s life is null and void.

However, the CCCN has allowed agreements over future inheritances as long as the covenants only fall over the equity of companies or other business ventures with the aim of maintaining the management unity or preventing or solving conflicts, and the dispositions do not deprive forced heirs of their reserved portions, nor do they affect the spouse or third parties’ rights.\(^{16}\)

### iii Inheritance proceedings

After an individual has passed away, a judicial proceeding must commence (the inheritance proceeding) with the purposes of identifying the heirs, determining the content of the inheritance, collecting any outstanding credit, paying the debts, bequests and devises, and filing certain assets before the public registries.\(^{17}\)

\(^{13}\) Please note that relevant case law (although prior to the CCCN) has ruled that: (1) the fact that a foreign trust [in the analysed case, an UK trust] was subject to foreign law, does not prevent the transfer from being subject to Argentine law for the purposes of an inheritance proceeding; and (2) to the extent that the beneficiary had the right to demand the delivery of the proceeds of the trust and that such trust was incorporated for no consideration against the beneficiary, such trust should be deemed a gift under Argentine law (for the purposes of the equalising and reduction action).

\(^{14}\) CCCN, Article 2,459.

\(^{15}\) CCCN, Article 2,560.

\(^{16}\) CCCN, Article 1,010.

\(^{17}\) CCCN, Article 2,335.
The inheritance proceeding is filed before the judge with jurisdiction in the decedent's last domicile or, in the case of real property located in Argentina, where the assets are located.\textsuperscript{18} If real property is located in several of the Argentine provinces, the applicant may (but is not required to) file its application in any of those jurisdictions.

The administration of the estate must be carried out by an administrator, to be appointed either by the testator or the heirs acting by majority. Non-resident individuals may be appointed as executors of the estate.

The length of inheritance proceedings varies according to the complexity of the case. A straightforward case (e.g., with few assets located in urban areas and no minors involved) can take approximately five to six months, from its commencement to the recording of the heirs’ title at the relevant registries.

iv Wills

Wills are unusual in Argentina, and are generally only made by wealthy individuals. Most people die without making a will, in which case the rules on intestacy described above apply.

If made in Argentina, a will is only valid when made pursuant to the formalities provided by Argentine law.

Therefore, a will made by a foreigner in his or her country’s consulate in Argentina may not be considered valid by an Argentine court, with the exception mentioned above in the Montevideo treaties for the country members of such treaties.

Under general principles contained in the CCCN, a will made abroad is enforceable if it complies with the law of the place of its making, the testator's place of residence or the country of the testator's nationality.

v Marital property regime

The conflict of laws rules provided in the CCCN states that the marital property regime – in all that is not forbidden on matters of property by the law of the place where the assets are located – is ruled by the spouses' agreement.

If the agreement was entered prior to the marriage, it will be governed by the laws of the first marriage domicile. The agreements entered after the date of marriage will be governed by the laws of the spouses domiciles at the time of the signing of the agreement.

Under the CCCN, the future spouses have the possibility (by entering into a marriage agreement) of choosing between a communal property regime or a separate property regime.

CCCN\textsuperscript{19} provides that in the event that no marriage agreement is made or if the marriage agreement does not set forth any provision regarding the property regime, the traditional shared property regime will be applied.

Conventions may be created for the purpose of: (1) designation and appraisal of the goods that each of the future spouses bring to the marriage; (2) admission of debts; (3) donations made between each other; or (4) choice of marriage regime.

The CCCN provides that in order for the marriage agreements to be valid, they must be executed by means of a public deed, but in order for the marriage agreements to be effective towards third parties, the marriage certificate must include a side note stating the regime chosen.

\textsuperscript{18} CCCN, Articles 2,336 and 2,643.
\textsuperscript{19} CCCN, Article 463.
In the event that the spouses decide to change the regime, the amendment must also be made through public deed, after one year of the marriage agreement’s date.

Creditors affected by this change may object within one year from the date they became aware of the change.

When a marriage is terminated (by death or divorce), the assets that qualify as shared property are grouped together and, after the applicable liabilities and claims of each spouse have been cancelled, divided and distributed equally between the spouses.

vi  Same-sex marriages and cohabitation

Argentine law recognises marriage between same-sex couples, so the same marital property regime applies in such cases.

The CCCN also recognises certain rights to cohabitees provided they have been together for at least two years.

Through the means of cohabitation agreements, cohabitees will be able to regulate different aspects of their life together, such as economic aspects and other responsibilities.

The CCCN also provides protection for the family home and, in the event of the death of one partner, the survivor is granted the right of free housing in the home they shared for a period of two years. However, the CCCN does not recognise cohabitees’ inheritance rights over their partner’s assets.

IV  WEALTH STRUCTURING & REGULATION

i  Commonly used vehicles for wealth structuring, such as trusts, foundations or partnerships

As mentioned in Section I, only a small group of wealthy people has taken advantage of sophisticated structures in order to improve their estate and business organisation from a tax and succession law standpoint. Within this group it is common to see structures that take advantage of foreign trusts and foundations, combined with other structures that are more frequently used, such as company reorganisations and gifts _inter vivos_ (usually structured in a way by which the grantor withholds the legal right of using and enjoying the fruits or profits of the property until his or her death). After the CCCN entered into force the change of marriage regime emerged as another instrument for estate reorganisation.

ii  Legal and tax treatment of commonly used vehicles and typical advantages and disadvantages to personal ownership or control

In the case of Argentine residents that invest their wealth abroad, typically either a corporation or a trust is incorporated in a foreign jurisdiction.

In the case of foreign corporations (or entities that issue shares), if they are incorporated in jurisdictions deemed to be ‘cooperative for fiscal transparency purposes’ (i.e., non tax havens), profits generated by such entities are not subject to taxation in Argentina, until (and if) dividends are effectively paid to the shareholders (no CFC rules are applicable). Thus, income tax on those profits is deferred.

The Argentine Tax Authority has published the list of the jurisdictions deemed to be ‘cooperative’ on its website and regularly updates it. This list currently includes several jurisdictions that have historically been deemed to be tax havens by other countries, including, for instance, British Virgin Islands, Cayman Islands, Panama and many others.

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However, in these structures the shares owned by the individual would be subject to personal assets tax.

Another traditional structure used involves the creation of an irrevocable trust abroad. This type of structure also allows income tax deferrals, given that only the disbursement of utilities by the trust to its beneficiaries would be subject to income tax. In addition, if the beneficiary is capable of proving that the amounts paid to him or her do not derive from profits obtained by the trust, but rather from redemption of capital originally contributed to it, such amounts would not be subject to taxation.

The main advantage of this type of trust would be that the settlor would not have to pay personal assets on the assets transferred to the trust, provided that it is not disregarded by the tax authority and the assets deemed to be owned by him or her, as an application of the substance over form principle.

Although in the past other structures using double taxation treaty benefits might have been used, their use for these purposes has dwindled significantly as a result of the termination of the treaties that previously allowed them. The Argentine–Austrian Treaty was terminated in 2008 and the Spanish, Swiss and Chilean treaties were terminated in 2012 (and later renegotiated but with considerably fewer benefits to taxpayers).

Tax-free reorganisations procedures are typically used to split family companies between their members, without any tax burden. These are complex procedures that require the compliance of several formal and substantial requirements, among which stand out the prohibition for the owners to sell the reorganised entities or change their activities within two years of the reorganisation.

To avoid commencing an inheritance proceeding and the costs involved (court tax and attorney’s fees), it is customary for individuals to grant gifts *inter vivos*.

###iii applicable anti-money laundering regime

The Argentine Criminal Code and Law No. 25.246 are the main regulations that govern and punish anti-money laundering (AML) offences.

This law sets forth a list of ‘regulated entities’ (which involve both public and private entities, as well as natural persons) that are obligated to, among other duties, to perform know-your-client procedures and report any suspicious operation to the Financial Information Unit.

Likewise, pursuant to AML Law, persons or legal entities that act as trustees or that own or are affiliated with trust accounts, trustors and trustees in connection with trust agreements must carry out AML measures, which include, as mentioned before, but are not limited to: know-your-client procedures, issuance of an AML manual, training employees on the subject, etc.

Argentina is a member of the Financial Action Task Force on AML in South America, the Egmont Group and the Group of Experts for the Control of Asset Laundering, as well as other AML-specific organs within the region and the Organisation for Economic Co-operation and Development.
V CONCLUSIONS & OUTLOOK

Even though there are some wealthy Argentine individuals and families that have been duly assessed in order to plan their estate organisation from a financial, tax and succession standpoint, a significant portion of Argentina’s wealthy population still lacks accurate advice with regard to its estate planning.

Recently a tax amnesty has taken place in Argentina. This, and the fact that AML regulation is becoming tighter, may cause individuals to start structuring the organisation of their assets and succession.

Finally, the government is planning a tax reform. Although no extension of the gifts and succession taxes to a national level is foreseen for the time being, such extension should not be discarded in the medium term.
Austria is a landlocked country in central Europe with a population of approximately 8.5 million. It is one of the most attractive countries in the world to live in. It combines economic and political stability, a clean and safe environment and an excellent infrastructure. It is bordered by the Czech Republic and Germany to the north, Hungary and Slovakia to the east, Slovenia and Italy to the south and Switzerland and Liechtenstein to the west. Austria’s territory covers approximately 32,400 square miles and is highly mountainous because of its location within the Alps. Historically speaking, the origins of modern-day Austria date back to the time of the Habsburg empire.

Austria has a GDP (PPP) per capita of approximately US$48,000, making it one of the richest countries in the world. Major industries in Austria are tourism, banking, foodstuffs, luxury commodities, mechanical engineering, steel construction, chemicals and vehicle manufacturing.

Austria is a member of the EU (including the eurozone and Schengen), the OECD and the WTO. Austria therefore offers the opportunity to become resident in the Schengen territory with minimal bureaucratic requirements.

In the worldwide ranking of cities based on quality of living conducted by the HR consultancy Mercer in 2017, Vienna is in first place, and has consistently been ranked among the top three in the past.

While Austria admittedly has high income tax rates, the fact that no wealth, gift and inheritance taxes are levied is often the reason for high net worth individuals to consider relocating to Austria.

II TAX

i Income tax

Residency

For income tax purposes, Austrian tax law distinguishes between residents and non-residents. Individuals having a domicile or their habitual abode in Austria are considered as residents and are subject to unlimited income tax liability on their worldwide income. All other

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1 Niklas JRM Schmidt and Karl Binder are partners at Wolf Theiss.
individuals (i.e., individuals having neither a domicile nor their habitual abode in Austria) are considered non-residents and are subject to limited income tax liability, only on their Austrian-source income.\(^3\) Citizenship is thus not decisive for the purposes of tax residency.

A domicile for tax purposes is maintained where a taxpayer has a dwelling place under circumstances that permit the conclusion that the taxpayer intends to keep and use it.\(^4\) Such dwelling place must consist of one or more rooms that are furnished for the purpose of living there regularly. In most cases, a dwelling place consists of rooms that are either owned or rented by the respective taxpayer. However, the legal title of the dwelling place is not decisive, but rather the factual possibility to make use of it. Thus, a hotel room or a holiday home can also qualify as a domicile. Merely having a dwelling place is not enough: in addition, there have to be circumstances that permit the conclusion that the taxpayer intends to keep and use it for a longer period of time (typically at least six months). A residence notification to the respective municipal authorities may, for example, serve as an indication thereof.

An habitual abode for tax purposes is maintained where a taxpayer stays under circumstances that permit the conclusion that the taxpayer intends to dwell there not only temporarily – staying in Austria for more than six months irrefutably leads to an habitual abode, even for the first six months.\(^5\) Whereas a taxpayer can have more than one domicile, it is never possible to have more than one habitual abode. It is not necessary to stay in the same municipality; rather, dwelling anywhere in Austria is decisive. Temporary stops in or visits to Austria do not result in an habitual abode in Austria. Furthermore, repeated short-term stays in Austria are generally not added up for the purposes of the six months clause.

However, apart from the statutory rules of the Austrian Income Tax Act, attention also has to be paid to an ordinance regarding secondary residences issued by the Austrian Minister of Finance. Pursuant thereto, in case of taxpayers whose centre of vital interests is outside of Austria for more than five calendar years, an Austrian dwelling place qualifies as a domicile only in such years in which the dwelling place is used (alone or together with other Austrian dwelling places) for more than 70 calendar days. This rule is only applicable if the taxpayer keeps a list of the days during which the dwelling place is used.

**Tax rates and tax basis**

An individual’s income is subject to progressive income tax, with the following rate bands applying:

\[\begin{align*}
 a & \text{ up to and including } €11,000: \text{ zero per cent;} \\
 b & \text{ over } €11,000, \text{ up to and including } €18,000: \text{ 25 per cent;} \\
 c & \text{ over } €18,000, \text{ up to and including } €31,000: \text{ 35 per cent;} \\
 d & \text{ over } €31,000, \text{ up to and including } €60,000: \text{ 42 per cent;} \\
 e & \text{ over } €60,000, \text{ up to and including } €90,000: \text{ 48 per cent;} \text{ and} \\
 f & \text{ over } €90,000: \text{ 50 per cent.} \quad \text{\(^6\)}
\end{align*}\]

Additionally, for the years 2016 to 2020, a new maximum tax rate of 55 per cent shall become applicable to income exceeding €1 million. Interest on bank accounts is subject to

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\(^3\) Cf. sec. 1(3) of the Austrian Income Tax Act.

\(^4\) Cf. sec. 26(1) of the Austrian Federal Fiscal Procedures Act.

\(^5\) Cf. sec. 26(2) of the Austrian Federal Fiscal Procedures Act.

\(^6\) Cf. sec. 33(1) of the Austrian Income Tax Act.
a flat rate of 25 per cent; interest on bonds, dividends on stocks, capital gains from financial instruments and income from derivatives are subject to a flat rate of 27.5 per cent; and capital gains from real estate are subject to a flat rate of 30 per cent.\textsuperscript{7}

The income tax base is defined as the sum total of the following categories:

\begin{itemize}
\item[a] income from agriculture and forestry;
\item[b] income from professional and other independent services;
\item[c] income from an active trade or business;
\item[d] employment income;
\item[e] investment income;
\item[f] rent, lease payments and royalties; and
\item[g] other specified income (including certain annuities and capital gains on private property).\textsuperscript{8}
\end{itemize}

Certain personal allowances exist for the taxpayer and family members.\textsuperscript{9}

\textbf{Procedural aspects}

While income tax is levied by way of assessment, income tax on employment income is generally levied by way of withholding by the Austrian employer.\textsuperscript{10} Such wage tax is a prepayment of the employee’s final income tax and is credited against the employee’s assessed income tax liability if the taxpayer files (voluntarily or in certain cases on an obligatory basis) an annual tax return.

Austria does not provide for a married couples’ tax-splitting concept. Husband and wife are, rather, taxed separately on a stand-alone basis with their respective individual incomes.

Individuals are obliged to file their income tax returns electronically – paper-based filing is only exceptionally permissible. The income tax return must be filed by 30 April or, if electronic filing is made use of, by 30 June of the following year. Taxpayers represented by tax advisers benefit from longer deadlines. An extension of the filing date is possible in justified cases.\textsuperscript{11}

Quarterly prepayments of income tax are due on 15 February, 15 May, 15 August and 15 November. Such prepayments are creditable against the final amount of income tax assessed. Any balance is payable within one month after receipt of the corporate income tax assessment notice.\textsuperscript{12}

\textbf{Preferential tax regime for persons relocating to Austria}

Pursuant to Section 103 of the Austrian Income Tax Act, the Austrian Minister of Finance may eliminate an additional tax burden resulting from an individual’s relocation to Austria, namely for people whose relocation to Austria serves the promotion of science, research, arts or sports and is thus in the public interest (additionally, in the case of scientists and researchers, 30 per cent of their income may be exempted from tax for five years). The Austrian Minister of Finance may prescribe such regulations as may be necessary or appropriate to carry out these provisions. In this respect, a regulation has recently been made available, which deals with certain procedural and substantive issues in connection with the above-mentioned provision.

\textsuperscript{7} Cf. secs. 27a and 30a(1) of the Austrian Income Tax Act.
\textsuperscript{8} Cf. sec. 2(3) of the Austrian Income Tax Act.
\textsuperscript{9} Cf. sec. 33 of the Austrian Income Tax Act.
\textsuperscript{10} Cf. sec. 78(1) of the Austrian Income Tax Act.
\textsuperscript{11} Cf. sec. 134 of the Austrian Federal Fiscal Procedures Act.
\textsuperscript{12} Cf. sec. 45 of the Austrian Income Tax Act.
First, the regulation deals with the mandatory content of an application for preferential tax treatment (which generally has to be submitted before the individual’s relocation to Austria, but at the latest, six months thereafter). Second, it defines in which cases the relocation to Austria of a scientist, researcher, artist or athlete serves the public interest. Third, it outlines in detail how an additional tax burden resulting from an individual’s relocation to Austria (which, as described above, is a high-tax country) is to be eliminated: non-Austrian sourced income is to be subjected to a flat tax rate. This is determined by dividing the individual’s non-Austrian taxes paid in the three years prior to the relocation through its non-Austrian income earned in this period of time, with a minimum rate of 15 per cent applying. After 10 years, the flat rate rises by two percentage points per year; the preferential regime ends once the tax rate reaches at least 48 per cent. Interestingly, if a taxpayer avails himself or herself of the flat rate on non-Austrian sourced income, double-tax treaties may not be relied on (clearly a treaty override). Finally, the draft stipulates the cases in which the preferential tax treatment is prematurely forfeited (e.g., if the individual ends his or her relevant activities).

ii Wealth tax

Austria does not levy a general wealth tax on all types of personal assets. A special type of wealth tax only on Austrian real estate is currently being levied by the Austrian municipalities.13

iii Gift and inheritance tax

Austria does not currently levy a gift or inheritance tax. Such taxes were abolished in August 2008. There have been ongoing political discussions regarding a reintroduction, but since 2008 the coalition parties have not come to a consensus.

A special notification obligation exists for gifts of money, receivables, shares in corporations, participations in partnerships, businesses, moveable tangible assets and intangibles.14 The notification obligation applies if the donor or the donee has a domicile, habitual abode, legal seat or place of effective management in Austria. Both the donor and the donee are obliged to effect the gift notification within three months of the donation. The notification has to be done electronically. Intentional violation of the notification obligation may lead to the levying of fines of up to 10 per cent of the fair market value of the assets transferred. Not all gifts are covered by the notification obligation. In case of gifts to certain related parties, a threshold of €50,000 per year applies; in all other cases, a notification is obligatory if the value of gifts made exceeds €15,000 during a period of five years. Furthermore, gratuitous transfers subject to Austrian foundation entry tax are exempt from the notification obligation.

The sale of Austrian real estate triggers real estate transfer tax of normally 3.5 per cent,15 with the tax basis being the sale price. Similarly, gifts and inheritances of Austrian real estate are also taxable. In the case of transfers between relatives, the tax basis of such transactions is the value of the transferred real estate with the tax rate being:

- 0.5 per cent for amounts between €0 and €250,000;
- 2 per cent for amounts between €250,000 and €400,000; and
- 3.5 per cent for amounts over €400,000.

14 Cf. sec. 121a of the Austrian Federal Fiscal Procedures Act.
Gifts and inheritances of assets to Austrian private foundations are generally subject to a foundation entry tax at a rate of 2.5 per cent.

**iv  Bank confidentiality and exchange of information between tax authorities**

Bank confidentiality is a highly cherished tradition in Austria and a very emotional topic for the public at large. It was introduced into statutory law in 1979. Although the provisions were originally quite strict, they have in the last few years been progressively loosened, mainly because of pressure from abroad regarding taxation. The starting point for this development was certainly the passing of the EU Savings Directive. In 2009, this was followed by the OECD’s push for facilitating the cross-border exchange of banking information upon request between tax authorities, and in 2014, by the expanded initiative to exchange such information automatically between tax authorities under what is known as the Common Reporting Standard. Finally, in 2015, as a direct result of the concessions made in an international context by granting foreign tax authorities access to Austrian banking information, the scope of Austrian bank confidentiality in a purely domestic tax context was dramatically eroded. Today, bank confidentiality in Austria pales in comparison with former times.

**III  SUCCESSION**

**i  Introduction to succession**

There are two different approaches that could be decisive for the allocation of a deceased person’s estate. The first principle is that of family succession, according to which the estate shall be distributed among the family members of the deceased. This is based on the consideration of blood relationship on the one hand and on cohabitation and joint housekeeping on the other. The second principle is the idea of unrestricted disposal, which shall allow the testator to provide for an allocation that he or she deems reasonable.

**Statutory law**

Austrian succession law reflects elements of both principles. If a person passes away without having left a will, it is the closest relatives who are legal heirs: usually the children of the deceased person, his or her spouse or his or her ‘registered partner’ (a registered partnership is a comparably new concept, similar to a marriage, that has been introduced for same-sex life partners). Under particular circumstances, the parents or siblings or even a life partner of the deceased can be legal heirs as well.

The share of a legal heir in the estate depends on the relationship to the deceased. If the deceased was married and had children, the surviving spouse is entitled to one-third of the estate and the children to the remainder in equal shares. If the deceased was married but had no children, the spouse would be entitled to two-thirds, whereas the parents of the deceased would be entitled to one-third.

**Compulsory portion**

Generally, a testator is free to deviate from the statutory concept outlined above, but must take into account the ‘compulsory portion’. This means that a certain group of persons (statutory heirs) is entitled to claim a portion of a deceased’s estate, even if there is a conflicting testamentary
disposal or contractual agreement. There are only very limited grounds for which a testator could deprive statutory heirs of their compulsory portion. In terms of Austrian succession law, statutory heirs are descendants of the deceased and his or her spouse or registered partner.

Moreover, Austrian succession law comprises a variety of rigid provisions safeguarding that testators cannot diminish their estate to the detriment of the statutory heirs. As a consequence, even donations that have been effected well before the death of a testator can be taken into account upon the request of statutory heirs when determining their compulsory portion. Although time limits for such claims may apply, the legal position of statutory heirs is well protected.

The compulsory portion is typically half of the statutory quota (see above).

**Acquisition of the estate by the legal successors**

Once a person passes away, that person’s rights and obligations are assumed by his or her estate. The estate is deemed a legal entity that is either represented by the legal heirs or a court-appointed administrator. The estate ceases to exist once probate proceedings are completed and the heirs assume the estate’s rights and obligations. Such transfer of rights and obligations to the heirs does not happen by way of law, but requires an explicit declaration to be given by the heirs in writing upon the probate court’s request within an adequate time, not exceeding one year.

**ii Key legislative changes affecting succession**

As of 1 January 2017, a considerable part of the provisions of succession law comprised by the Austrian Civil Code (which dates back to 1811) has been amended and modernised. The main changes are the following:

- **a** The rescission of the compulsory portion of the ascendants of a testator.
- **b** The position of life partners has been strengthened.
- **c** The due date of the compulsory portion can be deferred for up to five years (10 years in exceptional cases). This should avoid fire sales of companies or family businesses caused by liquidity shortages, following claims of statutory heirs who have not received sufficient assets from the estate to cover their compulsory portion.
- **d** Stricter formal requirements for last wills apply.

**iii Relevant cross-border developments**

On 17 August 2015, the European Regulation on jurisdiction, applicable law, recognition and enforcement of decisions and acceptance and enforcement of authentic instruments in matters of succession and on the creation of a European Certificate of Succession entered into force.

This meant a significant change to the existing Austrian legal framework in succession matters, which essentially referred to the citizenship of a testator, rather than to its habitual residence at the time of death, to answer the question of jurisdiction and of the applicable substantial law. Practical experience still needs to show whether the regulation indeed facilitates the handling of cross-border inheritance matters. Up until now, case law is, of course, still rare and many questions are yet unanswered.
IV  WEALTH STRUCTURING & REGULATION

i  Private foundation

The most important wealth-structuring vehicle used in Austria is the private foundation. This is a legal entity without owners or shareholders that is endowed with assets by the founder and that, by way of the use, management and investment of its assets, shall serve a legally valid purpose determined by the founder. The private foundation is established by way of a unilateral declaration of intent by the founder and comes into legal existence by way of registration with the Austrian commercial register. A private foundation has legal personality.

The private foundation may serve any permissible purpose. The purpose can be freely chosen by the founder, but must be described in such a way that it may serve as a general guideline for the actions of the bodies of the private foundation. In practice, the financial support of the beneficiaries as well as the preservation, investment and administration of assets are the most common purposes. However, a private foundation must not be founded with the sole purpose of preserving its assets. Further, it has to be noted that a private foundation may neither carry out a commercial activity exceeding a mere ancillary activity nor be a shareholder with unlimited liability of a registered partnership.

A private foundation can be set up both inter vivos or mortis causa. The founder has to be designated in the deed of foundation with his or her name, address and date of birth. In addition, the deed of foundation has to contain the following information:

a. the endowment (at least €70,000);

b. the purpose of the private foundation (e.g., financial support of the beneficiaries);

c. the designation of the beneficiaries or of a body that has to determine the beneficiaries;

d. the name of the private foundation (which must contain the wording Privatstiftung);

e. the seat of the private foundation (which must be in Austria); and

f. the term of the private foundation (which may be limited or unlimited).

The deed of foundation may further include provisions regarding the appointment, revocation and office period of members of the bodies (board of directors, auditor and supervisory board, if any), the establishment of an optional supervisory board or of further bodies to ensure the pursuit of the purpose of the private foundation (e.g., advisory board). Certain rights of the founder have to be contained in the deed of foundation to be valid, such as the right of amendment of the deed of foundation, the admissibility of the setting up of a supplementary deed of foundation, as well as the right to revoke the private foundation. Furthermore, the deed of foundation may contain rules on the determination of beneficiaries, as well as of ultimate beneficiaries.

Some provisions can be contained in the supplementary deed of foundation, which does not need to be disclosed to the commercial register and thus to the public. The supplementary deed of foundation usually contains provisions regarding the types and amounts of distributions by the private foundation to beneficiaries and further endowments exceeding the minimum endowment of €70,000.

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16 Cf. sec. 1(1) of the Austrian Act on Private Foundations.
17 Cf. sec. 7(1) of the Austrian Act on Private Foundations.
18 Cf. sec. 1(2) of the Austrian Act on Private Foundations.
19 Cf. in detail sec. 9(1) of the Austrian Act on Private Foundations.
Tax aspects of private foundations

In connection with private foundations, three levels of taxation exist, namely:

a. The taxation of endowments to a private foundation – gratuitous endowments to a private foundation are subject to foundation transfer tax at, in general, a rate of 2.5 per cent of the fair market value of the assets endowed.

b. The taxation of income on the level of the private foundation – the private foundation is generally subject to corporate income tax at a rate of 25 per cent, with dividends received generally being tax-exempt. Some types of income (such as interest income) are instead subject to a 25 per cent interim tax. Interim tax is not payable if and to the extent certain distributions are made.

c. The taxation of distributions to beneficiaries – distributions of any kind to a beneficiary being an individual are subject to a withholding tax of 27.5 per cent, having the effect of final taxation. In contrast, distributions of substance may normally be effected tax-neutrally. Distributions to beneficiaries resident outside of Austria for tax purposes can ultimately be effected free of Austrian tax under many double taxation treaties.

Tax aspects of trusts

Neither the Austrian Income Tax Act nor the Austrian Corporate Income Tax Act contains explicit provisions dealing with trusts. Given the fact that Austria is a civil law jurisdiction, this is hardly surprising. The trust concept is actually alien to Austrian civil and tax law. Very few court cases exist and not much guidance has been given by the tax authorities concerning the tax consequences of setting up a trust, being a beneficiary of a trust and receiving benefits from a trust. In addition, until recently, not much scholarly literature had been written on this topic.

Depending on their set-up, trusts can be seen for income tax purposes as either non-transparent (i.e., separate taxable entity) or transparent (i.e., look-through). Broadly speaking, non-transparency is the case if neither the settlor nor the beneficiary has comprehensive instruction and supervision rights regarding the management of the trust assets. The settlor, for example, has no such rights: (1) in the case of a testamentary trust; (2) in the case of a trust inter vivos where he or she dies after setting up the trust; and (3) in the case of a discretionary trust where he or she has transferred the entire management to the trustees (who have full discretion) and where he or she has only determined the beneficiaries.20 Transparency would, for example, be the case with bare trusts, where the trustee acts on the instruction of the beneficiaries and has to transfer the assets to them upon request; the same would be true if the settlor had strong rights regarding the trust assets and these were transferred to the beneficiaries after his or her death (except, obviously, if the beneficiaries had no knowledge of the trust or their rights).

V CONCLUSIONS & OUTLOOK

Austria, as a wealthy and sophisticated jurisdiction with a stable political system in the centre of the EU, remains a strong candidate for attracting high net worth individuals in the years to come.

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20 Cf. Austrian Supreme Administrative Court, 20 September 1988, 87/14/0167; EAS 2378; EAS 2804.
Chapter 8

BAHAMAS

John F Wilson

I INTRODUCTION

It is not by chance that the Bahamas has over numerous decades distinguished itself as a leading international financial centre. Much thought, effort and focused attention have gone into producing the ideal environment in order to position the Bahamas as the pre-eminent offshore tax-neutral jurisdiction with the physical resources and legislative framework necessary to attract the business of the ultra high net worth individuals and families. In addition, its progressive residency regime and available physical resources make it possible for the ultra-high and high net worth individuals to follow their wealth and to live where they bank. With its close proximity to the US, and established links and direct air lifts to North American, European and Latin American markets, the Bahamas’ geographic advantage is unequalled by its competitors.

The Bahamas’ mature and sophisticated financial services industry is home to a number of the world’s largest wealth providers but there are also a number of well-capitalised and financially strong boutique institutions available for those who prefer a more personalised relationship. The industry is serviced by a well-trained cadre of professionals, from private bankers to lawyers and accountants, and there is no shortage of available professional talent. Further, with the increasing move towards liberalisation of the Bahamas’ immigration regime, the ability to import the necessary talent to service the needs of the ultra and high net worth individuals is becoming increasingly easy.

The key points that make the Bahamas an important jurisdiction for private client matters are:

a Location: the Bahamas is situated a few miles off the coast of the United States, making it a hub for regional investment and business in the United States, Canada and Central and South America.

b Political and economic stability: the Bahamas has more than 280 years of uninterrupted parliamentary democracy. The Bahamas ushered in a new government in May 2017 following a highly anticipated general election but that has not affected its stance as the mecca in the financial services industry. Additionally, its currency is on a par with the US dollar.

c Wealth and asset management services: the Bahamas offers a significant number of financial institutions, delivering services including banking, private banking and trust

1 John F Wilson is a partner at McKinney Bancroft & Hughes.
services, accounting and legal services, e-commerce, insurance, and corporate and shipping registries. Additionally, there is in excess of 700 funds that are licensed in the Bahamas, with assets under management totalling over BD$200 billion.

d Infrastructure: the Bahamas has the infrastructure in place that allows for international business, with some 21 international airports, 10,000 acres on Grand Bahama Island earmarked for an industrial and commercial free zone area, one of the deepest harbours in the region, and modern facilities connected globally via fibre optic cable. Additionally, there are world famous residential communities such as Albany, Lyford Cay and Old Fort Bay, which allow the ultra and high net worth families to live, work and play where their wealth is both maintained and preserved.

e Highly educated workforce: most Bahamian wealth management practitioners attain their degrees from universities in the United States, Canada and the United Kingdom.

f Taxation: the Bahamas remains a tax-neutral platform where international persons receive the same tax benefits as Bahamians. There are no income, capital gains and inheritance taxes for all residents of the Bahamas.

g Regulation: the Bahamas adheres to all international regulatory principles and is also active in multilateral organisations established to set and monitor standards for regulation and Anti-Money Laundering and Countering of Terrorist Financing (AML/CFT). In this way all of its institutions continue to have access to the international banking and investment markets.

h Permanent residency: the Bahamas has a liberal policy for granting economic permanent residency. The minimum residential investment threshold for application for permanent residency is BD$500,000; for accelerated consideration an investment of BD$1.5 million or greater enables the application to be considered within 21 days.

II TAX

What differentiates the Bahamas from most jurisdictions is that it remains a tax-neutral platform, where international persons receive the same tax benefits as Bahamians. This includes:2

a no income, capital gains and inheritance taxes for all who conduct business or reside in the Bahamas;

b a modest business licence tax for companies carrying on business in the Bahamas;

c a 2.5 per cent government stamp tax and a 7.5 per cent value added tax on the purchase of a new home;

d real property taxes of 1.5 per cent of the property value;

e a modest monthly national insurance payment for employees;

f a 7.5 per cent value added tax on most forms of consumer spending – both goods and services;

g companies, meanwhile, operate tax-free within the free trade zone of Freeport on Grand Bahama Island, under the terms of the 99-year Hawksbill Creek Agreement, signed by the government in 1955;

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developments relating to personal taxation for individuals both in relation to gift and succession taxes; and

there are no gift and succession taxes in the Bahamas.

i  **Issues relating to cross-border structuring**

The Bahamas Trust (Choice of Governing Law) Act 1989 makes it permissible for a trust administered anywhere in the world to designate Bahamian law as the governing law. In addition, the Bahamas has very facilitative rules allowing for corporate entities to be continued into and from the Bahamas.

A key component of the Bahamas’ wealth management regime is its adherence to the principle that persons have a right to confidentiality with respect to the conduct of banking affairs. This right has been codified under the Banks and Trust Companies Regulations Act 2000. In relation to requests for information from foreign regulatory bodies the Bahamas will share information only on agreed and transparent protocols agreed to under a tax information exchange agreement (TIEA) reflecting the Organisation for Economic Co-operation and Development (OECD) standard for tax information exchange.

ii  **Regulatory issues relevant to high net worth individuals generally or that impact the general market of private wealth services**

In compliance with the OECD standard for tax cooperation between countries, the Bahamas has committed to international standards of international tax cooperation by signing TIEAs with 30 countries to date.

All of the agreements signed by the Bahamas are in accordance with the OECD model TIEA. Accordingly, the Bahamas will only cooperate with countries in the same manner as all countries that adopt Article 26. In particular, through agreements, the Bahamas commits to cooperating only upon requests where specific information is provided. This requirement for specific information is critical in furtherance of the Bahamas’ stated position of trying to prevent ‘fishing expeditions’.

The Bahamas has also entered into an intergovernmental agreement with the United States of America signalling its compliance with the United States Foreign Accounts Tax Compliance Act (FATCA). FATCA imposes automatic reporting requirements on all foreign financial institutions relating to their dealings with US persons. The implementation of reporting requirements under FATCA presented certain challenges under Bahamian law as it had to be reconciled with the duty of confidentiality as outlined under Section 19 of the Banks & Trusts Companies Regulation Act 2000 (BTCRA), the Data Protection Act 2003 and the Bahamian Common Law. In many instances, financial institutions have reconciled this conundrum by having their clients provide written waivers of the rights under Bahamian confidentiality and privacy laws that would allow foreign financial institutions to report relevant information to the United States Tax Authorities.

The Bahamas has also joined the growing list of countries that have agreed the OECD’s Common Reporting Standard (CRS) for the automatic exchange of information, which the Bahamas has agreed to implement in 2017. Following this, the Bahamas enacted the

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3 Section 4.
4 Section 84 of the International Business Companies Act.
Automatic Exchange of Financial Account Information Act on 29 December 2016 to give effect to the CRS and confer the necessary powers on the competent authority to enter into an agreement with the government of another country for the automatic exchange of financial account information in tax matters. Under the former government of the Bahamas, the Bahamas was to take a bilateral approach to its CRS obligation. However, the new government has taken a different track and has indicated its intention to implement CRS by way of the Multilateral Convention on the Mutual Administrative Assistance in Tax Matters on a non-reciprocal basis.

Accordingly, with this wider approach, all financial institutions operating in the Bahamas are now required to collect and retain CRS information and be ready to report it for all account holders and transmit same once notified to do so by the Competent Authority.

The Bahamas remains strongly committed to the principle that persons have a right to confidentiality and privacy in relation to the conduct of their affairs. This right is an essential cog in Bahamian jurisprudence. Moreover, respect for the rule of law is a fundamental element to the success and strength of the Bahamas as a jurisdiction. Consequently, the ultra-high and high net worth can be assured that the Bahamas will only exchange information on agreed and transparent protocols.

The Bank and Trusts Companies Regulations Act 2000 (BTCRA) allows foreign banking regulators that regulate a bank or trust company with a branch or subsidiary incorporated in the Bahamas, to conduct an inspection, under conditions of confidentiality, solely for the purposes of consolidated supervision, of the books and accounts of any branch or subsidiary of that bank and trust company in the Bahamas. However, it should be noted that the BTCRA provides individual customers with a degree of confidentiality, with limited exceptions, with regard to their assets under management of a bank and trust company in the Bahamas. The following are examples of exceptions of a bank and trust company’s duty to maintain confidentiality of banking information:

\[ a \] to assist the Central Bank Governor in functions conferred by Bahamian law; and
\[ b \] for the institution of, or for the purpose of:
- criminal proceedings; or
- disciplinary proceedings in the Bahamas or abroad relating to a lawyer, auditor, accountant, valuer or actuary, or public officer or employee of the Central Bank.

### III SUCESSION

A key factor for wealth preservation in the Bahamas is that there is no inheritance tax within the jurisdiction.

The Bahamas is a common law jurisdiction and its probate and administration of estates legislation is based mainly on the laws of England and Wales. Under the Probate and

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6 The Data Protection (Privacy of Personal Information) Act 2003 provides for the protection of privacy of individuals with regard to personal data.
7 Ibid.
9 Ibid.
Administration of Estates Act 2011,\textsuperscript{10} the Supreme Court of the Bahamas has jurisdiction to make a grant of representation in respect of a deceased person who was ordinarily resident in the Bahamas, or whose estate consists of property in the Bahamas.

\textbf{i} Relevant cross-border developments

The court will issue a resealed grant in respect of any grant of probate or other testamentary disposition issued by any member state of the Commonwealth; any state of the United States of America; or in any other country specified by order by the Attorney General provided that the requisite certified and duly authenticated copies of such foreign grant, etc. are produced to support the application.\textsuperscript{11}

Notwithstanding that the Bahamas is a common law jurisdiction, the law adequately provides for administration of estates emanating from civil law jurisdictions such as the European countries (e.g., Switzerland, Germany, France), the South American countries (e.g., Argentina, Brazil, Chile) and other territories such as the Dutch Antilles and Quebec.\textsuperscript{12}

The court will also issue a grant of letters of administration with the will annexed where a deceased testator owns Bahamian assets but for some specific reason it was not necessary to apply for a grant in respect of his or her will in his or her place of domicile.

Where a person dies intestate in a common law jurisdiction, the court will issue a grant of letters of administration in respect of his or her estate in the first instance to the surviving spouse or to such other person approved by the court and by which grant the administrator is vested with powers and duties similar to those of an executor.\textsuperscript{13}

\textbf{ii} Applicable changes affecting personal property

\textit{Developments on prenuptial agreements in the Bahamas}

Traditionally Bahamian courts did not give effect to prenuptial agreements. In more recent times, however, the courts have taken the view that the terms of a prenuptial agreement are a factor to take into account when exercising the court’s discretion under the Matrimonial Causes Act 1879.

In \textit{M v. F}\textsuperscript{14} a decision delivered on 7 June 2011 by the Supreme Court of the Bahamas, following the law in the United Kingdom, held that under Bahamian law a prenuptial agreement was merely persuasive and not binding on the distribution of marital assets upon the breakdown of a marriage. The Court held that to give effect or determination to prenuptial agreements the Court must be satisfied that the agreement was entered into freely and voluntarily by both parties with full appreciation of its implication and if it was, whether it would be unfair to give effect to the agreement.

\textsuperscript{11} Ibid.
\textsuperscript{12} Ibid.
\textsuperscript{13} Ibid.
IV  WEALTH STRUCTURING & REGULATION

i  Commonly used vehicles for wealth structuring, such as trusts, foundations or partnerships

The International Business Companies Act 2000

An international business company (IBC) may be used to establish a private trust company (PTC) or a family office, or to create an investment fund. The IBC is the basic building block used in the Bahamas to create structures to preserve and accumulate wealth; as such, it is an indispensable tool for estate planning.\(^\text{15}\)

An IBC is incorporated under the International Business Companies Act 2000 by two or more persons subscribing to a memorandum that satisfies the requirements of the Act, and may be established for a limited duration. The memorandum and articles must be registered with the Registrar of Companies who will issue a certificate of incorporation certifying that the IBC is incorporated. An IBC can usually be incorporated within a day or two. There is no requirement that a national of the Bahamas be a participant, manager or director of the IBC and there are no restrictions on capitalisation. An IBC may have only one director, and it must maintain a registered office in the Bahamas.

There are no tax consequences for utilising an IBC if the IBC does no business in this jurisdiction. Further, an IBC and its shareholders are not subject to any income tax, corporate tax, business licence fees or stamp duty on transactions concerning an IBC, except that stamp duty is payable in relation to real property situated in the Bahamas that it owns, or is owned by any company in which it holds shares or for which it holds a lease.\(^\text{16}\) This statutory relief from taxation is valid for 20 years from date of incorporation.\(^\text{17}\) The applicable fees and taxes for IBCs are:

- Government fees for incorporation are BD$330 upon filing the Memorandum and Articles of Association.
- On 1 January each year, the IBC must pay an annual fee of either BD$350 depending on whether the authorised capital is BD$50,000 or less or BD$1,000 if the authorised capital is BD$50,000 or more.

ii  Trusts

Trusts are recognised in the Bahamas and are governed by the Trustee Act 1998. The trust under Bahamian law is a relationship whereby one party (settlor) transfers assets to another (trustee) to be held for the benefit of a third party (beneficiary). Assets transferred to a trustee under trust cease to be legally owned by the transferor and become subject to the terms of the trust.

There is no legal requirement for trusts to be registered or for public disclosures to be made. Exchange control regulations do not apply to non-resident settlors, donors, beneficiaries and trustees participating in an offshore trust. An exemption exists in respect of trusts with non-resident beneficiaries, in connection with the payment of taxes, including stamp duty on transfers of property into trusts.

\(^{15}\) Supra, n. 2.


\(^{17}\) Ibid.
Other features of a Bahamian trust include the ability of a settlor to retain a wide range of powers without the trust being declared a sham. Subject to the terms of the trust, trustees have wide statutory investment and management powers, and a protector may be appointed to oversee the trust. The Trusts (Choice of Governing Law) Act 1998 provides protection against forced heirship laws.

iii Asset protection trusts (APTs)
The operation of asset protection trusts in the Bahamas is supported by the provisions of the Fraudulent Dispositions Act 1991.\(^\text{18}\) The Act protects the assets of a settlor by placing them out of the reach of creditors who commence litigation in relation to those assets more than two years after the assets were transferred into the trust. Under the Fraudulent Dispositions Act forced heirship laws are not recognised.

iv Purpose trusts
Persons investing in the Bahamas may use a purpose trust as a component of their investment scheme. A purpose trust can be created for purposes that are not charitable and will not require an individual or corporate beneficiary. The intent behind a purpose trust must be possible and sufficiently certain to allow the trust to be carried out, and not be contrary to public policy or unlawful. Purpose trusts can be fixed or discretionary and unless otherwise expressed in the trust instrument, the trustee may distribute capital and income between different authorised purposes, individuals, corporations and charitable purposes. With the exception of land, and any interest in land, almost any assets can be the subject of a purpose trust.

v PTC
A PTC is a company incorporated under the Companies Act or the International Business Companies Act that acts as trustee only for a trust or trusts created or to be created by or at the direction of a designated person or persons or an individual or individuals who are related to the designated person described within the designating instrument. The establishment of the PTC allows for the trusteeship of a defined class of trusts by reference to the designated person. All other settlors of trusts for whom the PTC acts as trustee must be related to the designated person or persons.

vi Foundations
As an alternative to trusts and corporations, wealth management planners may employ the use of a Bahamian foundation. This distinctly European concept was introduced into Bahamian law by the Foundations Act 2004.\(^\text{19}\) The foundation is best understood as a hybrid between a trust and a company. The foundation will have beneficiaries and may have a protector. It can be established by a will and no forced heirship rules apply. It may be revoked by the founder if provided for in the charter by which it is established. Upon registration, the foundation will be a legal entity, resident and domiciled in the Bahamas with the capacity to sue and

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be sued in its own name. It may enjoy unlimited duration, subject to the revocation of the charter, winding up, liquidation or being otherwise terminated. The assets transferred to the foundation will become exclusively its assets and shall cease to be the assets of the person who made the endowment. The foundation documents will identify its beneficiaries, which may be individuals, a charity or the public at large. The foundation assets will not become the assets of a beneficiary unless and until distributed in accordance with the provisions of the foundation charter, the articles (if any) and the Foundations Act. The foundation must have assets valued at not less than US$10,000 or the equivalent thereof in another currency.

The foundation will have a stated purpose or object that may be any lawful purpose and may, but need not, be charitable. The Foundations Act describes the main purposes or objects of a foundation, including the management of its assets. This may involve the buying and selling of such assets.

vii General partnership
There is no requirement that a national of the Bahamas or a related state be a partner in a general partnership arrangement. Fees for establishing a general partnership relationship will vary depending on the complexity of the arrangement and will usually be restricted to fees for professional services rendered in connection with advising generally on the partnership and for preparation of documents. A partner in a general partnership will potentially be personally liable for debts contracted on behalf of the firm although as between partners his or her liability may be limited to the proportionate value of his or her share in the partnership. Value added tax of 7.5 per cent is payable on goods and services provided by the partnership where the annual taxable sales of the partnership’s business exceeds BD$100,000.

viii Applicable anti-money laundering regime and other key aspects of regulation of service providers dealing with private wealth
Over the years, the Bahamas has developed an extensive regulatory regime for private wealth service providers, in order to comply with 21st century international standards, and to maintain its reputation as a reputable international financial centre.

The Bahamas operates in a globally integrated market for financial services. As a result the country’s counter-money laundering legislation meets global best practices and standards.20

The Bahamas is a member of the Caribbean Financial Action Task Force (CFATF), a FATF-style regional body composed of 30 member states from the Caribbean Basin. The CFATF conducts peer reviews of its members’ Anti-Money Laundering (AML)/(CFT) laws, policies and procedures and assesses the extent to which countries comply with the Financial Action Task Force’s 40+9 Recommendations for preventing money laundering and countering the financing of terrorism. The jurisdiction’s efforts to assess and strengthen its AML/CFT framework are ongoing.21

21 Ibid.
Regulation of private wealth management service providers

The Central Bank of the Bahamas

With more than 270 banks and trust companies operating in the Bahamas, and the banking industry itself the cornerstone of the country's financial services industry, the Central Bank plays a lead role among the country's regulatory agencies and enjoys full autonomy. Its stature within the Bahamas is reinforced by its long-standing presence in the jurisdiction; the Bahamas, in fact, has been regulating banks and trust companies since 1965.

The Central Bank fills the traditional roles as issuer of legal tender, banker to both domestic banks and the government, and regulator and supervisor of the banking sector. As supervisor of banks, the Central Bank promotes the soundness of banks and trust companies through the effective application of international regulatory and supervisory standards. It is a member of various regional and international agencies, including the Association of Banks of the Americas (ASBA); Offshore Group of Banking Supervisors (OGBS); Caribbean Group of Banking Supervisor (CGBS); and also serves on the Financial Expert (Mutual Evaluations) Committee of the CFATF. The OGBS has worked closely with the Basel Committee on the supervision of cross-border banking, as well as with the FATF on anti-money laundering initiatives.

Continued vigilance is required to secure an effective regulatory environment. Legislative initiatives have been designed to provide products relevant to the international market place, to enhance the regulatory oversight and supervision of the financial service sector, and to further its counter-money laundering regime. These initiatives include a focus on risk management and continually updated AML/CTF guidelines following the publication of revised FATF 40+9 Recommendations. In all, the Central Bank's overall policy objective is the promotion of a stable economic environment conducive to high levels of domestic production, employment and growth.

The Securities Commission of The Bahamas

The Securities Commission (SCB) was established in 1995. As part of its endeavour to keep abreast of an ever-changing global regulatory environment, and to ensure a Bahamian contribution towards improving the efficiency and conduct of international markets, the SCB is a member of the International Organization of Securities Commissions (IOSCO) – signatory A status under its MMoU – and the Council of Securities Regulators (COSRA). The SCB’s mission is to effectively oversee and regulate the activities of the securities and capital markets, and to protect investors, while strengthening public and institutional confidence in the integrity of those markets.

The principal areas of focus are the securities industry, including the oversight of broker dealing and securities investment advisory services, and investment fund management and administration.

Insurance Commission of the Bahamas

The Insurance Commission of The Bahamas is responsible for the prudential regulation of all insurance activity in or through the Bahamas. It is concerned with the ongoing monitoring and control of insurers, agents, brokers, salespeople, underwriting managers and external insurers.

Its mandate is to undertake all of the due diligence necessary to guarantee that companies that come to the Bahamas are reputable, high-quality businesses and its supervisory regime
is also geared to ensure that it safeguards the interests of the policyholders involved. The ICB has developed a risk-based supervisory methodology, and a principles-based approach that allows flexibility.

The Bahamas is a member of the International Association of Insurance Supervisors (IAIS), which is recognised as the standard-setting body for insurance regulators. It is also a member of the Group of Offshore Insurance Supervisors (OGIS) and a member of the Caribbean Association of Insurance Supervisors. Organisations such as these instil a consistent and frequent exchange of regulatory information that helps the regulator to craft and hone world-class legislation.

V CONCLUSIONS & OUTLOOK

Like many other offshore jurisdictions, the Bahamas has had to rethink its approach to the development of its international financial services industry. Given the evolution in the financial services industry globally over the past decade, the Bahamas has moved from being a tax-free to a tax-neutral jurisdiction and some have advocated that the Bahamas migrates to a low-tax fully transparent jurisdiction. Initiatives such as these will continue to aid the Bahamas in distancing itself from the perception that has dogged international financial centres of being the jurisdictions of tax cheats and providing a means for hiding wealth. Through its accession to the TIEA regime and compliance with FATCA and adherence to the CRS, while continuing to hold fast to the universal right of privacy of the individual, the Bahamas continues to demonstrate that it is a well-regulated, respected and mature jurisdiction.
Chapter 9

BELGIUM

Ferenc Ballegeer

I INTRODUCTION

Taxation of individuals in Belgium depends partly on the region where the individual lives (i.e., where he or she has his or her principal place of residence). Belgium is a federal state and consists of three regions: the Brussels Capital Region, the Flemish Region and the Walloon Region. The main tax laws were originally conceived at the national level.

Following subsequent state reforms, aspects of gift and inheritance tax (including applicable rates and exemptions) and, more recently, aspects of personal income tax, have been regionalised. Consequently, the taxation of individuals is diverging from one region to another and it is expected that this evolution will continue, although the basic rules remain controlled by the national government.

Matters such as property law, gifts and succession law are national law and based on the Civil Code. Hence, contractual freedom is the basic principle in these areas of the law.

Belgium has not enacted legislation aimed specifically at attracting foreign wealthy individuals. Specific tax incentives are focusing on companies, especially in the science and technology sectors.

Foreign wealthy individuals who choose to become Belgian residents, and thus administer their worldwide businesses and assets from Belgium, benefit from the same rights and obligations as Belgian nationals. As Belgian residents for tax purposes, they have access to the extensive network of treaties for the avoidance of double taxation that Belgium has with other jurisdictions across the globe.

In these turbulent times, the consensus remains so far uncontested that Belgium must continue to put itself in line with good legal and tax practices applicable in other jurisdictions within the European Economic Area and its internal market.

To illustrate what the jurisdiction has to offer to private individuals, Belgium does not apply its capital gains tax regime to capital gains within the scope of the normal administration of private assets. The scope of ‘normal administration’ is quite large and applies, in principle, notwithstanding the importance of the capital gain involved. It must be noted, however, that this ‘normal administration’ principle is under increasing pressure, following some recent share deals that were widely commented on in the national press. It seems rather unlikely, however, that the principle would be overturned in the short term.

1 Ferenc Ballegeer is a Belgian lawyer and the founder of FB-Private Wealth Law.
2 Article 11 Civil Code.
A second example is that a gift of moveable assets does not have to be subject to gift tax. Belgian gift tax is a stamp duty: there is no obligation to register a gift of moveable assets. Depending on the region where the donor resides, inheritance tax is due on unregistered gifts from the three or seven years preceding the donor’s decease.

It must be noted that within the scope of this chapter, only the basic principles of existing legislation and new developments can be mentioned. The terminology used herein refers to the terminology of Belgian law.

II TAX

i Personal income tax

Private individuals who are Belgian residents for tax purposes are subject to personal income tax on the basis of their worldwide income, notwithstanding their nationality. Non-residents may be subject to Belgian income tax on their Belgian source income (non-resident income tax).

Personal income tax involves income from real estate, income from moveable assets, professional income and a residuary category. In the latter category, there is no catch-all approach, since income within the scope of the normal administration of private assets is not taxable.

Income tax rates are progressive, and even relatively moderate income is subject to high rates. The first €7,090 is exempt from personal income tax. The basic tariff scheme is as follows:

- 25 per cent from €0.01 to €11,070;
- 30 per cent from above €11,070 to €12,720;
- 40 per cent from above €12,720 to €21,190;
- 45 per cent from above €21,190 to €38,830; and
- 50 per cent from above €38,830.

Interest and dividend income are taxed at a flat rate, which has been increased several times and significantly over the last few years. As from 1 January 2017, interest and dividend income tax is now at the basic rate of 30 per cent.

What differentiates Belgium is, first of all, its capital gains tax regime. Capital gains within the residuary category of taxable income, arising from whatever speculation or operation, are taxable, except for capital gains arising within the scope of the normal administration of the private assets of the taxpayer. These principles apply also to capital gains on shares, which is of particular interest for private individuals as the notion of ‘normal administration’ has quite a large scope. Consequently, capital gains on share or asset deals may be tax-exempt.

A specific tax regime applies to capital gains on shares in a Belgian corporate legal person (i.e., legal persons that are companies) that are transferred to a legal person outside the European Economic Area, if and to the extent the taxpayer holds (or held) directly or indirectly 25 per cent in the Belgian corporate legal person. The applicable basic rate is 16.5 per cent, even if the operation would be within the scope of the ‘normal administration’ test.

Taxable capital gains (i.e., capital gains outside the scope of the exception and specific rule) are taxed at a basic rate of 33 per cent.

\[\text{The amounts in euros are applicable to taxable income from the year 2017.}\]
Especially in the past, the advantageous Belgian capital gains regime was at the basis of merely internal (within the same group of companies) operations aimed at withdrawing cash or assets from a corporate legal person without paying dividend tax (now 30 per cent). Anti-abuse rules and more restrictive ruling practices in recent years aimed to curb these operations. Since 1 January 2017 a new specific anti-avoidance rule has been put in place to further restrict such operations.

It is also noteworthy to mention the Belgian expat tax regime. Qualifying expats are, sometimes fictiously, considered as non-resident taxpayers for income tax purposes. They are taxable in Belgium on their Belgian source income only. The additional relocation costs paid by their employer are not considered to be part of their taxable salary (professional income). As for the company employing the expat, these relocation costs are tax-deductible in its corporate income tax.

‘Look-through’ tax
In 2012, Belgium strengthened its general anti-abuse rule significantly to arrangements in breach of the purpose of a tax rule or a tax benefit.

Following international developments, notably the series of ‘leaks’ in recent years, Belgium enacted a legal obligation, initially for private individuals, to declare the existence of trusts and similar legal arrangements as well as foreign legal persons (i.e., having legal personality distinct from its shareholder or settlor) of which they are settlor or third-party beneficiary in their yearly tax return.\(^4\) As far as the latter are concerned, this involved mainly legal persons from outside the European Economic Area, not subject to tax at all or subject to a low tax rate.\(^5\)

These new rules involve a self-assessment exercise for Belgian residents: first of all they need to assess whether the legal arrangement(s) or foreign legal person(s) of which they are settlor or third-party beneficiary must be declared.\(^6\) Since 2016 also legal persons subject to the legal persons income tax, such as foundations (see below), may be subject to this duty to declare legal arrangements and foreign legal persons of which they are settlor or third-party beneficiaries.

The second part of the self-assessment exercise is the new ‘look-through’ tax since 2016 for private individuals subject to personal income tax and legal persons subject to legal persons income tax: a duty to declare the revenue of the legal arrangement or legal person of which they are settlor. This revenue is now taxable income of the private individual or legal person directly insofar as the taxpayer cannot prove that a third-party beneficiary within the European Economic Area received or is entitled to the revenue.

Following the most recent Panama Papers leak, there is increasing pressure to at least evaluate the existing ‘look-through’ tax and possibly even further strengthen it. The reader understands that the purpose of this legislation is discouraging offshore tax planning.

\(^4\) The tax duties imposed on settlors and third-party beneficiaries of legal arrangements or legal persons are often referred to as ‘Cayman tax’.

\(^5\) EEA: EU Member States, Iceland, Norway and Liechtenstein. So far only three EEA legal persons are within the scope of this Belgian legislation: the Liechtenstein ‘Stiftung’, the Liechtenstein ‘Anstalt’ and the Luxembourg ‘Société de Gestion de Patrimoine Familial’.

\(^6\) Please note that settlor and third-party beneficiary are defined by the Belgian Income Tax Code. The notions differ from what may be understood by it in other jurisdictions.
In response to a parliamentary question, the finance minister answered that the look-through tax also applies to ‘double structures’ (i.e., legal entities constituted by legal arrangements or legal persons). The reasoning is that it would be unacceptable to avoid its application by setting up ‘double structures’.7

The significant increase in interest and dividend income tax that was mentioned earlier is a noteworthy recent development, illustrating a ‘tax shift’ from a very high taxation of professional income to taxation of other types of income (such as interest and dividend income) and towards taxation of non-sustainable behaviour and consumption.

ii Inheritance tax

Belgian inheritance tax is due on the worldwide assets of the deceased if the deceased had his or her principal place of residence in Belgium at the time he or she passed away. The applicable regional tax regime is the tax regime of the residence of the deceased in the five years preceding his or her death. The top rate for descendants and spouses or partners is 27 per cent (Flemish Region) and 30 per cent (Brussels Capital Region or Walloon Region).

Recent developments

Although essential aspects of inheritance (and gift) tax are regionalised, the collection of these taxes remained entrusted to the national tax administration. Since 2015, the Flemish Region collects the inheritance (and gift) tax allocated to its territory itself.

This has given rise to differing administrative interpretations of sometimes long-established legislation and practices at the national level even if the law was not altered by the Flemish parliament. Consequently, legal uncertainty arose as to some important aspects of inheritance tax law or existing planning schemes in the Flemish Region. To resolve this, the Flemish tax administration puts forward its view to issues in this regard by means of administrative positions.

An example of an unresolved matter is the residency test in the Flemish inheritance tax. The residency test refers to a complex of factual circumstances indicating that a person has its principal place of residence in Belgium. Contrary to Belgian income tax, Belgian (and Flemish) inheritance tax do not provide in a legal presumption that persons registered in Belgium (including expats and other immigrants) are considered to have their tax residency for inheritance tax purposes in Belgium (or in the Flemish Region), the principle being that presumptions overturning the burden of proof must be created by law.

If necessary, it would, therefore, be up to the tax administration to prove that the deceased was a Belgian resident for inheritance tax purposes.

The Flemish tax administration, however, proclaimed that persons registered in the Flemish Region are deemed to have their tax residency for inheritance tax purposes in the Flemish Region. The Flemish tax administration put forward that it would be up to the heirs to prove that the deceased was not a tax resident, thus overturning existing rules without altering the law. The statement by the Flemish tax administration does not mention expats or other registered immigrants in Belgium, even if they do not have their principal place of residence in Belgium. This has created legal uncertainty.

As for the Brussels Capital Region and the Walloon Region, the national tax administration continues to collect the Brussels and Walloon inheritance and gift tax. No such presumption is applicable in these regions.

As mentioned before, since 1 January 2017 a new specific anti-avoidance rule has been put in place to further restrict internal operations aimed at avoiding dividend tax.

**Outlook: taxation on investment accounts**

The national budget agreement (a political agreement by the national government) from July 2017 involves a taxation on investment accounts (accounts on which financial instruments are held). The rate would be 0.15 per cent on the value of the assets. On the basis of what is known at this point the tax would only apply above €500,000.8

Legislative proposals to implement the budget agreement may be expected in the second half of 2017.

**iii Recent developments in income tax regarding cross-border structuring**

The look-through tax, as mentioned above, should also be highlighted here.

Worth mentioning further is that legal persons that are subject to legal persons’ income tax, such as foundations, are subject to the look-through tax on revenue of legal arrangements or legal persons of which they are settlor.

Another matter to be mentioned concerns a Belgian issue regarding the EU Parent Subsidiary Directive that exempts dividend payments between associated companies from withholding tax. The minimum participation to benefit from the exemption is 10 per cent. Under 10 per cent, the exemption from withholding tax does not apply.

Should a Belgian parent company have received dividends that were subject to a withholding tax at the level of the subsidiary, Belgian corporate income tax provides for a ‘dividends received deduction’ (DRD) at the level of the Belgian parent company: subject to conditions, 95 per cent of the dividends received are deductible from the parent’s taxable profit (corporate income tax). As for the parent subsidiary exemption, the DRD applies as from a minimum participation of 10 per cent, but the Belgian DRD is also applicable under 10 per cent if the purchase price of the participation is a minimum of €2.5 million.

The latter DRD rule, however, is not applicable if the parent company is not a Belgian company. The European Court of Justice held this contrary to the free movement of capital.9 Since 28 December 2015, the Belgian withholding tax on such dividend payments is (subject to conditions) reduced to 1.6995 per cent (which corresponds to the DRD deduction) for parent companies within the European Economic Area or in a jurisdiction with which Belgium has a double taxation treaty.

In December 2016, the existing catch-all rule in the Belgian non-resident income tax regime (NRIT) has been modified to the benefit of private clients. The principle is that non-resident tax payers pay NRIT on their Belgian source income. A catch-all rule exists to avoid non-taxation of income that would have been taxable if the taxpayer was a resident taxpayer. The catch-all rule now applies only to professional income from ‘whatever service’

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8 This text has been finalised in July 2017 also.
9 Court of Justice of the European Union, Case C 384/11 (*Tate & Lyle Investments v. Belgium*).
the non-resident taxpayer rendered. The new rule applies retroactively on income as from 1 July 2016. If no other Belgian taxation on it would be due, Belgian income of non-residents from private investments are also out of scope of the catch-all rule.

III SUCCESSION

i Forced heirship rules

Belgium's succession law will be modernised significantly in 2018. Belgium will prune its forced heirship rules and adopt more flexible rules allowing donors and testators to give away or to bequeath more. However, the forced heirship principle is withheld.

Belgium's succession law is Civil Code-based and, therefore, forced heirship rules apply. Descendants and spouses are the main protected heirs, but without descendants, spouse or legal partner, ascendants are also protected heirs. The latter changes: ascendants will no longer be protected heirs.

Legal partners are not protected by forced heirship rules. They have a limited intestate claim on the inheritance (i.e., they are entitled to the usufruct of the family home).

The forced heirship rules do not prevent giving away more than the unprotected portion of one's assets, nor do they prevent someone from bequeathing more than the unprotected portion. Protected heirs have the right to take back what was given away beyond the forced heirship rules or may object to the execution of a will that would have failed to take care of their rights.

If the deceased has children, the unprotected portion of the estate is half the estate (one child), one-third of the estate (two children) or one-quarter of the estate (three or more children). This changes: the unprotected portion will be half of the estate regardless of the number of children. The spouse is entitled to at least the usufruct of half of the estate. Spouses are entitled to the usufruct of the family home, even if the value of it would be more than half of the estate. The usufruct is the right to use an asset and the right to collect the revenue of an asset.

Belgium is bound by the EU Succession Regulation. Belgian forced heirship rules may be put aside if a different applicable succession law on the basis of the regulation would be applicable following a valid and effective choice of law. To a limited extent, an agreement as to succession will become possible under Belgian law.

Contractual arrangements between spouses or legal partners determine the composition of the estate. Without a matrimonial contract, spouses have a limited community regime: earnings are common, whereas gifts and inherited assets remain outside the community. Legal partners without an agreement are subject to rules comparable to a separation of goods.

Both marriage and legal partnership are open to same-sex couples.

ii Co-maternity

Since 1 January 2015, Belgium has had a co-maternity law. The female spouse of the mother of the child is automatically the co-mother of the child. The female legal partner of the mother can recognise the child and become the co-mother.

Consequently, forced heirship rules apply given the co-maternity relation between co-mothers and the children of their spouse or legal partner.
iii  Future developments

Following the modernisation of Belgian succession law, it is expected that matrimonial property law and property law between partners will also be dealt with in the near future.

IV  WEALTH STRUCTURING & REGULATION

i  Overview of commonly used vehicles

Commonly used vehicles for structuring private wealth in Belgium include partnerships and corporate legal persons (i.e., legal persons that are companies). Less commonly used is the private foundation.

The principle that a trust is ruled by its applicable law is recognised in Belgium. Belgian law, however, does not provide for its own trust arrangement. The principle is that trust arrangements may not violate forced heirship rules, but if the trust fund (i.e., the property held in trust) is held abroad, forced heirship claims may be ineffective.

A partnership is a body without legal personality, ruled by its by-laws (i.e., the partnership agreement). Both private individuals and legal persons may participate in a partnership. A partnership may be used as a vehicle to administer private and business assets, or as a holding company. As there are few legal constraints and no publication formalities to partnerships, it is a flexible and private planning instrument. A partnership may facilitate a gift as the rules to administer the gift can be laid down in the by-laws instead of having to be detailed as conditions to a gift by a private individual.

Corporate legal persons are also widely used as planning vehicles, in particular as holding companies. Corporate legal persons are subject to publication formalities, but may offer a more adequate framework for asset protection and administration than a partnership, especially if more complex relations with third parties are involved. Corporate legal persons have a legal personality distinct from their shareholders. Belgian law provides for a corporate legal person with only one shareholder.

Private foundations are legal persons and are construed to set apart assets for a philanthropic purpose. A private foundation does not have shareholders. Private foundations are subject to publication formalities. A private foundation is administered by at least three directors. The obligatory philanthropic purpose may be taking care of family members.

A private foundation can be dissolved once its purpose has been realised. The principle rule is that its assets must then be assigned to the philanthropic purpose. Its by-laws, however, may provide that the settlor or his or her successors may take back the property that was put into the foundation or its equivalent value if the purpose of the foundation has been realised.

ii  Overview of the tax regime

Contributions of assets to a vehicle

It must be repeated that within the scope of this chapter, only the basic principles can be mentioned.

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10 Article 124 Private International Law Code.
Belgium

Belgian capital duty is a (national) stamp duty. Its rate has been reduced to zero per cent and cannot be increased again by Belgian law, thanks to EU legislation. Contributions of moveable assets to a partnership do not have to be registered in Belgium. No Belgian capital duty is therefore due.

In the (presumably uncommon) situation where immoveable assets are put into a partnership that has either its centre of effective management in Belgium or its registered office in Belgium and its centre of effective management outside the EU, such contribution must be registered, but the rate is zero per cent (i.e., the contribution must be registered, but in fact no proportional capital duty is due as the rate is zero per cent).

Contributions of assets to a corporate legal person must be registered and are subject to a capital duty of zero per cent. Belgian capital duty is due if the corporate legal person has either its centre of effective management in Belgium or its registered office in Belgium and its centre of effective management outside the EU.

Contributions of property, with a residential purpose or used as such situated in Belgium, to a private foundation are subject to the stamp duty applicable to a sale of immoveable property (the basic rate is 10 per cent in the Flemish Region and 12.5 per cent in the Brussels Capital Region and in the Walloon Region).

As for contributions to private foundations, the principle is that these are subject to a flat rate of 7 per cent in the Brussels Capital Region and in the Walloon Region. In the Flemish Region the flat rate of 5.5 per cent for ‘gifts’ to private foundations also applies to contributions to a private foundation.

Income tax

As a body without legal personality, a partnership is considered tax transparent. Income of a private partnership allocated to private individuals is taxable on the basis of their share in the partnership. Such income is subject to personal income tax if the shareholder is a private individual and Belgian-resident for tax purposes. NRIT may be due on the Belgian source income of partnerships held by non-resident persons.

Belgian corporate legal persons are subject to Belgian corporate income tax (CIT). ‘Belgian’ means that the company has either its registered office, its principal establishment or its centre of effective management in Belgium.

Although a series of deductions may apply, the basic CIT rate is 33.99 per cent. Given developments in neighbouring countries, however, particularly but not exclusively in the UK, the aforementioned budget agreement decreases the CIT to 29 per cent in 2018 and to 25 per cent in 2020. For SMEs the CIT would be decreased to 20 per cent in 2018 on the first €100,000 of taxable profits. A minimum CIT for large corporate legal persons, i.e. with taxable profits of at least €1 million, would be introduced to compensate for these tax cuts. The purpose of these measures is to keep Belgium aligned with its neighbours and predominant trade partners.

Private foundations that have their registered office, principal establishment or centre of effective management in Belgium are subject to the legal persons’ income tax. As regards the legal persons’ income tax, only the revenue defined by law is taxable. Interest and dividend income is taxable and has to be subjected to a withholding tax (the basic rate is 30 per cent).

12 Article 19, 5° and Article 115 Stamp Duty Code.
13 Ruling 16049 of 14 November 2016.
Since 2015 (i.e., revenue from 2015), legal persons subject to legal persons’ income tax, including private foundations, are subject to the above-mentioned look-through tax.

Recent developments: tax on transactions of listed financial instruments
The tax on transactions in listed financial instruments has been modified as from 1 January 2017. The following are now also regarded as taxable Belgian transactions: orders (such as a purchase, sell) via a foreign intermediary; (1) by a private individual having its principal place of residence in Belgium; and (2) by a corporate legal person acting for a registered office or an establishment in Belgium. The tax may thus also apply if no Belgian intermediary intervenes. Bonds and the like are subject to a rate of 0.09 per cent; other financial instruments (such as shares) are subject to a rate of 0.27 per cent and often even 1.32 per cent.

Outlook
The gradual but significant decrease in CIT as from 2018 has been discussed above.

On the basis of the above-mentioned budget agreement the tax on transactions of listed financial instruments would increase as follows from 2018: 0.09 per cent would become 0.12 per cent; 0.27 per cent would become 0.35 per cent.

Inheritance tax
The share of a deceased person in a partnership is subject to inheritance tax. The same applies to shares of a deceased person in a corporate legal person.

The inheritance tax regime for private foundations is very different and may offer opportunities for private individuals that are Belgian residents for inheritance tax purposes insofar as the philanthropic purpose of the private foundation is sincere and the directors act accordingly. It is noteworthy to mention that a general anti-abuse rule also applies to inheritance tax (and gift tax).

The decision to grant benefits to a private individual, not the settlor or one of the directors (as this is prohibited by law) and always within the scope of the philanthropic purpose of the foundation, would not be subjected to inheritance tax as this is a decision by the directors of the foundation on the basis of its by-laws. This would apply if and to the extent that the by-laws normally cannot be considered as a contract granting a direct right to a beneficiary. The national tax administration (competent for the Brussels Capital Region and the Walloon Region) confirmed in 2015 its previous individual rulings on the matter.14

The Flemish tax administration, competent since 2015 for gift tax within its territory, seems to adhere to this.15

The national tax administration ruled in 2014 that benefits granted by a foundation (during the lifetime of the settlor) would not be subject to gift tax or income tax.16 The Flemish tax administration seems to adhere to this.17

Regarding trusts, the competent tax administrations have maintained their much-criticised position that benefits obtained from a trust should either be subject to

14 Ruling No. 2015.083 of 13 May 2015. A ruling is a decision on a case-by-case basis and does not technically apply to other cases.
15 Ruling 16049 of 14 November 2016.
17 Ruling 16049 of 14 November 2016. The ruling does not deal with income tax.
inheritance tax at the time of death of the settlor (non-discretionary trusts) or at the time the benefit is granted (discretionary trusts). Please note that the notions ‘discretionary’ and ‘non-discretionary’ as used by the Belgian tax administrations may not have the same meaning under the law that governs the trust.

iii Developments in anti-money laundering rules

As the reader will be aware, Belgian lawyers, notaries, financial institutions and accountants, *inter alia*, are subject to strict anti-money laundering rules according to EU standards. This involves client identification obligations, including identification of beneficial owners.

Belgium needs to implement the Fourth Anti-Money Laundering Directive, which requires ‘corporate and other legal entities incorporated’ in Belgium to obtain and hold ‘adequate, accurate and current information on their beneficial ownership, including the details of the beneficial interests held’.18 This information must be centralised and made accessible to the competent authorities and financial intelligence units of Member States ‘without any restriction’.

Belgian financial institutions have to file the identity of their clients and the reference number of their contracts (not the amounts or transactions) to a central register. This register has now been made accessible for all tax matters. It must be noted that not only the tax administration has access to the central register, but also notaries.

V CONCLUSIONS & OUTLOOK

The Belgian capital gains tax regime remains friendly to private individuals, as capital gains within the scope of the normal administration of private assets are tax exempt.

Gifts of moveable assets do not have to be subjected to Belgian gift tax; however, afterwards inheritance tax may apply.

There is a large consensus in Belgium that aggressive tax evasion should be tackled effectively and to some extent there is even a tendency to gold-plate international rules or standards on the matter. Less aggressive tax evasion schemes (e.g., dealings within a group of companies) were also curbed in recent years. The greater scope of the Belgian tax on transactions of listed financial instruments may also be mentioned.

The previous government introduced an obligation for private individuals who are Belgian residents for tax purposes to declare trust-like legal arrangements and not-taxed or low-taxed foreign legal persons in their yearly income tax return. The present government enacted a look-through tax for these legal arrangements and legal persons, applicable to private individuals and legal persons, subject to legal persons’ income tax.

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As from 2018 the corporate income tax rate (CIT) will be decreased gradually but significantly to 25 per cent.

The new succession law eases Belgian forced heirship rules and thus grants more planning opportunities and flexibility to private individuals. The new succession law will also allow, within boundaries, agreements as to succession. The second phase of this modernisation should follow shortly: a new matrimonial property law for spouses and partners.

It is also expected that Belgian company law will be modernised significantly in the near future. The guiding principles here are to reduce the number of corporate structures and to enable more flexibility as to enhance the attractiveness of Belgian corporate structures, in particular from an international perspective.
Chapter 10

BERMUDA

Alec R Anderson

I  INTRODUCTION

Bermuda has long been recognised as an attractive, sophisticated and secure jurisdiction for private wealth management for the international private client. It is the United Kingdom’s oldest overseas territory and has been self-governing since 1622, with a strong economy primarily as a result of its trust, insurance and reinsurance and investment fund sectors supported by a sophisticated and well-established advisory and financial services infrastructure.

Bermuda has an independent, stable legal and judicial system and over the past 20 years has made regular and innovative reforms of its trust laws with trust legislation that is both modern and facilitative of succession planning and asset protection. In implementing new trust legislation Bermuda’s legislature collaborates with private sector associations such as the Bermuda Association of Licensed Trustees, the Bermuda International Business Association and the Society of Trusts and Estate Practitioners as well as the Bermuda Business Development Agency, an organisation created to support international business. Recent legislative initiatives in the trusts arena include new legislation on reserved powers, the introduction of a statutory Hastings-Bass rule and amendments to make it easier for historic trusts to extend their perpetuity period (the rule was abolished for most new trusts in 2009). This cooperative approach and innovative modernisation initiatives demonstrate the willingness and ability of Bermuda to adapt to changing product needs of clients around the world.

Bermuda’s trust law is largely based on English common law, including the doctrines of equity, but it has been enhanced and amended by Bermuda trust-related legislation. English common law remains of highly persuasive authority in Bermudian courts. The Supreme Court of Bermuda is the court of first instance in Bermuda with the right of appeal in certain circumstances to the Court of Appeal in Bermuda. The ultimate right of appeal lies to the Privy Council of the United Kingdom.

Two key pieces of legislation in Bermuda are the Trustee Act 1975 (the Trustee Act) (as amended by the Trustee Amendment Acts of 1999, 2004 and 2014) and the Trusts (Special Provisions) Act 1989 (the Special Provisions Act) (as amended by the Trusts (Special Provisions) Acts of 1998, 2004 and 2014). The Trustee Act is largely patterned on the English Trustee Act 1925. It grants certain powers to trustees of Bermuda trusts, which apply unless excluded by express terms in the relevant trust deed, and, pursuant to the 1999 Amendment Act, also provides for delegation of certain trustee functions and modern trustee investment powers. With the Special Provisions Act, Bermuda was the first offshore jurisdiction to

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1 Alec R Anderson is a director at Conyers Dill & Pearman.
introduce legislation permitting non-charitable purpose trusts with most other international financial centres subsequently following Bermuda’s lead by incorporating the concept into their legislation. The Special Provisions Act also contains a number of other innovative and modern provisions that include some of the terms of the Hague Convention on the Recognition of Trusts 1987, which applies in Bermuda.

Bermuda was also one of the first offshore jurisdictions to introduce modern and flexible legislation on private trust companies (PTCs), with over 40 years’ experience establishing and administering PTCs. Unlike PTCs in some other jurisdictions, Bermudian PTCs have never been required to be licensed and so the incorporation and conduct of their affairs has been straightforward, private and efficient.

Bermuda has robust anti-money laundering legislation and tax information exchange agreements (TIEAs), which has led to the Organisation for Economic Co-operation and Development (OECD) including Bermuda on its white list as a cooperative and compliant jurisdiction. In fact, Bermuda has now signed 38 TIEAs, including with the United States and the United Kingdom. On 19 December 2013, Bermuda signed a Model 2 intergovernmental agreement with the US Treasury under the US Foreign Account Tax Compliance Act (FATCA). Bermuda has also entered into a similar agreement with the United Kingdom. Additionally, it has committed to a wider exchange of information process with the G5 countries of the European Union and signed a Multilateral Competent Authority Agreement to start exchanging information using the Common Reporting Standard (CRS) framework from 2017.

Bermuda’s anti-money laundering legislation, along with the regulatory enforcement provided by the Bermuda Monetary Authority (BMA), has ensured that Bermuda is a leader in international anti-money laundering measures, reinforcing Bermuda’s status as a premier offshore jurisdiction.

II  TAX

In Bermuda there is no income or profits tax, withholding tax, capital gains tax, capital transfer tax or inheritance tax. There is no exit or similar such tax based on a resident’s wealth when ceasing to be resident, and there are no other consequences of leaving the jurisdiction. Customs duties and stamp duty are major government revenue earners, with stamp duties charged at different rates and in different manners on a variety of legal documents, excluding wills.

The Stamp Duties Act 1976 is the governing legislation. However, pursuant to the Stamp Duties (International Businesses Relief) Act 1990, no stamp duty is imposed on instruments to which international businesses are a party and there are certain exemptions in the trust area in respect of instruments dealing with foreign currency denominated assets so that generally the imposition of stamp duty is of minimal impact in relation to the international private client. Exemptions from stamp duty are applicable in respect of registered pension trust funds and trusts of non-Bermudian property that are executed by a local trustee, as well as trusts to which an international business is a party and in respect of transactions involving shares in Bermudian-exempted companies and publicly listed local companies. Non-Bermudian property basically refers to all assets except Bermudian currency denominated assets, Bermuda land and shares in non-listed local companies. There is no ad valorem stamp duty on non-Bermudian property in the trust context.
There are no gift taxes in Bermuda on lifetime gifts although stamp duty may be payable in respect of certain gifts or transfers of moveable or immoveable property where a transfer document is executed. In relation to any such property that is not Bermudian property for the purposes of the Act (if an applicable exemption is not available), the rate of stamp duty is 1 per cent of its value. The subject matter of voluntary transfers must be adjudicated as to value by the Tax Commissioner and stamped accordingly for the transfer deed to be deemed properly stamped.\(^2\) Conveyances of Bermudian real estate attract stamp duty at a sliding rate related to value, as follows: 2 per cent on the first BD$100,000, 3 per cent on the next BD$400,000, 4 per cent on the next BD$500,000, 6 per cent between BD$1 million and BD$1.5 million, and 7 per cent over BD$1.5 million. Transfers of shares in publicly listed, exempted or foreign companies are stamp duty exempt.\(^3\)

Transfers of non-Bermudian property to a charitable trust are stamp duty exempt and transfers of Bermudian property to such a trust will also be exempt if: (1) the trust constitutes a charity that is registered under the Charities Act 1978; or (2) the trust’s purposes are in favour of a body of persons or institutions whose purposes, in the opinion of the Minister of Finance are charitable. Exemption (2) principally applies to charities operating locally in Bermuda where the trust affords a benefit to Bermuda.

Although there is no inheritance tax as such in Bermuda, stamp duty may be payable in respect of affidavits of value filed on applications for grant of probate or letters of administration depending on the net value of any Bermudian property comprised therein. The first BD$100,000 of the net estate value (i.e., assets less debts) is stamp duty free, the next BD$100,000 attracts duty at a rate of 5 per cent, the next BD$800,000 at 10 per cent, and the next million at 15 per cent, and 20 per cent duty is levied for everything over BD$2 million.

As Bermuda does not impose income tax it has not entered into any full double taxation treaties with other countries although, as noted earlier, it does have a number of tax information exchange agreements with various countries, some of which contain provisions relating to foreign taxes. Additionally, as alluded to above, Bermuda has signed a Model 2 agreement with the US Treasury under FATCA and has entered into a similar agreement with the United Kingdom. As noted above, CRS also applies in Bermuda.

Predominantly, the private client trust work in Bermuda involves settlors and families who are not residents of Bermuda. It is common for several jurisdictions to be involved if the various beneficiaries are resident in different countries or if the assets owned by the trust are located in different jurisdictions. Consequently, Bermudian lawyers regularly engage with onshore tax lawyers or tax accountants in the relevant jurisdictions to ensure the tax-efficient structuring of any Bermudian entities created for the international private client.

### III SUCESSION & LAND OWNERSHIP

The concept of freedom of testation sets Bermuda apart from various civil law jurisdictions, where such freedom may be curtailed by compulsory inheritance provisions. Bermuda, as an established and forward-thinking jurisdiction for wealth management, has utilised and expanded on the concept of the trust for estate planning and asset protection purposes. The concept is, however, subject to statutory checks designed to preserve the integrity of the

\(^2\) Section 39(1) of the Stamp Duties Act 1976.
\(^3\) Head 15, Schedule to the Stamp Duties Act 1976, exemptions c and d.
jurisdiction by avoiding dispositions to defeat eligible creditors as that term is defined in the
Conveyancing Act 1983. There are also laws to ensure that natural family obligations are met; however, it should be noted that for the purposes of succession, Bermuda currently does not recognise common-law marriage, same-sex marriage or civil unions. Accordingly, persons in such relationships have no rights to inherit from a deceased partner in the absence of a will.

Intestate succession is governed by the Succession Act 1974, which specifies who can inherit the property (both real and personal, without distinction) of a person dying intestate. Section 5 of the Act contains various case scenarios based on who survives the intestate, and all offspring (whether born in or out of wedlock) have equal rights to succession in the various cases. The rationale of Section 5 is that family members with the closest nexus are benefited in priority to those with a more remote connection.

The Act also contains provisions similar to the United Kingdom’s Inheritance (Provision for Family and Dependants) Act 1975, giving certain family members and dependants the right to make a claim against a decedent’s estate (whether dying intestate or not) on the basis that adequate provision was not made for them.

The Wills Act 1988 codifies the law relating to the formalities pertaining to, and validity of, wills. These provisions generally follow English law. Bermuda is not a party to the Hague Convention on the Conflicts of Laws relating to the Form of Testamentary Dispositions; however, to facilitate international estate planning, the salient provisions of the Convention have been inserted in the Act:

A will shall be treated as properly executed if its execution conformed to the internal law in force in the territory where it was executed, or in the territory where, at the time of its execution or of the testator’s death, he was domiciled or had his habitual residence, or in a state of which, at either of those times, he was a national. The Administration of Estates Act 1974 governs the scope of the duties and powers of executors and estate administrators. It also makes provision for the resealing of foreign probate or administration grants in the Bermuda court, under which reseal a foreign executor or administrator would derive his or her authority to administer any Bermudian property covered under the provisions of the foreign estate.

The ability to reseal a foreign grant, however, is limited to grants that were made by a court in the United Kingdom or any British possession, colony or dependency, or a member nation of the Commonwealth or the District of Columbia or any state of the United States of America. In situations where a foreign national dies owning Bermudian property, the devolution of which is governed only by a foreign will, such will would have to be probated in the Bermudian courts.

Where a person dies domiciled outside Bermuda, Rule 27 of the Non-Contentious Probate Rules 1974 allows the Registrar to issue a grant to the person entrusted with the administration of the estate by a foreign court, or to the person entitled to administer the estate by the law of the place where the deceased died domiciled.

4 Section 36.
6 Children Amendment Act 2002.
7 Section 37 of the Wills Act 1988.
In the event a foreign national dies owning Bermudian real estate, then his or her estate representative is subject to a time limit within which to apply for permission from the Department of Immigration for a certificate entitling him or her to defer the application for a licence to hold the land.8

Ownership of land by foreigners in Bermuda is closely regulated and each foreign owner must have a licence to own land. The ability of a foreign owner to pass real property on to heirs is subject to the property falling in a category that qualifies it for foreign acquisition. The main qualifying factor for foreign persons, with no special nexus to Bermuda by way of family ties or permanent residence, is that the real property in question must have an annual rental value (ARV) over a certain value ($126,000 for freehold properties and $25,800 for certain leasehold properties).

IV WEALTH STRUCTURING & REGULATION

Bermuda trusts are the primary legal vehicle of choice used to provide wealth-preservation structures to the high net worth international client. Bermuda trusts can be employed to achieve a variety of estate, personal, financial, tax or other business planning objectives including provision for inheritance by spouses and dependants; protection of assets from unforeseen, future personal liability; minimisation of estate or inheritance tax, income tax and capital gains tax; preservation of family wealth and continuity of family businesses; efficient and timely distribution of assets upon death; protection against exchange controls or political instability; making provision for charities or philanthropic purposes; and confidentiality of ownership of assets.

i Bermuda trusts

While the trust concept is well defined in the common law, statutory clarity as to the characteristics of a Bermuda trust is found in the Special Provisions Act, which codifies the common law position and states that the term ‘trust’ refers to the legal relationship created, either inter vivos or on death, by a person, the settlor, when assets have been placed under the control of the trustee for the benefit of a beneficiary or for a specified purpose.

The beneficiaries of a Bermuda trust may be individuals, companies and other legal entities. The settlor of a Bermuda trust may be an individual over the age of 18 years or a corporation if it has the corporate capacity to make a gift of its assets or otherwise dispose of them for the purpose of establishing a trust.

There are no Bermudian residency requirements with respect to the trustees of a Bermuda trust who may be individuals, PTCs or public trust companies. The property constituting the trust fund can be any type of real or personal property (e.g., cash, securities, real estate, personal effects or other tangible or intangible property). It is common in Bermuda trusts to designate a protector, who may be an individual or a corporation. There is no definition of a ‘protector’ in the statutes or case law of Bermuda or provisions specifying the functions and duties of a protector other than the Special Provisions Act, which provides that a protector or enforcer may be appointed to enforce a purpose trust. The general law treats protectors in accordance with their functions and duties as stipulated in the trust document itself. The nature of a protector’s powers will determine how the court treats them. For example, a

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8 Section 85 of the Bermuda Immigration and Protection Act 1956.
protector’s power to appoint and remove trustees has been determined by the Bermudian courts to be fiduciary in nature (though the new reserved powers legislation permits certain powers to be characterised by the trust instrument as non-fiduciary).

There are no public registration requirements or other disclosure requirements concerning the establishment of trusts in Bermuda. Trust records kept by a trustee are generally not disclosed to regulatory authorities or third parties unless required by law. All information passing from a settlor to the trustee is treated by the trustee as private and confidential. Such information will only be disclosed to beneficiaries on a case-by-case basis where permitted by the trust deed or as required by the trustee’s fiduciary duties.

While Bermuda’s trust law substantially reflects English law and principles of equity, Bermuda has enacted legislation designed to facilitate the use of trusts for modern commercial and private client applications.

Sections 23 and 24 of the Bermuda Trustee Act are almost identical to Subsections 31 and 32 of the English Trustee Act, with one notable difference in Section 24(1)(a) of the Bermuda Trustee Act, which (unlike the English Trustee Act) does not restrict the exercise of the power of advancement to one half of the presumptive share of a beneficiary. Section 24 of the Act confirms that the statutory power of advancement may be exercised by transfers to other discretionary trusts and to permit delegation of duties. This amendment provides flexibility to those trusts that do not contain express delegation powers.

The Trustee Amendment Act 2004 repealed Section 24(3) of the Trustee Act to enable the statutory power of advancement to apply to all trusts governed by Bermudian law whenever created and not just to trusts created after 1 March 1975. This change allows trustees, through the exercise of a power of advancement, to modify the terms of a trust to adapt to the modern environment, and thereby ensure that the trust better reflects the original intentions of the settlor.

Section 47 of the Trustee Act (Section 47) (which is a hybrid of the language of Section 57 of the English Trustee Act and Section 64 of the English Settled Land Act 1925) confers on trustees and beneficiaries of Bermuda trusts advantages that are not available under English law. Like Section 57 of the English Trustee Act, Section 47 allows the court to authorise trustees to enter into otherwise restricted transactions where the court is satisfied that the transaction is expedient and for the benefit of the trust as a whole. The English court’s jurisdiction under Section 57 is limited to matters of management and administration of the trust property and does not sanction changes in equitable interests or dispositive provisions. By contrast, the Bermuda court’s jurisdiction under Section 47(4) broadens the ambit of authorised transactions by importing the provisions of Section 64(2) of the Settled Land Act 1925. ‘Transaction’ is defined in both Section 64(2) and in Section 47(7) to include any disposition, application of capital or other dealing or arrangement. The breadth of this definition of transaction assists the justification of the court’s jurisdiction to approve the potential modification of the beneficial provisions under a trust.

The provisions of Section 47 may be employed by trustees wishing to secure authority to distribute income where failure to do so would incur tax penalties or approval of the exercise of a power of advancement that may technically be outside the scope of the power but that achieves a tax-driven restructuring.

Unlike applications to vary trusts under the English statute, under Section 47 the consent of all beneficiaries is not required. This proves beneficial where general consent by beneficiaries would trigger adverse tax consequences or where obtaining consent from a particularly broad beneficial class would be cumbersome.
Choice of governing law provisions may be inserted in trust instruments by virtue of the Special Provisions Act, with the ability to have a severable part of a trust (such as a part dealing with administration matters) governed by a different law. The Special Provisions Act, in Section 11, also preserves the primacy of the Bermuda court in having sole jurisdiction with respect to trusts validly created in Bermuda and further precludes the recognition or enforcement of foreign judgments insofar as they are inconsistent with this particular section of the Act.

Section 10 of the Special Provisions Act codifies the previously unclear common law position as regards capacity to create a trust by stipulating that in respect of moveable property (not real estate) that the settlor is deemed to have capacity to create an inter vivos trust if he or she would have had capacity under the domestic laws of Bermuda. Where a trust of moveables is created by a will, the question of capacity is determined by the law of the domicile of the testator. Where the trust property is land, the question of capacity is determined by the law of the jurisdiction in which the property is situated.

Section 10(2) also excludes the application of foreign rules of law to questions of capacity of a settlor of a trust governed by Bermudian law.

The Trusts (Special Provisions) Amendment Act 2004 amended Sections 10 and 11 of the Special Provisions Act to clarify that a trust validly created under Bermudian law can only be varied or set aside pursuant to the laws of Bermuda. This makes it clear that provisions of foreign laws giving rise to interests under marriage or analogous relationships, forced heirships and creditors’ rights will not be permitted to vary Bermuda law trusts.

Foreign judgments based on such laws or rights will not be recognised in Bermuda; for example, a foreign court order in a divorce dispute purporting to vary a Bermuda law trust in circumstances where the Bermudian trustee was not a party, will not be enforced in Bermuda.

The Special Provisions Act also legitimates and regulates the use of non-charitable purpose trusts for estate planning. For such a trust to be valid under Bermudian law, it must:

- be sufficiently certain to allow the trust to be carried out;
- be lawful; and
- not be contrary to public policy.

The Act also requires such trusts to be made in writing and conveniently exempts them from the application of the rule against perpetuities, although such trusts are precluded from owning any interest in land in Bermuda, directly or indirectly.

The Perpetuities and Accumulations Act 2009, which came into force in Bermuda on 1 August 2009, disapplied the common law rule against perpetuities in relation to all Bermudian law instruments taking effect on or after 1 August 2009, except in respect of trusts holding Bermudian real estate. For the purposes of the 2009 Act, instruments include inter vivos trusts settled on or after 1 August 2009 and trusts drafted under wills executed on or after 1 August 2009. The ability to create perpetual trusts provides greater flexibility and opportunity in multigenerational wealth and tax planning. The Act does not change the application of the rule to trusts created before the operative date of the Act (Pre 2009 Trusts).

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10 Section 8 of the Trusts (Special Provisions) Act 1989.
11 Section 11(2) of the Trusts (Special Provisions) Act 1989.
12 Section 12A(2) of the Trusts (Special Provisions) Act 1989.
However, the perpetuity period of Pre 2009 Trusts can be extended under the existing law by application to court. The process of extending the perpetuity period of Pre 2009 Trusts was made even more streamlined and cost-effective by the Perpetuities and Accumulations Amendment Act 2015.

Further legislative modernisation includes recent amendments to the Special Provisions Act to introduce innovative reserved powers provisions. The recently added Subsection 2A(2) of the Special Provisions Act lists certain interests and powers that can be retained by a settlor or granted to a third party (e.g., a protector or beneficiary) without prejudicing the validity of a trust (i.e., without laying the trust open to attack on the basis that it is a sham, or an allegation that its assets are not trust property but should be regarded as part of the settlor’s personal estate).

The powers listed (which are non-exhaustive) include powers to:

- revoke the trust;
- vary or amend the trust;
- decide on distributions of trust property;
- direct investments;
- appoint, add, remove or replace trustees, protectors, enforcers or other office holders or advisers;
- add, remove or exclude beneficiaries or purposes; or
- change the governing law of the trust.

The Special Provisions Act (as amended) clarifies that the holder of such a power will not (unless formally appointed as trustee) be deemed to be a trustee by reason only of the grant or reservation of the power.

It also authorises a trust deed governed by Bermudian law to provide that the person who holds the powers listed in new Subsection 2A(2) shall not be subject to a fiduciary duty. This is helpful where, for example, powers are being given to protectors who are family friends. Further, it creates certain presumptions (which can be overridden by the terms of the trust) about when reserved power holders will or will not be fiduciaries.

Bermuda also recently enacted legislation to restore the ‘rule in Hastings-Bass’ as it stood prior to the English Court of Appeal (2011) and Supreme Court (2012) decisions in Pitt v. Holt and Futter v. Futter. Pursuant to the new law, if: (1) a fiduciary has failed to take into account a ‘relevant consideration’ or has taken an ‘irrelevant consideration’ into account; and (2) but for this flaw in his or her decision-making, the fiduciary would not have exercised the power; would have exercised it but on a different occasion to that on which it was exercised; or would have exercised the power, but in a different manner to that in which it was exercised, then the court has a discretion to set the exercise of the power aside in whole or in part. The new legislation clarifies that breach of trust or fiduciary duty is not a necessary component in the exercise of the court’s Hastings-Bass jurisdiction.

ii PTCs

Integral to multigenerational wealth planning requirements involving trusts is the use of PTCs, which offer a host of benefits to private clients and their families, including: (1) the ability to have more involvement in or control over the administration of their trust assets,
where tax considerations permit; (2) the involvement of family members or close family advisers on the board of directors who will have more familiarity with the settlor’s family and affairs than an institutional trustee, and will be able to provide more continuity in terms of management personnel (directors and administrators) than an institutional trustee that may have a high turnover of staff; (3) greater control of the circulation and disclosure of confidential information relating to the trust and a family’s affairs than might be the case with an institutional trustee; and (4) administrative flexibility, as the PTC structure can be tailor-made to best serve the settlor’s intentions. PTCs allow for the harmonisation of trusteeship among a group of trusts that may be governed by laws of different jurisdictions and dispenses with the need to have trustees in each country. Grouping assets into one structure is a particularly convenient planning tool for multinational families.

A PTC may be incorporated in Bermuda if its objects are limited to acting as trustee or co-trustee of a single or specified group of related trusts. In Bermuda, a PTC can be incorporated either as a company limited by shares (which may have different classes of shares (i.e., voting and non-voting)) or as a company limited by guarantee pursuant to the provisions of the Companies Act 1981. Guarantee companies are the preferred structure for PTC formations since the directors and members can be the same individuals. This simplifies the structuring. In some circumstances, where ownership of shares by the settlor would be tax disadvantageous, a PTC may be owned by a non-charitable purpose trust as a means of orphaning ownership.

A PTC will typically be incorporated as an exempted company. Bermuda law distinguishes between local companies (those that are predominantly owned by Bermudians) and exempted companies (those that are predominantly owned by non-Bermudians). Generally, with some exceptions, exempted companies may only carry on business from Bermuda in connection with transactions and activities that are external to Bermuda. PTCs are permitted to carry on their business wholly in Bermuda where the settlor is not ordinarily resident in Bermuda at the time of the creation of the relevant trust.

The application to incorporate a PTC is made to the BMA, which must approve the incorporation of all exempted Bermudian companies. It is a requirement that the identity of the ultimate beneficial owners must always be disclosed and each ultimate beneficial owner holding 5 per cent or more of the shares of the proposed PTC must sign a personal declaration attesting to his or her good standing in any other Bermudian operations or generally. Where, as is common, the company is owned by a purpose trust, the settlor of the underlying trusts should make the declaration. After the BMA’s consent is obtained, the memorandum of association is filed with the Registrar of Companies to incorporate the PTC. The memorandum will set out the objects that specifically recite the name of the trust or trusts that the company is to be trustee of or the name of the family who will be beneficiaries of the trust or trusts. The incorporation process normally takes about one week from the date of submission of the complete application with supporting information to the BMA.

Every Bermuda exempted company is required to have: (1) at least one director who is ordinarily resident in Bermuda; (2) a secretary that is ordinarily resident in Bermuda; or (3) a resident representative that is an individual or a company that is ordinarily resident in Bermuda. If the PTC is incorporated as a company limited by shares, it must have a minimum of one shareholder, and the names of all shareholders must be maintained in a register of members that is maintained in the company’s registered office.
iii Regulation and anti-money laundering

The Trusts (Regulation of Trust Business) Act 2001, which came into effect on 25 January 2002, was passed as a result of recommendations of the KPMG report on Bermuda. It covers the regulation of trust companies and individual trustees with a view to upholding international standards in the provision of trust services to local and international clientele. It provides that any person who carries on trust business in or from Bermuda must be licensed unless he or she is covered by an applicable exemption. Trust business is defined as 'the provision of the services of a trustee as a business, trade, profession or vocation'.

There are two types of licences available: unlimited and limited. Only trust companies are permitted to hold unlimited licences whereas individuals or partnerships are restricted to limited licences. A limited licence trustee may only hold trust assets in an amount not exceeding an authorised amount. The underlying policy objective is that all trust business of significant size and complexity should be conducted inside a licensed, and therefore regulated, trust company. Trust licensees are regulated by the BMA.

As mentioned above, a PTC is exempted from the licensing requirements although it is required to make a one-time filing of a letter to the BMA stating that: (1) the nature and scope of its business is limited to the objects as set out in the memorandum of association; and (2) confirming that the company qualifies for exemption.

Know-your-customer safeguards impose statutory duties on licensed trustees, professional legal advisers, professional accountants and corporate service providers. The Proceeds of Crime (Anti-Money Laundering and Anti-Terrorist Financing) Regulations 2008 (BR 08) (the Regulations) necessitate verification of the identity of customers and beneficial owners, close monitoring of business relationships, recognition and reporting of suspicious transactions, maintenance of records for a prescribed period, assessment and management of risks based on criteria set out in the Regulations, as well as training for employees and staff.

Corporate service providers in Bermuda are required to be licensed and are regulated under the Corporate Service Providers Business Act 2012 (the CSP Act). Undertakings that carry on company or partnership formation, nominee, registered office, secretarial and other similar services are required to apply for a licence from the BMA. The BMA has broad powers of supervision and the ability to impose penalties should a licensed entity fail to comply with its obligations under the CSP Act.

V CONCLUSIONS & OUTLOOK

Bermuda continues to build on its established reputation as a centre of excellence for offshore trust and estate planning. Bermuda’s trusts, corporate and other products can be used in a broad array of private and commercial transactions with its legislation reviewed and updated regularly to assist in meeting and adapting responsively but responsibly to changing client requirements, as demonstrated by the 2014 and 2015 legislation dealing with settlor reserved powers, the statutory Hastings-Bass rule and perpetuities. Looking forward, there will very likely be further legislative developments with a view to continuously improving Bermuda’s technical financial services and providing new vehicles to enhance the wealth planning options available to the international private client.

For many private clients affected by the current volatile economic climate, the events of recent years may have resulted in increased pressure on the clients personally and on their trust structures. This has resulted in an increase in trust-related applications to Bermuda’s courts to seek amendment to the structures for tax efficiency purposes. Bermuda’s courts
are well equipped to deal expeditiously and cost-effectively with both contentious and non-contentious applications. There is robust judicial support for the quick and efficient resolution of such applications, with the courts showing a sensible pragmatic approach to assisting clients with a variety of matters including trust restructurings. With its responsive and cooperative approach to the demands of international initiatives in relation to regulation, transparency and anti-money laundering, and in providing innovative solutions to the changing needs of the international client in light of such initiatives and tax policy and other developments in their home jurisdictions, Bermuda is well placed to maintain its position as a leading international financial centre for private wealth management and planning.
I INTRODUCTION

Brazil is a jurisdiction home to individuals with significant wealth. Due to political and economic instability, wealthy individuals often use foreign jurisdictions to protect part of their assets. For decades, having assets in international banks that were not registered before the Brazilian authorities was very common among Brazilians, even though it was considered a crime.

Nowadays, however, after the alignment of national policies with the international initiatives of tax transparency, control of base erosion and profit shifting – led by the G20 and OECD – Brazilian individuals have been invited to review their compliance with tax rules and their wealth management has been an important part of this procedure.

The recent reopening of the Brazilian tax amnesty programme exemplifies this process. In view of the latest changes in international rules, which led to a greater transparency regarding financial assets, Brazilians are currently facing a new challenge: to manage assets held internationally with full disclosure to Brazilian tax authorities.

Brazil has a complex tax system, and any transaction requires careful analysis: errors or inaccuracies can lead to heavy fines and sanctions by the Treasury. Therefore, investment in private wealth management advisory can represent important savings to a private client through compliance with the tax system.

Furthermore, estate planning has been in full development in the last few years in Brazil. The country has good opportunities for companies and professionals that intend to offer their capabilities to wealthy individuals.

II TAX

Individuals residents in Brazil are taxed on their worldwide income, and non-residents are taxed exclusively on their income sourced in Brazil. The residence of the income payer determines the source of the income, regardless of where the work is performed.

To be considered an individual resident in Brazil, a foreigner living in Brazil should meet one of these requirements: hold a permanent visa or hold a temporary visa on the date of arrival in Brazil while: (1) working under a labour agreement; (2) residing in Brazil for more than 183 days (not necessarily consecutive) in any given 12-month period; or (3) obtaining a permanent visa or a labour agreement before the 184th day of residence in Brazil, within a 12-month period.

1 Silvania Tognetti is a partner at Tognetti Advocacia.
There are no special tax conditions or concessions for foreigners living permanently or temporarily in Brazil.

All departing foreigners (holders of temporary visas, with labour agreements or permanent visas) or Brazilians that decide to live permanently or temporarily abroad should notify the Brazilian Federal Revenue of their departure and file an individual income tax return regarding the period from 1 January up to the departure date. In this case, a federal tax clearance certificate must also be presented.

Afterwards, the foreigner or Brazilian citizen is no longer considered resident in Brazil and as of that moment all income and gains earned in Brazil will be taxed at source (at a flat rate of 25 per cent), except on financial investments, which are taxed at the same rates applicable to Brazilian residents, as described below.

i  Income tax

Every year, by the end of April, the Brazilian individual taxpayer must file a tax return form declaring all income and gains received in the previous tax year (1 January to 31 December), including prizes, bonds, wages, commissions and other kinds of remuneration. The taxable income is very broad and includes everything that is directly or indirectly connected with work or assignment remuneration packages (salaries, 13th month salaries, bonuses, premiums, tips and other gratuities and allowances of any kind).

Stock option agreements are not covered by special tax legislation.

There is no legal option to obtain a deadline extension for filing tax return forms, and each late filed form is subject to an interest charge (calculated according to the financial market, which in Brazil can represent more than 10 per cent per year) and penalty (25 per cent at minimum). All income tax due shall also be paid until such deadline or in six instalments, with interest.

Income tax in Brazil has a lower rate than in other jurisdictions. On the other hand, the tax basis is higher because there are only few tax deductions and there are certain incomes that are segregated to be taxed without any deduction. Education expenses, for example, may be deducted to the limit of 3,561.50 reais. For dependants (e.g., children, stepchildren or spouse), the limit is 2,275.08 reais per person, per year.

The income tax rates are progressive and follow a table that changes with the effect of inflation on Brazilian currency (the progressive table):

<table>
<thead>
<tr>
<th>Monthly income (BRL)</th>
<th>Percentage</th>
<th>Deduction (BRL)</th>
</tr>
</thead>
<tbody>
<tr>
<td>1,903.98</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td>1,903.99 up to 2,826.65</td>
<td>7.5</td>
<td>142.80</td>
</tr>
<tr>
<td>2,826.66 up to 3,751.05</td>
<td>15</td>
<td>354.80</td>
</tr>
<tr>
<td>3,751.06 up to 4,664.68</td>
<td>22.5</td>
<td>636.13</td>
</tr>
<tr>
<td>Above 4,664.68</td>
<td>27.5</td>
<td>869.36</td>
</tr>
</tbody>
</table>

There are exceptions to the income tax progressive rates, such as capital gains, interest and revenue derived from financial instruments and income derived from the stock market.

As a general tax regime, entities withhold all payment to individuals on the amount calculated according to the progressive rates. On their annual income tax return, individual taxpayers declare all revenues from the preceding calendar year together with the entire
amount withheld. After considering income, taxes withheld and authorised deductions of expenses, taxpayers verify the actual annual income tax and pay or request a reimbursement of the difference from the taxes already paid during the previous year.

When an individual receives payment of revenue from another individual (or from a foreign individual or entity) he or she has to calculate the corresponding taxes according to the progressive table, and perform a provisional payment. The provisional amount in a year will be considered in the following year’s tax return (as described above) for the income tax withheld on payments received from Brazilian entities.

There are no special tax rules for shareholders or quota-holders of closely held corporations or private limited liability companies.

Care must be taken to ensure that shareholders’ or quota-holders’ transactions are perceived to be on an arm’s-length basis and, therefore, not deemed to be disguised profit distributions, which are subject to income tax.

The following tax exemptions are worth mentioning:

a equipment, clothing, board and transport provided free of charge by the employer, or the difference between the amount charged for these items and the market value;
b reimbursement of relocation costs when moving to a different area at the request of the employer;
c allowances to cover expenses when working outside the location in which the work is normally performed;
d indemnities in general, including indemnities for work-related accidents;
e contributions made by the employer to private social security programmes on behalf of employees;
f dividends received from a Brazilian corporate entity; and
g increase of corporate capital in kind.

ii Capital gains tax

With some exceptions, capital gains of individuals resident in Brazil are taxed at a progressive rate of 15 per cent to 22.5 per cent, depending on the total amount of the gain. This applies to assets and rights located both in Brazil and abroad.

There may be, however, an exemption (considered on a monthly basis) depending on the asset or right being sold where the sale price is less than certain thresholds. The sale of an individual’s principal residence is also exempt up to a certain amount.

Capital gains of non-resident individuals are subject to withholding tax of 15 per cent to 25 per cent, except for financial income held in bank accounts in Brazil, which may be subject to lower rates. Additionally, earnings from real estate rentals located in Brazil, received by non-residents, are subject to income tax withheld at source at a flat rate of 15 per cent.

This tax is also applied to foreigners abroad if the assets are located in Brazil; worth considering especially in real estate sales and investments in Brazilian companies.

For capital gains earned in reais, the variation of the exchange rates from the moment of acquisition to the point of sale will be considered on the calculation of the tax basis.

In case of capital gains earned in foreign currency, the variation of exchange rates will not be considered. The calculation will apply only to the exchange rate at the point of sale.

iii Other taxes

Despite it being in the Constitution, Brazil does not have a wealth tax. However, there is an ongoing discussion among the political parties about its creation.
Gift and inheritance tax is an estate tax that cannot be higher than 8 per cent. Each state has a different rate but, in general, Brazilian states apply a 4 or 5 per cent rate calculated over the asset’s market value or in case of interests in privately held companies, the net equity value of the company.

The taxpayer, in this case, is the donor. However, if the donor is not a Brazilian resident, the donee should pay the tax. This also applies if the donor and donee are not Brazilian residents, but the gift is located in Brazil.

iv Reopening of the Brazilian tax-amnesty programme

Following the G20 and OECD initiatives on tax transparency and compliance, in 2016 Brazil enacted the special regime for tax and exchange legislation (RERCT), which allows individuals eligible to join this special regime to report their non-declared assets held abroad during the period referred to in the programme.

This ‘tax amnesty’ was reopened in 2017. The main goal of the programme is to offer the opportunity to Brazilian taxpayers to regularise their tax affairs without facing criminal prosecution. In the first instance, they would pay a one-off tax charge of 15 per cent, plus a 100 per cent penalty of the income tax due.

The absence of a proper report of assets held abroad may contribute to many crimes, such as tax evasion, money laundering and forgery of documents, which can result in severe fines and even reclusion.

In addition to paying 15 per cent income tax on the value of the offshore assets, those taking advantage of the reopened programme would have to pay an increased penalty of no more than 100 per cent penalty, but 135 per cent over the same tax amount.

The term to declare to the programme ended on 31 July 2017.

v Cross-border issues

In addition to estate and capital-gains related taxes, all investments and funds sent abroad are subject to taxation in Brazil. Revenues derived from financial investments, as the relevant interests, are taxed separately and are not considered in the annual tax return. Therefore, the taxpayer cannot use personal deductions (or losses in other financial investment) to reduce income tax. A taxpayer will pay income tax on a financial investment’s revenues at a rate that will not consider the global annual income and any deduction.

In 2016, the Brazilian Federal Revenue included the payment of tourism services in the withholding income tax of individuals at the rate of 25 per cent. This means that even tourism services provided abroad are subject to the income tax.

Revenues derived from abroad are also taxed in case of capital gain and on the progressive income tax table referred to in Section II.i.

Dividends received from a Brazilian entity are exempt, but dividends received from abroad are subject to taxation according to the progressive table.

As mentioned in Section II.ii above, revenues from abroad are separated into two categories: amounts originally invested in reais and amounts originally invested in US dollars. All amounts originally invested in reais abroad are subject to exchange rate tax.

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2 Law no. 13,254/16.
3 Law no. 13,428/17.
vi Regulatory issues – the Brazilian Central Bank

Brazil has a Central Bank (BACEN), which controls all foreign exchange transactions performed therein. The negotiation of all types of currency is made directly by financial institutions that are authorised by the BACEN, which registers all funds remitted abroad.

The individual considered a Brazilian tax resident, who holds assets abroad, with a total market value of US$100,000 or higher as of December 31 of each year, is entitled to submit the Brazilian Central Bank Assets Information: no tax is due in view of this statement. Failure to provide the information requested by the BACEN may result in a penalty of up to 250,000 reais and the individual may also face criminal charges.

Furthermore, foreign nationals holding assets in Brazil must also register them with the BACEN. The foreign national must first request his or her individual or corporate taxpayer’s number (CPF or CNPJ, respectively) from the registry, after registering his or her personal information with the registry of individuals or companies in Brazil (CADEMP). As soon as the CPF of the individual or CNPJ of the entity is issued, all financial operations are ready to be performed. In the case of loans granted to individuals resident in Brazil, the applicable registry of the Brazilian Central Bank System (SISBACEN) is the Electronic Declaratory Registration and Financial Operations (RDE-ROF), while in case of assets held in Brazil such as corporate stock, the relevant registry of the SISBACEN is the Foreign Direct Investment Registration System (RDE-IED).

In the case of foreign individuals who die owning investments in Brazil, all heirs and successors thereof must have their own registries. In this case, the same CADEMP procedure shall be performed by each heir or successor. The change of registration of the investment in the case of death of the principal investor shall involve the simultaneous operations required by regulatory exchange control rules. These simultaneous operations require the issuance of foreign exchange agreements; however, they do not involve the effective liquidation of resources, since there is no issuance of payment order from abroad and the delivery of the coin is ‘symbolic’ (symbolic foreign exchange transactions).

vii Fiscal obligations and taxes on succession

The estate of a deceased person is separately taxed in Brazil as an specific entity: as it is a universality of assets and obligations, it is liable for all relevant due taxes on any tax event.

All taxes due in view of Brazilian legislation until the date of death are met by the estate. If the estate has not yet been submitted to the probate proceedings, the relevant taxes are paid accordingly and as per the assets’ value. However, if the assets have already been probated, the legal representative for the deceased’s estate do not respond for the payment of the due taxes. In this case, the successors must request to the federal authorities the cancellation of the deceased’s individual taxpayer’s registry (CPF/MF). The heirs are only responsible for the payment of all taxes due after the probate proceeding and division of the assets. Such responsibility is limited to the amount received from the estate by each heir.

It is important to bear in mind the risk of capital gain in the estate procedure after an individual dies. When property rights are transferred by means of probate proceeding, the assets, in general, are transferred by cost (acquisition value, as stated in the deceased’s tax return). However, there is also the option to re-evaluate the asset by market value (provided by authorised real estate agents). In this case, there may be a capital gain in comparison to the acquisition value that triggers capital gain taxes. The taxpayer is the estate (if still existent) or the heirs at a rate of 15 per cent.
III SUCCESSION

i Introduction to succession in Brazil

In Brazil, individuals may dispose of their assets by means of a testament or by means of the legitimate succession, which is determined by law. However, Brazilian legislation determines that there is a portion of an individual’s inheritance that must be divided among its successors – the legitimate succession.

The legitimate succession determines that the first individuals to be considered in the succession line are the descendants, who compete with the surviving spouse (depending on the marital regime, as per the section below). Subsequently, the next kin in the succession line as per Brazilian legislation are the ascending relatives, who also compete with the spouse (if existent). The collateral relatives are the last kin to be included in the legitimate succession. As per Brazilian law, all such individuals are entitled to at least 50 per cent of the deceased’s assets.

The inheritance is shared between the deceased’s descendants and the spouse according to the number of heirs; the status of the spouse is the same as of the descendants. Therefore, if there is one spouse and three children, the inheritance shall be divided into four parts. It is important to note that all descendants participate in the inheritance – even adopted children or children born out of wedlock.

If there are no descendants, the ascendants (i.e., the parents) may compete with the surviving spouse for the inheritance. In this case, the surviving spouse may continue to live in the real property owned by the deceased that was used as their daily residency, as long as it is the sole property of such nature. The surviving spouse may only benefit from the inheritance if he or she was not divorced or separated from the deceased, either judicially or in fact for more than two years. Only if there are no descendants and ascendants may the surviving spouse solely benefit from the legacy.

The collateral relatives until the fourth degree (siblings, aunts or uncles, cousins, great-uncles or aunts) may benefit from an inheritance if there is no surviving spouse, descendants and ascendants. In this case, the closest degree of kinship of collateral relatives exclude the most distant ones, i.e., siblings take precedence over aunts and uncles in receiving the legacy.

ii Marital regimes

The most common marital regime is the partial communion of assets, by means of which all assets acquired after the date of marriage are common to both spouses – therefore, all assets acquired before the marriage are considered the individual property of each spouse.

However, if the spouses do not wish to accept the partial communion of assets regime, a prenuptial agreement shall be executed at the date of marriage. The first marital regime, in this case, is the universal communion of assets, when all current and previous assets acquired by the spouses are common to both. The second regime, that of the total separation of assets, determines that all current and future assets of the couple are considered the individual property of each spouse. This regime is mandatory if: (1) one spouse is older than 70 years; (2) all parties depend on judicial authorisation to wed; (3) one of the spouses is a widow or widower with children from a deceased individual whose assets have not yet been settled; (4) one of the spouses is a widow or widower to a marriage that was cancelled within 10 months of the deceased’s death; (5) one of the spouses is divorced and the estate has not yet been settled; or (6) the marriage is between the tutor, guardian or trustee of the other spouse.
Furthermore, a companion is considered by Brazilian law as a legitimate family member – the automatic marital regime for this institution is the partial division of assets. However, the parties may decide to adopt a different type of regime upon the execution of a companionship agreement.

Brazilian law now provides for same-sex marriage, as in May 2017 the Superior Court extended the current inheritance procedures to include same-sex partnerships, which means that all companions (heterosexual or same-sex) may benefit from a spouse or partner’s inheritance in the event of death.

iii Cross-border issues

In Brazilian law, regardless of the nationality of an individual, the succession rights are governed by the law of the country in which the deceased was last domiciled. Hence, in the case of death of an individual whose last residence was established in Brazil, whether he or she is not, in fact, of Brazilian nationality, his or her assets (whether located in Brazil or abroad) will be divided among the successors according to Brazilian law. This will be the case even if the successors are not resident in Brazil.

On the other hand, in the case of individuals resident outside of the country who hold assets in Brazil, the succession will be governed by the law of the deceased’s last domicile. If the succession law of the deceased’s country is not favourable to his or her Brazilian spouse or children, the latter may request the succession to be regulated by the Brazilian law.

Furthermore, the Brazilian judiciary has exclusive jurisdiction over the probate of all assets located in Brazil. In this sense, the Brazilian judge shall apply the relevant foreign law; if the assets are spread across multiple locations in Brazil, the competent judge will be the one where the majority of them are concentrated.

In recent years it has become very common for Brazilian individuals to protect their assets for many reasons, including from high taxes in Brazil. Several Brazilian individuals, while trying to protect their assets, set up several corporate and tax structures during their lifetime – such as limited liability companies, corporations, corporate structures established among family members, etc. The incorporation of companies that separate assets to be held by spouses, siblings and descendants is quite usual in our jurisdiction.

However, common foreign structures, such as trusts, are not very common in Brazil, mainly because they are not often recognised, since Brazil has a civil law system. Since the incorporation of trusts involves the remittance of proceeds abroad and having a separate capital structure from Brazil, they are not often used by our citizens, who usually prefer the most ordinary structures, such as local companies or even setting up smaller companies abroad.

Additionally, trusts are not recognised by civil law jurisdictions, such as Brazil and many other Latin American countries. Since the local legislation does not typify the trust structure, it becomes rather difficult to propose such structures to Brazilian individuals who have never had contact therewith. Brazilians are more comfortable with structures they are familiar with and tend to prefer foundations when considering asset protection.

IV WEALTH STRUCTURING & REGULATION

i Commonly used vehicles and tax regimes for wealth structuring

Private clients in Brazil are allowed to set up either domestic or international vehicles, such as companies or investment funds for wealth structuring.
The holding companies are the most common vehicle domestically used for property planning, for the following reasons:

a. real estate contributions (as capital contributions) are not subject to a real estate transaction tax (ITBI);\(^4\)

b. distribution of dividends by Brazilian companies is tax-free;

c. it is possible to make contributions in kind to increase corporate capital with cost value. In this case the cost value will be equal to the declared values of an individual’s last income tax declaration, avoiding payments of taxes over the capital gain;

d. it is possible to define succession agreements in the articles of association or by-laws of the holding company; and

e. holding companies improve the governance of family businesses.\(^5\)

Another option for investments are the exclusive investment funds that are also a common domestic structure that private clients choose as an alternative to preserve the family heritage.

Usually individuals are taxed only in the event of receiving amounts from the fund, whether income or capital gains for sale of quotas.\(^6\) However, when a fund is invested in fixed assets, individuals are taxed for the anticipated profit every six-month period, without any deduction (losses are not deducted from future tax payments).

Even in the wealthiest families in Brazil, it is quite common for individuals to make investments in a specific fund with the aim of insurance called VGBL (only offered by licensed financial institutions) as a practical solution for succession purposes that allows the individual to invest in the following circumstances:

a. in the event of the investor’s death or incapacity, the resources are made available to the elected beneficiaries, either with prompt full payment or monthly payments, without incurring in a grace period or in legal and judicial costs;

b. the beneficiaries may be changed at any time;

c. the investment must be reported in the income tax declaration, but it is excluded from the investor’s assets; and

d. investments in funds created with the aim of insurance, VGBLs and PGBLs,\(^7\) are taxed as payments from the fund. In the first instance tax is levied on income and in the second instance the total amount, including the amount invested, is taxed.

It is also usual for Brazilian private clients to create funds and companies outside the Brazilian jurisdiction, as wealth structuring vehicles to investments, since this kind of structure defers the Brazilian income tax while the assets remain outside Brazil.

In addition, those vehicles provide a way to access more sophisticated structures that are not legally recognised in Brazil.

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\(^4\) Real estate transactions are subject to a municipal tax (ITBI) at a rate of 2 per cent to 3 per cent, depending on the municipality where the real state is located, with the exemption of its incorporation to the patrimony of a legal entity as its object is not real estate business.

\(^5\) For instance, succession disputes and assets verifications are very usual when individuals participate directly in family business.

\(^6\) The Brazilian Federal Administrative Court (CARF) has recently issued a precedent confirming that the capital gains arriving from investment funds are only subject to taxation in the redemption of the investment, at a 15 per cent income tax rate (Precedent No. 2202-01.591).

\(^7\) A PGBL is used to reduce the income tax due on the annual tax return, because it is deducted from the total amount of taxes to be paid.
ii Legal and tax treatment for wealth structuring vehicles

With regard to wealth structuring and planning, high net worth Brazilian individuals are no different from individuals in other parts of the world. They share the same will to protect, preserve and enhance their wealth.

Notwithstanding, the Brazilian Constitution and laws derive from Roman law, the civil law model of absolute ownership, which represents a barrier to the existing structures such as trusts and other sophisticated arrangements that would provide the mechanism through which they could achieve such goals under Brazilian jurisdiction.

As a result of this legal non-recognition and, taking into account forced heirship rules in Brazil, trusts, funds and foundations incorporated outside Brazil are commonly used as wealth structuring and estate planning, thereby allowing greater flexibility in allocating assets and defining rights and obligations among the individual’s heirs.

Heretofore, and differently from other countries, Brazil did not adopt a full controlled foreign corporation (CFC) regime. Profits earned by foreign corporations controlled by Brazilian individuals are not subject to Brazilian income tax until such profits are actually distributed and received inside the country.

Not so long ago, it was quite common for Brazilians investors to simply invest outside Brazil, in this manner obtaining a tax deferral, but also avoiding the reporting requirements. From now on, hiding foreign assets will be much more difficult, since Brazil has recently signed the Multilateral Convention on Mutual Administrative Assistance in Tax Matters during the signing ceremony held at the G20 Summit in Cannes, France, in November 2011 and also executed several tax information exchange agreements (TIEAs)\(^8\) that will start to exchange automatic tax information in 2018.

Nevertheless, by doing such wealth planning abroad, as per Section II.iv above, if the sum of investment abroad\(^9\) is equivalent to US$100,000 or more, Brazilian individuals are obligated to report such assets to the BACEN.

Finally, all the foreign assets must be declared on an annual basis to the Brazilian Federal Revenue.

iii Anti-money laundering regime

As a result of several international conventions, e.g., the Vienna Convention, the Palermo Convention, the UN Convention against the Financing of Terrorism, the UN Convention against Corruption and the Financial Action Task Force (FATF) 40+9 Recommendations, among others, the Anti-Money Laundering (AML) Regime Law No. 9.613/98 was created in Brazil, defining money laundering crimes in broader terms than in some other jurisdictions, setting out the legal and preventive measures, the system for reporting suspicious activities, and the procedures for international cooperation.

After the corruption scandal known as Mensalão, in 2005, that involved the purchase of congressional votes by the ruling political party in Brazil, several of the defendants had money laundering charges dropped due to the fact that the Brazilian AML law at the time required actual knowledge of the origin of the funds by the Brazilian authorities.

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\(^8\) Brazil has signed eight TIEAs, accordingly to the Exchange of Tax Information Portal: http://eoi-tax.org/jurisdictions/BR#agreements

\(^9\) It is required to report the market value of the foreign assets or, when it is not available, the net worth of the companies held outside the Brazilian jurisdiction.
Because of that incident, in July 2012, an amendment to the AML Law was signed (Law No. 12.683/2012), changing the definition of money laundering as the concealment of proceeds of any crime or misdemeanour, no matter the graduation, also excluding the requirement of actual knowledge of the origin of the illicit fund.

The AML Law created an obligation for individuals and companies to keep internal controls, in the case of an eventual administrative inspection, of relevant transactions, to clarify the identification of clients and confirm if the transactions carried out are compatible with the net worth involved.

The AML Law has also created an obligation to report any suspicious information verified by any party in a transaction. All suspicious information, as determined by the AML Law, has to be reported to the Council for Financial Activities Control (COAF), a financial intelligence unit linked to the Ministry of Finance that is actively involved in international initiatives related to the prevention of money laundering and financing of terrorism.

The Complementary Law No. 105 signed in 2001 introduced new rules on bank secrecy and extended the access powers of the COAF. In addition, Law No. 10.701, signed in 2003, created a national register of bank accounts and provided the COAF with even more power to obtain information from third parties.

V CONCLUSIONS & OUTLOOK

Despite the political crisis that began in March 2014 with Operation Car Wash, which implicated the highest levels of power in political and business corruption, Brazil has been trying to establish itself as a country with a suitable environment for the internationalisation of numerous Brazilian companies and also for the many foreign companies that have started to operate in the Brazilian market.

Not only are the current president and the former presidents, Luiz Inácio Lula da Silva and Dilma Rousseff, accused of corruption in this scandal, but traditional wealthy families such as the Odebrecht family are also involved. On the other hand, this also means that the country no longer permits such irresponsible behaviour.

Private clients now have the opportunity to declare whatever assets held outside Brazilian borders they might not have declared before with the amnesty in force, affording them a very good opportunity to review and improve the wealth structure and estate planning, according to the new transparency regime.

Brazil offers an ideal opportunity for advisory professionals in wealth and succession planning to turn the focus to every different vehicle and structure that complies with the current rules.

It is also possible that Brazil will face some relevant reforms in its tax law regime to comply with the OECD rules, so that it keeps following the path to be among the countries with a solid environment for international investors.
Chapter 12

CANADA

Margaret R O’Sullivan, Sara Beheshti and Emma Hamilton

I INTRODUCTION

i The current Canadian wealth situation

On its 150th birthday on 1 July 2017, Canada was hailed as a country that has lived up to its official motto of ‘peace, order and good government’. It is looked to increasingly as an oasis of calm and financial and political stability in a world that, in particular, in the last year, has been on a rollercoaster ride of unprecedented change rocked by a number of unexpected political events – the outcome of the US 2016 presidential elections and the election of Donald Trump, Brexit, and heightened tensions and serious conflict in the hotspots of the world.

But Canadians cannot be complacent. Lurking beneath the surface is a variety of undercurrents that spell potential turbulence and trouble ahead. One is the red-hot housing market, particularly in certain urban centres such as Vancouver and Toronto, and now the prospect of a potential housing correction, which, depending on its severity, could create a tidal wave of dislocation throughout the Canadian economy.

Canada has at the same time drawn the world’s attention by its move in July 2017 for the first time in seven years since the 2008 economic crisis to finally increase interest rates. The concern is that the harmful effects of an artificially induced low-interest rate environment now outweigh its benefits, and the time has come to move forward on the path to normalcy. But how increased rates will impact other aspects of the Canadian economy remain to be seen. Raising rates will increase the Canadian dollar and put a damper on exports. And that dampening effect, if not sufficiently gradual, could be the instigator of a sharp housing correction.

The government is also now more than just stretched – it is virtually tapped-out in terms of debt level, a topic that should be at the core of public debate, but that is not. And with that reality arises the prospect, and virtual certainty, of only increasing levels of taxation, but at the same time Canadians are also tapped-out and have unprecedented levels of personal debt.

The 2017 Canadian Federal Budget announced that the government intends to target private corporations and their shareholders, often high net worth individuals and professionals, who use tax planning to split income among family members or defer tax using private corporations. A package of tax proposals was released on 18 July 2017 for consultation, which contain the most significant changes to tax policy in over 40 years and have rocked

1 Margaret R O’Sullivan is principal and Sara Beheshti and Emma Hamilton are associate lawyers at O’Sullivan Estate Lawyers LLP.
the tax planning community as well as spelling significant problems for entrepreneurs and business owners. What the final proposals will be remains to be seen, but what is clear is the government is desperate and has no choice but to try to squeeze even more tax from those who have more ability to pay. The problem it faces is that at combined highest income tax rates of more than 50 per cent, a tipping point has been reached. While south of the border, the Trump tax proposals are to reduce personal tax rates to a maximum of 35 per cent, which would result in a huge gap of almost 20 per cent compared with Canadian rates should the Trump proposals be enacted, which Canadian politicians must keep in their sights.

In the last year, the Canadian banks and investment community has been embroiled in a lot of soul-searching and debate on their retail practices and on the key issues of who is an adviser and who is not, and whether the fiduciary rule should apply to prevent conflicted advice and ensure transparency of fees in providing financial and estate planning advice, following the lead of other jurisdictions that have adopted the rule, including the UK, Australia and proposals in the US to adopt the rule slated for enactment, and now delayed by the Trump administration.

No doubt the financial and estate planning industry is on the verge of modernisation and change to meet the needs of an ageing demographic, who in particular when it comes to financial and estate planning, need the ability to rely on professional, objective advice and transparency of compensation, fees and commissions.

Which is all to say as indicated at the outset, beneath the surface of Canadian calm lie several disruptive undercurrents taking hold that have the potential to achieve progressive change and carry us forward. What the outcome will be of what seems to be an inflection point on a variety of key issues that impact the Canadian private client and wealth management world remains to be seen. Let’s hope the hands at the tiller are steady ones as government and the private sector navigate some tricky waters ahead.

ii Key factors in respect of private clients

Canada’s constitutional system is a federal one, with a clear division of powers between different levels of government. Its primary legal heritage for all provinces and territories, with the exception of Quebec, is based on English common law; Quebec’s is based on civil law. From the private client perspective, Canada offers the stability of a highly developed legal and court system and charter-based human rights protections. Property law, including succession, is a matter of provincial jurisdiction. Many modern and innovative concepts affecting private clients have been pioneered or progressed ahead of other jurisdictions in Canadian law, including equalisation of property between spouses on marital breakdown and death in several Canadian provinces recognising marriage as an equal economic partnership, recognition of common law spouses’ and same-sex spouses’ property and support rights, and same-sex marriage. Many Canadian jurisdictions have modern laws governing incapacity and substitute decision-making to take into account the need for a modern infrastructure to deal with an increasingly ageing population. Canada’s multiculturalism and relatively ‘open-door’ immigration policy, which is required to maintain positive population growth and expand the Canadian economy and is increasingly geared to attracting more entrepreneurs and skilled workers, have together created and contributed to a dynamic, sophisticated, diverse and innovative Canadian culture.
II TAX

i Personal taxation

Federal and provincial income tax
Canada taxes Canadian residents on their worldwide income from all sources, and non-residents on certain Canadian-source income, subject to international tax treaties. Income for Canadian tax purposes includes income from employment, business, property, 50 per cent of capital gains, and various other income sources, less certain deductions.

Canada is a federal state consisting of 10 provinces and three territories. The provinces and territories also tax income generally on the same basis as the federal government, except for Quebec, and increased federal tax applies to certain income not earned in a province. Canadian tax is levied at graduated rates of up to approximately 54 per cent in combined federal and provincial rates on taxable income, less applicable tax credits.

Canada taxes non-residents on income earned in Canada, notably income from business or employment in Canada and from certain taxable Canadian property, including Canadian real estate. A withholding tax of 25 per cent is deducted from certain income relating to non-residents, subject to international tax treaties that reduce the applicable rates.

Capital gains regime
Unlike most jurisdictions, Canada has no gift or inheritance tax. Instead, it levies tax on capital gains. In 2016, 50 per cent of capital gains are included in income upon actual disposition or deemed disposition. There is an exemption for capital gains on a principal residence and a lifetime exemption (C$824,176 in 2016) for capital gains on certain qualified business-use property.

The basic tax unit is the individual. Limited opportunities exist for income splitting, including by the use of trusts. Tax on capital gains may be deferred on certain transfers of property, for example, between spouses.

ii Developments relating to personal taxation

Provincial tax brackets for high earners
The combined provincial and federal tax rates for high earners in 2017 range from 47.7 per cent in British Columbia to 54 per cent in Nova Scotia. The highest tax rate in 2017 in Ontario is 53.53 per cent. In 2015, Alberta introduced graduated tax rates for taxpayers. Prior to the new rates, all Albertans paid tax based on a flat provincial tax rate of 10 per cent. As of 1 October 2015, the new highest combined provincial and federal tax rate for Albertans will be 48 per cent.

Tax proposals for planning with private corporations
The consultation paper ‘Tax Planning Using Private Corporations’ and draft legislation released in July 2017 focuses on three main issues that the government says can result in ‘high income individuals gaining tax advantages that are not available to most Canadians’: sprinkling income using private corporations to lower tax-rate family members; holding passive investments inside a private corporation to gain the advantage of lower rates than personal rates facilitating the accumulation of earnings; and converting a private corporation’s regular income into capital gains to take advantage of the lower rate on capital gains. If the government’s proposals are ultimately enacted, they would profoundly change tax planning for business owners as practised over the last several decades, and restrict or eliminate many.
planning strategies, and in certain cases, result in double taxation and other anomalies. No doubt, these measures have introduced great uncertainty, but they have also raised concerns about government support for entrepreneurs and those who take risk, and how tax policy should foster it, as opposed to undermining it.

**Revised federal legislation on the taxation of trusts**

Certain estates and testamentary trusts have generally calculated federal tax using the graduated rates applicable to individuals, while trusts established during lifetime have been subject to the top federal marginal rate applicable to individuals. In 2016, graduated rates for certain estates and testamentary trusts were eliminated by the federal government. Now, the top federal marginal rate is applied to testamentary trusts and to certain estates. However, graduated rates will continue to be available to ‘graduated rate estates’ for 36 months and to certain testamentary trusts having disabled beneficiaries who are eligible for the Federal Disability Tax Credit. In addition, the taxation year end for testamentary trusts is now 31 December and testamentary trusts are now required to make instalment payments of income tax.

**Residence of trusts for tax purposes**

The Supreme Court of Canada in 2012 clarified the law on the tax residence of a trust in *Fundy Settlement v. Canada,* also known as Garron Family Trust and St Michael's Trust Corp. The Supreme Court of Canada held that the residence of a trust is where the central management and control of the trust occurs, a significant change from the former focus on a trustee’s residence. *Discovery Trust v. Canada* was the first decision to apply the test that was articulated in *Fundy Settlement*. In that case, the court held that the beneficiaries’ involvement in the administration of the trust did not result in the trust being resident in the province in which the beneficiaries resided as the trustee still made all decisions with respect to the administration of the trust. Instead, the court held that the trust was resident in the province in which the trustee resided.

**New principal residence rules**

In the Canadian system, capital gains are subject to taxation, and arise on the disposition of capital property. The capital gain is the difference between the property’s adjusted cost base plus costs of disposal, and the proceeds of disposition. The adjusted cost is the actual cost of the property, subject to certain adjustments. Proceeds of disposition are, generally, the actual proceeds, but are subject to certain deeming provisions that will deem the proceeds to be equal to the fair market value of the property in respect of dispositions which are not at arm’s length. A property is exempt from taxation on capital gains in the years that it is designated a principal residence.

Effective 3 October 2016, both individuals and trusts must report the disposition of a principal residence and make a principal residence designation in the prescribed form and manner. The period in which the CRA can reassess beyond the normal reassessment period is indefinitely extended if the disposition of a property is not reported and a penalty applies for

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3 *Discovery Trust v. Canada,* 2015 NLTD(G)86.
late filing. For dispositions on or after 3 October 2016, an individual who is a non-resident in the year of acquisition of a principal residence may not include the year that the property was acquired when calculating the exempt years for the principal residence exemption.

As of 2016, only certain eligible trusts may designate a property as a principal residence for any year of ownership after 2016. An eligible trust includes qualified disability trusts, an alter ego trust, spousal or common-law partner trust, joint spousal and joint common-law partner trust, and certain trusts for the exclusive benefit of the settlor during the settlor’s lifetime. An eligible trust also includes ‘orphan’ trusts where: (1) the settlor died before the start of the year; (2) the eligible beneficiary is a minor child whose parents died before the start of the year and is a minor child of the settlor; and (3) at least one beneficiary of the trust is a resident of Canada during the year and is a specified beneficiary of the trust for the year.

In order to benefit from the principal residence exemption, if a trust acquires a property on or after 3 October 2016, the terms of the trust must also provide the eligible beneficiary with a right to the use and enjoyment of the property as a residence throughout the period in the year in which the trust owns the property.

**Non-Resident Speculation Tax**

Effective 21 April 2017, the Ontario government introduced a 15 per cent tax on the value of the consideration when a residential property in the Greater Golden Horseshoe area is purchased or acquired by individuals who are not citizens or permanent residents of Canada, by a foreign corporation or by a taxable trustee, which include both foreign entities holding title in trust for beneficiaries and Canadian individuals or corporations holding title in trust for foreign entity beneficiaries. The new Non-Resident Speculation Tax (NRST) is in addition to the Ontario and Toronto land transfer taxes. Although the NRST is subject to the approval of the legislature, it is currently in effect and applies to any agreements of purchase and sale entered into after 20 April 2017. Effective 2 August 2016, British Columbia enacted a similar 15 per cent property transfer tax payable by foreign entities or taxable trustees in addition to the general property transfer tax on transfers of residential property located in the Greater Vancouver Regional District (also known as the Metro Vancouver Regional District).

**General anti-avoidance rule in respect of income tax**

There is increasing concern over the application of the general anti-avoidance rule (GAAR) in the Income Tax Act (Canada), which may apply to deny the tax benefit of provisions of the Income Tax Act (Canada) where certain conditions are met. In considering whether the GAAR applies, a court will generally consider whether there was a tax benefit, whether the transaction (or series of transactions) giving rise to the tax benefit was an ‘avoidance transaction’ and whether the avoidance transaction giving rise to the tax benefit was abusive.

**Whistle-blower rules, audit initiatives and compliance measures**

The CRA has launched the Offshore Tax Informant Program, under which the CRA will enter a contract to provide financial compensation to individuals who provide information that leads to the assessment or reassessment and collection of additional federal taxes in excess of C$100,000, and where the non-compliant activity involves property located outside Canada or certain other foreign elements. Banks and other financial intermediaries are required to report international electronic funds transfers of C$10,000 and over, to the CRA. Such transfers are currently reported to Canada’s Financial Transactions and Reports Analysis Centre of Canada (FINTRAC). The CRA’s Related Party Initiative is ongoing, under which
individuals, including high net worth individuals (generally over C$50 million) or those with complex planning using many related entities, have been asked to provide detailed information and supporting documents about Canadian and foreign interests. Thresholds relating to value and complexity have been relaxed, and individuals not under audit are also being asked for such information. An aggressive tax planning reporting regime generally requires advisers to report to the CRA information concerning certain transactions on Form RC312 by 30 June of the following year. Reportable transactions or a reportable series of transactions will generally include an avoidance transaction or series of transactions for the purposes of GAAR if they feature two of the following: contingent fees, confidentiality protection or contractual protection. Where the form is not filed, denial of tax benefits and possible penalties may result.

iii  Cross-border structuring

Immigration to Canada

Canada relies heavily on immigration and offers certain tax concessions to immigrants. These same concessions along with the lack of gift and inheritance tax make Canada an attractive destination. Upon immigration to Canada, an individual receives a ‘step up’ in the tax cost of his or her capital property (excluding taxable Canadian property), which eliminates Canadian tax liability for capital gains accrued to that point.

Non-resident trusts and immigration trusts

Certain non-resident trusts established by non-resident settlors provided various conditions are met are exempt from tax and can distribute trust capital to specified beneficiaries tax-free, which provides tax planning opportunities where a non-resident trust situated in a low-tax jurisdiction has Canadian resident beneficiaries. However, the opportunities for trust planning with non-resident trusts have been significantly curtailed by the revised Section 94 of the Income Tax Act (Canada), which prevents the avoidance of Canadian taxes by certain non-resident trusts with Canadian connections where there is a Canadian resident contributor or Canadian resident beneficiary by deeming these trusts to be Canadian resident and taxable on their worldwide income. Where a trust is deemed Canadian resident, Canadian resident beneficiaries can be liable for tax along with the trust.

Previously, an immigration trust could be set up to benefit an immigrant to Canada and his or her family, and the income and capital gains in the immigration trust could accrue tax-free for up to 60 months. If the trust was settled in a foreign jurisdiction (including a low-tax offshore jurisdiction) with foreign trustees who held the foreign investment assets, there could be significant tax savings depending on comparative tax rates. However, this planning opportunity was unexpectedly eliminated as a result of the 2014 federal budget. An immigration trust, including those established prior to the legislative changes, is now subject to tax on its worldwide income, and the 60-month exemption from the deemed residence rule is eliminated.

Emigration from Canada

A taxpayer emigrating from Canada must pay a departure tax, which taxes gains on his or her property that accrued during his or her Canadian residency, subject to exceptions including for certain Canadian situs property and retirement plans. Payment of the departure tax may be deferred upon providing security to the CRA in like amount.
Tax treaties

Canada is a party to many favourable tax treaties, which in part aim to prevent double taxation of income. Due, however, to variations in the internal taxation law of treaty nations, there can be mismatches in tax credits and timing that are not addressed in the treaties. Among other benefits, Canada’s tax treaties include tiebreaker rules relating to tax residency for treaty purposes, and reduce the amount of withholding tax required from income relating to non-residents (often to 15 per cent from 25 per cent and in certain cases to zero per cent). In 2014, Canada ratified an intergovernmental agreement (IGA) relating to the US Foreign Account Tax Compliance Act (FATCA), a US law that imposes strict reporting requirements to the US taxing authority, including on financial institutions located in Canada. Canada has also agreed to implement the Organisation for Economic Co-operation and Development’s Common Reporting Standard (CRS), which is based on FATCA. As of 1 July 2017, financial institutions located in Canada will be subject to the CRS and will be required to provide the CRA with certain information pertaining to accounts and account holders.

Foreign investment entity and foreign trust rules

Foreign trust rules designed to more effectively tax Canadian residents’ passive investment, including in non-resident trusts, have been enacted, following numerous amendments to draft legislation over a protracted period. The non-resident trust rules deem a trust Canadian resident based on the presence of a Canadian-resident contributor, broadly defined, or a Canadian-resident beneficiary, and require tax to be withheld on distributions from trusts deemed Canadian resident, subject to exceptions. An election may be made to treat a portion of the trust as non-resident that will not generally be taxable in Canada. New provisions for taxing offshore investment funds have also been enacted, along with transitional provisions for those who filed under proposed foreign investment entity rules that were never enacted.

Canadian taxpayers holding specified foreign property outside Canada with a cost amount of C$100,000 or more, are required to provide more detailed information about such property on a revised Form T1135, Foreign Income Verification Statement, including names of the countries and institutions where assets are held, foreign income earned on the assets, and a maximum cost amount of the assets in the year. If Form T1135 is filed late or contains certain errors or omissions, the normal reassessment period is extended for three years, and severe penalties apply for failure to file.

iv Regulatory issues

Regulation of banking and related industries

A significant portion of Canada’s private wealth services are highly concentrated in the hands of six major Canadian national banks. In 2017, Bloomberg Markets magazine ranked four Canadian banks among the world’s top 10 strongest banks with US$100 billion or more of assets. No other country dominated the list as Canada did. Banking is federally regulated by the Office of the Superintendent of Financial Institutions Canada, while the related investment industry, trust companies and insurance firms are regulated both federally and provincially. Canada’s major banks are strongly capitalised, and tend to have conservative lending policies relative to other banking institutions.

In 1986, the federal government began to eliminate the four pillars of Canadian finance: Canada’s traditional regulatory separation between banks, trust companies, insurance companies and investment companies. Numerous acquisitions of investment firms and trust
companies by the six largest Canadian banks followed. In 1998, the proposed merger of two of the largest major Canadian banks was rejected by the federal government. In the past decade, Canada’s major banks have expanded significantly into the United States. Canada’s major banks offer an increasing array of services, including daily banking, investment services, financial planning and insurance, and wealth management, which tend to be fairly uniform among the banks.

For Canada, deregulation resulted in a flurry of mergers and acquisitions in the 1990s leading to consolidation and the three largest insurance companies controlling about two-thirds of the domestic market.

v Issues affecting holders of active business interests

Corporate taxation

Canada’s favourable business environment includes low corporate taxes levied at flat rates, which have been reduced aggressively between 2007 and 2012. For active businesses, combined net federal and provincial corporate tax rates range between 26 and up to 31 per cent, and a similar rate applies to income not earned in a province.

Preferential tax treatment is offered to a ‘small business corporation’, a defined term, which receives typical combined federal rates between 10.5 per cent and 18.5 per cent in the provinces on the first C$450,000 to C$500,000 of active business income. A small business corporation includes a Canadian-controlled private corporation carrying on active businesses in Canada (depending on the province, there may also be a requirement that the taxable capital of the corporation be less than C$15 million). Shares of a small business corporation are eligible for a lifetime capital gains exemption of C$800,000 in total indexed for inflation from 2014 (C$834,714 in 2017), as are certain qualified farm and fishing properties.

Investment income earned in a corporation is taxed at approximately the highest personal income tax rate (approximately 48 to 54 per cent in the various provinces). A gross-up and dividend tax credit mechanism is designed to avoid double taxation of dividends earned in a corporation that are subsequently paid to an individual. In 2017, dividends paid by a small business corporation (in respect of income taxed at the small business tax rate) will be grossed up by 17 per cent and the dividend tax credit will be equal to 21/29 multiplied by the amount of the dividend that was grossed up.

A tax-deferred transfer or rollover of certain eligible property to a taxable Canadian corporation for consideration, which must include shares of the corporation, is available subject to conditions. The property may retain its tax cost or receive a higher tax cost within limits. Among other results, the corporation assumes tax liability relating to gains in the property, payment of which is deferred to a later date.

Goods and services tax or harmonised sales tax

Canada levies a 5 per cent supply-side tax on most services and goods, including those made in Canada and imported, and certain property. The goods and services tax applies at all stages of production, subject to an input tax credit for tax paid at an earlier stage, and businesses are responsible for collecting and remitting the tax. In five provinces, the tax has been harmonised with the provincial sales tax and is known as harmonised sales tax, with combined rates between 13 and 15 per cent.
III SUCCESSION

i Overview of succession in Canada

Provincial and territorial jurisdiction
In Canada, succession to property on death is generally a matter within the jurisdiction of the provinces and territories. Of Canada’s 10 provinces and three territories, 12 are governed under common law, and one – the province of Quebec – under civil law. With respect to aboriginal Canadians who are subject to the Indian Act, succession to property on death falls within the jurisdiction of the federal government. Certain First Nations, however, have entered into self-government agreements that permit enactment of individualized laws, including those that relate to succession. These two latter scenarios are beyond the scope of this chapter.

Conflicts of laws
With regard to determining the applicable law, the law governing succession to moveables is generally that of the testator’s domicile and the law governing succession to immoveables typically the jurisdiction where the property is located. Formal validity, which includes such matters as execution requirements for a will, is determined by conflicts of law principles (and in respect of succession to moveables is also generally that of the testator’s domicile at date of death and in respect of succession to immoveables is typically the jurisdiction where the property is located), and in several provinces has been expanded by statute.

For clients with certain connections to both Canada and a participating EU Member State, it is important to consider the impact of the EU Succession Regulation (Regulation (EU) No. 650/2012), which is, in effect, for deaths post 17 August 2015, including as it relates to a client’s ability to choose the law of his or her nationality to govern certain succession issues.

Probate or equivalent court process
The common law principle of testamentary freedom is the general rule in Canadian succession law, as modified by contract or legislation. After the testator’s death, a will is typically submitted to probate or equivalent court process, whereby it is validated and the executors’ appointment as legal representatives confirmed. In this process, the will and supporting documents, which may include a detailed asset listing, become public. Probate fees are typically levied in the form of a flat fee, or tax based on a percentage of estate assets (e.g., approximately 1.5 per cent in Ontario). In some provinces, in particular those with a high rate structure to probate a will, the option of creating a second, non-probate will that governs private company shares and other assets that do not require a court grant of probate to administer is often used to minimize probate fees and tax. A Quebec notarial will need not be submitted to probate in that province.

Once probate has been granted, the resulting certificate, grant or other like document is used by the personal representative to deal with third-party institutions and entities in the process of transferring title to the personal representative and gathering in the assets.

Legislative provisions for succession on intestacy
In an event of intestacy, each province and territory provides for a scheme of property division: typically between the testator’s surviving spouse and children – if any – failing which to other relatives as specified. Some provinces allocate the spouse a preferential share prior to
dividing the estate between spouse and children. In this context, spouses are married spouses, including same-sex married spouses and, in some provinces and two territories, de facto spouses, providing certain conditions are met. A court process for letters of administration or equivalent provides for the appointment of estate trustees on intestacy.

As of 1 January 2017, under Part III of the Succession Law Reform Act4 in Ontario, Section 47(1) was amended to state that for the purposes of determining the beneficiaries on intestacy, the deceased’s descendants and relatives conceived and born alive after the deceased’s date of death shall inherit as if they were born during the deceased’s lifetime and survived, provided specific statutory conditions are met.5

**Legislative provisions for dependants’ support**

In all provinces, a dependant can claim support from the deceased’s estate, provided he or she stands in a certain relationship with the deceased (typically including a spouse, de facto spouse or minor child) and the deceased was providing him or her with support or had a support obligation at the time of death. The quantum of support is determined circumstantially and with judicial discretion, usually taking into account needs and means,6 and in some cases, the dependant’s accustomed standard of living.7 Some provinces recognise a moral entitlement to share in a deceased’s estate and will vary the distribution in a will or award support on this basis.8 Recent decisions have also shown that support may be awarded to a dependant in spite of an existing domestic contract if its terms have become unfair with the passage of time.9

Within Canada, it appears that cases involving entitlement to support in modern ‘non-traditional’ relationships (usually involving de facto spouses) are on the rise, including recent decisions in Alberta10 and British Columbia.11

**Legislative provisions for matrimonial property rights on death**

Property law in Canada falls under the jurisdiction of the provinces and territories; thus the availability and scheme of statutory property division claims by surviving spouses upon death of a spouse vary throughout Canada. The matrimonial property regimes of most provinces and territories provide a surviving spouse with property rights on a first spouse’s death. For example, in Ontario, a surviving spouse has a right to elect to claim against the deceased spouse’s estate to notionally equalise the property acquired during marriage as between the two of them. If such an equalisation claim is made, he or she thereby loses entitlements, if any, under the deceased spouse’s will and to certain other benefits. In New Brunswick, Newfoundland and Labrador, Ontario and Quebec, claims for division of property on death of a spouse are available to legally married spouses only as well as, in the case of Quebec, the survivor of a couple who have entered into a civil union. Currently, in British Columbia, Alberta, Prince Edward Island and the Yukon, death does not trigger a statutory property

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5  Ibid, see s 1.1(1).  
6  See, for example, Bath v. Bath Estate, 2016 BCSC 1239.  
7  See, for example, McKenna Estate (Re), 2015 ABQB 37; Morisset v. Jaczynski, 2015 ONSC 502.  
8  See, for example Tippett v. Tippett Estate, 2015 BCSC 291; Philp v. Philp Estate, 2017 BCSC 625.  
9  See, for example, McKenna Estate (Re), 2015 ABQB 37.  
11 Coombes Estate (Re), 2015 BCSC 2050; Re Richardson Estate, 2014 BCSC 2162; Kish v. Sobchak Estate, 2016 BCCA 65.
claim for the surviving spouse. All other provinces and territories provide a statutory claim to division of property on death and extend its availability to surviving de facto spouses provided the specific requirements of the governing legislation have been met.

ii Key legislative or case law changes affecting succession

Increased Ontario compliance to probate a will

In Ontario in 2011, legislative measures were enacted under the Estate Administration Tax Act permitting the Minister of Finance to assess estates for payment of additional Estate Administration Tax. No practical means or process for determining which estates to assess was put in place until 1 January 2015 when with little forewarning, a new regulation under the Act came into effect. The changes usher in a new reporting regime that is triggered by applying for and receiving a certificate of appointment of estate trustee. Estate representatives must now, in addition to the paperwork relating to the certificate, provide an estate information return to the Ministry of Finance within 90 calendar days of the court issuing the certificate of appointment. Most significantly, the return (an approved form of which is available from the Ministry) requires detailed information about each estate asset and its fair market date of death value. The estate representative must be able to corroborate the reported asset values. Penalties include fines and even imprisonment for failing to file a return or where the information filed was false or misleading. Amending returns must be filed within 30 days of discovering a prior return was incorrect or incomplete, except where the value previously provided for an estate asset has been determined to be incorrect and more than four years have passed since the issuance of the certificate of appointment. The Ministry has broad audit powers in conducting its review of the returns, including assessment of further tax if the estate date of death value is determined to be higher than originally reported.

Gifts in wills altered for public policy reasons

Recent Canadian lower court decisions (one decision from New Brunswick and another from an Ontario court) had limited testamentary freedom by altering gifts in wills for public policy reasons. The New Brunswick decision of McCorkill v. Streed had the effect of striking an unconditional bequest to a racist corporation on the basis of public policy. This decision was upheld on appeal and an application for leave to appeal to the Supreme Court of Canada was dismissed. In the Ontario decision of Spence v. BMO Trust Co, a court struck the entire will of a testator who was survived by two adult daughters (neither of whom qualified as dependants) where one daughter was entirely left out of the distribution of the estate. The will stated the testator had excluded the daughter because she had not communicated with him for years. Based on affidavit evidence, however, the court concluded that the real reason for the daughter’s exclusion was that she had had a child with a man of a different race. Again the doctrine of public policy was employed and the entire will was struck down with the result that both daughters shared in the estate equally on intestacy. The Ontario Court of

14 Spence v. BMO Trust Co, 2015 ONSC 615.
Appeal reversed the decision, thereby confirming in this instance that testators do not have any obligation to benefit persons who they have no legal obligation to support or otherwise benefit (e.g., non-dependent adult children).\textsuperscript{15}

**Mutual wills**

In a recent Ontario lower court decision, two spouses executed wills simultaneously leaving everything to the survivor of them, followed by an identical gift over to their four children (each spouse having two children from a prior marriage). After the husband’s death, the wife made a new will and gifted her estate to her two adult children and she subsequently died. On an application commenced by the husband’s two adult children, the court found that while there was not a direct written or oral agreement that the spouses’ original wills were mutual wills, as a result of the extrinsic evidence presented – including with respect to the family context – an oral contract had existed between the spouses and by virtue of it, neither spouse was entitled to vary his or her will without the consent of the other spouse. The court held that the estate of the surviving spouse was to be divided among all four children.\textsuperscript{16} In a similar case, the testator and his wife executed wills without receiving legal advice. The testator left his entire estate to his wife and if she predeceased him, the estate went to his two stepchildren. The wife died and two days later, the testator executed a will leaving his entire estate to his biological children. The testator’s stepchildren brought an application regarding validity of the second will, questioning the capacity of the testator. However, the Court found no evidence or agreement to support the argument that mutual wills existed between the couple. The second will was valid.\textsuperscript{17}

**iii Cross-border developments**

*Changes to US transfer tax*

Canada is home to many dual citizens, including US-Canadian citizens and many Canadians own holiday property in the United States or other US real or personal property, or spend significant time in the United States. A number of Canadians are, as a result, subject to the US transfer tax regime and attentive to any changes in it. Following the American Taxpayer Relief Act of 2012, which became law on 2 January 2013, the US exemption from estate tax remains US$5 million indexed for inflation from 2011 (US$5.49 million for 2017) and the maximum rate of US estate tax increased from 35 per cent to 40 per cent, both permanently subject to future legislation. Where applicable, the US estate and gift tax exemption remains unified. The Trump administration has proposed to eliminate US estate tax, but there is great uncertainty with regard to these proposals at the time of writing.

*Income tax-related reporting requirements*

FATCA, introduced to combat offshore tax evasion, will affect Canadians with US connections and Canadian financial institutions. Final regulations under FATCA set out detailed reporting and withholding requirements for non-US financial institutions with respect to accounts with certain US connections, including those beneficially owned by US citizens.

\textsuperscript{15} *Spence Estate (Re)* 2016 ONCA 196, application to the Supreme Court of Canada for leave to appeal dismissed 2016 CanLII 34005.

\textsuperscript{16} *Rammage v. Estate of Roussel*, 2016 ONSC 1857.

\textsuperscript{17} *Lavoie v. Trudel*, 2016 ONSC 4141.
The requirements under FATCA will be phased in generally, ending in 2017. Information to be reported includes identifying information, information about the values of the accounts, and transaction amounts. Other non-US entities (and it is expected certain Canadian trusts) will also be required to report the ownership or beneficial interests of US citizens.

Under FATCA, such information is generally required to be provided directly to the US Internal Revenue Service (IRS) by non-US financial institutions and entities. Canada has ratified a Model 1 type IGA with the United States and passed legislation that aims to implement the IGA. Designed to ease compliance with FATCA, the IGA modifies FATCA’s provisions in respect of Canadian financial institutions and other Canadian entities, and expands the tax information exchange provisions between Canada and the United States. Pursuant to the IGA, Canadian financial institutions will generally report information to the Canada Revenue Agency rather than directly to the IRS, although they are generally required to register with the IRS to obtain an identification number. It is intended that by complying with the IGA, Canadian financial institutions will avoid a 30 per cent withholding requirement under FATCA on certain payments to them. Also, certain Canadian-registered plans are exempt from reporting under the IGA, and local financial institutions may be entitled to additional relief.


In June 2015, Canada signed the Multilateral Competent Authority Agreement (MCAA), which provides for a coordinated arrangement for the automatic exchange of financial account information among various countries. As of June 2017, over 93 countries have signed the MCAA, with Bahrain being the most recent.

Under the MCAA, Canada agreed to implement the Organisation for Economic Co-operation and Development’s CRS. As of 1 July 2017, financial institutions located in Canada will be subject to the CRS and will be required to provide the CRA with certain information pertaining to accounts and account holders. The first information exchanges are set to take place in 2018. The CRS is based on FATCA and is similar in effect.

**United States income tax penalties for Canadian residents**

The Canadian government has expressed its concern to the US authorities and certain concessions have been granted to Canadian residents who are dual citizens of Canada and the United States. The US Internal Revenue Service has provided measures to assist such persons to fulfil their filing and reporting obligations. In June 2014, the IRS announced streamlined filing compliance procedures for certain US taxpayers who non-wilfully failed to disclose offshore assets, eliminating former requirements that taxpayers owe US$1,500 or less per taxation year and a former risk questionnaire, and requiring a certification regarding the taxpayer’s non-wilful conduct. Certain penalties or enforcement actions may be avoided, and taxpayers may claim retroactive deferral of income earned in Canadian retirement plans. The IRS also announced its intention in June 2014 to modify the 2012 offshore voluntary disclosure programme.
Uniform Substitute Decision-Making legislation

The Uniform Law Conference of Canada (ULCC) adopted the Uniform Interjurisdictional Recognition of Substitute Decision-Making Documents Act (Uniform Act) in August 2016. The Uniform Act is a joint project of the ULCC and the Uniform Law Commission of the United States (ULC), which was undertaken to promote cross-border portability and utility of substitute decision-making documents for property and personal care. The ULC adopted its version of the Uniform Act in July 2014 and US states may now consider enacting it internally. To date, Idaho and Connecticut have enacted it and it has been introduced in Alaska and Colorado. It is up to each Canadian province and territory to consider adopting and implementing the Uniform Act. This new uniform legislation in each jurisdiction marks a significant step forward in promoting cross-border effectiveness of powers of attorney.

Under the ULCC Uniform Act, which differs from the ULC one, a ‘substitute decision-making document’ will be formally valid if it complies with any of the following: (1) the law indicated in the document, or if none; (2) the law of the jurisdiction in which it was executed; (3) the jurisdiction in which the individual was habitually resident; or (4) the law of the place it is to be used. In the Canadian Uniform Act, the application of the governing law can only be refused if its application would be manifestly contrary to the public policy of the enacting province or territory, which the notes to the Uniform Act indicate in matters relating to personal care, including specific medical procedures. The Uniform Acts provide for the ability of a third party to rely on a document as well as, subject to certain exceptions, the obligation of third parties within a reasonable time to accept a substitute decision-making document and not require an additional or different form of authority. It also provides for a court order mandating acceptance and liability for legal costs for refusal to accept a substitute decision-making document in violation of each Uniform Act.

iv Applicable changes affecting personal property

Same-sex marriage and Quebec civil unions

In 2005, Canada legalised same-sex marriage and, as a result, a broad array of statutory and common law rights have been available to same-sex married spouses for over a decade, including rights to share in an estate upon intestacy and any rights to property division under provincial family law statutes. Quebec also solemnises a civil union for same-sex or opposite-sex couples, which confers similar rights to marriage.

Rights of de facto spouses

For unmarried de facto spouses Canada recognises a limited subset of legal rights. De facto spouses are treated similarly to married spouses for various purposes, including taxation and certain government benefits, but significant gaps remain in respect of property rights on relationship breakdown and death, although this varies by province and territory.

Spousal support provisions for de facto spouses in Quebec

In early 2013, the Supreme Court of Canada delivered its decision in Quebec (Attorney General) v. A.,18 also known as Lola v. Eric. Lola (not her real name) claimed spousal support and property rights from her billionaire de facto spouse Eric. The province of Quebec has a greater percentage of de facto spouses than any other province (approximately 32 per cent in

2011, with the national average being 16.7 per cent) and there are few legal rights provided to these spouses on relationship breakdown. While a majority of the Supreme Court agreed with the Quebec Court of Appeal in finding that Article 585 of the Quebec Civil Code, which does not provide spousal support for de facto spouses although it provides for support among married or civil union spouses, discriminates against de facto spouses on equality grounds, the discrimination is justified on the principle of respecting individual couples’ choice and autonomy.

Common law property division for de facto spouses

In Kerr v. Baranow and Vanasse v. Seguin, the Supreme Court reviewed the principles of unjust enrichment and resulting trust applicable to de facto spouses on relationship breakdown. After a relationship of over 25 years, Ms Kerr claimed property and support entitlements. Both parties had worked and Mr Baranow had cared for Ms Kerr after she had suffered a stroke. The court reviewed the law of unjust enrichment applicable to de facto spouses not included in most provincial statutory property division schemes. The elements of the claim are enrichment of one spouse, the corresponding deprivation of another and absence of juristic reason (such as a contract), and remedies have included a constructive trust and monetary amounts, including amounts relating to value received. Where appropriate, the claimant should be treated as a co-venturer in a joint family venture and should share the couple’s mutual gains. Indicia of a joint family venture include mutual effort, economic integration, intention and priority to the family, and there must also be a link between the contribution and wealth accumulated. A new trial was ordered in Kerr regarding unjust enrichment. A monetary remedy is not limited to a value-received approach, and in Vanasse, the Supreme Court upheld a monetary award granted at trial to a partner who had cared for a young family and given up career opportunities during a 12-year relationship.

Discretionary trust interests as matrimonial property

British Columbia’s Family Law Act is the first Canadian family law statute to expressly address discretionary trust interests in the division of family property by categorising certain beneficial interests in property held in discretionary trusts as excluded property. Problems with the original wording of the Act have been rectified by amendments that came into force on 26 May 2014, thereby clarifying that only the increase in value of the spouse’s beneficial interest in a discretionary trust will be subject to division on separation (rather than the increase in value of all of the property in the trust, as originally drafted). Valuation of these interests on separation will continue to remain a live and litigious issue in this province and throughout Canada, as evidenced by recent reported decisions in Saskatchewan, Alberta and Ontario with relatively little valuation analyses having been reported to date.

Legal presumptions relating to jointly held personal property clarified and effect of transfer examined

In two companion cases, *Pecore v. Pecore*\(^{24}\) and *Madsen Estate v. Saylor*,\(^{25}\) the Supreme Court of Canada clarified the common-law presumptions of resulting trust and advancement, which are legal presumptions subject to being rebutted on the civil standard of proof. The Court clarified that a recipient of gratuitously transferred personal property is generally presumed to hold it on resulting trust for the donor. The presumption that the property so transferred is advanced to the donee that has historically applied to certain family relationships, now applies only to transfers between a parent and minor child (not from husband to wife or from parent to adult child). The Court also canvassed issues of evidence. In *Pecore*, the Court found that a father who had placed financial accounts into joint names with his daughter had an actual intention to gift these, whereas in *Madsen* the opposite result prevailed. In *Bradford v. Lyell*,\(^{26}\) a Saskatchewan court held that if an *inter vivos* transfer of a condo property into joint ownership by a grandmother to her granddaughter was found to be intended as a gift of the right of survivorship at the time of the transfer, both the legal and equitable title vested when the joint title was created such that the gift was complete at that time and the grandmother could not later change her mind in her will, thereby entitling the granddaughter to the beneficial ownership of the property upon the grandmother’s death.

Joint ownership continues to be a legal minefield in the context of estates and estate planning. Two subsequent Ontario Court of Appeal decisions have added further outcomes to gratuitous transfers of property into joint ownership. In *Sawdon Estate v. Sawdon*, the court found that evidence of intention regarding the transfer may not only show that the presumption of resulting trust has been rebutted, but also that a transfer of personal property into joint names created a trust of the beneficial right of survivorship for certain beneficiaries in addition to the surviving joint owners (two of the deceased’s children) such that the property passed outside the deceased’s estate and was divided equally among all five of the deceased’s children.\(^{27}\) In *Mroz (Litigation guardian of) v. Mroz*,\(^{28}\) the Ontario Court of Appeal reviewed a mother’s transfer of her home into joint ownership with her daughter where the mother’s will directed that the proceeds of sale from the home be used to fund two legacies to her grandchildren. In this instance and based on the findings of the trial judge regarding the mother’s intentions at the time of the transfer, the Court held that the daughter had not rebutted the presumption of resulting trust, held the property as trustee and the property was to be dealt with in accordance with her mother’s will. *Mroz* was distinguished from *Sawdon* given that the trust obligation in *Sawdon* arose at the time of the transfer (it was *inter vivos*) and in *Mroz* the trust obligation was not to arise until after the mother’s death. In other words, it would appear from these two decisions that trust obligations must take effect prior to a joint owner’s death for the result in *Sawdon* to occur.

Even more recently in Ontario, the Court of Appeal in *Andrade v. Andrade*,\(^{29}\) found that the presumption of resulting trust applied where a mother purchased a property using funds provided to her by her children who lived in the home with her, which were applied to

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\(^{26}\) *Bradford v. Lyell*, 2013 SKQB 330 (CanLII).

\(^{27}\) *Sawdon Estate*, 2014 ONCA 101 (CanLII).

\(^{28}\) 2015 ONCA 171.

\(^{29}\) *Andrade v. Andrade*, 2016 ONCA 368.
the down payment, mortgage and expenses, but the property was held in the names of two of her seven adult children at any given time. The court indicated that the trial judge had erred in finding that the mother had not contributed any of her own funds to the home, and that once her children had provided funds to their mother, the funds became hers. The court also noted that while the tax treatment of the asset post-transfer is one factor to be considered in determining intention at the time of a transfer of a property (in this case, units in the home had been rented out to third parties over the years and the title-holders had reported the rental income on their returns, while their mother had actually received the rent), but it is not determinative of the transferor’s intention. Adding a further dimension to the presumption of resulting trust, a 2015 Alberta Queen’s Bench decision considered, among other matters, whether the presumption applies when a person designates a beneficiary of a retirement plan (or other financial products capable of being designated). The judge ultimately avoided deciding the issue by finding evidence of the deceased’s intention on a balance of probabilities to gift the retirement plans proceeds to his son as the named beneficiary, leaving the question open for future judicial determination.

In Quebec, there is no equivalence to joint tenancy or rights of survivorship. In Gauthier v. Gauthier, the deceased and his son signed an account opening agreement in Florida that held the deceased’s inheritance. The will named the deceased’s three children as beneficiaries, but the son submitted that the account agreement left the inheritance to him, or in the alternative, his father intended to gift the account. The Court did not apply Pecore, but rather looked to the deceased’s intentions. The Court held that the deceased did not intend to gift the account.

Most recently, in the British Columbia Court of Appeal decision in McKendry v. McKendry, the deceased transferred property into joint tenancy with her son and executed a trust declaration to support her intention that the property was to be held in trust. The deceased later decided to gift the property to her son. The deceased executed a two-page document drafted by her lawyer and revised her will to include a clause outlining that the property was to be a gift. The trial court held that the property was held in trust for the deceased by the son and an executed deed would have perfected the gift, but the Court of Appeal found the deceased’s intentions to be ‘manifest and unambiguous’ in providing an inter vivos gift to her son. The presumption of resulting trust was not considered in this case.

This decision highlights the importance of providing clear evidence of intention, whether that is through a third party or supporting documentation.

**Legal presumption of advancement as between spouses in BC**

In F(VJ) v. W(SK), the British Columbia Court of Appeal recently confirmed the common law presumption of advancement between spouses was not abolished by the enactment of that province’s new Family Law Act in 2011, and noted that a BC statute contained no express provision altering the impact of or abolishing the presumption as was the case in the family law statutes of other Canadian jurisdictions such as Alberta, Saskatchewan and Ontario.

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30 Morrison Estate (Re), 2015 ABQB 769.
31 2016 QCCS 2333.
32 2017 BCCA 48; similar decision by the Ontario Court of Appeal in Laski v. Laski, 2016 ONCA 337.
33 2016 BCCA 186 (currently under appeal).
34 SBC 2011, c.25.
Exempting certain matrimonial property from the equalisation regime

The 2012 Ontario Court of Appeal decision in *Spencer v. Riesberry* held that in the circumstances, a matrimonial property held by a family trust where one of the beneficiaries resided did not qualify as a matrimonial home for the purposes of Ontario’s Family Law Act and excluded it from the equalisation calculation as the beneficiary in question did not have an ‘interest’ in the property within the meaning of the Act (although the value of the interest in the trust was still included for the purposes of the calculation). This case represents a frustration of the matrimonial home protection contained in the Act, as well as a potential circumvention of the usual requirements for the spouse’s consent on the sale or encumbrance of a matrimonial home and the right of possession for the non-titled spouse.

Proprietary estoppel

The equitable claim of proprietary estoppel has been successfully used in two recent Ontario cases as the basis for a cause of action in respect of an unfulfilled or reneged promise or assurance relating to a cottage property. In both *Clarke v. Johnson* and *Love v. Schumacher*, the equity resulted in the appropriate remedy being, based on the facts and the exercise of judicial discretion, a proprietary one in the form of an exclusive, irrevocable and time-specific licence (as a monetary award was found in both instances to be inappropriate or insufficient). In both decisions, the courts followed the modern UK test to establish proprietary estoppel, being the establishment of three criteria:

- encouragement or acquiescence in respect of land;
- detrimental reliance; and
- unconscionability.

A third case arising in BC, resulting in a successful proprietary estoppel claim involving a horse farm that saw the trial judge award the entire horse farm to the applicant, has been remitted back to the trial judge to assess the outstanding claims of unjust enrichment and express or implied trust, as well as the proportionality of the trial judge’s remedy to the proprietary estoppel claim. An application for leave to appeal this decision was recently dismissed by the Supreme Court of Canada. *Cowper-Smith v. Morgan* is a recent BC Appellate Court decision in which the proprietary estoppel claim was unsuccessful as the person against whom the claim was advanced did not own the property in question at the time the assurance or representation was made.

IV WEALTH STRUCTURING & REGULATION

i Common vehicles for wealth structuring

Trusts and holding companies are perhaps two of the most common vehicles used in wealth structuring.

38 Jesse Sabey v. Warren Scott Beardsley as executor of the will of Kim Louise von Hopffgarten, deceased, et al. 2015 CanLII 16734.
39 2016 BCCA 200 (currently under appeal).
Trusts

Income splitting

Trusts can be established inter vivos or by will. Inter vivos trusts are often used to split income between family members who have lower tax rates, where the trust earns income and acts as a conduit to allocate income, including taxable capital gains, among lower rate taxpayers. Effective planning involves careful attention to the possible application of the attribution rules, which can attribute income back to a high tax rate taxpayer.

Trusts used in conjunction with an ‘estate freeze’

Trusts are also commonly used in conjunction with an estate freeze to hold growth property, such as common shares of a private holding company, which reflect the future growth of appreciating assets to defer taxation of capital gains to the next generation, as opposed to on death of a founder, thereby achieving significant tax savings. Use of a trust can allow for control of the timing of distribution of property and selection of beneficiaries, and for general wealth protection purposes, and a fully discretionary trust is often used for such purpose.

Trusts as will substitutes

Trusts are also increasingly used as will substitutes, in particular ‘alter ego’ and ‘joint partner’ trusts that are specifically defined under Canadian income tax legislation and allow persons aged 65 and over, provided certain conditions are met, to roll over capital property on a tax-deferred basis, as opposed to triggering capital gains. The alter ego and joint partner trusts are often used to provide for primary succession to property on death as a substitute to a will. They offer several perceived benefits, including: (1) avoiding expensive court fees and tax paid to probate a will, as well as the attendant court process, which can be protracted; (2) more privacy than a will; (3) ensuring capital succession to property on death; and (4) protection against estate litigation, including will challenges and other claims arising on death. They are also an effective and sophisticated vehicle to manage assets on incapacity in contrast to a power of attorney.

Use of testamentary trusts for income splitting and other benefits

Testamentary trusts, that is those created by will, have been used to provide for income splitting on death. Generally, certain estates and testamentary trusts calculate federal tax using the graduated rates applicable to individuals, whereas trusts established during lifetime are subject to the top federal tax rate applicable to individuals. Prior to 2016, testamentary trusts allowed for income splitting between the trust and one or more beneficiaries, which resulted in significant tax savings. However, commencing in 2016, testamentary trusts are now subject to the top federal tax rate applicable to individuals and, consequently, the above tax benefit has been eliminated, but it will still be possible to ‘sprinkle’ income among a group of beneficiaries of a discretionary testamentary trust if the trust terms permit. Also, use of a testamentary trust provides for probate fee minimisation, capital succession planning and can safeguard against beneficiaries’ matrimonial and possible creditor claims, among other benefits.

Multiple wills used to minimise probate fees

Multiple wills are increasingly used in certain provinces to minimise estate administration tax and probate fees. For example, in Ontario, estate administration tax is approximately 1.5 per
cent of the value of estate assets. Assets are often segregated under two wills: a primary will and a secondary will. Assets that generally do not require a probated will to administer by way of proof of executors’ authority to third parties, such as financial institutions and others, are segregated under a secondary will, including private company shares, family loans, tangible personal property and beneficial trust interests. Only the primary will is typically probated, and applicable tax or court fees are then based on a more modest asset base.

**Holding companies**

Holding companies are a common feature of Canadian estate planning. They are commonly used to hold US securities and certain other US situs assets to protect against exposure to US estate tax, to defer tax on active business income where shares of an active business are held by the holding company, to split income, including in conjunction with use of a family trust, and for asset protection and retirement planning.

**Potential tax advantages of holding companies**

The utility of an investment holding company to earn investment income at a lower tax rate than if earned personally will depend on changing tax rates, which historically have at certain times offered tax advantages and at other times are neutral and less advantageous.

Holding companies are also used in conjunction with probate fee and estate tax minimisation strategies as outlined above. Private company shares can pass under a secondary will, which typically may not need to be probated, thereby saving fees and tax, which can be significant where the shares have a high value. There is potential for double taxation on death where assets are held in a holding company, since a deceased person will be subject to personal taxation on the deemed disposition of the shares of the holding company giving rise to possible taxable capital gains, and also the same gains may be reflected in the holding company’s underlying assets, on which tax will be paid at the corporate level on sale of the assets or wind-up of the company. It is therefore necessary to implement proper post-mortem tax planning to avoid potential double taxation on death.

**Anti-money laundering regime**

The federal Proceeds of Crime (Money Laundering) and Terrorist Financing Act came into effect in 2001. It introduced requirements for a compliance regime, record-keeping, client identification and reporting. Reporting entities must implement a compliance regime, keep certain records, obtain certain client identification and report suspicious transactions to an independent agency, the FINTRAC. Certain other financial transactions, as well as terrorist property must also be reported. Reporting entities include financial institutions, such as banks, trust companies, loan companies, life insurance companies, brokers and agents, securities dealers, accountants and accounting firms carrying out certain transactions, real estate brokers, and certain others. The legislation imposes harsh financial and criminal penalties, including imprisonment for failure to report. Reporting entities have to send large-cash-transaction reports to FINTRAC when they receive an amount of C$10,000 or more in cash in the course of a single transaction and financial entities, money service businesses and casinos have to report incoming and outgoing international electronic funds transfers of C$10,000 or more in a single transaction.
V CONCLUSIONS & OUTLOOK

The ominous pronouncements in the 2017 Canadian federal Budget left a sense of apprehension with regard to what the government’s plans were with respect to tax planning for private corporations and their shareholders. Certainly, with its statements, the government set the groundwork for the controversial changes contained in the tax proposals released in July 2017, which will undoubtedly have the effect of further curtailing tax opportunities for entrepreneurs, business owners, and professionals, and create an unfriendly tax environments for the many small business owners that drive much of the economy.

The prospect of increasing taxation in future to meet exploding government debt is certainly not a cheery one. At the same time, the relative stability of the Canadian wealth scene, our sound banking system, and the attractiveness of Canada as a safe haven continues, which perhaps underscores that there is a real price tag for social cohesion and the high quality of life that most Canadians are privileged to enjoy, relative to most other countries.

On its 150th birthday, Canadians had the opportunity to reflect on their good fortune, on all that has been achieved when it comes to the most important issues, to take a balanced perspective, and with pride and a sense of great satisfaction, celebrate the results.
Chapter 13

CAYMAN ISLANDS

Alan Milgate

I INTRODUCTION

The Cayman Islands is a British Overseas Territory located in the western Caribbean. The jurisdiction is recognised as a major international financial centre with leadership in a number of areas, including the offshore trust industry.

Private and institutional users are attracted to the Cayman Islands because of its network of top qualified global advisers, professional and efficient infrastructure, business-friendly approach, adaptability, English common-law framework, economic and political stability, effective regulation and tax neutrality.

The law in the Cayman Islands is derived from an amalgamation of common law and equity, English statutes and local statutes. Trust legislation is supported by a strong and highly regarded local and independent judiciary, court system and legal community. Public and private sectors are continuously reviewing and updating key legislation so that it remains current, viable and relevant in a global context, and also creating new legislation to meet ongoing needs.

In addition to traditional private wealth planning, Cayman Islands trusts and companies are used extensively in corporate structuring, capital markets transactions and structured finance deals. The Special Trusts Alternative Regime (STAR) developed in 1997, created an innovative trust-planning opportunity, providing for trusts to be established for any purpose, provided it is lawful and not against public policy. Advocates of STAR continue to find new uses for this regime in their planning.

The Banks and Trust Companies Law (2013 Revision) and the Private Trust Companies Regulations (2013 Revision) give the Cayman Islands Monetary Authority (CIMA) the responsibility of regulating the trust industry in the Cayman Islands. This includes licensing, registration and ongoing supervision and is a critical feature in the context of a continued focus on compliance in the finance world. CIMA strives to remain first-in-class through ongoing investment in top-quality staff and education and through its collaboration with the private sector in understanding how to meet the needs of Cayman Islands products while upholding the swiftly increasing global standard required of proper regulation.

The Cayman Islands continues to play a leading role in the fight against illegal activities and tax evasion to maintain its position as a premier global financial centre. The jurisdiction takes pride in its forward-thinking, cooperative and dynamic attitude, which saw it counted as one of the first countries (referred to as the ‘Early Adopter Group’) that have agreed to

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1 Alan Milgate is a partner at Rawlinson & Hunter.
implement Automatic Exchange of Information exchanges under the Common Reporting Standard (CRS) by September 2017 and leads the way with a sophisticated approach to Beneficial Ownership Registers.

II  TAX

The Cayman Islands is a tax-neutral jurisdiction rather than a low-tax jurisdiction. There has never been direct taxation in the Cayman Islands either on individuals or corporations and the only fiscal impositions are stamp duty and import duty. The Cayman Islands has no corporation tax, income tax, capital gains tax, inheritance tax, gift tax, wealth tax or any other direct tax.

An exempted company, one whose objects are to be carried out mainly outside the Cayman Islands, can be granted a renewable 20-year guarantee that it will not be subjected to taxation. This is an additional comfort for users of the jurisdiction, even though there are presently no taxes in the Cayman Islands. A trust can also be registered as an ‘exempted trust’ and obtain an undertaking that exempts the trust from the risk of future taxation for 50 years.

III  SUCCESSION

The Cayman Islands adopts the concept of freedom of testamentary disposition. This sets it apart from most civil law jurisdictions where there are forced heirship rules. In the Cayman Islands, there is no obligation on death to provide for any specified persons and no obligation to maintain dependants.

The Cayman Islands is also bound by the conflict of laws rules in England. Under conflict of laws rules, immovable property in an estate will be determined by the laws of the country in which the immovable property is located. Therefore, the Cayman Islands succession law will apply to any immovable property located in the Cayman Islands. Conflict of laws rules further provide that succession of moveable property is governed by the law of the deceased’s last domicile. Therefore, where a foreign-domiciled person leaves a will disposing of moveable property located in the Cayman Islands, the will is only valid to the extent that it is valid under the laws of the deceased’s last domicile.

It is the responsibility of the deceased’s personal representatives to ensure that the estate is dealt with in accordance with the law. The personal representative will apply to the Civil Registry Probate Section of the Grand Court Registry in the Cayman Islands for a grant of representation that serves as proof that the person named within is entitled to collect and distribute the estate. A grant of probate is issued where a will is left by the deceased and the will is proven to the satisfaction of a judge to be valid. A grant of letters of administration will be issued by a judge where no valid will has been left.

Foreign grants of representation from foreign courts in respect of the estates of persons who died domiciled outside the Cayman Islands, leaving assets or property within the Islands, can be resealed by the Grand Court in the Cayman Islands. Once resealed, the grant will be valid under Cayman Islands law. Generally, this process is not available where the deceased dies domiciled in a civil law country as grants of probate are unique to common law.

Applications for a grant of representation must be made within six months of the date of death of the deceased. In the event of failure to do so, leave of the Court must be obtained before an application can be made.
Where the assets of the deceased are held within a Cayman Islands trust structure, it is unusual for a grant of representation to be required in the Cayman Islands to access those assets. This is one of the significant benefits of using a Cayman Islands trust to own Cayman Islands-situated assets.

In addition, a Cayman Islands trust can help to ensure that the Cayman Islands-situated assets can be dealt with according to the wishes of the settlor, rather than according to forced heirship rules of other jurisdictions.

IV WEALTH STRUCTURING & REGULATION

i Cayman Islands trusts

Cayman Islands trusts frequently form an important part of a family’s wealth planning for many reasons. For example, they can be used to preserve capital while providing an income stream for current and future generations, or they can be established to ensure that the family wealth is professionally managed and protected for its intended purpose beyond the lifetime of the current generation. Trusts may also be established to avoid the inconvenience and publicity of probate, or perhaps to create certainty as to the devolution of assets on death where forced heirship laws might otherwise be argued to apply. Depending on the particular circumstances, there can be advantages in setting up trusts in a jurisdiction like the Cayman Islands that has developed a specialised industry.

Trusts established under Cayman Islands law adopt the common law concepts of a trust, whereby a trustee (the legal owner of the assets under a trust) holds the assets beneficially for the beneficiaries of the trust in accordance with the terms of the trust instrument. Indeed, a Cayman Islands trust does not have a separate legal personality.

As mentioned previously, the law of trusts in the Cayman Islands is primarily grounded in the rules of common law and supplemented by local statutes, including the Trusts (Amendment) Law 2016. The Trust Law is the main source of legislation governing the creation and administration of trusts in the Cayman Islands, while CIMA regulates the services provided by trust companies.

The Hague Convention on the Law Applicable to Trusts and on their Recognition 1985 (the Hague Trusts Convention) has not been extended to the Cayman Islands. However, there is nothing in local legislation that would prevent most types of internationally accepted trusts as being recognised in the Cayman Islands.

ii Reserved powers

The Cayman Islands was the first jurisdiction to adopt reserved powers legislation that replaces the common law position in regard to the settlor-directed trust. The legislation, now part of the Trust Law, lists certain powers that may be reserved by a settlor, or conferred upon the protector, without invalidating the trust. In particular, the legislation expressly confirms that it is quite proper and shall not cause the trust to be set aside for the trust instrument to reserve the following unto the settlor:

\[ a \] any power to revoke, vary or amend the trust instrument;
\[ b \] a general or special power to appoint either income or capital of the trust property;
\[ c \] any limited interest in the trust property;
\[ d \] a power to act as director or officer of a company wholly or partly owned by the trust;
\[ e \] a power to give binding directions to the trustee in connection with the purchase, holding or sale of trust property;
a power to appoint, add or remove any trustee, protector or beneficiary;
a power to change the governing law; or
a power to restrict the exercise of any powers of the trustee by requiring that they shall only be exercisable with the consent of the settlor or any other person specified in the trust instrument.

Many other jurisdictions have subsequently introduced similar forms of restricted powers legislation.

### iii STAR trusts
The Cayman Islands created a special type of trust, commonly known as a STAR trust, enacted by The Special Trusts (Alternative Regime) Law 1997 (STAR Law) and is now consolidated with, and contained in, the Trust Law. The intent of the STAR Law was to create an alternative regime under which a new trust, whether for purposes or persons or both, could be created.

To create a valid STAR trust, the trust instrument must include a declaration that the STAR Law provisions apply. In addition, at least one of the trustees of a STAR trust must be a trust company licensed in the Cayman Islands.

There are a number of features that distinguish the STAR provisions from the purpose trust legislation of other jurisdictions. These include the following:

a The objects of a STAR trust may be persons or purposes: the persons may be of any number and the purposes may be of any number or kind, charitable or non-charitable, provided they are lawful and not contrary to public policy. This differentiates from the position in other jurisdictions, where it must be decided whether a trust is a purpose trust or a person trust before deciding whether the purpose trust law applies.

b The rule against perpetuities that limits other types of trusts in the Cayman Islands to the statutory perpetuity period of 150 years does not apply to a STAR trust and, therefore, a STAR trust can have perpetual existence.

c The STAR provisions stipulate that a STAR trust is not rendered void by uncertainty as to its objects or mode of execution. It allows the trust deed to give the trustee or any other person power to resolve an uncertainty as to its objects or mode of execution.

d The STAR provisions deal comprehensively with the issue of enforcers. They provide that the only persons who have standing to enforce a STAR trust are such persons, whether or not beneficiaries, as are appointed to be enforcers by the terms of the trust deed, or in certain circumstances by order of the court. Therefore, beneficiaries who are not enforcers have no right to enforce the trust or to obtain information regarding the trust.

### iv Foundations
The Foundation Companies Law, 2017 introduced a new vehicle to the Cayman Islands that can be used for a wide variety of applications including private, commercial or philanthropic purposes. The foundation company employs the well-known advantages of a company but has greater flexibility over the objects, management and supervision to enable it to be tailor-made to the founder’s objectives. This vehicle is especially attractive to those clients in civil law jurisdictions who are considering a wealth planning structure as the instrument feels like a company while retaining the adaptability of a trust.
In order for a new company to qualify as a foundation company (or for an existing company to convert to a foundation company) it will be required to register as a foundation company and have the following characteristics:

- the foundation company can be limited by shares or by guarantee, with or without share capital;
- in its Memorandum of Association, it must state that it is a foundation company, include a description of its objects (which may but need not, be beneficial to other persons), provide for the disposal of any surplus assets on winding up and prohibit dividends or other distributions of profits or assets to members;
- in addition to adopting articles of association, the foundation company may adopt bespoke by-laws that provide greater flexibility; and
- appoint a qualified person as secretary of the foundation company.

The foundation company is a legal person and thus any uncertainty over the validity of a structure are negated where this vehicle is used for wealth planning. Another significant comfort to potential founders is that the ‘firewall provisions’ ingrained in the Cayman Islands Trust Law will also apply generally to assets contributed to foundation companies.

**Regulation**

Trust companies in the Cayman Islands are regulated by CIMA through the various licences granted and registrations required. Generally, there are two types of licence granted to trustees carrying on a trust business in Cayman:

- a full trust licence entitles the holder to provide trustee services to the public generally; and
- a restricted trust licence is issued subject to the condition that the trust business is limited to certain named clients. A restricted licence trust company is restricted to acting as trustee to specific named trusts that are for related parties or a specific group. All directors and senior officers (including any changes after licensing) must be approved by CIMA.

**Registered private trust companies**

The Cayman Islands has been a leading jurisdiction for the creation of registered private trust companies (PTCs). A PTC is generally established by a wealthy family to act as trustee of specific family trusts. It allows stakeholders to retain a level of influence over their family trusts as they can have input into the choice of the directors of the PTC or potentially to serve as directors themselves. The PTC may also allow greater flexibility when it comes to the choice of investment strategy and advisers, or generally to fulfil the trustee role in a different way to a fully licensed trust company because it has a more focused mandate and risk profile. Often, a PTC is run in conjunction with a family office or with a specific group of trusted advisers that have a legacy connectivity and familiarity with the family.

The Private Trust Company Regulations (the Regulations) introduced in 2008 allow a trust company that is incorporated in the Cayman Islands and that conducts no trust business other than connected trust business to register as a registered PTC. Connected trust business is defined as trust business in respect of trusts, the contributors of which are all, in relation to each other, connected persons.
The effect is that PTCs set up to act as trustees of specific family trusts can be exempt from licensing. Where a PTC chooses not to be licensed and to rely on the exemption allowed by the Regulations, it must register with CIMA by paying an initial registration fee and by filing an annual declaration.

vii Data security and confidentiality

The Confidential Information Disclosure Law 2016 came into force in July 2016 with the repeal of its predecessor, the Confidential Relationships (Preservation) Law (2009 Revision) (CRPL). The new Confidential Information Disclosure Law revises the Cayman Islands’ approach to confidential information to be in line with the UK and most common-law jurisdictions. The criminal penalties that accompanied the old CRPL have been removed, but importantly, it retains the mechanism for seeking court approval for certain disclosures, which ensures that the rights to privacy of information remain well protected. The new Confidential Information Disclosure Law also preserves many of the previous statutory exemptions through which disclosure of confidential information was permitted, including with prior consent or in the normal course of business. Notably, the new Confidential Information Disclosure Law also introduces a whistle-blower defence for disclosures made in good faith in certain scenarios. Overall, the Law is a more user-friendly piece of legislation that continues to protect privacy and the unwarranted publication of confidential information, while allowing compliance at the global level with adequately substantiated information requests.

The Data Protection Law 2017 was passed by the Cayman Islands Government in March 2017 and introduces a legislative framework for data protection that will apply to many of the entities established in the Cayman Islands. The legislation, which is based on the Data Protection Act 1998 of the United Kingdom, regulates specific protection of personal privacy rights and instructs Cayman Islands entities on how they must handle personal records. There are eight data protection principles that form the basis of the law:

- personal data shall be processed fairly and only when specific conditions are met, for instance where consent has been given, where there is a legal obligation, or where it is necessary for performance of a contract to which the data subject is a party;
- personal data ought to be obtained only for one or more specified lawful purposes;
- personal data shall be adequate, relevant and not excessive in relation to the purpose or purposes for which they are collected or processed;
- personal data shall be accurate and, where necessary, kept up to date;
- personal data shall not to be kept for longer than is necessary for the purpose;
- personal data shall be processed in accordance with the rights of individuals as specified under the legislation;
- personal data shall be protected by appropriate technical and organisational measures against unauthorised or unlawful processing, and against accidental loss, destruction or damage; and
- personal data shall not be transferred abroad unless the country or territory to which it is transferred ensures an adequate level of protection for the rights and freedoms of data subjects in relation to the processing of personal data.

It is noted that the Data Protection Law 2017 contains a number of exemptions that may apply, including in relation to trusts, which ensure the integrity of the trust structure is maintained against prejudiced claims.
The Cayman Islands recognises that the vulnerability of entities operating in international financial centres, such as the Cayman Islands, has been heightened, as have the consequences of security breaches. Given the heightened risks, CIMA has reviewed and strengthened its own security strategy. Along with central government and the Information and Communication Technology Authority, CIMA has taken the decision to adopt the National Institute of Standards and Technology Cybersecurity Framework, which is a risk-based set of guidelines designed to help organisations assess current capabilities and create a prioritised roadmap towards improved cybersecurity practices. Going forward, CIMA will review the approach of licensed trust companies to data security risk management. Depending on the trust company’s business and risk profile, they will examine one or more of the following areas: technical controls, incident response and staff training. As part of the reviews, CIMA will also consider the trust company’s ability to protect the confidentiality, integrity and availability of sensitive customer and other information.

viii Money laundering regime

As a leading international financial centre, the Cayman Islands has framed its regulatory system around international standards of supervision and cooperation with overseas regulatory authorities. Professionals working in the financial services industry in the Cayman Islands must abide by the Proceeds of Crime Law, as supplemented by the Money Laundering Regulations and Guidance notes.

The Cayman Islands has accepted the Financial Action Task Force’s (FATF) Forty Recommendations on the Prevention of Money Laundering and Nine Special Recommendations on Countering Terrorist Financing, which are the international standards for effective anti-money laundering and counter-terrorist financing regimes.

The Cayman Islands is a member of the Caribbean Financial Action Task Force (CFATF) and observes the CFATF’s 1992 Kingston Declaration on money laundering. This declaration endorsed the implementation of the 1988 United Nations Vienna Convention, the Organisation of American States Model Regulations, the FATF’s Forty Recommendations and the 19 Regional Specific Objectives.

ix Beneficial ownership

The Cayman Islands commenced new laws on 1 July 2017 that will introduce enhancements to its existing beneficial ownership regime. The new legislation requires certain companies incorporated under the Cayman Islands Companies Law to maintain a register of beneficial ownership at the registered office of the relevant company. This information will be uploaded to a non-public, secure centralised platform maintained by the government. The register must contain the names and details of all individuals and certain relevant legal corporate entities holding (directly or indirectly) more than 25 per cent of the shares or voting rights in the company or the right to appoint or remove a majority of the company’s board of directors. There are some exceptions to the regime and companies out of scope will include those registered or licensed under a Cayman Islands regulatory law.

x FATCA and CRS

The Cayman Islands signed a Model 1(b) (i.e., non-reciprocal) intergovernmental agreement with the United States to implement the US Foreign Account Tax Compliance Act (FATCA). The jurisdiction has also signed an intergovernmental agreement with the United Kingdom to implement UK FATCA, which will be phased out and replaced by the CRS.
The jurisdiction is an ‘early adopter’ of the CRS, having agreed to the exchange of financial account information with the first group of participating jurisdictions by September 2017.

The Department for International Tax Cooperation (DITC) in the Cayman Islands has issued guidance notes for FATCA and CRS and all reporting under the regimes will be directly submitted to the DITC in the Cayman Islands.

V CONCLUSIONS & OUTLOOK

The Cayman Islands is cognisant of the fact the jurisdiction’s thriving trust industry exists as part of a global economy. Therefore, every effort is made to increase international cooperation and collaboration, without compromising proper rights to confidentiality of its users to ensure compliance with financial services best practice.

As with other sectors, trust legislation in the Cayman Islands continuously evolves to meet the ever-changing needs of the financial and private client industry, as well as to adapt to the need for effective compliance at the highest global standard. At present, there is proposed legislation for further amendments to the Trust Law legislation.

Recently, there has been continued dialogue regarding the transparency of beneficial ownership in all jurisdictions. The government has been proactive in this regard and its solution maintains the confidentiality and security of client data for private entities by ensuring the platform is offline and not open to the public at large, while ensuring proper authorities conducting legitimate investigations can obtain relevant information on a timely basis.

While historically the creation of trusts offshore was often driven by efficient tax planning, for the current generation this has changed. Tax considerations continue to be a factor; however, the focus is now on planning for the wealth succession for future generations of the family and protection of assets from improper external threats. The Cayman Islands provides a tax-neutral, stable, sophisticated environment for such planning.

Looking forward, local substance of services and potentially family office presence in the relevant jurisdiction may become ever more important. There is proposed family office legislation in the pipeline which will ensure family offices can establish a substantive presence in the Cayman Islands efficiently. The Cayman Islands boast world-class living accommodation, restaurants, schools, political stability and a legal framework that is attractive to families considering establishing a presence in the jurisdiction. The expert service providers in the Cayman Islands can assist stakeholders with an efficient and effective strategy to establish or move structures to the jurisdiction.
I INTRODUCTION

Despite being among the smallest countries in terms of area and population, Cyprus has developed into one of the world’s most important financial and business centres. It has numerous advantages, including a strategic location, membership of the EU and the eurozone, a mature and transparent legal system, world-class professional and financial services and a modern, business-friendly tax regime, which offers attractive planning opportunities.

During the years following perestroika, Cyprus developed into the portal of choice for investment from the West into the rapidly developing economies of Russia and central and eastern Europe.

Even the largest Russian and eastern European companies have a substantial degree of owner involvement, and high net worth individuals from the region have found Cyprus an excellent location for their personal financial affairs. In 1992 Cyprus enacted the International Trusts Law, which gave investors from overseas formidable asset protection and tax mitigation opportunities and allowed individuals from jurisdictions with forced heirship regimes effectively to regain testamentary freedom.

The links between eastern Europe and Cyprus extend beyond finance. Both share a common Orthodox religious culture and Cyprus is home to tens of thousands of Russians and eastern Europeans.

Today, Cyprus is a low-tax jurisdiction with a modern tax regime and an extensive network of double taxation treaties, allowing effective tax planning. All forms of succession taxes were abolished in 2000. It has world-class professional and financial services and a robust legal infrastructure founded on common law. It enjoys an excellent climate and a high standard of living, and its strategic location at the crossroads of Europe, Asia and Africa gives it a cosmopolitan atmosphere. While Russia and central and eastern Europe remain the key markets for Cyprus, China, India and the Middle East are also significant. The island is home to a large number of extremely wealthy individuals and the financial base for many thousands of non-residents.

II TAX

i Introduction

Cyprus offers a benign personal tax system, with generous allowances and a top rate of 35 per cent on taxable income in excess of €60,000. Passive interest and dividends are exempt from...
income tax. A special defence contribution (SDC) tax is payable on interest, dividends and rents received by individuals if they are both resident and domiciled in Cyprus (see below); individuals who are resident but not domiciled in Cyprus are not liable to SDC. There are no succession taxes and all capital gains apart from those deriving from the disposal of real estate located in Cyprus are exempt from taxation.

**ii Personal income tax**

The tax year is the calendar year and individuals are considered to be resident if they are present in Cyprus for more than 183 days in the relevant year. Cyprus residents are taxed on the basis of worldwide income, irrespective of whether it is remitted to Cyprus. Husbands and wives are taxed separately. Persons who are not resident in Cyprus are subject to income tax on income accruing or arising from sources in Cyprus.

Personal income tax rates are as follows:

<table>
<thead>
<tr>
<th>Income band</th>
<th>Tax rate</th>
<th>Cumulative tax at top of band</th>
</tr>
</thead>
<tbody>
<tr>
<td>€0–€19,500</td>
<td>0 per cent</td>
<td>0</td>
</tr>
<tr>
<td>€19,500–€28,000</td>
<td>20 per cent</td>
<td>€1,700</td>
</tr>
<tr>
<td>€28,000–€36,300</td>
<td>25 per cent</td>
<td>€3,775</td>
</tr>
<tr>
<td>€36,300–€60,000</td>
<td>30 per cent</td>
<td>€10,885</td>
</tr>
<tr>
<td>€60,000 and above</td>
<td>35 per cent</td>
<td>--</td>
</tr>
</tbody>
</table>

Relief is given for donations to approved charities, professional and trade union subscriptions, life insurance premiums and contributions to pension, social insurance and welfare funds. Relief may also be available under a double taxation treaty.

Resident expatriate employees or secondees are subject to income tax on their worldwide income at the rates shown in the table above.

For tax years up to and including 2014, individuals becoming tax-resident and taking up employment in Cyprus were entitled to an exemption of 20 per cent of their annual income from employment in Cyprus for the first three years of residence. The exemption was limited to €8,550 per annum. With effect from the 2015 tax year, the exemption will be extended to five years, but it will be available only until the year 2020.

In 2012, an alternative exemption was introduced for highly paid individuals, exempting 50 per cent of the first five years’ income from employment in Cyprus of a person who was not previously resident in Cyprus, provided the income from employment in Cyprus exceeds €100,000 per annum. With effect from the 2015 tax year, the exemption period of five years was extended to 10 years. In respect of employments beginning on or after 1 January 2015, the exemption is not available to anyone who was resident in Cyprus in any three of the five tax years preceding the year in which the employment in Cyprus began, or to anyone who was resident in Cyprus in the year preceding the year in which the employment began.

The exemption is available in respect of any tax year in which income from employment exceeds €100,000, irrespective of whether the income falls below that amount in any intermediate year, provided that when the employment started the income exceeded €100,000 and the tax authorities are satisfied that the variations in the annual income are not made for the purpose of obtaining this tax benefit.

The two exemptions are mutually exclusive and each taxpayer may only claim one of them.
Exemptions and special cases

The following are exempt from income tax:

a. passive interest and dividends receivable by individuals (these are subject to SDC tax – see below);

b. lump sums received on retirement;

c. profit from the sale of shares;

d. capital sums from approved life assurance policies and provident or pension funds;

e. income from employment services provided abroad to a non-resident employer or an overseas permanent establishment of a resident employer for a period exceeding 90 days in the tax year;

f. certain pensions, such as a widow’s pension;

g. salaries of officers and crew of ships owned by a Cyprus shipping company that sail under the Cyprus flag and operate in international waters; and

h. income from a qualifying scholarship, exhibition, bursary or similar educational endowment.

For income tax purposes a 20 per cent deduction is allowed from rental income received.

The first €3,420 per annum of any foreign pension is free of tax and the excess over that amount is taxed at 5 per cent.

Special defence contribution tax

SDC tax is payable by individuals who are both resident and domiciled in Cyprus on interest, dividend and rentals received at the rates set out below. Individuals who are resident but not domiciled in Cyprus enjoy a full exemption from SDC on all investment income generated on a worldwide basis. Residence is determined in the same way as for income tax purposes.

The principles set out in the Wills and Succession Law, which follow the principles of English common law, are used to determine domicile. In summary, an individual acquires a domicile of origin at birth. It is generally the same as the domicile of the father at the time of birth, and in exceptional cases that of the mother. A domicile of origin may be replaced by a domicile of choice if in actual fact an individual permanently establishes himself or herself in another country with the intention of living there permanently and dying there. However, an individual will be deemed to be domiciled in Cyprus if he or she has been a tax resident for 17 or more of the 20 tax years immediately preceding the year of assessment.

Taken together with the income tax exemption, this means that an individual who is not domiciled in Cyprus is exempt from all Cyprus taxation on interest and dividends from all sources.

Relief or credit for tax paid abroad may be available either under the terms of a double tax treaty or by way of unilateral relief.

<table>
<thead>
<tr>
<th>Type of income</th>
<th>Rate</th>
</tr>
</thead>
<tbody>
<tr>
<td>Dividends</td>
<td>17%*</td>
</tr>
<tr>
<td>Interest</td>
<td>30%</td>
</tr>
<tr>
<td>Rents</td>
<td>3% of 75% of the rent</td>
</tr>
</tbody>
</table>

* 3% on dividends paid by collective investment schemes
iii  Capital gains tax
There is no taxation of capital gains in Cyprus apart from gains made on the disposal of real estate located in Cyprus or on the shares of companies directly or indirectly holding real estate in Cyprus (in which case the taxable gain is the gain attributable to the real estate holding). To stimulate the real estate market, an exemption was introduced for immovable property acquired between 16 July 2015 and the end of 2016, provided that the property was acquired on an arm’s-length basis and not under the foreclosure provisions of the Transfer and Mortgage of Immovable Properties Law. Any gain on the disposal of the property will be exempt from capital gains tax, irrespective of the date of disposal.

As an added incentive, the normal transfer fees payable to the Department of Lands and Surveys on acquisition of immovable property were discounted to 50 per cent of the standard rate until the end of 2016, provided that the property was acquired on an arm’s-length basis and not under the foreclosure provisions of the Transfer and Mortgage of Immovable Properties Law. Alternatively, if VAT is payable on the purchase of the property, no transfer fee is payable at all, provided that the sale agreement is deposited with the Land Registry by 31 December 2016. In July 2016, the reduction in transfer fees was made permanent by the Lands and Surveys Department (Fees and Rights) (Amendment) (No. 2) Law.

iv  Succession taxes
There are no succession taxes in Cyprus.

III  SUCCESSION
Cyprus’s succession law reflects the cosmopolitan nature of the island and gives an interesting insight into its history. The current succession law dates back to when Cyprus was a British colony and the wording of the law and many of its provisions are unmistakably English, but Cyprus succession law also enshrines the concept of forced heirship, usually associated with civil law and Islamic countries, and recognises the rights of widows of polygamous marriages.

It was modified in 2015 by the entry into force of the European Succession Regulation, which applies a single national law of succession to a person’s moveable and immovable property on death, both for testate and intestate succession. The applicable law is that of the country of the deceased’s habitual residence at the time of death, unless the deceased was manifestly more closely associated with another country, or the deceased elected in his or her will for their national law to apply, regardless of whether the European Succession Regulation applies in the state of their nationality or not.

Cyprus succession law is set out in a number of enactments, the most significant of which are the Wills and Succession Law (WSL) and the Administration of Estates Law. The WSL deals with both wills and intestacy. The part dealing with wills is based on the English Wills Act of 1837, whereas the part dealing with intestacy is based on the Italian Civil Code and reflects continental law. Cyprus succession law therefore can be said to represent a mixture of common and civil law, in roughly equal proportions.

If an individual dies leaving certain categories of relatives, part of his or her estate, known as the statutory portion, is reserved for them and distributed according to the rules of intestacy. The actual proportion of the net estate taken up by the statutory portion varies according to which relatives survive the deceased person and can be as much as three-quarters of the net estate.
Individuals who would otherwise be subject to the forced heirship provisions can easily regain the freedom to dispose of their property as they wish by using a domestic trust or a Cyprus international trust.

IV WEALTH STRUCTURING & REGULATION

i Introduction

As with succession law, Cyprus offers wealth-holding structures typical of both common law jurisdictions (in the form of trusts) and civil law jurisdictions (in the form of foundations). Foundations are rarely used in practice because of the high degree of bureaucracy under the Associations and Foundations Law of 1972 and trusts overwhelmingly predominate. However, a new law on foundations is expected to be enacted shortly, which will simplify procedures and which should lead to an increase in the use of foundations.

Cyprus’s first law on trusts, the Trustee Law of 1955, dates back to when the island was a British colony and is a near replica of the English Trustee Act 1925. The English doctrines of equity were formally introduced into the post-independence legal order by Section 29 of the Courts of Justice Law, Law 14 of 1960, which requires the courts to follow English common law and equitable principles unless there are other provisions to the contrary under Cyprus law or such adherence would be inconsistent with the Constitution of Cyprus.

ii The Cyprus international trusts

In 1992 Cyprus created a state-of-the-art international trusts regime with the enactment of the International Trusts Law, Law 69 of 1992 (the 1992 Law), which provides a framework for the establishment of trusts in Cyprus by non-residents.

The 1992 Law introduced a new type of trust, known as an international trust, with tax planning advantages and robust asset protection features. Like similar laws in other jurisdictions, the 1992 Law was not a comprehensive codification and the Trustee Law 1955 applies to international trusts except where the 1992 Law provides otherwise.

Cyprus international trusts proved extremely popular with high net worth individuals and professionals and a number of other jurisdictions introduced similar regimes. Towards the end of the first decade of the current century it became apparent that the international trusts regime in Cyprus had fallen behind those of its competitors. The International Trusts (Amendment) Law of 2012, which entered into force in March 2012, addressed the perceived deficiencies and brought Cyprus back to the forefront of leading trust jurisdictions. It clarified the eligibility provisions for Cyprus international trusts, strengthened their already formidable asset protection features, gavesettlers far more flexibility than under the 1992 Law and widened trustees’ investment powers. It also made several technical amendments and aligned the International Trusts Law with the EU acquis communautaire. The Amending Law of 2012 does not repeal and replace the 1992 Law but instead builds on it. Section 16 provides that it applies to trusts created before it came into effect.

The Cyprus international trust is the structure of choice for non-resident settlers and in the following paragraphs the main features under the International Trusts Law, as amended, are described.

Definition of a Cyprus international trust

The 1992 Law restricted the availability of international trusts to prevent tax avoidance by Cyprus residents. It provided that neither the settlor nor any beneficiary could be a permanent
resident of Cyprus, but this is inconsistent with the EU principle of free movement of persons. Under the International Trusts Law, as amended, the restrictions were relaxed and a Cyprus international trust is now defined as a trust in respect of which:

\[ a \] the settlor (whether a natural or legal person) is not a resident of Cyprus for the calendar year prior to the creation of the trust;

\[ b \] at least one of the trustees for the time being is, during the whole duration of the trust, a resident of Cyprus; and

\[ c \] no beneficiary (whether a natural or legal person) other than a charitable institution is a resident of Cyprus for the calendar year prior to the creation of the trust.

All references to the term ‘resident’ of Cyprus in the amended law now have the same meaning as under the Income Tax Laws, 118(I) 2002 as amended. Moreover, the removal of the prohibition against residence in Cyprus ensures full compliance with EU law regarding the free movement of persons and capital, and freedom of establishment. The removal of the prohibition on ownership of immoveable property in Cyprus avoids any difficulties that might otherwise arise if the settlor or any beneficiary were subsequently to take up residence in Cyprus.

**Asset protection features of Cyprus international trusts**

Asset protection trusts ring-fence the settlor's assets from persons who may have a claim against him or her. They developed as a response to the substantial amounts of damages awarded by juries in civil liability cases in the United States, particularly in medical malpractice claims. Notwithstanding the availability of professional indemnity insurance, some professions still involve a high risk of being on the receiving end of a claim that could be financially disastrous. An asset protection trust adds another layer to the defences. They are also invaluable in a variety of other contexts. In personal life, in light of the substantial awards that courts in certain jurisdictions are making, an asset protection trust may be used to provide added reassurance against claims on breakdown of marriage or civil partnership, particularly for individuals from jurisdictions where prenuptial agreements are ineffective. Many countries have forced heirship provisions in their succession law, reserving a specified portion of the deceased's estate for relatives, and an asset protection trust may provide a means of regaining freedom of testation.

By their nature, all trusts provide an element of asset protection, by segregating the assets held in trust from the settlor's general assets, which would be available to satisfy his or her debts or, in the worst-case scenario, would pass to his or her trustee in bankruptcy; however, Cyprus international trusts have several further advantages.

The first is that the International Trusts Law contains a very strong presumption against avoidance of a Cyprus international trust. Unless the court is satisfied that the trust was made with intent to defraud persons who were creditors of the settlor at the time when the payment or transfer of assets was made to the trust, the trust will not be void or voidable, notwithstanding the provisions of any bankruptcy or liquidation laws of Cyprus or any other country and notwithstanding the fact that the trust is voluntary and without consideration or that it is for the benefit of the settlor or his or her family members. The burden of proof of the settlor's intent to defraud lies with the person seeking to set aside the transfer. Furthermore, any action for avoidance of the trust or setting aside of the transfer must commence no later than two years after the assets were transferred to the trust.
These provisions, particularly the requirement to prove intent to defraud on the part of the settlor, set the bar very high for the claimant trying to set aside a transfer to a Cyprus international trust. Even though the standard of proof is the balance of probabilities, rather than the criminal standard, the claimant must still establish that the trust was more likely than not a fraud. This is a difficult standard to meet in practice and the burden of proving fraud is higher than is usual for civil cases. In practice, the claimant would need very strong evidence to show that the settlor intended to defraud his or her creditors. A claimant domiciled outside the EU without assets in Cyprus would be required to provide security for costs under Order 60 of the Civil Procedure Rules.

Protection against forced heirship and similar claims is provided by Section 3(i) of the 1992 Law, which stipulates that the laws of Cyprus or of any other country relating to inheritance or succession will not in any way affect any disposition of assets to a Cyprus international trust.

The Amending Law of 2012 strengthened these defences by explicitly providing that any question relating to the validity or administration of an international trust or a disposition to an international trust will be determined by the laws of Cyprus without reference to the law of any other jurisdiction. It also makes it clear that the fiduciary powers and duties of trustees, and the powers and duties of any protectors of the trusts are governed exclusively by Cyprus law. Furthermore, it provides that dispositions to a trust may not be challenged on the grounds that they are inconsistent with the laws of another jurisdiction, for example regarding family and succession issues, or on the grounds that the other jurisdiction does not recognise the concept of trusts.

Finally, the Amending Law of 2012 entrenches jurisdictional protection by providing that an international trust containing a choice-of-law clause in favour of Cyprus law is fully protected from unfounded foreign judicial claims as a matter of public policy and order.

These provisions further reinforce the already formidable asset protection features of the Cyprus international trust.

In another area, Cyprus has a distinct advantage over many other Commonwealth countries, in particular the Caribbean islands and Bermuda, in that it is not a party to the arrangements set out in Section 426(4) and (5) of the Insolvency Act 1986, in terms of which British courts and the courts of certain other jurisdictions are required to assist each other in insolvency cases.

Furthermore, it should also be noted that the Charitable Uses Act 1601 (also known as the Statute of Elizabeth), which invalidates arrangements made to hide assets from future creditors, is expressly negated in Cyprus.

Reserved powers and interests

The Amending Law of 2012 allows the settlor of a trust to reserve powers to himself or herself, to retain a beneficial interest in trust property, or to act as the protector or enforcer of the trust, all without affecting the validity of the trust. The powers that may be reserved are extensive, and include the power to revoke, vary or amend the terms of the trust, to apply any income or capital of the trust property, to act as a director or officer of any corporation wholly or partly owned by the trust, to give binding directions to the trustee in connection with the trust property and to appoint or remove any trustee, enforcer, protector or beneficiary. The settlor may impose a general stipulation that the trustees’ powers are exercisable only with the consent of the settlor or any other person specified in the terms of the trust. The settlor may also reserve the power to change the governing law of the trust.
These provisions, which are similar to the corresponding provisions of Jersey and Guernsey law, give settlors great flexibility to adapt to changes in circumstances or objectives.

**Duration of trusts**

As was usual at the time, the 1992 Law restricted the maximum life of international trusts to 100 years from the date on which the trust came into existence. Only charitable trusts and non-charitable purpose trusts were allowed to exist in perpetuity. In the intervening period this restriction on the maximum life of trusts came to be seen as a disadvantage of trusts compared with foundations and several jurisdictions have removed any restriction on the duration of trusts.

The Amending Law of 2012 removed the restriction, by providing that from the date the amendment takes effect and subject to the terms of the trust, there will be no limit on the period for which a trust may continue to be valid and enforceable, and no rule against perpetuities or remoteness of vesting or any analogous rule will apply to a trust or to any advancement, appointment, payment or application of property from a trust. Except where the terms of a trust expressly provide to the contrary, no advancement, appointment, payment or application of income or capital from the trust to another trust is invalidated solely by reason of that other trust continuing to be valid and enforceable beyond the date on which the first trust must terminate.

Cyprus international trusts may, therefore, now be established with unlimited duration.

**Trustees’ investment powers**

The 1992 Law gave trustees freedom in terms of investment powers, merely requiring them to be exercised in accordance with the trust instrument and with the diligence and the prudence that a reasonable person would be expected to exercise when he or she makes investments. The Amending Law of 2012 extended trustees’ investment powers, giving them the same investment powers as those of an absolute owner, allowing them to invest in a broader range of investments for the best interests of the beneficiaries. This brings trustees’ investment powers into line with those of a trustee in England and Wales, and other trust jurisdictions that have followed the English Trustee Act 2000.

The Amending Law of 2012 also removed any doubt regarding trustees’ ability to invest in Cyprus by including a new section specifically empowering trustees to invest in moveable and immoveable property both in Cyprus and overseas, including shares in companies incorporated in Cyprus.

**Confidentiality**

Section 11 of the International Trusts Law, as amended, sets out strict confidentiality obligations. It provides that, subject to the terms of the instrument creating the trust, the trustee, protector, enforcer or any other person may not provide any documents or information that disclose the name of the settlor or any of the beneficiaries or that relate to the trustees’ deliberations regarding the exercise or proposed exercise of their powers and the discharge of their duties, or that relate to the financial position of the trust, except in accordance with a court order requiring disclosure. It gives the trustees power to provide a beneficiary with financial statements or any documents or information relating to their receipts and payments that form part of those accounts if the beneficiary has requested them and if, in the trustees’
opinion, disclosure is necessary and in the best interests of the trust. Disclosure is limited to the accounts and the underlying documents and information concerning receipts and payments.

To remove any uncertainty over the consistency of these provisions with Cyprus's anti-money laundering legislation the Amending Law of 2012 introduced a clause specifically requiring trustees to comply with and implement the relevant provisions of the Prevention and Suppression of Money Laundering Activities Law.

**Taxation of Cyprus international trusts**

Section 12 of the International Trusts Law as amended provides for a uniform tax regime applicable to all persons on the basis of a tax residency test. In the case of a beneficiary who is resident in Cyprus the worldwide income and profits of the trust are subject to Cyprus tax. In the case of a non-resident beneficiary only income and profits earned from sources within Cyprus are subject to Cyprus tax.

Any beneficiaries who elect to become Cyprus tax residents will be subject to taxation on their worldwide income, like any other Cyprus tax resident. Non-resident beneficiaries will be subject to Cyprus taxation only on any Cyprus-source income.

For trusts that have only resident beneficiaries or only non-resident beneficiaries, the application of these principles is very straightforward. Where a trust has both resident and non-resident beneficiaries, the tax authorities will determine the tax treatment by reference to the scope of rights that the respective beneficiaries have in the trust, as set out in the trust instrument.

**Regulation of fiduciary service providers**

The Law Regulating Companies Providing Administrative Services and Related Matters of 2012 (Law 196(I) of 2012) as amended (the ASP Law) provides a comprehensive framework for the regulation of fiduciaries, administration businesses and company directors. As well as implementing the Third EU Anti-Money Laundering Directive as it applies to trust and company service providers, it aims to protect users of trust and fiduciary services by putting in place a robust regulatory system and accounting and reporting requirements.

The ASP Law applies to persons and companies providing relevant fiduciary and other corporate services relating to the administration or management of trusts and companies in or from Cyprus, including directorship and secretarial services provided by a legal person, including acting as an alternate director or secretary, services such as holding of shares of legal persons in a nominee or trustee capacity, provision of a registered office, services related to the opening and operation of bank accounts and services for the ownership of financial assets on behalf of third parties. Providers of relevant services must comply with specified criteria regarding their professional and academic qualifications, experience and their internal procedures. Private trustee companies belonging to the beneficiaries of the trust or their close relatives are outside the scope of the ASP Law provided that they have a representative in Cyprus who is accessible and accountable for anti-money laundering purposes.

The ASP Law provides that relevant services may be offered only by persons or legal entities that hold a licence from the Cyprus Securities and Exchange Commission (CySEC) or who are specifically exempted from the licensing requirement. Lawyers and accountants who are regulated by their respective regulatory bodies (the Cyprus Bar Association (CBA) and the Institution of Certified Public Accountants of Cyprus (ICPAC)) are exempt from the need to obtain a licence but must comply with the other requirements of the ASP Law.
When establishing trusts, service providers are required to obtain documentary evidence of identity of the settlor, the trustees, the beneficiaries (or information on the class of beneficiaries including the beneficiaries to whom any distributions have been made pursuant to the trust) and others associated with the trust, as well as information on the activities of the trust, and keep this information available for inspection by the relevant supervisory body on request. Service providers must put in place adequate arrangements to segregate and account for clients’ funds and they must comply fully with all anti-money laundering legislation. They are subject to continuous monitoring in this regard and CySEC may appoint inspectors to investigate their affairs.

Each of the supervisory bodies for the purposes of the ASP Law (CySEC, the CBA and ICPAC) is required to maintain a register of trusts established by the service providers they regulate, containing the following information:

- the name of the trust;
- the name and full address of every trustee at all relevant times;
- the date of establishment of the trust;
- the date of any change in the law governing the trust to or from Cyprus law; and
- the date of termination of the trust.

Any Cyprus-resident trustee of a trust governed by Cyprus law is obliged to notify the relevant supervisory body of the relevant information within 15 days of the creation of the trust or the adoption of Cyprus law as the law governing the trust, as applicable. Subsequent changes in any relevant information, including termination of the trust or a change in the governing law from Cyprus law, must similarly be notified within 15 days. In the event of termination of the trust or a change in the governing law from Cyprus law, the register will indicate that the trust has been terminated and the information on the trust will be kept for five years.

V RESIDENCE & CITIZENSHIP

High net worth individuals are attracted to Cyprus because it gives them the best of all worlds, combining a benign tax and trusts regime without having to sacrifice quality of life or convenience. Cyprus is a highly developed EU Member State offering a high standard of living, excellent physical and institutional infrastructure and communications, and a very low incidence of crime, all in a Mediterranean climate. Furthermore, it offers individuals of good character investing in Cyprus the benefits of accelerated citizenship by naturalisation, with all the benefits of an EU Member-State passport.

The Civil Registry Law, 141(I) of 2002 provides for non-Cypriots of full age and capacity to acquire citizenship by naturalisation. Applicants are generally required to have lived in Cyprus for seven years prior to submitting an application, and applications generally take years to process. However, in 2013 the Cyprus government introduced a fast-track procedure that allows qualifying persons investing substantial amounts in qualifying assets in Cyprus to obtain Cypriot citizenship by naturalisation on an accelerated basis, typically within three months. Applicants must own a permanent residence in Cyprus with a value of €500,000 or more excluding VAT and have no criminal record and no asset-freezing orders outstanding against them.

The scheme originally required a minimum investment of €3 million but in September 2016 the Council of Ministers approved a number of changes to the programme,
making it even more attractive than before and allowing investors to file a stand-alone application on the basis of a €2 million investment plus purchase of residential accommodation in Cyprus at a cost of at least €500,000.

In addition, several other changes were made:

a the parents of the applicant are also entitled to be granted citizenship, provided they purchase a home in Cyprus;
b purchase of undeveloped land is now an eligible form of investment provided that a master plan for the development of the land is submitted;
c purchase of special government bonds is an eligible form of investment, up to a limit of €500,000;
d purchase of units in qualifying investment funds based in Cyprus is now an eligible form of investment;
e bank deposits are no longer an eligible form of investment; and
f applicants are now required to apply for a residence permit in tandem with the main application.

VI CONCLUSIONS & OUTLOOK

The International Trusts Law of 1992 gave Cyprus a state-of-the-art international trusts regime, with excellent tax mitigation and asset protection features. It was very well received, as evidenced by the large number of trust service providers established in Cyprus, and Cyprus’s continuing popularity with settlors from the former Soviet Union. Over the ensuing 20 years, as other jurisdictions modernised their trusts legislation, Cyprus lost some of its competitive edge, though the basic structure provided by the International Trusts Law remained sound. The 2012 amendments brought the Cyprus international trust regime back to the cutting edge internationally, giving Cyprus the most modern and favourable trust regime in Europe, and providing settlors and beneficiaries with the highest possible degree of protection, confidentiality, flexibility and assurance. This protection has been reinforced by the implementation of an effective, but unobtrusive, regulatory regime, which preserves confidentiality. The accelerated citizenship programme has proved effective in attracting investment into Cyprus and the new ‘non-domiciled’ regime, which exempts investment income from all forms of Cyprus tax, together with income tax exemptions for higher earners and capital gains tax exemptions, will be a further incentive. The proposed new law on foundations will make available an alternative structure for those who may prefer that option.
Finland is a northern European country with a population of 5.5 million, a substantial portion of which lives in the metropolitan area in the south of the country, including the Finnish capital Helsinki. Finland joined the European Union in 1995 and was among the first Member States to adopt the euro in 1999. Finland’s geographical position as a western European market economy and a stable parliamentary democracy sharing a long border with Russia is unique and has shaped the history of the country. Russia has been, and remains, an important trade partner. In 2017, Finland celebrates the centenary of its independence from Russia. Finland is now one of the safest and least corrupt countries in the world, with a high standard of living and a high degree of income equality. It also boasts a world-renowned school system, contributing to most Finns having a very good command of English. Finland is the home of a significant Swedish-speaking minority and the country has two official languages, Finnish and Swedish.

The success of the cell phone and networks manufacturer Nokia Corp, along with a number of high-tech companies, was a major factor contributing to a long period of strong economic growth that Finland enjoyed in the 1990s and 2000s. Finland has, on the other hand, suffered heavily from the recent financial crisis, which coincided with a sharp decline in Nokia’s businesses, as well as a downturn in trade with Russia. This combination lead, inter alia, to a very slow recovery in terms of GDP growth and to Finnish long-term debt being downgraded from its previous AAA-rating by all major credit agencies. The government is now struggling with increasing levels of national debt and an ageing population. The government is also particularly busy with the remarkably extensive health, social services and regional government reform, which is expected to enter into force within the next couple of years.

The Finnish economy was dominated by agriculture until the 1950s, and rapid industrialisation and growth took place during the following few decades. Since the 1970s, Finland has been among the wealthiest countries in the world. As the emergence of a modern economy dominated by industry and services is quite recent, wealth is less accumulated than in most other countries. Finland is also a Nordic welfare state, characterised by free market capitalism combined with a significant public sector, large-scale income redistribution and high tax rates. Because of these factors, wealth is quite evenly distributed among Finns and Finland is home to relatively few high net worth individuals (HNWIs).  

1 Lauri Lehmusoja is a counsel and Stefan Stellato is an associate in the tax group of Hannes Snellman Attorneys Ltd in Helsinki.

2 The former mobile phone manufacturer Nokia (and the Nokia cluster as a whole) generated a handful of HNWIs, but over the past years HNWIs generated by the gaming industry have received more attention.
Despite, for example, a broad network of tax treaties, the Finnish high-tax environment is, perhaps, unlikely to attract HNWIs to Finland. Other factors, such as safety, northern nature, stable institutions, low corruption and a renowned education system are, in this regard, more important assets for Finland.

II TAX

i Recent developments

One issue stands out particularly clearly in the recent developments of Finnish tax law – the ever-increasing disapproval of tax avoidance and planning. In addition, the reputational damage to persons and companies engaging in such activities has grown. Finnish persons and companies involved, for instance, in matters concerning the LGT Bank in Liechtenstein or in arrangements published in the ‘Panama Papers’ are likely to agree.

As a main rule, tax-related information is secret, including, for example, rulings and tax returns. However, taxable income and taxes payable (as determined in the annual tax assessment) are public information in Finland. Unsurprisingly, access to this information attracts significant media attention and each year the media publishes listings on the income and effective tax rates of high income people and companies. Because of the fact that not all tax-related information is public (e.g., later decisions amending the taxation of a given year remain secret) and that tax-exempt income does not show in the statistics, these listings may be somewhat misleading.

The worsening of the general tax atmosphere can also be seen in that the Finnish general anti-avoidance rule (GAAR) is being applied ever more frequently. The GAAR now appears to be engaged in attacking practices that were previously widely considered acceptable. The Tax Administration is, for example, broadly questioning the deductibility of intra-group interest expenses in corporate taxation and closely scrutinising various holding and personal services company arrangements. It also appears that the Tax Administration may begin to challenge certain types of tailored insurance wrappers, a common tax planning strategy. Also legislative changes are expected to reduce the differences in tax treatment of these insurance wrappers as compared to other types of investments.

Another general trend in Finnish taxation over the past years is the increase of both tax rates and progressivity. To name a few examples, the tax on capital income, which for a long time was proportional, became progressive in 2012. New tax brackets have been added at the high end of the scale for earned income, gift and inheritance tax, although all of these taxes were reduced slightly as of 2017.

A reverse trend can be discerned in the taxation of corporations – the corporate income tax rate has gradually decreased and the present 20 per cent rate was introduced in 2014. The focus of taxation is also shifting from taxation of income to the taxation of consumption, and the standard VAT rate is 24 per cent. Taxation with underlying environmental or health-related goals is common, for example, within excise taxation. Finland levied a wealth tax for a long time, until it was eliminated in 2006. At about the same time, the avoir fiscal dividend tax system was abolished because of its incompatibility with EC law.

3 EU rules on state aid forced Finland to abolish its recently introduced sweets tax, an excise tax, from the beginning of 2017.
ii International agreements

Finland has a wide network of bilateral tax treaties. It is also a signatory of the Nordic Multilateral Tax Treaty, which is a multilateral double taxation convention largely based on the OECD Model Tax Convention. Finnish tax treaties typically follow the OECD Model closely and most of them provide for double taxation relief through the credit method. A number of Finnish tax treaties contain provisions that extend the taxing rights of Finland for a number of years after a Finnish citizen moves abroad.

Finland has an agreement with the US to exchange information under the US Foreign Account Tax Compliance Act (FATCA). Finland has also agreed on automatic exchange of information in the context of the OECD Common Reporting Standard (CRS), implemented at the EU level through the DAC2 directive (2014/107/EU). Finland is among the countries that start reporting in 2017. Finland also requires, based on OECD and EU transfer pricing initiatives, multinational groups with revenues exceeding a certain global threshold to file country-by-country reports starting in 2017. Specific plans for amendments to Finnish tax laws necessitated by the Anti-Tax Avoidance Directive (ATAD) and its 2017 amendment (ATAD II) have not yet been released by the government. Furthermore, as an EU Member State, Finland is committed to implement the OECD and Base Erosion and Profit Shifting (BEPS) recommendations.

In 2016, in a case related to the LGT Bank/Liechtenstein tax affair, the Supreme Administrative Court ruled that documents received from a foreign authority may be taken into account as evidence, even if it is possible that the documents were obtained through a criminal act.

iii Income tax

Two categories of tax liability exist in income taxation: unlimited and limited tax liability. People that reside in Finland (as defined in the Income Tax Act) are subject to unlimited tax liability and pay tax on their worldwide income. Conversely, people who do not reside in Finland are subject to limited tax liability and pay Finnish taxes solely on their Finnish-sourced income, as defined in the Income Tax Act.

A three-year rule applies to Finnish citizens when they move abroad. Under the rule, a Finnish citizen is considered a Finnish tax resident during the year of emigration and for the subsequent three calendar years, leading to tax liability for both Finnish and foreign-sourced income. However, if the person establishes, to the satisfaction of the tax authority, that no ‘close ties’ to Finland remain, Finnish tax non-residency (and limited tax liability) may begin before the end of the three-year period.

Taxable income is calculated separately for earned income and capital income. Capital income is income generated through the possession of wealth and earned income is defined as all other income. Earned income is typically salaries, directors’ fees or benefits in kind and is taxable at progressive rates of up to approximately 55 per cent. Capital income is taxable at a rate of 30 per cent up to €30,000 per calendar year and the excess at a rate of 34 per cent.

In some situations, taxation is complicated by the fact that taxable income is assessed separately under three different acts, depending, among others, on if the source of the income is

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4 The signatory countries of the Nordic Multilateral Tax Treaty are Denmark, Finland, Iceland, Norway and Sweden.
5 It should be noted that this three-year rule does not apply to foreign citizens.
income is employment, business or farming.\(^6\) Losses from one source of income may not be offset against another source of income, apart from in rare exceptions. Changes to the rules, introducing among others a presumption that the income of a limited liability company is income from business, are expected as of 2018 or 2019.

Capital gains are generally taxable at the capital income tax rate of 30 or 34 per cent.\(^7\) Some capital gains are exempt, including the sale of a house or apartment that has been used as a permanent home for two consecutive years.

The extensive taxation of capital gains creates an incentive for persons with inherent capital gains to move abroad and realise the gains while no longer subject to Finnish unlimited taxation, or at least resident in another state under the applicable tax treaty. However, moving abroad before realising a significant capital gain requires careful examination of the applicable tax treaty and tax law provisions, including the above-mentioned three-year rule.

Interest income is also taxable at the capital income tax rates. However, interest paid on deposits in Finnish bank accounts and Finnish bonds is subject to a final tax at source at a flat rate of 30 per cent. As far as interest expenses are concerned, deductions are generally granted only where interest is paid with an aim to obtain taxable income. The interest on loans to buy a permanent home was, however, fully deductible until 2012, when the deductible portion started a gradual decrease. It is projected that in 2019 only 25 per cent of home loan interests will be deductible.

The taxation of dividend income is very complex, and the tax rates range from approximately 7.5 per cent to above 55 per cent. These discrepancies highlight the importance of careful tax analysis, but may also offer significant tax advantages. Examples of factors that may have an impact on the applicable tax rate are whether the company distributing the dividend is listed, the value of the company’s net assets, the place of incorporation and on what basis the amount of the dividend is determined.

As far as natural persons resident in Finland are concerned, the least tax is payable when receiving from an unlisted company a dividend that meets two conditions: it equals less than 8 per cent of the shares’ calculated mathematical value and is less than €150,000 in a calendar year. When these requirements are met, 75 per cent of the dividend is exempt and 25 per cent is taxed as capital income, leading to a tax rate of around 7.5 to 8.5 per cent. At the other extreme are, among others, dividends paid in place of wages and dividends paid by companies in non-EU/EEA and non-treaty countries. Such dividends are fully taxable as earned income at progressive tax rates of up to approximately 55 per cent.

Limited liability companies and certain similar types of companies are subject to 20 per cent corporate income tax on their profits. Cross-border restructurings may in some situations trigger exit taxation; for example, where assets are transferred outside the reach of Finnish taxation. In the case of exchange of shares, the tax deferral allowed is forfeited, if a person who has been granted shares in consideration moves his or her residence, as intended in the relevant tax treaty or national laws, outside the EEA within five years after the end of the year in which the exchange of shares was carried out.

Finland introduced CFC legislation in 1995. Since then, the legislation has been amended many times to reflect developments in EU law. In addition, an interest limitation

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\(^6\) These acts are the Income Tax Act, the Business Tax Act and the Act on the Taxation of Farm Income.

\(^7\) The rules were changed as of fiscal year 2016 so that capital losses of individuals and death estates are deductible against all capital income. Under the previous rules, capital losses could only be offset against capital gains.
Finland

rule was introduced recently, roughly barring deductions for net interest expenses that exceed 25 per cent of tax-EBITDA on loans between related parties within the business source of income. There is a safe haven for net interest expenses that do not exceed €500,000. The scope of the current rule will have to be broadened significantly to render it compliant with the requirements of the ATAD as of 2019.

iv Gift and inheritance tax

Inheritance or gift tax is payable, if the place of residence of the decedent or donor, or the place of residence of the beneficiary or donee, was in Finland at the time of death or donation. In addition, tax must be paid on Finnish real property and on shares in any corporate body in which more than 50 per cent of the assets consist in Finnish real property, even if both the decedent or donor and the beneficiary or donee resided overseas. Only inheritances that are at least €20,000 and gifts that are at least €5,000 are subject to tax.

Inheritance tax is assessed on each beneficiary’s net portion of the estate. Tax is payable on portions that are at least €20,000, but widows may deduct an additional €90,000 and minors in immediate lineal descent an additional €60,000 from their portions. The favourable tax treatment of certain insurance indemnities paid to close relatives will be abolished as of 2018.

For the purposes of both inheritance and gift tax, the value of any rights of possession is deducted from the beneficiary’s portion, if such a special possession has been provided for in a will or a deed of gift. The value of the right of possession is not as such taxable, but income derived from the right of possession constitutes taxable income. For example, the title of a house may be donated to person A, but the donor may retain the right to use the house. In this case, person A is taxed on the value of the house less the value of the possession right (calculated according to a formula) and the donor is taxed only on income received from the right of possession (e.g., rental income).

Both gift and inheritance tax have two brackets – the lower tax bracket I applies to close relatives and the higher tax bracket II applies to more distant relatives and to beneficiaries and donees that are not relatives of the decedent or donor. The taxes are progressive within both brackets. As an example of the applicable rates in 2017 in tax bracket I, the tax payable on an inheritance portion of €200,000 is €21,700. An inheritance portion of €1 million is subject to a tax of €149,700 at the lower limit of €1 million and at 19 per cent on any part exceeding €1 million. In tax bracket II, rates are roughly double those of bracket I.

The Inheritance and Gift Tax Act leaves considerable room for tax planning. It may, for example, be wise to pass down property to a greater number of beneficiaries to multiply recipient-specific allowances and thresholds, but also to mitigate progressivity. The same goals

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8 This extended definition of real property is found also in some other tax laws and in tax treaties.

9 Under the rules that are to be abolished certain insurance indemnities could be exempt up to €35,000 or in the case of a widow, up to half or at least €35,000.

10 Tax bracket I for gift and inheritance tax purposes includes, among others, the donor’s or the decedent’s spouse or registered partner, any heir in lineal ascent or descent and any heir of the spouse in lineal descent. As a general rule, cohabitants come under tax bracket II, but they may come under tax bracket I, for example, if they have earlier been married or have a child together.
may be obtained by skipping generations by willing or donating property to, for example, grandchildren. Rights of possession are also frequently retained to lower the valuation of the donated property and hence the payable gift tax.

There are, however, rules aimed at curbing tax planning. Gifts received from the same donor during a three-year period are aggregated. Loans with no intention to pay back and sales at less than 75 per cent of fair market value are subject to gift taxation. There is also an exception to the general rule, according to which the donee may use the gift tax value as his or her acquisition cost – if the donee disposes of the gift within one year from receipt, the acquisition cost will be the donor’s original acquisition cost. Also, in inheritance taxation the value for inheritance tax purposes becomes the beneficiary’s or heir’s acquisition cost, but there is no one-year rule like the one in gift taxation.

The media regularly brings to the public’s attention cases where people move abroad with the aim to avoid gift or inheritance tax. Finland’s neighbours Sweden and Norway, which levy neither inheritance nor gift tax, are particularly attractive from this point of view. However, among others, the tax provisions concerning Finnish real property and Finnish real estate holding companies place hurdles for such tax planning strategies. Similar media attention was attracted by people moving to Spain or Portugal to avoid tax on their private-sector pensions, as the relevant tax treaty did not allow Finland to tax such pensions. New treaties allowing Finland to tax such pensions have now been negotiated with both countries and are currently expected to enter into force in 2018.

The Income Tax Act and the Inheritance and Gift Tax Act provide for relief for certain transactions that aim at passing a business or a farm to the next generation. The relief is implemented, for example, through favourable valuations in inheritance and gift taxation, non-taxation of capital gains, allowing sales at 50 per cent of fair market value without triggering gift taxation or longer tax payment times. The types of relief depend on the way in which the change of generation is carried out and on whether relief is granted under the Income Tax Act or the Inheritance and Gift Tax Act.

Relief is subject to various conditions, which include that at least 10 per cent of the activity is transferred and the activity is continued by the transferee after the transfer. A further sale of a company, farm or other business that has been transferred to the next generation in a transaction enjoying change of generation relief leads to forfeiture of the relief and to a penalty payment if the sale occurs within five years of the purchase agreement or the tax assessment in which the relief was granted. The tax provisions on change of generation transactions are a politically highly sensitive topic in Finland.

Wills may be, partially because of their flexibility, an attractive tool for inheritance tax planning. For example, suspensive conditions that give ownership rights to the beneficiary only after certain conditions are fulfilled have been used to create an interim ownerless period and thus defer the payment of inheritance tax. It should be noted that this strategy has obvious pitfalls.

Until 2017, a further sale at a later point was treated favourably: the capital gain was calculated using as the acquisition cost the full fair market value at the time of the generation-shift transfer (and not the actual taxable value that was lowered based on the above-discussed reliefs). This rule was changed as of 2017 and the capital gain is now calculated using as acquisition cost the (lowered) taxable value that was actually applied.

One common argument against taxes on inheritances is that they endanger the prerequisites to continue a business, especially where the transferred business has no liquid assets that could be used to pay the tax due.
v  Property and transfer taxes
Owners of real property pay real estate tax, which is typically around 1 per cent of the value of the real estate per year. When acquiring real estate, a transfer tax of 4 per cent is payable by the purchaser. The transfer tax rate applicable to housing and real estate companies is 2 per cent, in which case the tax base also includes certain loans of the company, and 1.6 per cent for other shares. No transfer tax is generally payable on listed shares or assets received as a gift or inheritance.

III  SUCCESSION

i  Legal implications of marriage, registered partnership and cohabitation
Marriage and registered partnership have almost identical legal effects, the main differences being that the possibilities to take the other partner’s last name and adoption are more limited in registered partnerships.\textsuperscript{14} Cohabitation, in turn, does not create any immediate legal rights or obligations. The possibility to conclude new registered partnerships ended in March 2017, when legislation allowing same-sex marriages entered into force. Existing registered partnerships can now be turned into marriages with a notification.

Marriage does not cause changes in the ownership of property. Nor is there liability for debt taken by the other spouse, but there may be joint liability for debt taken for the maintenance of the family. The common home is protected by requiring both spouses’ consent to its sale, even where owned by one spouse alone.

A petition for divorce may be filed by the spouses jointly or by only one of them. The reasons for divorce are not examined. Upon granting a divorce, normally after a reconsideration period of six months, one of the spouses may be ordered to pay maintenance to the other spouse, if deemed equitable.\textsuperscript{15}

At divorce, the net marital property is totalled and divided into two in order to determine the share of each spouse. The spouse with less property receives an equalisation payment, which is tax exempt, from the other spouse so that each spouse leaves the marriage with the same amount of what used to be matrimonial property. However, prenuptial agreements are relatively common and they frequently entirely remove the duty to make equalisation payments.\textsuperscript{16}

ii  Intestacy and wills
Finland is a signatory of the Nordic Convention of 19 November 1934 concerning Inheritance, Testamentary Dispositions and the Administration of Estates of Deceased

\textsuperscript{14} Because of significant similarities, in the text below, references to marriage apply also to registered partnerships.

\textsuperscript{15} Since 2011, there is a somewhat limited possibility to receive compensation also upon a cohabitation separation if one partner has assisted the other in accumulating property over a long period.

\textsuperscript{16} Prenuptial agreements cover around a third of all marriages and registered partnerships. Some flexibility as to how a prenuptial agreement is drafted is allowed and it is, for example, quite common to provide that the agreement shall apply only at divorce (but not death of a spouse) or that the prenuptial agreement only affects property accumulated before the marriage. In order to be effective, a prenuptial agreement must be concluded in writing, dated, signed, attested and registered by the local register office.

As an EU Member State, Regulation No. 650/2012 on international successions is of particular importance for Finland. This Regulation governs issues such as applicable law, recognition and enforcement of decisions and the creation of a European Certificate of Succession. It brings more choice, simplicity and clarity to cross-border successions and is binding on most EU Member States.17

In some situations, gifts and other payments received during the decedent's lifetime are taken into consideration in determining the size of the estate to be distributed. After a married person passes away, a division of property is carried out between the spouses. Thus, if the decedent's net assets exceed the net assets of the surviving spouse, the death estate makes an equalisation payment to the surviving spouse. No inheritance or gift tax is due on equalisation payments. A surviving spouse with more net assets than the decedent may decide not to make an equalisation payment to the estate of the deceased person. No division of property is carried out if the spouses' marital rights in each other's property have been removed through a prenuptial agreement.

In the case of intestacy, the children inherit the whole estate even if the decedent was married. If there is no spouse and there are no children, the parents inherit everything, and if there are no living parents, the decedent's brothers and sisters inherit.

A will can be used as a tool to choose the heirs and give them either a share of the estate or a legacy. As a main rule, for a will to be effective, it has to be made in writing and signed in the presence of two witnesses. Direct descendants are protected by a forced heirship regime that gives them the right to claim a reserved portion that equals half of the share that they would have received absent the will. The surviving spouse is protected almost invariably through retention of possession (but not ownership) of the undivided common home.

**IV WEALTH STRUCTURING & REGULATION**

**i Wealth structuring vehicles**

Finnish law does not recognise the common law institution of trust.18 In addition, the use of foundations for wealth structuring purposes is very limited, because foundations are typically required to have a charitable purpose and they are subject to strict supervision enforced with even criminal sanctions. Limited partnerships, on the other hand, are mainly used by private equity investors and in other circumstances where the features of a transparent entity are desirable.

Thus, the most common vehicle for wealth structuring remains the limited liability company. As the taxation of dividends in the hands of an individual shareholder is affected by the value of the dividend-distributing company's net assets, accumulating property in a limited liability company is often advantageous from a tax perspective.19 Setting up a limited

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17 Denmark, Ireland and the UK do not participate in the Regulation.
18 There is, however, some case law, e.g., regarding foreign trusts and their treatment in Finnish taxation.
19 As noted above, the taxation of dividends in Finland is very complex. Another factor affecting the use of holding companies is that dividends from listed companies received by unlisted companies with at least a 10 per cent shareholding, are tax exempt, whereas there is no similar exemption if the shares are held by an individual personally.
liability company is very straightforward and requires a minimum incorporation capital of €2,500. At least one member of the board has to reside within the EU or the EEA, unless a special permission is granted.

Another reason why corporations are an attractive vehicle for accumulating wealth is that invoicing through personal service companies or holding companies, especially in the field of professional services, may to some extent be used as an alternative to receiving the same amount of income as wages. As discussed above, earned income is taxed at rates of up to approximately 55 per cent, whereas the tax burden when charging through a corporation may be more modest – the corporate tax rate is 20 per cent and dividend distributions are often taxed at only 7.5 per cent. Depending on the circumstances, there might not even be a need to distribute dividends, resulting in ulterior tax savings.

The possibilities to use a corporation to mitigate the very heavy taxation of earned income, for example, by medical doctors at private clinics, have been limited through a legislative change in 2010. As a result of the legislative change, the Income Tax Act now provides that dividends received instead of wages are fully taxable as earned income. Even before this amendment, companies with only one shareholder could under certain circumstances be disregarded for tax purposes under the GAAR.

As mentioned above, insurance wrappers, resulting in tax deferral, are frequently used for tax planning purposes. They also offer many tax planning opportunities in cross-border situations. In these arrangements, an insurance policy is ‘wrapped’ around the policy owner’s assets (e.g., shares) that are transferred to the insurance company for the lifetime of the policy. However, it appears likely that the Tax Administration may challenge some of these arrangements, especially those involving the use of a tailored insurance wrapper to hold unlisted assets with personal ties to the insurance holder. Also legislative changes to limit the use of insurance wrappers to obtain tax deferral are anticipated, a discussed alternative having been yearly taxation of a deemed yield.

### ii Regulation of financial service providers and prevention of money laundering

Marketing and offering of services in Finland by investment firms and fund managers of UCITS or alternative investment funds require prior registration with the Finnish Financial Supervisory Authority, which is also the supervising authority. When marketing is directed to non-professional investors (retail investors), certain additional requirements, such as providing Key Investor Information Documents (KIIDs) and the Finnish Consumer Protection Act, apply. The definition of professional investor under the Finnish Investment Services Act is based on MiFID requirements.

Finnish legislation on the prevention of money laundering is largely based on international standards, which include the EU’s Anti-Money Laundering Directives, which are based on recommendations of the Financial Action Task Force on Money Laundering. Requirements under the Finnish Act on the Prevention of Money Laundering and Financing of Terrorism apply to, *inter alia*, investment firms, fund managers, credit institutions and other entities offering financing in Finland. The duties include identification and verification of customers, ongoing monitoring of customer relationships, record-keeping, detecting and analysing suspicious transactions and reporting suspicious transactions to the Financial Intelligence Unit, which operates in connection with the National Bureau of Investigation.

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20 The new provision has encouraged quite creative tax planning schemes to circumvent it.
Violations are subject to administrative and criminal sanctions, and negligence towards the obligations may lead to criminal liability for individual employees. Money laundering offences are sanctioned in the Finnish Penal Code.

V CONCLUSIONS & OUTLOOK

A government proposal to introduce a temporary tax amnesty for undeclared income and assets was given in the autumn of 2015, but heavy criticism ultimately caused the government to call off its proposal. However, increasing exchange of information is a clear future trend. Finland has agreed on automatic exchange of information in the context of the OECD Common Reporting Standard, implemented at the EU level through the DAC2 directive (2014/107/EU). Finland takes part for the first time in 2017, reporting and presumably receiving information for year 2016.

As far as tax planning is concerned, the generation-shift reliefs as well as holding company and personal service company arrangements and potentially insurance-based structures may present attractive opportunities, but careful planning is essential, as tax planning is becoming tolerated less than before. The GAAR is being interpreted ever more broadly and new measures against tax planning are introduced. Implementation of OECD BEPS proposals and EU legislation against tax avoidance and aggressive tax planning, chiefly ATAD and ATAD II, can also be anticipated. As ever fewer tax planning alternatives remain available and, for example, because Finland levies inheritance tax, moving abroad may at present be a relatively effective planning strategy.

There has been a small shift from taxation of income to taxation of consumption and the government has signalled that this will continue to be the emphasis. However, this is by its very nature uncertain, as a change in government coalition may bring alterations to this thinking. What is clear is that Finland will remain a high-tax jurisdiction for individuals, but other factors for which Finland is well known, such as institutional stability, low levels of corruption, good education and a clean environment, are also likely to stay.
Chapter 16

FRANCE

Line-Alexa Glotin1

I INTRODUCTION

France has traditionally been home to individuals of significant wealth as well as one of the most important destinations for foreign investment (including notably real estate investment). The French tax system is becoming, however, less and less attractive and predictable.

Indeed, personal and estate planning for individuals offers fewer opportunities and those that remain are plagued with uncertainty. Moreover, new rules introduced by the preceding and new governments are ever more stringent.

Business immigrants still enjoy significant income and wealth tax exemptions for a limited period of five years, on the condition that they were not tax residents of France during the five years preceding their relocation to France. The downside is that after five years, business immigrants become fully exposed to the French tax system, including to the exit tax (see Section II.v, infra).

If it were not for its tax system, the French system could be regarded as generally protective of individuals, families and their assets. Also, transfer of assets through generations can be structured with flexibility and security. Even the forced heirship rule allows for some planning or may now be circumvented.

Last, it is noteworthy that the general trend in civil law matters is for more room to be given to contracts and less to rigid statutes, hence the current development of private family governance structures.

Divorce law is a complex matter that cannot be summarised in a few sentences. In particular, the area of international divorce requires a good knowledge of the relevant treaties and of the applicable EU regulations, and, more generally, of private international law principles. Division of assets on divorce is a matter where the issue of the applicable matrimonial property regime very often comes into play. Also, one should be aware of the fact that spouses or future spouses cannot contract on the matter of compensatory payments (clean break), the matter being governed by Civil Code principles and subject to the divorce judge’s interpretation of the facts of the matter.

The principal concern therefore is the French tax system, which lately has become so burdensome that France is losing ground in the international tax competition as an attractive place for businesses, entrepreneurs and high net worth individuals.

Indeed, the trend today is for young entrepreneurs to establish themselves and their businesses abroad, for wealthy individuals to leave France and business executives in France and abroad are more and more tempted to exclude France as a candidate for future investment.

1 Line-Alexa Glotin is a partner at UGGC Avocats. The information in this chapter is correct as of 2016.
The bottom line is that France is a country where the middle class and the wealthy contribute heavily but are nonetheless generally regarded as abusers of the economic system.

II  TAX

i  Introduction to personal taxation for individuals

There is no equivalent in France to the common law concept of domicile. Residence is the criteria for liability to tax. Nationality is generally not relevant in the French tax context. It is, however, a criterion that is used in some tax treaties signed by France (tie-breaker rules).

Tax residents of France are subject to: (1) income tax on their worldwide income; and (2) wealth tax, gift tax and inheritance tax on their worldwide assets. Subject to tax treaty, non-residents of France are liable to (1) income tax by reason of their French source income and (2) wealth tax, gift tax and inheritance tax on their French assets.

Domestic law applies first and foremost to determine residence. Tax treaty provisions apply only in these cases where double taxation arises.

In practice, the revenue considers that a person who is predominantly in France (even for less than 183 days) or whose centre of vital interests is located in France, is a resident of France. The day count is therefore not relevant in many situations and some individuals living outside France, but having interests and properties in France where they spend most of their time must consider the tax implications of those rules with great care.

Personal income tax is calculated according to a progressive bracket system with a marginal rate of 45 per cent above €152,000 on net income (wages, bonus, commissions, industrial or commercial profits, professional fees, rental income, etc.) plus social contribution tax.

An income surtax is due: (1) at the rate of 3 per cent between €250,000 and €500,000 and 4 per cent above €500,000 for a taxpayer who is single, (2) at a rate of 3 per cent between €500,000 and €1 million and 4 per cent above €1 million for married couples and members of a PACS (civil pact between different or same-sex couples).

Specific personal income tax rates apply when non-cooperative jurisdictions and territories are involved (75 per cent).

In addition to income tax proper, taxable income is subject to social contribution charges at a global rate of 15.5 per cent on passive income (dividends, interest and capital gains), 7.5 per cent on wages and 6.6 per cent on pensions. Thus, the maximum marginal tax rate income can reach 45+3+15 (63 per cent) and could be as much as 75+3+15 (93 per cent).

ii  Developments relating to personal taxation for individuals

Liability to French gift or inheritance tax depends, with reference to the time of gift, namely death (transfer), (1) on the tax residence of the donor (deceased), (2) on the tax residence of the donee (heir) or legatee, and (3) on the location of the assets for tax purposes (which may be different than for civil law purposes). Hence, a careful analysis of the assets’ nature and location has to be made.

As between parents and direct descendants, the tax is calculated in accordance with a brackets system. The marginal rate is 45 per cent above €1.805 million, subject to a basis reduction of €100,000, available every 15 years.

There is no inheritance tax between spouses or members of a PACS.
France

Lifetime gifts between those couples are subject to tax at the marginal rate of 45 per cent above €1.805 million subject to a basis reduction of €80,000.

Other rules apply to brothers and sisters (45 per cent above €24,000) and non-relatives (60 per cent).

Transfer of business assets enjoys a favourable tax regime depending on the nature of the business. Full or partial exemption applies, one of them consisting in applying a 75 per cent rebate for the purpose of calculating the gift or inheritance tax basis.

### iii Issues relating to cross-border structuring

Private clients’ estate planning in a cross-border environment necessitates that one consider issues such as:

- testamentary freedom;
- surviving spouse and family members’ protection;
- asset protection and transfer to the next generation;
- family governance and control; and
- inheritance, income tax and wealth tax planning.

### iv Regulatory issues

Quite aside from the issue of taxation, privacy in financial matters is nowadays non-existent. Indeed, beyond KYC rules as they are now applied throughout the world, the personal details of owners of French assets, moveable or immoveable, need to be disclosed to satisfy the requirements of our tax laws, notably in relation to the ‘3 per cent tax’, trustees reporting obligations and National Registry, wealth tax, income tax, gift and inheritance tax. Owning assets through French or offshore vehicles is not a solution as this usually attracts even more confiscatory taxes.

### v Issues affecting entrepreneurs at the proprietor level

The high level of social charges and taxes and the lack of flexibility of our labour laws are also severely affecting the situation of entrepreneurs in France.

In another respect, the exit tax regime has a very significant impact on French entrepreneurs, especially for those who need international mobility. The exit tax provides that, subject to specific deferral rules, an individual who was a resident of France for income tax purposes during the six years preceding the exit date will be subject to exit tax on latent gains pertaining to direct or indirect participations (crystallised on the day preceding the exit date), to the extent that, alone or together with other members of the household, the individual’s participation represents 50 per cent of the annual profits or €800,000, irrespective of whether the entity is French, provided only that it is subject to corporate tax or an equivalent tax.

An automatic payment deferral (without collateral) of the income tax component is available if the taxpayer transfers his or her residence from France to another EU Member State or EEA Member State, provided that country has signed an administrative assistance agreement or mutual assistance agreement with France. Payment deferral may be also granted in other situations (e.g., transfer of residence for professional reasons).
III  SUCCESSION

i  Introduction to succession

One of the most notable differences between the common law and civil code systems in the area of the law that will be reviewed here is that, generally, civil law systems do not recognise the concept of ‘estate’. This is true in France. The nearest conceptual equivalent is the notion of *masse successorale*, which refers to the whole of the assets and liabilities of the deceased at the time of death.

Under French inheritance civil law, the conceptual approach is that the estate of the deceased passes directly to his or her heirs at the very moment of death.

Another difference between the two legal systems is the existence under most civil law systems of a limitation on testamentary freedom.

In France, issue of the deceased and, in the absence of issue, certain close relatives and, in most cases, the deceased’s surviving spouse, enjoy special protection by operation of law, the effect of which is to guarantee that they receive a set portion of the estate depending on the number of children of the deceased, if any, as follows: if there is one child, the reserved portion is half; two children, two-thirds; and three or more children, three-quarters. In the event a child dies leaving issue, then the same rules apply per stirpes. In the absence of children, another reserve rule applies to parents, depending on whether there are survivors in one or two ascending lines. In private international law terms, the EU Regulation 650/2012 on International Successions, adopted in June 2012, and which applies to successions opened since 17 August 2015, avoids the fragmentation of successions and enables people living in the EU to organise their succession in advance and guarantees the rights of heirs and legatees. Since that date, the succession is subject to a single law: that of the nationality of the deceased or of his or her last domicile.

The regulation provides a European certificate of succession, which will constitute proof of the capacity of heir or legatee and of the powers of the executors of wills or third-party administrators.

ii  Key legislative or case law changes affecting succession

Under the Civil Code it is now possible for an individual who wishes to plan for the time he or she is no longer alive, to agree separately with one, several or all reserve heirs that the latter waive their right to challenge violations of their reserved portion. This opens the way for transfers of estate assets in excess of the free portion, to the extent of the rights that the relevant heir or heirs have waived. However, this can only be done by written deed under the strictest conditions of form, which notably involve the presence of two French notaries. Only those reserve heirs that are of age can enter into one of those agreements. This waiver is not a taxable event excepting a modest stamp duty.

In addition to the foregoing, it is also now permissible for a person who is planning ahead for his or her succession to delay the moment when the heir has access to his or her share in the estate, for instance when the heir is a minor or needs to finish his or her education.

This can be achieved by way of a special deed signed in the presence of a notary. This is known as a power of attorney with posthumous effect, which survives the death of the principal.

Under such a power of attorney, the principal can entrust to any person, including a legal entity, the management of certain designated assets for a limited duration (two or five
years, depending on the circumstances, renewable by court order. The power of attorney must be precise in the description of the agent’s powers and must designate the heir or heirs with respect to whom the document is written.

Another development in our law now makes it permissible for an individual, instead of transferring all or part of the future succession assets unconditionally, to make a lifetime gift or a bequest subject to the condition that:

\[ a \] the transferee on his or her death leave whatever remains of the gift or bequest to a named third party (residual gift or bequest);\(^2\) or

\[ b \] the transferee keeps the gift or bequest during his or her lifetime and leaves it to a named third party on his or her death (\textit{libéralité graduelle}).\(^3\)

The tax system applicable to gradual and residual gifts and bequests is quite complex but attractive.

\[ \text{iii \ Cross-border developments} \]

\[ \text{Transnational giving} \]

As regards international gifts, French domestic law provides for very limited flexibility in terms of permitting tax deductible gifts from a French tax resident to a foreign philanthropic body, except (rarely) when a treaty provides for more favourable rules or when the charity is situated in the European Union.\(^4\)

Concerning the Brexit vote, the tax treatment of the gifts made by EU donors to UK charities is yet to be confirmed.

\[ \text{IV \ WEALTH STRUCTURING & REGULATION} \]

\[ \text{i \ Commonly used vehicles for wealth structuring} \]

Vehicles appropriate for wealth structuring depend mainly on the jurisdiction of residence of the owner and on applicable tax treaty provisions, if any. French residents generally opt for direct detention of their assets or through a civil law company and are keen on life insurance products. Business assets are generally owned through corporations, frequently European corporations. Trusts and family foundations have been used by individuals and families in recent decades, but the new law against trusts introduced by the previous government has put a stop to that. This has generated huge difficulties for those families whose assets were structured on the basis of fiduciary relationships, even for those families that were established in common law high-tax jurisdictions.

The traditional vehicles used for planning in a French context are the following.

\[ \text{Civil companies} \]

France does not have partnerships properly speaking but civil companies (as well as other types of structures), which operate very much as partnerships. Civil companies are transparent for civil law purposes and semi-transparent for tax purposes.

\[ \text{2 \ Articles 1057 et seq.} \]

\[ \text{3 \ Articles 1048 et seq.} \]

\[ \text{4 \ C318/07 Hein Persche, 27 January 2009.} \]
By way of example, real estate may be held through a real estate investment company, commonly known as an SCI. The SCI share value can therefore be reduced by bona fide bank loans (but no longer by shareholder loans), provided such bank loans were taken out for the purpose of purchasing the property or with respect to structural work in the property.

Life insurance
Life insurance products provided they are EU-law compliant, offer a solution to reduce the scope of application of forced heirship rules. Indeed, under the Insurance Code, monies paid to a beneficiary on the occasion of the death of the owner of the policy are excluded from the succession of the deceased, which means in particular that they are not subject to forced heirship rules.

However, this freedom is subject to a rule of reason that was elaborated in case law, so that great prudence must be exercised if the sums invested as premiums in life insurance exceed the likely value of the free portion on the death of the policyholder.

ii Legal and tax treatment of commonly used vehicles
France does not have a trust law of its own. It signed, but did not ratify, the 1985 Hague Convention on the Recognition of Trusts; however, France, to a large extent, recognises foreign trusts under its own principles of private international law. Indeed, under such rules, a foreign trust should be recognised as a fact, subject to proper evidence being provided.

In addition, for several years, certain French laws have referred directly to trusts: Article 120(9), Article 123-bis and Article 990 D of the Tax Code.

French courts have also recognised foreign trusts as a specific legal concept that should be recognised as such. Since 2011, a trust is now fully transparent for tax purposes, notably wealth tax, gift tax and inheritance tax. As a result, owning French assets, especially French properties through a trust, requires filing of information with the French revenue on a yearly basis in regard to the fair market value of the property and the name of the ultimate beneficiary. Failing that, a 3 per cent tax is assessed on the fair market value of the underlying property and is payable each year. In some cases the trustee may have to pay penalties of 12.5 per cent of the trust assets. A national registry listing trusts involving residents of France or French assets is now in place and records the personal details of settlors, beneficiaries and trustees, as well as the annual value of the trust assets. How accessible it is to the public is debatable, but in any case, it is at the disposition of the French tax administration.

Life insurance
Life insurance provides protection against income tax while the funds remain invested, as well as significant income tax reductions when the owner of the policy decides to withdraw funds. Life insurance can also be used as a planning tool to reduce exposure to wealth tax.

Last, sums passing to an insurance beneficiary on the death of the owner are not subject to inheritance tax (except as regards premiums paid by the policyholder after his or her 70th birthday), but rather to a flat 20 per cent tax up to €700,000 and 31.25 per cent above that amount, assuming that the share received by each beneficiary exceeds €152,500. This rate applies irrespective of whether the policyholder is a French tax resident or not.
iii  Key aspects of regulation of service providers dealing with private wealth

**Anti-money laundering regime**

In France, subject to the following, all transactions suspected of involving money laundering or terrorist financing are reported to a ‘cell’ of the Ministries of Finance and Budget: the Intelligence Processing and Action Against Clandestine Financial Circuits cell, TRACFIN.

France has implemented the third EU Money Laundering Directive by way of an Ordinance dated 30 January 2009 and subsequent implementation decrees.

French lawyers do not report directly to TRACFIN. Rather they must declare any suspicions of money laundering to the president of the relevant bar. The president then passes on such declarations to TRACFIN, unless he or she considers the suspicions to be unfounded.

In addition, French lawyers are, to an extent, exempted from certain obligations under anti-money laundering laws when they act in the context of legal proceedings to defend a client or provide advice in the interest of the defence of a client, excepting naturally the case of advice that would place the lawyer in the position of an accomplice.

**EU Savings Tax Directive**

The Savings Tax Directive establishes a system of declaration of savings income paid to non-resident investors to facilitate taxation in the Member State where the beneficial owner resides. France opted for the systematic declaration approach.

On regulatory matters it is worth noting that beyond the modernisation of a number of bilateral treaties (e.g., with the United Kingdom, Luxembourg, Belgium and Switzerland), France has entered into a number of tax information exchange agreements (TIEAs), which, subject to some specifications, are in line with Article 26 of the OECD Model, notably with Andorra, Anguilla, the British Virgin Islands, Belize, Brunei, the Cayman Islands, the Cook Islands, Costa Rica, Dominica, Gibraltar, Guernsey, Liberia, Liechtenstein, the Isle of Man, Jersey, the Netherlands Antilles, San Marino and Uruguay.

**EU FATCA legislation**

New legislation similar to the US FATCA is in force in the EU territory and in France, submitting financial institutions to annual or occasional reporting obligations to the EU tax authorities regarding individuals owning, directly or indirectly, bank accounts or financial investments.

French internal rules also provide strict controls and substantial penalties for hidden bank accounts.

**V  CONCLUSIONS & OUTLOOK**

Due to the budget deficit, the future remains bleak. The past and present governments have increased existing tax rates, however, the future government may decrease them.

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5 In November 2013 the United States and France signed a bilateral agreement requiring French banks to report to the French government information about their US account holders. The government of France will forward that information to the IRS and in return the IRS will provide similar information to France about French account holders at US financial institutions.
I  INTRODUCTION

Private wealth and private client law in Germany is characterised by a high number of tax and legal regulations on the one hand and a high level of judicial review on the other. Not only the civil and finance courts, but also the state and federal constitutional courts ensure the consistent and proportionate application of German civil and tax law.

In recent decades, private wealth and family-owned enterprises have been growing. Accordingly, private wealth and private client law in Germany primarily deals with individuals living in Germany and German family-owned companies structuring assets in Germany and other jurisdictions.

II  TAX

i  Introduction

Unlimited tax liability in Germany is determined by the concept of residence for both income tax and inheritance and gift tax purposes. Residence is assessed using objective criteria. An individual is a German resident if he or she has either a permanent home or a habitual abode in Germany. The resident individual's worldwide income or assets are subject to income tax, as well as inheritance and gift tax. The concept of domicile, however, is not recognised by German law.

With regard to income tax, there is a progressive tax rate ranging from 14 to 45 per cent. Additionally, a solidarity surcharge of 5.5 per cent of the tax due is levied. This surcharge is intended to finance the German reunification of 1990. As mentioned, income tax is levied on the worldwide income of residents. Non-residents pay tax on income from German sources (e.g., income effectively connected with a permanent establishment in Germany, income from employment in Germany (including self-employment), income from German real estate or dividends and capital gains from German companies in cases of a substantial shareholding). Non-residents do not pay income tax on non-business interest income. Income from capital investments (e.g., dividends) is subject to withholding tax at a flat rate of 25 per cent plus the solidarity surcharge; a tax treaty may allow a partial refund.

Concerning inheritance and gift tax, each successor or donee (hereinafter both referred to as transferee) is liable for the tax on the value of the assets received, regardless of his or her personal wealth. The inheritance and gift tax rates range from 7 to 50 per cent, depending on the relationship between the deceased or donor (hereinafter both referred to as transferor)
and the transferee, and on the value of the assets received. Spouses and descendants pay inheritance and gift tax at a rate of 7 to 30 per cent. Spouses receive a personal allowance of €500,000 and a maintenance allowance of up to a maximum of €256,000. Children receive a personal allowance of €400,000 and an age-dependent maintenance allowance of up to €52,000; grandchildren receive a personal allowance of €200,000. Transfers between most other relatives are taxed at a rate of 15 to 43 per cent. Between unrelated persons, the applicable tax rate is 30 or 50 per cent (for a transfer of more than €6 million).

Unlimited tax liability is triggered if either the transferor or the transferee is resident in Germany, regardless of whether the assets received are effectively connected to Germany. If neither the transferor nor the transferee is resident, inheritance and gift tax is only due on certain assets situated in Germany (e.g., real estate and business property). The transfer of a German bank account between non-residents generally does not trigger inheritance or gift tax.

Besides income tax and inheritance and gift tax, only a few other taxes are relevant for private clients. A real estate transfer tax with different regional rates ranging from 3.5 to 6.5 per cent applies to the acquisition of real estate or a substantial shareholding (at least 95 per cent) in a company holding real estate. Furthermore, real estate tax is levied annually and is calculated on the basis of rates determined by the local authorities, and property values, which were last assessed in 1964 or 1935. Thus, real estate tax is still low in comparison to the property’s current market value. There are, however, plans to reform the real estate tax regime, possibly resulting in significant increases of the tax burden in the future. Wealth tax has not been levied in Germany since 1997.

ii Inheritance and Gift Tax Act

Since 1 July 2016, a new Inheritance and Gift Tax Act has been in force in Germany. The reform was necessary after the German Federal Constitutional Court held that the former Inheritance and Gift Tax Act was inconsistent with the constitutional principle of equality of taxation. Both the judgment and the subsequent reform triggered extensive political debate concerning the taxation of business assets. At the heart of the matter lies the question of if and how business assets should be exempt from taxation to prevent insolvency because of the tax burden carried on succession. In particular, the transferee might, for example, receive the shares of an enterprise, but no cash assets from which he or she could pay the inheritance tax.

Under the new law, exemptions of the Inheritance and Gift Tax Act for business assets are generally available as before. The transferee may choose between a basic relief and an optional relief. According to the basic relief, 85 per cent of the business assets do not form part of the tax base and the remaining 15 per cent only are taxed. If the taxpayer chooses the optional relief, 100 per cent of the business assets are not considered part of the tax base. The relief is, however, conditional upon the continuing operation of the business for a certain amount of time (retention period) and the preservation of jobs. The retention period amounts to five years for the basic relief and seven years for the optional relief. Regarding the preservation of jobs, depending on the relief model chosen and the number of employees, after the retention period, the total payroll has to amount to at least 250–700 per cent of the payroll before the transfer.

Furthermore, business assets can only benefit from the relief as far as they do not constitute so-called passive non-operating assets. Passive non-operating assets are, generally
speaking, leased real estate, minority shareholdings of 25 per cent or less, securities, certain movables like artworks, antique cars and yachts, and liquid funds if they exceed, after deduction of debt, 15 per cent of the business' total value.

The passive non-operating assets are fully taxable at the regular rate, as far as their value exceeds 10 per cent of the total business assets (the contamination clause). In extreme cases, if the passive non-operating assets equal 90 per cent or more of the value of the whole business, the remaining potentially tax-privileged assets of up to 10 per cent are excluded from all relief too in order to avoid any misuse. 'New passive non-operating assets' (i.e., those assets that were contributed to the business assets within a period of two years before the relevant transfer) are completely excluded from any form of relief.

In contrast to the old law, relief can no longer be claimed independently from the value of the business assets transferred. If the value of the assets exceeds €26 million, the transferee may choose between two relief models: an ablation model or an economic needs test. According to the ablation model, the extent of relief is reduced by 1 per cent for each €750,000 in company value exceeding €26 million. The result is, that there is no longer any relief for acquisitions of approximately €90 million. The economic needs test, on the other hand, focuses on the transferee as a person and examines his or her assets. Out of his or her entire non-exempt assets after the transfer, the transferee is required to spend up to 50 per cent for the taxes due on the transferred business assets. Only if the 50 per cent of assets are not sufficient will an exemption from inheritance tax be considered upon request. Finally, it is noteworthy that the reform introduced the possibility of an advance deduction for family companies whose articles of association contain clauses typical for such family companies. However, this is only applicable if the provisions in the articles of association were already incorporated two years before the relevant transfer and if they are not revoked for 20 years thereafter. Therefore, it is highly recommended that family companies examine their articles of association and incorporate the appropriate clauses, if they are not in place already.

iii Tax treatment of trusts

Trusts are generally not recognised in Germany (see Section IV.iii, infra). Trusts can, however, trigger inheritance and gift tax in several ways. The establishment of a trust by residents (see Section II.i, supra) or of a trust comprising assets located in Germany is considered to be a transfer of assets that is taxable in accordance with the Inheritance and Gift Tax Act. Distributions to beneficiaries during the trust period or on the trust's dissolution may trigger income tax and gift tax as well, if the beneficiary is a German resident or if German situs assets are distributed. The relationship between gift tax on the one hand and income tax on the other with regard to trust distributions has not yet been ultimately clarified by the courts.

In addition, corporate tax can be triggered if income is received by a foreign trust from German sources. The worldwide income of a foreign trust may be subject to corporate tax if the trust's management is in Germany and if certain other conditions are met; for example, if the effective management of a trust is vested with a trustee resident in Germany.

Undistributed income received by a foreign trust can be attributed to the settlor or the beneficiaries if they are German residents. In this case, it can be subject to the settlor's or the beneficiary's personal income tax.
CFC rules in Germany – Sections 7–14 of the Foreign Tax Act

Taxation in Germany generally cannot be avoided by establishing a foreign entity in a low-tax country. The German rules for the taxation of controlled foreign companies (CFCs) meanwhile have an extensive scope of application. The CFC rules are settled in Sections 7–14 of the Foreign Tax Act (AStG).

These CFC rules extend the unlimited tax liability of residents to certain undistributed income of foreign corporations. The income may be attributed to domestic shareholders. The additional taxation under the CFC rules generally requires a substantial shareholding of German residents of more than 50 per cent of the corporation's shares (in certain cases, 1 per cent may suffice). The foreign corporation has to be an intermediate company, which receives passive or tainted income instead of income from its own business activities. Passive income is defined negatively by a list of active income in Section 8 of the AStG. Cumulatively, this passive income has to be subject to low tax rates of less than 25 per cent. Income that meets both criteria is added to a resident individual's income, to the extent to which the individual holds shares in the corporation. The taxable person can choose whether the taxes paid on income received from an intermediate company in a foreign country will be deducted from the amount subject to the additional taxation in Germany or whether the foreign taxes shall be credited against the additional taxes levied in Germany. In most cases, the second alternative is advantageous for the taxable person.

A foreign corporation is not, however, supposed to be an intermediate company if, *inter alia*, its effective place of management or statutory seat is located in a Member State of the EU or the European Economic Area and if the corporation carries out substantial economic activities.

III SUCCESSION

i Wills

According to Section 2064 et seq. and 2229 et seq. of the German Civil Code, there are two valid forms of wills: the holographic and the public will. The holographic will has to be handwritten, dated and signed by the testator. The public will has to be signed before and certified by a notary public. Neither form of will requires a witness.

A testator can also enter into a contract of succession with another person or set up a joint will with his or her spouse or civil partner. A contract of succession must be signed before and certified by a notary public; a handwritten contract does not meet the formal requirements.

By making a will, an individual can choose his or her heirs and state what share each heir receives. Additionally, an individual can make a legacy; that is, a person can be empowered to make a claim against the heirs, without being an heir him or herself. This claim can be for an amount of money, a share of the deceased's estate, an item or anything else.

Wills made in a foreign jurisdiction can be valid in Germany. Germany recognises the HCCH Convention on the Conflicts of Laws Relating to the Form of Testamentary Dispositions 1961. A will is valid if it complies with the law of the state where the testator made the will, the state of the testator's nationality or residence, or – in the case of real estate – the location of the assets. Foreign grants and probates are not recognised. An heir must ask the competent probate court to issue a German certificate of inheritance.
ii Intestacy and forced heirship regime

If an individual dies intestate, intestacy rules apply. Under the intestacy rules, the deceased’s estate is distributed among his or her relatives and spouse or civil partner in accordance with a strict order of succession. Children and their descendants constitute the first category, followed by parents and their descendants, grandparents and their descendants, and great-grandparents and their descendants. Relatives within a particular category inherit in equal shares (succession per stirpes). Where German law applies, the surviving spouse or civil partner also has a right of inheritance, determined by the matrimonial regime. Within a community of accrued gains, the surviving spouse or civil partner gets at least 50 per cent of the estate. If the deceased and his or her spouse or civil partner chose separation of property or community of property as their matrimonial regime, the surviving spouse or civil partner receives at least 25 per cent of the inheritance.

There is a forced heirship regime under which the descendants, the spouse or civil partner and the parents of the deceased are entitled to make a claim for a compulsory share of the deceased’s estate, if they are excluded from the testator’s will or if the share granted to them is less than their compulsory share. A relative’s compulsory share generally amounts to 50 per cent of the value of that relative’s hypothetical share on intestacy. It is a monetary claim and not a claim for a share of the estate. The compulsory share comprises all assets governed by German succession law (regardless of the beneficiary’s residence). Therefore, the forced heirship regime can be avoided by acquiring assets that are situated abroad and that German succession law does not govern. The forced heir can renounce his or her right to his or her compulsory share during the testator’s lifetime by signing a contract with the testator before a notary public. If the testator has died, a forced heir can also refrain from claiming his or her compulsory share.

iii Conflict of laws rules

Under old conflict of laws rules in Germany, the applicable succession law was that of the deceased’s nationality. If the deceased was a foreign national, German succession law applied only if the law of the deceased’s nationality provided for a reference back to Germany (renvoi). This could be the case if the deceased was domiciled in Germany, if the deceased’s habitual abode was in Germany or if the deceased held property or assets in Germany on the date of his or her death.

For successions as of 17 August 2015, new conflict of laws rules apply because of the EU Succession Regulation. They are valid in all EU Member States except Denmark, Ireland and the United Kingdom. According to the Regulation, the deceased’s habitual abode at the time of his or her death instead of his or her nationality is relevant for the question of which succession law is applicable. If it is obvious that the deceased had a closer relationship to another state, that state’s law will apply under certain circumstances. There is, however, the opportunity to opt for the succession law of an individual’s nationality through a will, a joint will or by conclusion of an agreement regarding succession.

In addition, provisions on legal jurisdiction, recognition and enforcement of decisions and authentic instruments and on the European Certificate of Succession are part of the Regulation. As a general rule, the jurisdiction will be determined by the habitual abode at the time of the individual’s death.
IV WEALTH STRUCTURING & REGULATION

i Commonly used structures: corporations and partnerships

Two structures are commonly used in Germany to hold assets: corporations and partnerships.

A corporation is subject to German corporate tax on its worldwide income if its effective place of management or statutory seat is located in Germany. The corporate tax amounts to 15 per cent plus the solidarity surcharge (see Section II.i, supra). In addition to corporate tax, a trade tax is also levied. The trade tax due depends on the rates determined by the local authorities. A participation exemption may apply, however, for dividends and capital gains. Profits distributed to shareholders of the corporation are subject to withholding tax at a flat rate of 25 per cent plus the solidarity surcharge.

A foreign corporation with income from German sources might be subject to German corporate tax. If a foreign corporation has a branch in Germany that constitutes a permanent establishment, the corporation will be subject to German corporate tax and trade tax on all income effectively connected to this permanent establishment.

Partnerships are fiscally transparent in Germany for income tax purposes. The partners are subject to income tax at their individual tax rates plus the solidarity surcharge. If the partnership is engaged in trade or business, the partnership itself is subject to trade tax. Trade tax levied from the partnership is (to a large extent) credited against the income tax of the partners if they are individuals.

ii Foundations

Foundations in Germany can be established either as charitable foundations or as family foundations. Charitable foundations are tax-privileged. Recognition as a charitable foundation requires that the foundation’s activities are dedicated to the altruistic advancement of the general public in material, spiritual or moral respects. These purposes must be pursued altruistically, exclusively and directly. A charitable foundation may, however, use one-third of its income for the maintenance of the founder and his or her family. The formation of a charitable foundation neither triggers any inheritance or gift tax, nor real estate transfer tax if real property is transferred gratuitously to the foundation. A charitable foundation is released from almost every current form of taxation, especially corporate tax and trade tax.

In contrast, a family foundation is not tax-privileged. It is conducted for the personal benefit and the advancement of one or more families. The formation of a family foundation and later donations to the foundation generally trigger inheritance and gift tax. The current taxation of a family foundation generally complies with the taxation of other legal persons. A family foundation can, however, receive income not only from trade or business but any type of income. In addition, only family foundations are liable for a substitute inheritance tax. This special tax accrues every 30 years. Moreover, distributions to beneficiaries are subject to income tax. The liquidation of a family foundation leads to an acquisition of assets on the level of the beneficiaries. This acquisition is treated as a lifetime gift. Therefore, it is subject to gift tax. Income tax may be triggered as well. The classification of the tax bracket depends on the relationship between the founder and the beneficiary.

In contrast to German family foundations, foreign family foundations are not liable to pay substitute inheritance tax. However, the undistributed income of a foreign family foundation may be attributed to the personal income of the founder or the beneficiaries if they are resident for tax purposes in Germany. This does not apply to family foundations that have their seat in a Member State of the EU or the European Economic Area, if the
foundation’s assets are legally and effectively separated from the beneficiaries’ property and that a treaty regarding mutual administrative assistance exists between Germany and the state in which the foundation has its seat. These conditions have to be satisfied cumulatively.

iii  Trusts

Neither domestic nor foreign trusts are recognised in Germany. Germany does not have its own trust law. Germany did not ratify the HCCH Convention on the Law applicable to Trusts and on their Recognition 1985. Therefore, German property law does not recognise the transfer of assets located in Germany to a trust. In these circumstances, the terms of a trust are interpreted in accordance with German law for civil law and tax purposes.

Where assets governed by foreign property law have been transferred to an irrevocable trust effectively formed under foreign trust law, the trust can shelter these assets from the settlor’s or beneficiary’s creditors. German courts generally do not recognise claims against trust assets on the dissolution of a marriage or partnership after 10 years from the date of the transfer.

Foreign trusts are disadvantaged in terms of tax issues when they are established or when distributions to beneficiaries are made (see Section II.iii, supra).

V  CONCLUSIONS & OUTLOOK

The German legal and tax system offers some flexibility for private wealth and estate planning. If structured appropriately, the taxpayer can take advantage of certain relief mechanisms for the succession in family-owned businesses. In particular, flexibility was gained when the EU Succession Regulation came into effect.

Usually, corporations and partnerships are used to structure assets and transfer them to the next generation. Family foundations and charitable foundations may be considered an alternative instrument in estate planning from time to time. Trusts, however, are not recognised in Germany. In comparison with corporations and foundations, they are disadvantaged if beneficiaries of a foreign trust have their permanent home or their habitual abode in Germany.
I INTRODUCTION

Gibraltar is a self-governing, economically diversified and multicultural British Overseas Territory that joined the European Union (subject to a number of important derogations) with the UK in 1973. It voted in the Brexit referendum of 2016 (strongly favouring the remain option). Gibraltar will be included in the negotiating process seeking to define the UK and Gibraltar’s new relationship with the EU.

The Gibraltarians are British nationals, bilingual in English and Spanish and fiercely loyal to the British Crown. Elections to Gibraltar’s parliament take place every four years and deliver a ‘government’ and an ‘opposition’ in the style of Westminster.

Gibraltar has historically enjoyed the trading and commercial opportunities that derive from its strategic location at the entrance of the Mediterranean and unique status. While Gibraltar is a small jurisdiction, it boasts a diversified trading, tourist, shipping, e-commerce and financial services economy. Given Gibraltar’s access to the EU single market, its policy priority in financial services has been to develop as an onshore centre. There has, therefore, been an increasing focus on substance and regulatory accountability. This is reflected in the corporate and private wealth management arrangements established for international clients.

Gibraltar attracts wealthy individuals for both private client services and residence, given its lifestyle and taxation offering. It is extensively used as a tax-neutral platform for the planning, structuring and preservation of private wealth and is home to a number of important family offices.

Gibraltar operates a territoriality-based tax system. Income tax is charged on income that accrues in or derives from Gibraltar. The Income Tax Act 2010 (the 2010 Act) was designed to introduce a competitive, internationally compliant tax regime. It provides for corporate taxes on profits at 10 per cent.

Gibraltar has no wealth taxes or any taxes on capital gains, inheritance or gifts. Gibraltar does not levy VAT and is exempt from the provisions of the Customs Union. This has provided a number of interesting planning opportunities. It represents a real advantage to companies based in Gibraltar that can access services externally without incurring a liability to VAT.

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1 Peter Montegriffo QC is a senior partner at Hassans International Law Firm. The author would like to thank Louise Lugaro for her assistance with the writing of this chapter.
II TAX

i Introduction

The basis on which tax is determined is whether income accrues in, or is derived from Gibraltar, regardless of the residence of the recipient.

The test for determining whether income accrues in, or is derived from Gibraltar follows the established jurisprudence set out in various leading UK Privy Council decisions (binding in Gibraltar in the absence of any Gibraltar cases) and related authorities.2 Regard must, therefore, be had to the whole of the activities undertaken, where these take place and which activities give rise to the income in question.

Section 74 of the 2010 Act makes clear, however, that in the case of businesses that undertake licensed and regulated activities in Gibraltar, the profits from these activities accrue in or are derived from Gibraltar (provided they are not generated by a branch or permanent establishment outside Gibraltar).

The tax year runs from 1 July to 30 June, and tax is payable on the actual taxable profits for the year.

Given Gibraltar’s very competitive corporate tax rate and the fact that various significant income streams are exempt from tax (e.g., passive investment income) many international operators regard the 10 per cent rate as an entirely reasonable regime. This is complemented by the absence of any capital gains tax or stamp duty (except in the case of Gibraltar real estate).

There is no charge to tax on the receipt by a Gibraltar company of dividends from any other company, regardless of where it is incorporated.

There is no tax on dividends paid by a Gibraltar company to another company and no tax (or withholding) on a dividend to any person not resident in Gibraltar.

Royalties received or receivable by a company in Gibraltar are chargeable to tax (at the usual corporate rate of 10 per cent).

ii Individual taxation

An individual (not company or trust) who is a tax resident as defined in the 2010 Act is also liable to pay tax on a worldwide basis in respect of the taxable heads of income.

There are certain incentives, however, designed to attract high net worth individuals and executives possessing particular skills. These make Gibraltar a very attractive base for suitably qualified individuals and their dependants or for retirees or entrepreneurs wishing to live in a tax competitive jurisdiction.

Generally with regard to residence, it should be noted that the 2010 Act provides that an individual is ordinarily resident in Gibraltar if:

a he or she is present in Gibraltar during any year of assessment for at least 183 days; and

b when considering three consecutive years of assessment, an individual has been present in Gibraltar for more than 300 days over that three-year period.

Any presence in Gibraltar in any 24-hour period commencing at midnight shall be counted as a day, irrespective of whether accommodation in Gibraltar is used or not.

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The 2010 Act provides two main systems that individual taxpayers are able to choose between so as to ensure a lower tax payment. These are described respectively as the ‘allowance-based system’ and the ‘gross income-based system’.

**Allowance-based system**

This allows an individual taxpayer to claim a large number of allowances and deductions against his or her chargeable income. These allowances include personal, spouses and civil partners allowances (£3,300 each), nursery and blind persons allowances (maximum of £5,160) and in respect of one child an allowance (£1,135) and for each child studying abroad (£1,290). Medical insurance premium payments (£5,155) and a one-off residential property purchase allowance (£12,000) are also allowed. Mortgage interest relief to acquire Gibraltar property to be used as a taxpayer’s principal residence is available on loans up to a value of £350,000.

The tax rates applicable to the allowance-based system are as follows:

<table>
<thead>
<tr>
<th>Taxable income bands</th>
<th>Rate (%)</th>
</tr>
</thead>
<tbody>
<tr>
<td>£0–£4,000</td>
<td>14</td>
</tr>
<tr>
<td>£4,001–£16,000</td>
<td>17</td>
</tr>
<tr>
<td>£16,001–</td>
<td>39</td>
</tr>
</tbody>
</table>

**Gross income-based system**

This system allows for a much smaller number of deductions or allowances but applies reduced rates of tax on gross income as follows:

<table>
<thead>
<tr>
<th>Taxable income bands</th>
<th>Rate (%)</th>
</tr>
</thead>
<tbody>
<tr>
<td>£0–£17,000</td>
<td>16</td>
</tr>
<tr>
<td>£17,001–£25,000</td>
<td>19</td>
</tr>
<tr>
<td>£25,001–£40,000</td>
<td>25</td>
</tr>
<tr>
<td>£40,001–£105,000</td>
<td>28</td>
</tr>
<tr>
<td>£105,001–£500,000</td>
<td>25</td>
</tr>
<tr>
<td>£500,001–£700,000</td>
<td>18</td>
</tr>
<tr>
<td>£700,001–</td>
<td>5</td>
</tr>
</tbody>
</table>

The gross income-based system is generally regarded as the most simple and beneficial for taxpayers. It is usually the case that this assessment will deliver the lowest level of income tax.

**iii Property rental scheme**

This new measure was introduced in the 2016 Budget. This provides that the owner of any property constructed in the 30 months following 1 July 2016, that is then rented for residential purposes, will receive a tax credit equal to the tax payable on the profits earned on the first 24 months’ rent occurring in the first five years after the completion of the construction of that property. The tax credit will not be refundable and may be set off against tax payable to extinguish any liability to tax.
iv Developments related to personal taxation for individuals generally and in relation to gift and succession taxes

One current feature of the tax system worthy of note is the regressive rates (under the gross income based system) in respect of higher incomes. Recent budget measures further enhanced this aspect providing that taxable income over £700,000 is subject to tax at 5 per cent (see table above). These measures are, of course, quite separate to the Category 2 or HEPSS schemes (described below) and are applicable to all taxpayers.

Gibraltar does not levy any gift, succession or inheritance taxes. It does not have any capital gains or wealth taxes. There is also no stamp duty in respect of share transfers, other than on Gibraltar real estate transactions and nominal (£10) capital duty on incorporation of a company.

There is no tax on passive investment income (including bank interest or dividends from quoted securities or funds invested in these).

Gibraltar does charge tax on intergroup corporate interest (subject, however, to a de minimis threshold of £100,000 per year interest) in respect of any such group lending.

As noted previously, there is no VAT.

v Issues relating to cross-border structuring

The two main issues impacting on the nature of private client and corporate cross-border structuring are the inexorable drive towards (perhaps complete) transparency and the international agendas designed to eliminate taxation arbitrage which is regarded as overly aggressive.

We are also witnessing heightened levels of vigilance and scrutiny from certain European domestic tax authorities (e.g., Spain and Portugal), which are driving clients to reconsider their residence, family office and private holding structures. Gibraltar has been the beneficiary of some of these developments by providing a safe and convenient alternative. As described below in Section II.vi these developments have increased the interest and use of Gibraltar as a residential base and wealth planning platform. It is not uncommon for new Gibraltar residents who rent or have bought property in Gibraltar to spend some time in Spain or Portugal (a perfectly workable arrangement provided they are careful not to spend more than 183 days a year in Spain or Portugal and they do not have their centre of economic and family interests based in those jurisdictions). The recent Brexit vote has also increased the number of queries from British expatriates settled in the Iberian peninsular. Gibraltar is regarded as a potential and close-at-hand alternative if the outcome of Brexit negotiations makes it more difficult to reside in either Spain or Portugal.

More broadly, Gibraltar’s EU passporting rights allowing for cross-border services has redefined the banking sector locally and remains very relevant across the financial services and e-commerce industries. The future shape and scope of the private banking sector locally continues to be a critical issue in common with the concerns in other banking centres and following the Brexit vote. Increased regulatory, compliance and governance costs challenge the business models of some existing operations. These pressures are unlikely to wane and may, therefore, bring about further realignment or consolidation.

Gibraltar has adopted the EU Savings Directive, the Mutual Assistance Directive and the Mutual Legal Assistance Convention. It has also entered into an extensive network of tax information exchange agreements. There are now 27 bilateral tax information exchange agreements with various countries, including the United States, the United Kingdom, France,
Germany and most other European territories. The effect of Gibraltar’s adoption of various international conventions and directives is that exchange arrangements extend to a very large number of countries, including Spain.

Gibraltar has transposed the EU Directive 2014/107/EU on automatic exchange of information with all Member States of the EU via the introduction of regulations. These Regulations implement the EU Common Reporting Standard (CRS) into Gibraltar law.

On the 26 June 2017 the new Register of Ultimate Beneficial Owners Regulations came into operation. These Regulations create a central register of beneficial owners. By doing so, Gibraltar aims to improve tax transparency within the jurisdiction.

Gibraltar is an excellent location for the headquartering of corporate activities. The combination of robust regulatory and governance regimes and competitive taxation work well to deliver a strong environment. The majority of the work being attracted to Gibraltar currently involves the establishment of a bricks and mortar presence. The fact that Gibraltar is not an island (but is physically connected to southern Spain) assists significantly in giving this process real traction. It effectively permits Gibraltar to act as an economic engine for the area (putting to use the surrounding area as a residential and facilities base). This commercial relationship has an almost unlimited potential for further growth for the benefit of both Gibraltar and the surrounding region.³

The OECD Base Erosion and Profit Shifting agenda and the related EU initiatives will continue to push cross-border corporate structures towards greater transparency and substance. The focus on ensuring no ‘double non-taxation’ and on the challenges posed by the digital economy are particularly significant. Gibraltar’s approach is to view these developments as an opportunity for a greater physical presence and more demonstrable control, management and regulatory accountability. This will affect various aspects of international families’ businesses and administration arrangements. In particular, the location, function and operation of family offices will require renewed consideration.

vi

Regulatory issues and special arrangements relating to high net worth individuals or specialist skills

**High net worth Category 2 individuals**

The Qualifying (Category 2) Individuals Rules 2004 provide for a well-established regime that limits income tax for high net worth individuals wishing to reside in Gibraltar.

The Category 2 programme has enjoyed great success since it was first introduced in the early 1990s. In order to apply for a certificate, an individual is required to verify that he or she has a minimum net worth of £2 million (usually in bank deposits or securities) and is of good character. The holder of a Category 2 certificate is taxed in Gibraltar on the basis of the normal rates applicable under the gross income-based system but only on the first £80,000 of assessable income. There is, however, a minimum annual tax payment of £22,000. Any income in excess of £80,000 is not subject to income tax in Gibraltar (irrespective of whether the income is remitted locally or otherwise). This effectively gives rise to a maximum tax liability in the order of £28,000, irrespective of worldwide income (at current 2016 rates).

³ See Gibraltar Chamber of Commerce commissioned report entitled ‘An Economic Impact Study and Analysis of the Economies of Gibraltar and the Campo de Gibraltar – update 2015’. Among its findings the report highlights that the number of jobs supported by the Gibraltar economy (i.e., within Gibraltar) is equivalent to one-quarter of the total jobs in the Campo surrounding area.
The benefits of a Category 2 certificate (which is a lifetime status subject to the eligibility criteria being satisfied on an ongoing basis) can extend to the worldwide income of a spouse or civil partner and of dependent children (up to 18 years or end of higher education).

A Category 2 individual is required to either rent or buy appropriate accommodation in Gibraltar for his or her exclusive use.

It should be noted that the general principle is that Category 2 individuals should not seek mainstream employment in Gibraltar or carry out business in competition with ordinary taxpayers. This principle holds whether the individual is carrying out business personally or via a legal entity such as a company.

Thus, it follows that a Category 2 individual should not derive ‘earned’ income from activities in Gibraltar unless it can be proved, to the satisfaction of the Ministry of Finance, that there is exceptional economic benefit for Gibraltar, which, in the opinion of the Ministry of Finance, warrants a departure from the general principle. In practice, this latitude has developed to encompass what is currently a wide spectrum of activities.

There are, therefore, various examples of economic activity that a Category 2 individual can undertake in Gibraltar. These are in accordance with published guidelines and include the following:

- owning a Gibraltar company for investment purposes in, (e.g., bank deposits, equities and bonds);
- owning a Gibraltar company to invest and trade in properties throughout the world;
- owning a Gibraltar company for trading in goods outside Gibraltar;
- doing any of the above from a physical office set up in Gibraltar;
- receiving director’s remuneration as well as dividends in respect of any of the above;
- being only a shareholder in a company carrying out activities licensable in Gibraltar under applicable financial services or gambling legislation;
- being only a shareholder in a company carrying out a business in Gibraltar that is not in competition with other businesses in Gibraltar;
- investing, either personally or through a company or another entity, directly or indirectly, in the purchase of property situate in Gibraltar for investment purposes. However, the rental income arising from any such properties is taxable in Gibraltar either on the company or the individual and therefore does not form part of the individual's tax shelter deriving from his or her Category 2 status;
- providing consultancy services to non-Gibraltar companies or receiving employment income from companies outside Gibraltar, as long as those services or employment are physically carried out exclusively outside of Gibraltar; and
- from within Gibraltar providing consultancy services to companies or other entities trading outside Gibraltar if that individual owns and controls or is connected by a significant shareholding or ownership interest in such company or entity. ‘Consultancy’ in this paragraph means consultancy to a company or entity itself and not the provision of advice or services to a client of that company or entity.

The profile of Category 2 residents has changed considerably over the last 25 years. Category 2 certificate holders now tend to become longer term residents contributing to, and engaging socially, economically and often philanthropically, with Gibraltar. This has meant real estate of increasing quality has become more readily available locally, with a marked improvement
in the entertainment, restaurant and cultural scene. The policy direction is to encourage further residence by such entrepreneurs and high net worth individuals and to underpin this drive with increased investment in Gibraltar’s infrastructure.

**Entrepreneurs and individuals with specialist skills – HEPSS**

Gibraltar is keen to continue to attract individuals who bring special skills not available locally. The Higher Executives Possessing Specialist Skills (HEPSS) Rules 2008 provide a favourable tax regime for individuals who possess particular skills in key positions in a business established locally.

The basic requirements in respect of such applicants are the following:

- Basic salary of over £120,000 per year;
- The skills must not be available in Gibraltar;
- Exclusive accommodation must be arranged in Gibraltar (either rented or purchased);
- He or she cannot have been resident in Gibraltar within the past 36 months.

A person in possession of a HEPSS certificate is only taxed (on the basis of the gross income-based system) on the first £120,000 of assessable income (including any bonuses, prerequisites and other benefits in kind connected with employment). As at 2016, rates this would result in a maximum tax payment of around £30,000 per annum.

There are also various additional allowances (e.g., relocation provisions) to facilitate the attraction of specialist skills.

This HEPSS programme has played an important role diversifying and widening the skills base of the Gibraltar economy. HEPSS status has been particularly relevant in the remote gambling and financial services sectors. The creation of a critical mass of specialists in particular areas (e.g., e-commerce and IT) has generated the growth of peripheral activities (ranging from services to family offices to payment-processing operations).

### III  SUCCESSION

#### i  Introduction

As is the position in the United Kingdom, the basic principle of succession law in Gibraltar is freedom of testamentary disposition. There are no forced heirship rules applicable and we have not adopted the EU succession and wills regulation.

There are, however, rights for spouses and civil partners and certain dependants to make certain claims on the estate of an individual under the Inheritance (Provision for Family and Dependants) Act 1977 (largely based on the UK 1975 Act).

Probate and administration of estates in Gibraltar is generally similar in procedure to that of England and Wales. Because of the nature of Gibraltar’s international client base, the jurisdiction is very familiar with cross-border succession and probate matters. Practitioners regularly deal with international succession and planning.

#### ii  Key legislative or case law changes affecting succession

A significant development in succession and matrimonial arrangements relates to prenuptial agreements. Gibraltar has adopted legislation to allow for the recognition and enforceability of prenuptial arrangements in various circumstances. Amendments to the Matrimonial Causes
Act provide a framework for the entry into and enforcement of financial arrangements. The legislation allows for prenuptial agreements to regulate matters between spouses in respect of the following:

a. how, in the event of a breakdown of a marriage, all or any of the property or financial resources of either or both of the spouses at the time when the agreement is made, or at a later date and before divorce is to be dealt with; and

b. the maintenance of either of the spouses:
   • during the marriage;
   • after divorce; or
   • both during marriage and after divorce.

The position in respect of children and dependants is more qualified. Provision in a financial agreement relating to the maintenance of children is void unless approved by the court. Furthermore, there is a general provision that allows the court to revisit the terms of a prenuptial agreement if it is satisfied that, when the agreement came into effect, the circumstances of the party were such that, taking into account the terms and effect of the agreement, the party was unable to support himself or herself without an income or pension, allowance or benefit.

It is critical, therefore, that the parties are fully and independently advised to ensure the best prospects of validity. The need for independent legal advice for each spouse is a statutory requirement of enforceability.

It should be noted that a prenuptial financial agreement continues to be binding despite the death of one of the parties and operates in favour of and, is binding on, the legal representative of that party.

Another significant development has been the enactment of the Gibraltar Civil Partnership Act 2014 whereby Gibraltar introduced civil partnerships between same-sex couples. Such partnerships enjoy largely the same legal rights and responsibilities as married couples. This includes the entry into financial agreements (largely as applicable to marriages under the Matrimonial Causes Act) in respect of partners. There is currently a strong campaign underway seeking to extend marriage to same-sex couples. This is the subject of a public consultation process that will report to Parliament.

In Gibraltar the court has wide power and discretion to make financial orders in a case of a dissolution of either a marriage or civil partnership.

Recent legislative changes now also empower the court to allow for the sharing of a pension between spouses (including a state pension) upon divorce.

iii Relevant cross-border developments

Gibraltar has introduced a number of statutes that impact on arrangements relating to international families. Gibraltar has recently enacted:

a. the Trusts (Private International Law) Act 2015;

b. the Private Trust Companies Act 2015;

c. the Purpose Trusts Act 2015; and

d. amendments to the Perpetuities and Accumulations Act.

The Trusts (Private International Law) Act 2015 provides a new statutory framework for the disapplication of forced heirship rules and various other claims in defined circumstances connected to trusts. It should be noted that the legislation applies subject to the following:
a the Hague Trust Conventions;
b any EU regulation, EU directive or international convention by which Gibraltar is bound, or may become bound, which in relation to particular matters, contains rules as to jurisdiction or the recognition or enforcement of judgments; and
c Section 419A of the Insolvency Act 2011 (relating to asset protection trusts).

For the purposes of this Act, Gibraltar is regarded as a separate Member State in relation to the Member States of the EU or the EEA signatories to any of them.

Under Section 419A of the Insolvency Act 2011, provision is made for an increased degree of protection of assets transferred into trusts in certain defined circumstances. Assuming the appropriate conditions are met (in particular a settlor must not become insolvent as a result of a transfer), a disposition to a trust will not be voidable at the instance of, or upon application of, any creditor of the settlor. The trust requires registration and the transfer to the settlement must be supported by an affidavit of solvency provided by the settlor. Gibraltar’s asset protection trust legislation is generally regarded as being less aggressive than that of other jurisdictions but has nonetheless proved popular in structuring arrangements designed to deliver a higher level of creditor protection.

The Private Trusts Companies Act codifies and makes extended provisions for the use of private trust companies which have been common in Gibraltar. The Act provides for a voluntary form of registration of private companies (thus allowing, if thought desirable, the continued use of private companies on an unregistered basis).

The Act allows a private trust company to be used in respect of individuals connected to the settlor. These extend to:
a his or her spouse or civil partner; and
b the children and remoter issue of the settlor and his or her spouse or partner.

The Purpose Trusts Act introduces a regime for purpose trusts other than for charitable purposes.

The legislation follows the enactments in a number of other jurisdictions, providing for an enforcer and wide powers to make applications to the court by the enforcer, trustees, unless the trust document provides otherwise the settlor, or any person who upon application is declared by the court to have an interest in advancing the trusts purposes.

The Attorney General may also in certain limited default circumstances intervene and make an application to the court.

Amendments to the Perpetuities and Accumulations Act have extended the statutory perpetuity period to 250 years.

IV WEALTH STRUCTURING & REGULATION

i Commonly used vehicles for wealth structuring such as trusts, foundations or partnerships

As a common law jurisdiction, Gibraltar trusts are extensively used in succession and estate planning. These come in a variety of forms and are largely drafted along the lines of English settlements. Companies and partnership arrangements are also widely used. Gibraltar is planning shortly to introduce legislation to allow for foundations. Draft legislation has been prepared and is currently the subject of consultation.
Although there is no mandatory requirement (indeed, as in other jurisdictions the vast majority of trust arrangements remain confidential), Gibraltar law allows for the voluntary registration of trusts. The Registered Trusts Act 1999 provides for the registration of a certain minimum amount of information relating to a trust (name, identity of trustees and date of creation). Such a registration facility is often regarded as helpful to formally record, when appropriate, the creation of a trust (especially relevant for clients with a civil law background).

The Gibraltar Private Foundation Act 2017 introduced a new vehicle to Gibraltar’s offering. Foundations, which are commonly used in civil law jurisdictions, are now able to be established in Gibraltar. A foundation is an entity with separate legal personality that is able to hold and deal with property in its own name as absolute legal and beneficial owner, for the specific purposes that are detailed in the Foundation Charter. The purposes can be very wide, need not be charitable, and indeed can be ‘anything capable of fulfilment’ as long as they are not illegal, immoral or contrary to public policy. As long as the Foundation Charter permits, the purposes of the foundation can be amended, providing flexibility in the event of future changes of circumstances.

ii Legal and tax treatment of commonly used vehicles

Gibraltar law does not tax trusts settled by non-residents for exclusively non-resident beneficiaries except in the case of Gibraltar taxable source income. As previously noted, passive investment income (to include bank interest or dividends from quoted securities or funds invested in these) are not taxable in Gibraltar in any event.

A Category 2 individual, while being a resident in Gibraltar, is nonetheless regarded as non-resident for the purposes of the establishment of a Gibraltar trust.

Gibraltar resident beneficiaries pay tax upon a distribution of income to them. No income, however, will be deemed to be distributed to them until this occurs.

As noted earlier, Gibraltar companies are liable to pay tax at 10 per cent on the profits of income that accrues in or derives from Gibraltar. There is a limited exception in relation to utility companies that pay at a higher rate of 20 per cent (though telecommunications companies pay the lower 10 per cent tax on non-telecommunications income, e.g., data centres).

Partnerships (both general and limited) are regarded as see-through for tax purposes. It is, therefore, the constituent partners (individual or corporate) that are assessed for tax.

iii Applicable anti-money laundering regime and other key aspects of regulation of service providers dealing with private wealth

Gibraltar has adopted very strong anti-money laundering legislation, systems and administrative practices. The Proceeds of Crime Act 2015 brings together in a consolidated enactment previous obligations contained in a number of statutes. Gibraltar’s system derives from all applicable European Union legislation and is based largely on the standards and procedures in the United Kingdom.

Gibraltar’s legislation, systems and administrative practices have been independently tested and reviewed by the FATF, the IMF and others. They have found Gibraltar’s systems to be robust, effective and in accordance with best international standards.

Providers to the general public involved in company management and fiduciary services are required to be licensed and subject to regulation by the Financial Services Commission. Family office and private family holding management arrangements that do not provide services to third parties for profit do not come within the ambit of licensable activities.
V CONCLUSIONS & OUTLOOK

Gibraltar’s response to international developments relating to transparency, anti-money laundering requirements and aggressive tax planning has been to increasingly focus on substance.

The outcome of the Brexit vote will clearly require adjustments, both in the UK and Gibraltar, over the next few years. Indeed, there will be opportunities for Gibraltar (and the UK) to leverage the benefits of the less prescriptive regime that is likely to open up.

Naturally, OECD and EU tax-related agendas (e.g., base erosion and profit shifting) represent a major threat to some aspects of planning that advisers have historically promoted. They undoubtedly, however, also represent an opportunity for those jurisdictions committed to and operating to best international standards, first-tier regulation and with competitive tax and residence regimes.
INTRODUCTION

Greece remains a jurisdiction where medium and large businesses are owned and managed by Greek families who need advice on the structuring of the generational transfer of business. Furthermore, Greece attracts foreigners that relocate to Greece and require pre-immigration advice on the operation of the Greek forced heirship rules and the tax efficiency of existing ownership structures.

In addition, Greece attracts investments in real estate, by non-resident private clients, who need advice on the structuring of the acquisition, ownership and disposal of such investments. Furthermore, due to the beneficial tax regime of shipping companies operating under the L 27/1975, Greece attracts relevant activities. Lately, amendments have been introduced into the Greek tax legislation dealing with individuals’ wealth, such as provisions relating to controlled foreign companies (CFC) rules.

The new Income Tax Code (Law 4172/2013 (ITC)), effective from 1 January 2014, as recently amended, introduces a number of significant changes to the tax rules, including measures designated to combat tax avoidance and tax evasion. For instance, under the new ITC, any wealth increase deriving from an illegal, unjustified or unknown source or cause is considered as business profits subject to tax at 33 per cent.

In addition, the new Tax Procedures Code (Law 4174/2013 (TPC)), as recently amended, which is a separate piece of legislation, explicitly introduces a ‘general anti-avoidance provision’, as a measure to combat tax avoidance and tax evasion. In this frame, under Article 66 of the TPC, the meaning of acts of tax avoidance is broadened and the meaning of concealment of income is clarified.

Finally, in terms of ruling, from a tax perspective, wealth, income and succession planning, Greece may use an extensive double taxation treaty network (57 income tax treaties and five estate tax treaties).
II TAX

i Greek tax residence

Individuals who are tax residents of Greece are subject to Greek income tax on their worldwide income (Greek and foreign income) while a foreign tax credit is provided on foreign income declared in accordance with the OECD guidelines for the avoidance of double taxation. Non-Greek tax residents are subject to Greek income tax only for their income sourced in Greece. The Greek ITC provides an indicative list of income considered as arising in Greece (Greek-sourced income).

For income tax purposes, an individual is considered as a Greek tax resident, provided that he or she maintains in Greece his or her permanent or primary residence or habitual abode or the centre of his or her vital interests (i.e., personal or economic or social bonds) or he or she is a consular or diplomatic employee or public officer of similar status or a civil servant of Greek nationality and serving abroad.

Also, an individual residing in Greece continuously for a period of more than 183 days is considered as a Greek tax resident. This is not applicable in cases of an individual residing in Greece exclusively for tourism, medical, therapeutic or similar private purposes, if his or her residence does not exceed a period of 365 days, including short-term stays abroad. The above provision may not be applicable if a double taxation treaty (DTT) (ratified by law) exists, in which case DTT provides a different way of taxation from the tax residence of the other country – party of the DTT. It is mentioned that DTT, by its integration into Greek (domestic) law, has automatically acquired an increased legislative power over the domestic legislation, according to Article 28 of the Greek Constitution.

Greece has entered into DTTs with the following countries, providing beneficial income tax provisions compared to internal income tax legislation: San Marino, Azerbaijan, Egypt, Albania, Armenia, Austria, Belgium, Bosnia-Herzegovina, Bulgaria, France, Germany, Georgia, Denmark, Switzerland, Estonia, United Arab Emirates, United States, United Kingdom, India, Ireland, Iceland, Spain, Israel, Italy, Canada, Qatar, Netherlands, China, Korea, Kuwait, Croatia, Cyprus, Latvia, Lithuania, Luxembourg, Morocco, Mexico, Malta, Moldavia, South Africa, Norway, Hungary, Uzbekistan, Ukraine, Poland, Portugal, Romania, Russia, Saudi Arabia, Serbia, Slovakia, Slovenia, Sweden, Turkey, Czech Republic, Tunisia and Finland.

ii Income tax

The following four categories of income are subject to income tax under the current ITC:

a income derived from employment and pension;
b income derived from business activities;
c capital income; and
d capital gains income.

Different tax rates apply to the above categories for individuals. The applicable tax rates are either progressive or tax exhaustive (one-off tax). The above-mentioned types of income are taxed as follows.

Income derived from employment or pensions

Income derived from employment or pensions is considered to be the gross income from salaried work and pensions, and includes all types of income, in cash or kind acquired, in
the context of any current, past or future employment relationship. In addition, the ITC explicitly provides that the board of directors’ fees are categorised as employment income for tax purposes.

Apart from the general provision for the taxation of salaries, the ITC contains provisions for the taxation of specific benefits in kind annually exceeding €300 that are considered as taxable income derived from employment for the employee and are added to the gross income from salaried work and pensions. Benefits in kind indicatively include the following:

- **a** the value of goods represented by gift cheques;
- **b** the value of vouchers given free of charge to purchase goods or services at associated stores. In the case of food vouchers, the benefit in kind is assumed to be any amount exceeding €6 per working day;
- **c** use of company credit cards to cover expenses not incurred on behalf of the company, but to cover personal, family or other expenses unrelated to the business interests of the employer or not used in normal commercial transactions, where the cost is assumed by the employer;
- **d** the benefit accruing to employees, managers, administrators, board members and pensions or companies providing energy, telephony, water supplies, gas, subscriber services (such as television) from providing them with a certain quantity of electricity, phone calls, water, natural gas and subscriber channels, at either a reduced rate or free of charge;
- **e** various payments made directly by employers to third parties such as payments to extra tuition centres, schools, kindergartens, campsites, etc., to cover tuition costs, kindergarten fees, etc., direct payments to cover the cost of such persons participating in workshops, programmes or training, education training courses, or to cover subscriptions to journals or chambers, unrelated to their business activities or the post they hold; and
- **f** the provision of company mobile phone connections to employees, managers and board members to the extent that it goes beyond the cost of their tariff plan, provided that the excess above the tariff plan is used for personal reasons and not for reasons associated with the employer’s business activities.

From 1 January 2016, income from employment or pensions is taxed according to the following progressive tax scale:

<table>
<thead>
<tr>
<th>Taxable income</th>
<th>Tax rate</th>
</tr>
</thead>
<tbody>
<tr>
<td>≤20,000</td>
<td>22%</td>
</tr>
<tr>
<td>20,001 to 30,000</td>
<td>29%</td>
</tr>
<tr>
<td>30,001 to 40,000</td>
<td>37%</td>
</tr>
<tr>
<td>≥40,001</td>
<td>45%</td>
</tr>
</tbody>
</table>

From 1 January 2020 onwards, income from employment or pensions will be taxed according to the following progressive tax scale:
Income derived from business activities

Individuals are subject to income tax on business income, which is defined as the total revenue from business transactions as well as from independent professions after the deduction of any business expenses, depreciations and bad debts. The business income is taxed according to the following tax scale:

<table>
<thead>
<tr>
<th>Taxable income</th>
<th>Tax rate</th>
</tr>
</thead>
<tbody>
<tr>
<td>≤20,000</td>
<td>22%</td>
</tr>
<tr>
<td>20,001 to 30,000</td>
<td>29%</td>
</tr>
<tr>
<td>30,001 to 40,000</td>
<td>37%</td>
</tr>
<tr>
<td>≥40,001</td>
<td>45%</td>
</tr>
</tbody>
</table>

Moreover, according to the ITC, any increase of wealth for an individual deriving from an illegal, unjustified or unknown source or cause is considered as income derived from business activities and is further subject to tax at 33 per cent.

Capital income

Capital income is a distinct category of income and includes the income, in cash or in kind, from dividends, interests, royalties and immovable property.

Income from dividends is defined as the income from shares, founders’ shares, or other rights of participation in profits that are not debts, as well as income from other corporate rights, including interim dividends and actuarial reserves, profits from partnerships and any other distributed amount.

Income from interest is defined as the income on any kind of claims, either secured by mortgage or not, whether providing a right to participate in profits of the debtor or not. Specifically, this includes income from deposits, government securities, bonds (with or without security) and from every kind of loan agreement, including premiums, repurchase agreements or reverse repurchase agreements and rewards derived from shares, partnerships, bonds or securities. There is a tax exemption regarding the income by the interest of bond loans and treasury bills of the Greek state, received by individuals, as well as to the interest arising from bonds issued by the European Financial Stability Facility in application of the programme for the restructuring of the Greek debt.

Income from royalties is defined as the income gained in exchange for the use or the right to use any kind of intellectual property rights.

Income from real estate property is defined as the income (in cash or in kind) derived from leasing (rental), self-use or the free concession of the use of land or real estate property. The income received in kind is calculated at the market value. In addition, the income for self-use or the free concession of use is equal to 3 per cent of the objective value of the property. A tax exemption is applied to the aforementioned presumptive income in the
case of the free concession of the use of the real estate property – which shall not exceed 200 square metres – to a relative in the ascending or the descending line, who will use it as his or her main residence.

The capital income earned by an individual is subject to withholding tax as follows:

a dividends distribution is subject to a withholding tax at the rate of 10 per cent, with effect for payments performed up to the tax year 2016 and 15 per cent for the tax year 2017 onwards, exhausting any further tax liability for individuals (final tax);

b interest payments are subject to a withholding tax rate of 15 per cent, exhausting any further tax liability for individuals (final tax); and

c royalties payments are subject to a withholding tax at the rate of 20 per cent, exhausting any further tax liability for individuals (final tax).

Income from immovable property sourced by the leasing (rental) or by the self-using (presumptive income) of the real estate property is subject to income tax in accordance with the following tax scale, which is applicable to income gained from 1 January 2016:

<table>
<thead>
<tr>
<th>Income</th>
<th>Tax rate</th>
</tr>
</thead>
<tbody>
<tr>
<td>&lt;12,000</td>
<td>15%</td>
</tr>
<tr>
<td>12,001 to 35,000</td>
<td>35%</td>
</tr>
<tr>
<td>≥35,001</td>
<td>45%</td>
</tr>
</tbody>
</table>

**Capital gains income**

Any surplus that arises from the transfer of capital (i.e., real estate property, securities, listed shares, sovereign bonds, interest-bearing bills, company bills or derivative financial products as described in the ITC) is considered income from capital gains and is subject to tax at a rate of 15 per cent. The taxable surplus is the difference between the purchase (acquisition) price and the transfer (selling) price. An exemption from the said tax is applied in special cases. For example, any capital gains derived from the transfer of securities by individuals could be exempted from capital gains tax if said individuals are tax residents of another state with which a DTT has been signed, and provided that all the necessary documentation is submitted to the relevant tax administration authority, evidencing the residence of the aforementioned individuals to these states.

Taxation on capital gains from the transfer of real estate property is postponed until 31 December 2017.

**iii Special income tax provisions provided by the ITC**

**Alternative method for determining minimum taxation (deemed income)**

The ITC provides an alternative method for calculating the minimum tax obligation of individuals according to certain objective criteria. If, after application of those objective criteria, the deemed income of the taxpayer is higher than the declared income, he or she will be taxed according to his or her deemed income.

Deemed income may derive either from ‘living expenses’ from assets owned or from ‘actual expenses’ from the amount spent to purchase assets and is calculated after taking into account the following objective criteria:

a the surface area of the main residence of the taxpayer in combination with its tax value;

b the surface area of any secondary residences of the taxpayer;
c the size of the engines (e.g., 1,200cc, 1,400cc) of any cars of the taxpayer, in combination with the year of the car’s production;
d salaries of housemaids and other staff;
e fees for private schools for the taxpayer’s children;
f leisure boats;
g aeroplanes; and
h swimming pools.

Purchases of cars, motorcycles, boats, aeroplanes and other goods that cost above €10,000, the establishment or the participation in the capital increase of a company under the form of an unlimited or limited liability partnership or corporation or limited liability company or private corporation or society of civil law or joint venture or purchase of company parts or securities are taken into account in the calculation of the taxpayer’s annual deemed income. The taxpayer can, under certain conditions, cover the difference between actually declared income and income that is deemed after the application of the above rules, by showing that the amount in excess of the declared income is justified by savings made from income taxed in previous years.

Deemed income provisions are not applicable in the case of a foreign tax resident who does not earn income from Greek sources.

Controlled foreign companies
Controlled Foreign Company (CFC) rules have recently been introduced in the ITC, with the aim of dealing with the tax avoidance of Greek companies or individuals, through shifting revenues to subsidiaries in low-tax jurisdictions.

It is specified that the taxable income of an individual Greek tax resident includes the non-distributed income of legal or other entities tax-resident in another state, provided that the following conditions are cumulatively met:
a the taxpayer, on his or her own or jointly with related persons, holds, directly or indirectly, shares, parts, participations, voting rights or participations in the capital at a percentage exceeding 50 per cent, or is entitled to receive a percentage exceeding 50 per cent of the profits of the said legal or other entity;
b the above legal or other entity is subject to taxation in a non-cooperative state or state with a preferential tax regime, namely to a special regime allowing for a substantially lower level of taxation than the general regime;
c a percentage exceeding 30 per cent of the net income before taxes realised by the legal entity or other entity falls under one or more of the following categories:
   • interest or any other income generated from financial assets;
   • royalties or any other income generated from intellectual property;
   • income derived from dividends and the transfer of shares;
   • income derived from moveable assets;
   • income derived from real estate property, unless the Member State of the taxpayer, legal entity or other entity would not be entitled to tax such income according to an agreement concluded with a third country; and
   • income derived from insurance, bank and other financial activities; and
d it is not a company with a principal category of shares that are traded in an organised market.
The above shall not apply to cases where the legal person or legal entity is a tax resident of a Member State of the European Union or a tax resident of a country that is a party to the EEA Agreement, unless the legal person or legal entity’s establishment or economic activities are an artificial arrangement devised for the purpose of avoiding the corresponding tax.

This income is taxed at the rates applicable to income derived from business activities, as they are provided above.

iv Solidarity tax contribution on individuals’ income from tax year 2016

As a result of economic crisis, a special solidarity tax contribution is imposed on individuals’ total income (both declared and deemed income) of any source that exceeds €12,000 on an annual basis. From 1 January 2020 onwards, a special solidarity tax contribution will be imposed on individuals’ total income of any source that exceeds €30,000 on an annual basis.

For income earned from 1 January 2016, a solidarity tax contribution is imposed in accordance with the progressive rates below:

<table>
<thead>
<tr>
<th>Income</th>
<th>Tax rate</th>
</tr>
</thead>
<tbody>
<tr>
<td>≤12,000</td>
<td>0%</td>
</tr>
<tr>
<td>12,001 to 20,000</td>
<td>2.2%</td>
</tr>
<tr>
<td>20,001 to 30,000</td>
<td>5%</td>
</tr>
<tr>
<td>30,001 to 40,000</td>
<td>6.5%</td>
</tr>
<tr>
<td>40,001 to 65,000</td>
<td>7.5%</td>
</tr>
<tr>
<td>65,001 to 220,000</td>
<td>9%</td>
</tr>
<tr>
<td>≥220,001</td>
<td>10%</td>
</tr>
</tbody>
</table>

For income earned from 1 January 2020, onwards, a solidarity tax contribution will be imposed in accordance with the progressive rates below:

<table>
<thead>
<tr>
<th>Income</th>
<th>Tax rate</th>
</tr>
</thead>
<tbody>
<tr>
<td>≤30,000</td>
<td>0%</td>
</tr>
<tr>
<td>30,001 to 40,000</td>
<td>2%</td>
</tr>
<tr>
<td>40,001 to 65,000</td>
<td>5%</td>
</tr>
<tr>
<td>65,001 to 220,000</td>
<td>9%</td>
</tr>
<tr>
<td>≥220,001</td>
<td>10%</td>
</tr>
</tbody>
</table>

In addition, as of 27 May 2016, salaries and wages are subject to withholding tax against solidarity tax contributions in accordance with the above rates.

v Luxury living tax

As a result of economic crisis, from the tax year 2014, a luxury living tax applies on individuals’ income, calculated on the amounts of the annual deemed expenditures arising from the ownership or holding of private passenger cars, aeroplanes, helicopters, yachts and swimming pools, as follows:

a for passenger cars from 1,929cc to 2,500cc a tax rate of 5 per cent is applied;
for passenger cars more than 2,500cc a tax rate of 13 per cent is applied (private passenger car with more than 10 years’ use since their first year in traffic are exempted from said tax); and

for aircrafts, helicopters, swimming pools and yachts more than 5 metres long, a tax rate of 13 per cent is applied.

vi Real estate tax

Real estate transfer tax

The rate of the real estate transfer tax is 3 per cent calculated on the value of the real estate property. For tax purposes, a system has been established for the objective calculation of the value (i.e., based on a system of minimum values). According to this system, if contracting parties declare a price lower than the objective price, the taxes are based on the objective price (higher price). Lately, the actual sale prices of real estate in Greece have been significantly reduced and have been much lower than the objective values. As a result, the paid tax on the objective values provided by Greek law is higher than the tax that would be calculated on the actual sale price according to the contract.

Annual real estate tax

Annual real estate tax (ENFIA) is imposed on real estate property rights including main and supplementary tax (for real estate over €200,000) and applies to real estate located in Greece that is owned by individuals and entities. ENFIA is payable on an annual basis. The tax payable depends on a number of factors.

Special tax real estate

A special tax applies on the value of real estate situated in Greece and owned by a company that has its registered seat at a non-cooperative state, as provided under Article 65 of ITC, at a tax rate of 15 per cent. However, if the company discloses all of its shareholders or ultimate beneficiaries (individuals) who hold a tax identification number in Greece, it is exempt from the special tax. Many other exemptions are also provided.

III SUCCESSION

i Applicable law

According to international private law, Regulation No. 650/2012 of the European Parliament and of the Council of 4 July 2012 ‘on jurisdiction, applicable law, recognition and enforcement of decisions and acceptance and enforcement of authentic instruments in matters of succession and on the creation of a European Certificate of Succession’, with effect from 17 August 2015, shall apply. The regulation applies to all civil aspects of the succession to the estates of deceased people. It does not apply to revenue (for example, tax matters), customs or administrative matters. Areas of civil law other than succession, such as matrimonial property regimes, gifts and pension plans are not covered by the regulation.

Regarding the general jurisdiction, the courts of the EU country in which the deceased had his or her habitual residence at the time of death shall have jurisdiction to rule on the succession as a whole. As a rule, the law applicable to succession is the law of the country in which the deceased had his or her habitual residence at the time of death. It can be the law of either an EU or non-EU country. However, before his or her death, a person can instead
choose that the applicable law should be the law of his or her country of nationality. For example, a person of multiple nationalities (including Greek) may choose that the applicable law shall be the Greek law. A declaration of this shall be made in the form of a disposition of property upon death (i.e., a will).

The applicable law will govern, for example, the determination of the beneficiaries and their respective shares, the capacity to inherit, the powers of the heirs, the executors of the wills and the administrators of the estate, the liability for the debts under the succession and the sharing out of the estate.

The application of a single law by a single authority to an international succession avoids parallel proceedings, with possibly conflicting judicial decisions. It also ensures that decisions given in an EU country are recognised throughout the EU without need for any special procedure. Decisions enforceable in the EU country where they have been given are enforceable in another EU country when, on the application of an interested party, they have been declared enforceable there by the local court.

The aforementioned regulation also introduces a European Certificate of Succession (ECS) to be used by heirs, legatees having direct rights in the succession and executors of wills or administrators of the estate to invoke their status or exercise their rights or powers in another EU country. Once issued, the ECS will be recognised in all EU countries without any special procedure being required. In contrast with national certificates of succession, which have different effects depending on the EU country of issue, the ECS will have the same effects, set out in the Regulation, in all EU countries.

**Forced heirship rules**

Greek succession law provides for forced heirship rules. The rules on forced heirship protect the closest relatives of the decedent, who may not disinherit them. Forced heirs are always entitled to a certain percentage of the estate (legitimate portion of the estate).

Forced heirs are the descendants of the deceased (children), the surviving spouse and the parents of the deceased. According to Greek inheritance law, forced heirs are entitled to half of the portion they are entitled to in the case of intestacy.

Under forced heirship rules, any disposal by will of the decedent’s estate to the prejudice of the forced heirs is void. Moreover, if the testator donates his or her estate and as a consequence the estate at death is not sufficient to cover the legitimate portions of estate for the forced heirs, then said donation may be cancelled.

**ii Taxation of inheritance and gifts inter vivos**

According to Article 1 of Law 2961/2001 (the Code on taxation of inheritance, gifts *inter vivos* and lottery gains), tax is imposed to any asset acquired by inheritance, gift *inter vivos* and winnings in lotteries, whether acquired by an individual or a corporate entity.

**Inheritance tax**

The legislator provides for a list of assets that are subject to inheritance tax. These are property of any kind situated in Greece that belongs to Greek citizens or foreigners, and moveable property situated abroad that belongs to a Greek resident or (under conditions) to a foreigner residing in Greece. Moveable property that is located abroad and belongs to a Greek citizen who was established outside Greece for at least 10 consecutive years is exempt from Greek inheritance tax.
**Gift tax**

The legislator provides for a list of assets that are subject to gift tax. These are:

- *a* any moveable or immoveable property situated in Greece;
- *b* any moveable property of a Greek citizen situated abroad; and
- *c* any moveable property of a foreign national situated abroad that is being gifted or donated to a Greek or foreign citizen who resides in Greece.

The categories of rates of inheritance and gift tax depend on the relationship of the taxpayers to the deceased or donor. Taxpayers are classed into three categories depending on their proximity to the deceased. Category A includes:

- *a* the spouse;
- *b* the partner who has a contract for co-habitation according to the provisions of Law 3719/2008, provided that the partnership was in existence at the time of death and it lasted at least two years;
- *c* children;
- *d* grandchildren; and
- *e* parents.

Category B includes:

- *a* great-grandchildren et seq.;
- *b* grandparents and great-grandparents;
- *c* voluntarily or judicially recognised children as against the parents of the father who recognised them;
- *d* the children of a recognised child as against the father who recognised them and his parents;
- *e* brothers and sisters;
- *f* collateral relatives of the third degree;
- *g* stepfathers and stepmothers;
- *h* children of the spouse from a previous marriage; and

Category C includes the remaining relatives and aliens.

The following table illustrates the inheritance tax rates, also applicable on gifts, for the three categories of individuals:

<table>
<thead>
<tr>
<th>Value in €</th>
<th>Tax rate</th>
<th>Tax</th>
<th>Total value</th>
<th>Total tax</th>
</tr>
</thead>
<tbody>
<tr>
<td>Category A</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>150,000</td>
<td>–</td>
<td>–</td>
<td>150,000</td>
<td>–</td>
</tr>
<tr>
<td>150,000</td>
<td>1%</td>
<td>1,500</td>
<td>300,000</td>
<td>1,500</td>
</tr>
<tr>
<td>300,000</td>
<td>5%</td>
<td>15,000</td>
<td>600,000</td>
<td>16,500</td>
</tr>
<tr>
<td>Above</td>
<td>10%</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Category B</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>30,000</td>
<td>–</td>
<td>–</td>
<td>30,000</td>
<td>–</td>
</tr>
<tr>
<td>70,000</td>
<td>5%</td>
<td>3,500</td>
<td>100,000</td>
<td>3,500</td>
</tr>
<tr>
<td>200,000</td>
<td>10%</td>
<td>20,000</td>
<td>300,000</td>
<td>23,500</td>
</tr>
<tr>
<td>Above</td>
<td>20%</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

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As an exception, by virtue of Law 3842/2010, monetary gifts *inter vivos* are taxed at a rate of 10 per cent when the gift is given to a relative of category A, 20 per cent for category B and 40 per cent for category C.

**Tax treaties for the avoidance of double inheritance taxation**

Individuals who are subject to Greek inheritance tax on their worldwide assets can benefit from the Greece inheritance tax treaties. Greece has entered into tax treaties for the avoidance of double taxation in inheritance and estate tax with Germany, Italy, Spain and the United States to prevent double taxation. Thus, individuals who are subject to Greek inheritance tax on their worldwide assets can benefit from the Greek inheritance and estate tax treaties.

**IV WEALTH STRUCTURING & REGULATION**

**i Trusts and foundations**

Trusts and foundations are commonly used vehicles for private wealth structuring and planning. Recently, Circular Pol. Nr. 1114/2017 was issued by the Independent Authority of Public Revenue, providing for interpretative general guidelines with respect to the tax treatment both of the foreign trusts and foundations and their distributed or undistributed income to Greek tax residents within the framework of Greek income and gift and inheritance taxation. Specifically, pursuant to Circular Pol. Nr. 1114/2017, the tax treatment depends on the time period within which the taxable events take place as follows.

**Taxable events as of 1 January 2014 onwards**

As of 1 January 2014, the ITC recognises trusts and foundations as taxable legal entities for corporate income tax purposes.

On individuals’ taxation level, any distribution of profits, acquired by the settlor under his or her capacity as beneficiary of the foreign trust or foundation, falls within the definition of dividends, being that considered as taxable income, and is subject to Greek income dividend tax of 10 per cent, with effect for payments performed up to the tax year 2016 and 15 per cent, for the tax year 2017 onwards (plus solidarity tax contribution).

In case the settlor or founder and the beneficiary of the trust or foundation is not the same person, the transfer of the trust’s assets to the beneficiary is treated as a gift or inheritance for tax purposes and is taxed according to the gift or inheritance tax scale that is applicable based on the relationship between the settlor or founder and the recipient of the assets.

Undistributed income that arises in the trust or foundation could be treated pursuant to the provisions of CFC rules referred to above, provided that all the conditions are cumulatively met.

In the case of the trust or foundation’s dissolution and liquidation, the distributed amounts that exceed the initial capital transferred to the trust or foundation are considered

---

<table>
<thead>
<tr>
<th>Value in €</th>
<th>Tax rate</th>
<th>Tax</th>
<th>Total value</th>
<th>Total tax</th>
</tr>
</thead>
<tbody>
<tr>
<td>6,000</td>
<td>–</td>
<td>–</td>
<td>6,000</td>
<td>–</td>
</tr>
<tr>
<td>66,000</td>
<td>20%</td>
<td>13,200</td>
<td>72,000</td>
<td>13,200</td>
</tr>
<tr>
<td>195,000</td>
<td>30%</td>
<td>58,500</td>
<td>267,000</td>
<td>71,700</td>
</tr>
<tr>
<td>Above</td>
<td>40%</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>
as dividends and are subject to Greek income dividend tax of 10 per cent, with effect for payments performed up to the tax year 2016, and 15 per cent, for the tax year 2017 onwards (plus solidarity tax contribution). There is no taxable event to the extent the distributed amounts do not exceed the initial capital since they are considered as capital repayment.

Finally, the transfer of assets into the trust or foundation upon its settlement is not considered a taxable event.

**Taxable events until 31 December 2013**

Greek Law 2238/1994, which was applicable on income taxation up to 31 December 2013, recognised only foundations as taxable legal entities for corporate income tax purposes.

On individuals’ taxation level, any distribution of profits, acquired by the settlor under his or her capacity as beneficiary of a foreign trust, is subject to income tax at the level of the settlor of the trust depending on the source of income (e.g., interest, dividends, capital gains), while, as per the distribution of profits from a foundation, acquired by the founder under his or her capacity as beneficiary of the foreign foundation, is subject to income tax according to the tax scale applicable on freelancers pursuant to Greek Law 2238/1994.

If the settlor or founder and the beneficiary of the trust or foundation is not the same person, the transfer of the trust or foundation's assets to the beneficiaries is treated as a gift or inheritance for tax purposes and is taxed according to the gift or inheritance tax scale that is applicable based on the relationship between the settler of the trust or foundation and the recipient of the assets.

The trust’s dissolution and liquidation is not considered a taxable event, while, in case of the foundation's dissolution and liquidation, the distributed amounts that exceed the initial capital transferred to the foundation are subject to income tax according to the tax scale applicable on freelancers pursuant to Greek Law 2238/1994. There is no taxable event to the extent the distributed amounts do not exceed the initial capital since they are considered as capital repayment.

Finally, the transfer of assets into the trust or foundation upon its settlement is not considered a taxable event.

**ii Shipping companies operating under Law 27/1975**

Because of the beneficial tax regime of shipping companies operating under the L 27/1975, Greece attracts Greek or foreign ship-owning companies with vessels flying a Greek flag and foreign ship-owning companies with vessels flying a foreign flag, if their management is exercised by Greek companies or foreign companies established in Greece (operating under a special regime of offshore companies), which are subject to tonnage tax.

The Greek tonnage tax regime applies to vessels of categories ‘A’ and ‘B’. Category ‘A’ vessels includes cargo vessels, tankers, steel hull vessels for dry or liquid cargo that ply to or between foreign ports, passenger vessels, drilling platforms, etc., while category ‘B’ vessels include small boats and any other motor vessels not listed under category ‘A’. The gross tonnage is calculated by multiplying coefficient rates by each scale of gross registered tonnage. This taxable tonnage is then multiplied by an age-corrected rate. A credit for the tonnage tax paid abroad is provided.

The shipowner is liable to pay the ship's tonnage tax, whether an individual or a legal entity, who is the registered owner of the relevant ship on the first day of each calendar year.
The person managing the ship and collecting the hire as well as the manager’s representative, subject to the latter having accepted the relevant appointment in writing, are also jointly and severally liable to pay the ship’s tonnage tax.

Various exemptions and reductions of the tonnage tax apply, such as vessels built in shipyards in Greece, under a Greek flag, are exempt from tax for the first six years. Also, a 50 per cent reduction for vessels operating regular routes between Greek and foreign ports or solely between foreign ports.

The payment of the tonnage tax exhausts all income tax liability of the shipowner with respect to income derived from the ship’s operation; the exhaustion of tax liability also applies to the shareholders or partners of a (Greek or foreign) shipping company. It also covers all capital gains arising out of the sale of the vessel, realised at the level of either the shipowner, shipping company or their shareholders. If a company that owns a Greek-flagged ship also has commercial activities other than the operation of the ship, exemption from income tax applies to the net profits that correspond pro rata to the gross income the owner derives from ships, subject to the tonnage tax regime.

In addition, the shareholders of the above-mentioned companies are exempt from any tax, duty, contribution or withholding, up to natural person, for the income acquired from dividends or distribution of net profits, whether such profits are acquired directly or through holding companies. Exemption from any taxation of the transfer of shares or parts of Greek or foreign shipowner companies, under Greek or foreign flags, regardless of the reason that the transfer applies. On the contrary, a 10 per cent withholding tax is applicable on dividend distributions, exhausting any further tax liability, to Greek tax residents by offices that are engaged in activities such as chartering, insurance, brokerage, etc, other than the management and exploitation of Greek or foreign-flagged ships.

According to Article 29 of Law 27/1975, exemption from inheritance tax applies with respect to transfers of vessels, stocks or shares of Greek or foreign companies that own vessels flying a Greek or foreign flag with gross tonnage of over 1,500 and of stocks or shares of holding companies that hold stocks or shares of shipping companies, whether directly or through holding companies.

Finally, an annual contribution, at a regressive tax scale of 5 to 3 per cent, referring to the years 2012–15, and at a regressive tax scale of 7 to 5 per cent, referring to the years 2016–19, is imposed on offices or branches of foreign enterprises that have been established in Greece by virtue of Article 25 of L 27/1975 and that are engaged in the chartering, insurance, average (damage) settlements, purchase, chartering or shipbuilding brokerage, or chartering of insurance of ships under the Greek or foreign flag whose capacity exceeds 500 gross registered tons, as well as the representation of shipowner companies or undertakings, whose object is identical to the above-mentioned activities. Greek and foreign companies that have established an office or branch of L 27/1975 and are engaged in the management of vessels flying a Greek or foreign flag, as well as in other activities approved by their licence of operation, are exempt from the above-mentioned annual contribution.

iii Anti-avoidance tax provisions

A general anti-avoidance tax rule has been introduced for the first time under Article 38 of the Tax Procedures Code (TPC), according to which the tax administration may disregard any artificial arrangement or series of arrangements, performed either by individuals or legal entities, that aim to evade taxation and lead to a tax advantage.
An arrangement is considered artificial if it lacks commercial or economic substance. To determine whether an arrangement is artificial various characteristics are examined. For the purposes of this provision, the goal of an arrangement is to avoid taxation in the event that, regardless of the subjective intention of the taxpayer, it is contrary to the object spirit and purpose of the tax provisions that would apply in the other cases. In order to determine the tax advantage, the amount of tax due taking into consideration such arrangement is compared to the tax payable by the taxpayer under the same conditions in the absence of such arrangement.

Finally, by virtue of specific tax provisions, transactions (e.g., expenses) between domestic entities and entities of non-cooperative states or states with beneficial tax regimes (e.g., offshore entities) are not recognised for income tax purposes.

iv Infringements of tax avoidance (Article 55 of L 4174/2013)

Under Article 55 of the Tax Procedures Code (Law 4174/2013) (TPC), a taxpayer is considered to have committed the main offence of tax evasion in the following cases:

a Where the taxpayer conceals from the tax authorities taxable income from any source or assets, in particular by failing to submit tax returns, by submitting inaccurate tax returns, by recording (totally or partially) fictitious costs in his or her accounting records, or by using such fictitious costs so as not to disclose or to disclose reduced taxable income with the intention of avoiding to pay income tax, property tax or special property tax.

b Where the taxpayer fails to make payment, makes incorrect payment, offsets or incorrectly deducts taxes or misleads the tax authorities by presenting false facts as real or by concealing real facts by which he or she fails to make payment, makes incorrect payment or offsets or incorrectly deducts taxes or incorrectly receives a tax refund, or makes a tax withholding with the intention of avoiding to pay value added tax, turnover tax, insurance premium tax, withholding tax and contributions.

c Where the taxpayer fails to make payment, or makes incorrect payment, of the special vessels tax, with the intention of avoiding paying such tax.

V CONCLUSIONS & OUTLOOK

Wealth and succession planning for high net worth individuals is in demand in Greece. Greece has entered into many DTTs. Trusts are now recognised as taxable legal entities for corporate income tax purposes and are commonly used as a vehicle for wealth and succession planning purposes. It is also important to note that shipping companies operating under Law 27/1975 are attractive to wealthy individual for use as vehicles for Greek tax purposes because they fall under a beneficial tax regime.

On the other hand, new tax provisions have been introduced, such as the CFC rules and other ‘tax evasion’ or ‘artificial arrangement’ provisions, with the aim of addressing tax evasion and preventing techniques that lead to a tax advantage. In line with the aim of these provisions, Greek tax authorities have been adopting a stricter attitude and policy towards any kind of tax planning.
Chapter 20

GUERNSEY

Keith Corbin and Mark Biddlecombe

I INTRODUCTION

Guernsey is part of the Bailiwick of Guernsey, within the Channel Islands. It is located 164 miles south-west of London and 27 miles from the Brittany coastline of France, with a population of 63,000 people. The other islands in the Bailiwick are Alderney, Sark, Herm, Jethou and Brecqhou.

Constitutionally, Guernsey is a dependency of the British Crown having its own parliament, the States of Deliberation, but is reliant upon the United Kingdom for foreign representation and defence. The States of Deliberation generally meets on a monthly basis and consists of 38 deputies elected in districts, plus two representatives from the States of Alderney, a presiding officer (the Bailiff, or the Deputy Bailiff in his absence) and two law officers of the Crown (being Her Majesty's Procureur (Attorney General) and Her Majesty's Comptroller (Solicitor General)). Other than the deputies, the appointments are made by the Crown. There are no political parties and Guernsey deputies are elected for a period of four years. The Bailiff is also the senior judge of the Bailiwick. The Queen also appoints a Lieutenant Governor, who is her personal representative in the Bailiwick.

The States of Deliberation elects a president who is the most senior political office holder and chairs the policy and resources committee. This committee has oversight of six principal committees and a number of associated authorities, boards and commissions.

Guernsey enjoys a unique relationship with the European Union, along with the two other Crown Dependencies, the Isle of Man and Jersey. Under the terms negotiated by the UK in 1971, under Protocol 3 of the Treaty of Accession, Guernsey is within the common customs territory of the community. This means that goods exported from Guernsey into the EU are not subject to the common customs tariff. For all other purposes, Guernsey is outside the EU, but EU directives, which are binding on Member States, may be brought into force in the Bailiwick by an ordinance passed by the States of Deliberation if they are thought to be of value to the Bailiwick. Guernsey has a representative office in Brussels. Following the UK’s Brexit referendum on 23 June 2016, the Policy and Resources Committee issued a statement pointing out that Guernsey remains a ‘third country’ in the EU, with market access to the EU in a number of areas. Negotiations with the UK are being held to:

a protect Guernsey’s interests in the UK exit agreement with the EU;
b replace Protocol 3 in the new UK/EU relationship;

1 Keith Corbin is executive chairman and Mark Biddlecombe is in-house legal counsel at Nerine Trust Company Limited.
2 Treaty of Accession of the United Kingdom to the EEC signed 22 January 1972.
3 European Communities (Implementation) (Bailiwick of Guernsey) Law 1994.
c safeguard Guernsey’s long-standing constitutional relationship with the UK; and
d seek new opportunities as the UK establishes new trading relationships with the rest of the world.

Guernsey law has its origins in Norman law, the Bailiwick having been part of the Duchy of Normandy since 993, but in 1204 gained the right to self-government after pleading allegiance to King John as he fought to maintain his territory in France. The legal system has subsequently been increasingly influenced by English law and the Guernsey courts will refer to case law from England and other common law jurisdictions, with the Privy Council being the highest court which may deal with Guernsey court matters.

Today, Guernsey is regarded as a pre-eminent international financial jurisdiction and a centre of excellence for wealth planning matters. In addition, it has a long-standing reputation for political stability.

Guernsey’s regulatory standards have received global recognition through a succession of reviews since 1997 and meeting international standards set by bodies such as the Financial Action Task Force (FATF) and the IMF. The report into the most recent international assessment undertaken by MONEYVAL in 2014 was highly positive and found that Guernsey had surpassed the standards set in the equivalent IMF report on Guernsey in 2010. Guernsey has subsequently implemented harsher penalties for financial crime in line with recommendations in the MONEYVAL report.

The solid legal, political and regulatory platform is supported by a strong financial services infrastructure including international standard accountancy and law firms, a banking industry represented by leading international institutions, and other important support sectors such as insurance and investment management services.

Since the late 1960s when financial institutions and professional advisers first began to recognise the potential for Guernsey as an international financial centre, Guernsey has pursued a conservative and long-term approach to its position as a financial centre, resulting in state-of-the-art financial legislation that has evolved to meet the demands of international Ultra High Net Worth Individuals (UHNWI) clients.

As a jurisdiction, it offers world-class expertise for international clients and their wealth planning needs, but is also attractive to UHNWI clients as a home. A simple, low-tax environment (see below) is underpinned by good transport links with the UK by air and sea, international telecommunication standards and high-quality education and public services.

II TAX

Guernsey’s domestic budget is funded primarily by income tax receipts, supplemented by indirect taxes such as import duties on alcohol, tobacco and motor fuel. Property taxes are charged but at far lower rates than in many other countries.

i Individuals

Personal income tax is charged at a rate of 20 per cent on an individual’s worldwide income. However, during a tax year persons who are ‘resident’ (spend at least 91 days in Guernsey)

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but are not ‘solely resident’ or ‘principally resident’ (broadly meaning they spend 182 days or more in Guernsey) may elect to pay income tax only on Guernsey source income plus an annual ‘standard’ charge of £30,000 in respect of non-Guernsey source income.

Guernsey resident individuals may also elect to cap their income tax liability by paying £110,000 on non-Guernsey source income or £220,000 on their worldwide income.

Guernsey does not levy:

- capital gains tax;
- inheritance tax;
- GST or VAT; or
- wealth tax.

**ii Corporate**

Companies do not generally pay income tax on their profits as the standard rate of company tax is zero per cent. However, income from financial services (e.g., from banking, fiduciary and insurance business) is subject to a 10 per cent rate, and income from certain other sources, including ‘large retail business’ and utility providers, is subject to a 20 per cent rate.

**iii International agreements**

Guernsey has a policy of meeting internationally accepted standards on tax transparency. As at 16 June 2017, Guernsey had signed 60 tax information exchange agreements and 28 double taxation agreements.5

**III SUCCESSION**

As a leading international finance centre, with a globally diverse client base, Guernsey’s law in relation to succession has evolved in step with its laws for trusts and corporations. The most significant recent development is the Inheritance (Guernsey) Law 2011 (the Inheritance Law).

Before the Inheritance Law came into force on 2 April 2012, Guernsey’s succession law retained aspects of its Norman law origins and testamentary freedom was limited in a way that would be familiar to its European neighbours. The Inheritance Law is now more in keeping with Guernsey’s status as a pre-eminent trust jurisdiction.

Testamentary freedom and the rules on intestate succession vary according to whether or not the individual is domiciled in Guernsey, whether the estate consists of moveable or immovable property and, in the case of immovable property, whether that property is situated in Guernsey or otherwise.

For wills executed from 2 April 2012, a Guernsey-domiciled settlor will have complete testamentary freedom. There are safeguards for family and dependants in that the Inheritance Law allows defined persons to apply to the court if they feel that they have not been reasonably provided for in the will.6

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5 A list of TIEA and DTA partner countries is located at www.gov.gg/tiea and www.gov.gg/dta.
6 Inheritance (Guernsey) Law, 2011, Section 4(2).
Where the individual is domiciled outside Guernsey, the law of their domicile will govern their estate in relation to realty outside Guernsey and all personal property. If that law includes forced heirship provisions, then those provisions will have effect.

Guernsey law will, however, apply in relation to any realty situated in Guernsey.

### i Estate administration

When an individual dies leaving assets in their own name in Guernsey, their executor or personal representative will have to apply for a grant of probate (if there is a valid will in existence) or a grant of administration (where the deceased has died intestate). Assets held in joint names will generally pass to the survivor.

Unusually, the issue of a grant in Guernsey remains a matter for the Guernsey Ecclesiastical Court, a jurisdiction long since handed over to the civil courts on the mainland.

In order to obtain the grant, the executor or administrator will generally have to appear in person or be represented by their duly appointed attorney. 

The exception to this is where the estate consists of Guernsey realty; this passes automatically on death to the lawful heirs, be that on intestacy or under the terms of a valid will.

### ii Matrimonial issues

In matrimonial matters, Guernsey has modelled its approach on the equivalent legislation in the UK, and the court can be expected to take a similar approach in dealing with financial provision orders and the like. As a matter of principle, while Guernsey legislation recognises that pre and post-nuptial contracts exist, the court retains a discretion to vary or ignore them as it sees fit, in much the same way as its English counterpart. With a growing acceptance in England that prenuptial contracts have a role in divorce proceedings, the expectation is that Guernsey will follow suit, particularly when the parties are from a civil law tradition. If such a contract is recognised under the law of the testator’s domicile, then clearly it will have an effect on dealing with their personalty and non-Guernsey realty.

From 2 May 2017, same-sex marriages have been permitted in Guernsey. Guernsey does not permit same-sex civil partnerships, but does recognise certain overseas civil partnerships and registered overseas relationships.

Guernsey has long been an attractive destination for high net worth individuals looking for a place to live that is familiar, close to major markets and fiscally benign. Guernsey’s modernised succession law, increased recognition of diversity, and a modern flexible approach to matrimonial assets will add to its attractiveness. In a political climate where tax rates in the major economies continue to rise and the attractiveness of the UK for high net worth non-domiciliaries continues to be eroded, Guernsey is wellplaced to benefit.

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7 It is possible instead to arrange for a postal oath to be sworn before a notary public or the equivalent.

8 See, for example, *E v. E (Royal Ct.)*, 2003–04 GLR N [22] where the issue was not about policy, but about the circumstances under which the contract was entered into.

9 The Same-Sex Marriage (Guernsey) Law, 2016 (Commencement) Ordinance, 2017.

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IV  WEALTH STRUCTURING

Since the 1960s, Guernsey has demonstrated a willingness to adapt and innovate in order to meet the needs of an increasingly sophisticated and global market for wealth structuring, whether that be in its state-of-the-art trust law, its world-class collective investment regime or its continuously evolving company law.

Guernsey trust law was first codified in 1989, and then given a significant facelift in 2007. Since then, Guernsey has introduced a foundations law, an image rights registry (the first anywhere in the world), and an aircraft registry. It also continues to develop its company law for an increasingly international market. Guernsey’s latest focus is on promoting itself as a leading jurisdiction for fintech and digital businesses.

Guernsey in 2017 is very much a first rank international finance centre. The island has become a centre of excellence for fiduciary services, with access to first-rate law firms, accountants, banks and investment managers. The political system is stable, and the judiciary extremely well versed in dealing with very complex and high-value commercial and fiduciary matters.

While continuing to service institutions and advisers in London, Guernsey has a global significance. Service providers on the island have a distinct awareness and sensitivity to the needs of clients from very different cultures with consumers of Guernsey fiduciary services coming from Asia, the Middle East, eastern Europe and Latin America as much as from more traditional European economies and the UK.

i  Trusts

Guernsey trust law has developed from its English law roots to include features that are essential to meet the needs of this global client base, while retaining the fundamental characteristics of trust principles.

As well as a growing body of precedent of its own, Guernsey can also look to other common law jurisdictions for guidance on legal principles, and with the Privy Council as its ultimate appellate court, has access to the leading judicial minds in the field.

Guernsey’s trust law has a number of features that are designed to provide solutions for its global audience.

Examples of Guernsey’s approach include the following.

Duration

Guernsey law does not have perpetuities and accumulations restrictions as evident on the mainland and allows for trusts of unlimited duration.

Purpose trusts

A Guernsey law trust can be established for charitable or non-charitable purposes. This can be particularly useful for structuring family businesses, commercial structures or in a private trust structure as discussed later in this chapter. An enforcer must be appointed to a purpose trust to hold the trustee accountable.
Reserved powers

One of the challenges that settlors face when they establish a trust is to play an ongoing role in the administration of the trust without compromising the benefits that it provides. Under Guernsey law, settlors can reserve to themselves, or to others, a wide range of powers such as powers to:

a. revoke or vary the trust;
b. appoint income or capital;
c. direct investments;
d. appoint or remove trustees and directors of underlying companies;
e. change the proper law; and
f. veto trustee decisions.

Trustee liability

Trustees of a Guernsey trust have a wide range of duties under the law, including a duty (subject to the terms of the trust) to preserve and enhance the value of the trust, so far as is reasonable. There is also an overarching duty to act in the utmost good faith and ‘en bon père de famille’.\textsuperscript{10} Trustee liability can be excluded under the terms of the trust, but not so as to exclude liability for fraud, wilful misconduct or gross negligence. Claims for breach of trust must be brought within three years of the claimant becoming aware of the breach or they will be prescribed.\textsuperscript{11} Prescription differs from limitation under English law in that it operates to extinguish a claim, rather than denying relief from the claim.

Dispute resolution

Guernsey has recognised that where breach of trust claims are made against trustees, it is important that any settlement reached between the parties outside the court room has legal and binding effect. The 2007 law therefore provides, with appropriate safeguards, for claims settled under alternative dispute resolution to be binding against all beneficiaries of the trust, whether or not yet ascertained or in existence.\textsuperscript{12}

Company law

Guernsey’s company law continues to evolve, with the latest amendments set out in the Companies (Guernsey) Law, 2008 (Amendment) Ordinance 2015, coming into effect on 3 September 2015.

Among the many changes introduced, is an ability for a Guernsey company to be incorporated with, or register, an alternative name expressed in non-Roman alphabet,

\textsuperscript{10} This is a customary law principle, particular to Guernsey’s law. In trust law the Privy Council determined in Spread Trustee Co Ltd v. Hutcheson [2011] UKPC 13, that it was analogous to the English law prudent investor test.

\textsuperscript{11} The case of Broadhead v. Spread Trustee Company Limited & Ors (Guernsey Judgment 46/2014) determined that the clock starts to run once the claimant has enough information that would make any reasonable person begin to investigate whether there had been a breach of trust. They would see that a loss has been incurred, and have a sense that there was a real possibility (not a mere suspicion) that the loss had been caused by negligence on the part of the trustees.

\textsuperscript{12} Trusts (Guernsey) Law, 2007, Section 63.
characters or script. This was in response to demands from clients in the Far East and the Middle East. Other measures included provisions to align Guernsey’s legislation with the UK’s City Code on Takeovers and Mergers.

Given the number of Guernsey companies that list on the London Stock Exchange, there is a clear need for the company law to remain modern and flexible.

Incorporation in Guernsey is easy and quick with the use of Guernsey’s online registry through licensed providers. A company can be incorporated within a day and, for a modest premium, in less than two hours.

In 1997, Guernsey was the first jurisdiction to introduce the concept of the protected cell company (PCC), with a further innovation in the shape of the incorporated cell company (ICC) following in 2006. Both are attractive in collective investment and insurance situations, allowing segregation and insulation of assets as between cells in the company, with the principal difference being the need for cells in an ICC to be separately capitalised.

Guernsey law also provides for companies to be limited by guarantee, a facility that is particularly helpful in structures where there is a need for an orphan vehicle.

iii Limited partnerships

Limited partnerships established under the Limited Partnerships (Guernsey) Law, 1995 are used widely in Guernsey for collective investment schemes as well as in private family arrangements. Partners have the ability to elect for the partnership to be a body corporate, with separate legal personality.

The limited partnership will generally be a look-through entity, made up of a general partner (often a corporate) and one or more limited partners. The general partner holds the assets of the partnership and they are under its control. The profits of the partnership are allocated to the partners under the terms of the partnership agreement.

Limited partnerships are often used in private equity fund structures, but they can also be used in family situations where the tax consequences of establishing a trust would be unattractive. They allow a separation between ownership of an asset – such as a family business – and its control.

Limited liability partnerships have been available since 2014, following the enactment of the Limited Liability Partnerships (Guernsey) Law 2013. A limited liability partnership may be a useful vehicle for authorised or unauthorised collective investment fund structures, or for professional firms looking to incorporate for the purposes of limited liability.

iv Foundations

While trusts remain very important for Guernsey, it is not always easy for civil law clients to embrace the concept. In civil law countries, including many of the emerging markets (Brazil, Russia and China to name but three), the foundation may be more familiar and easier to accept.

With these issues in mind, and with an eye on some of the lessons learned in neighbouring jurisdictions, the Foundations (Guernsey) Law 2012 came into force on 7 January 2013.

The foundation is in some ways a hybrid between a trust and a limited company (often referred to as an ‘incorporated trust’). Like a company, the foundation has separate legal personality, a certificate of incorporation, a registered number and a Guernsey registered office. There is public certainty as to the foundation’s existence – a foundation cannot fail if it has no assets – like a company it can be ’re-capitalised’ by an additional endowment.
A foundation is established under a charter, which is in two parts. Part A is public and includes basic details of the foundation. Part B is maintained by the registrar but in strict confidence and will include a statement of the purpose of the foundation. This latter provision was included as a regulatory safeguard.

The other core document for the foundation is the rules. These are not registered and remain completely confidential between the founder and the council. The purpose of the rules is to set out how the foundation is going to operate.

All foundations must have a purpose, which can be charitable or non-charitable and can be drafted as widely as required. The foundation may also have beneficiaries, and if it does these can be enfranchised, with a right to information in respect of the foundation like a trust beneficiary, or disenfranchised, with no right to information.

Whenever there are disenfranchised beneficiaries, or if there is only a purpose, a guardian must be appointed with responsibility for holding the council to account.

Foundations are utilised as:

a. part of a succession planning structure for private families – be that a structure that includes a trust or as a substitute for a trust;
b. vehicles for charitable donations; and
c. orphan vehicles in corporate structuring, as opposed to using a purpose or charitable trust.

v Private trust company structures

As noted earlier, the Trusts (Guernsey) Law 2007 includes provisions allowing the settlor to reserve a broad range of powers. This allows settlors a degree of control over trustee actions and decisions without compromising the fundamental validity of the trust.

For a number of reasons, this may not always be the preferred approach, and may not go far enough in terms of giving the family the degree of influence and control over trustee decisions that they would like to have.

The solution for many families is to establish a private trust company (PTC) under their control to act as trustee of trusts established only for the family. Guernsey allows such a company to act outside the regulatory licensing regime so long as the PTC does not receive any remuneration.

The PTC allows the family to influence and control the structure in a number of ways:

a. The family can retain the ability to nominate directors of the PTC to sit alongside directors from the service provider and other professional advisers. These family nominated directors will often be members of the family.
b. The trust can still include reserved powers, giving the settlor additional comfort in relation to key decisions.
c. The settlor can provide the board of the PTC with guidance on an ad hoc basis or through a letter of wishes.
d. The settlor or family can control the composition of the board of subsidiary companies held by the trust.
e. The settlor or family can establish a set of rules dictating how the PTC should be run and how key decisions should be made through the drafting of the constitutive documents of the PTC alongside other documents, such as a family charter.
It is a lot easier for the family to change the composition of the board of directors of the PTC than it would be to remove and replace an independent trustee appointed in the more usual fashion.

When establishing a PTC structure, it is important that the family considers how the PTC should be owned. Traditionally, the PTC would be a company owned by a purpose trust. Alternatively, the PTC can be structured as a guarantee company, although care will need to be taken in order to ensure issues in relation to succession to guarantee membership are considered. More recently, foundations have been used instead of the purpose trust to own the PTC. Alternatively, the PTC can simply be established as a foundation.

V REGULATION

Guernsey has been at the forefront of the regulating and licensing fiduciary service business. Alongside Jersey, it was the first jurisdiction to introduce legislation for the licensing of fiduciaries in 2000.13

Under the auspices of the Guernsey Financial Services Commission (GFSC), fiduciary businesses in Guernsey are subject to a state -of-the-art regulatory regime. The GFSC operates a risk-based approach to regulation. According to its 2016 report, the fiduciary division of the GFSC had 154 full licensees under its supervision, each of which have been risk-assessed and all of which will receive regular visits from and reviews by the regulator.

All licensees are required to abide by core principles set out in the legislation, related rules, codes of practice and guidelines.

Guernsey has a comprehensive suite of legislation in relation to anti-money laundering (AML) and prevention of the financing of terrorism in keeping with the highest levels found internationally. A principal function of the GFSC is to ensure that licensed fiduciaries adhere to the requirements of the legislation and there is a separate division dealing with financial crime and a further division focused on enforcement. In this regard, the 2016 report noted that its enforcement policy focused on ensuring that licensees have adequate risk mitigation programmes in place, including for the ever-increasing prevalence of cybercrime.

Taken as a whole, the regulatory regime is a significant factor in Guernsey’s status globally and explains why Guernsey has received such positive reviews from the likes of MONEYVAL.

As ever, the regulatory environment does not stand still and the GFSC is working on a number of initiatives, including revisions to the AML handbook and a comprehensive revision of the regulatory laws.

Guernsey, like most other jurisdictions in the world, is also actively involved with the increased degree of reporting and sharing of information in response to FATCA and CRS. Guernsey will be playing its full part in the process of ensuring that its tax neutrality continues to operate in a way that is consistent with international law.

The UK has been leading the charge on the implementation of a public register of beneficial ownership of UK companies that is soon to be expanded to include non-UK entities owning UK real estate and a private register of trusts. Guernsey introduced its central register of beneficial ownership in relation to Guernsey entities on 15 August 2017. In contrast to the UK’s company beneficial ownership register, which is publicly available and searchable,

13 The Regulation of Fiduciaries, Administration Businesses and Company Directors, etc. (Bailiwick of Guernsey) Law 2000.
Guernsey’s register is centrally maintained, but the information on it is not publicly available. Instead, it is only available to certain Guernsey regulatory and law enforcement bodies (who will be able to disseminate this information to their counterparts in other countries when requests for such assistance are received).

VI CONCLUSIONS & OUTLOOK

From its beginnings in the 1960s, Guernsey has emerged as a major player in international finance. It has moved with the times, adapting its approach and its legislation in order to meet the ever-changing demands of its international client base and a rapidly evolving global approach to economic and fiscal change.

With the increasing momentum towards automatic exchange of information and increasing transparency of beneficial ownership of corporate vehicles across the globe, clearly Guernsey will need to continue to innovate in order to remain competitive while being recognised as a good global citizen. Its track record for over 50 years gives every reason for confidence that Guernsey is well placed to meet that challenge.
Chapter 21

HONG KONG

Ian Devereux and Silvia On

I

INTRODUCTION

Hong Kong, formally known as the Hong Kong Special Administrative Region of the People's Republic of China, is in a unique position: although it is part of the People's Republic of China (PRC), it has a separate and different legal system from the PRC. This system is called 'One Country, Two Systems'. As a former British colony, Hong Kong inherited the English common law system and much of Hong Kong's legislation is based on English legislation. Article 5 of the Basic Law\(^2\) allows Hong Kong to maintain its separate legal and judicial system for 50 years after its handover back to the PRC on 1 July 1997. Chinese and English are both official languages of Hong Kong.

Apart from having a separate legal system from the PRC, Hong Kong also has a separate financial and banking system, which is regulated by the Hong Kong Monetary Authority. Hong Kong continues to be a major financial centre and plays a major role in the world’s financial industry. According to figures released by the Hong Kong Stock Exchange, Hong Kong secured the position of the world’s largest initial public offerings (IPOs) listing venue in 2016. Breaking this down in detail, the figures showed that during 2016, Hong Kong recorded 126 IPOs, raising HK$194.8 billion.\(^3\) For the 15th consecutive year, the Hong Kong market was one of the world’s top five in IPO fundraising. Hong Kong is also one of the freest economies in the world, making it attractive and easy for businesses to set up in Hong Kong. Following its 2017 ranking, Hong Kong has been ranked the number one country on the Index of Economic Freedom for the past 23 years.\(^4\)

Hong Kong has one of the highest concentrations of high net worth individuals in the world. It is the only city in the world that has its own separate Forbes ‘rich list’. In addition to Hong Kong’s own high net worth individuals, the PRC’s high net worth individuals are also increasingly turning to Hong Kong, not only for the shopping, but also for their succession and estate planning needs. An increasing number of PRC companies have also applied for listing in Hong Kong, especially after the relaxation of rules in the PRC in 2013, which made it easier for PRC companies to list on the Hong Kong Stock Exchange. This makes Hong Kong not only the gateway to China, but also the gateway from China to the outside world.

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1 Ian Devereux is a partner and Silvia On is a consultant at Stephenson Harwood.
2 Article 5, Basic Law of the Hong Kong Special Administrative Region of the People’s Republic of China.
3 Hong Kong Stock Exchange website.
II TAX

i Taxation in Hong Kong

Unlike many other jurisdictions, Hong Kong has a territorial taxation system that means Hong Kong only imposes tax on income and profit arising in Hong Kong. Therefore, in most cases, the issue of whether an individual or company is subject to Hong Kong tax depends on whether the income or profit arises in or derives from Hong Kong.

The two main pieces of legislation dealing with taxation in Hong Kong are the Inland Revenue Ordinance (IRO) and the Stamp Duty Ordinance (SDO). The main forms of tax imposed in Hong Kong are set out below.

Salaries tax

As its name suggests, salaries tax is imposed on salaries received by individuals – an individual is subject to salaries tax if he or she receives income arising in or derived from Hong Kong from any office, employment of profit or pension. The tax residency of an individual is usually irrelevant when determining whether an individual is subject to Hong Kong salaries tax.

Salaries tax is essentially the only form of income tax levied on an individual and unlike some other jurisdictions, Hong Kong does not have a general income tax that is imposed on the individual’s income. Where an individual also receives other forms of income, such as rental income, this rental income is subject to property tax (see below), but the individual can elect for ‘personal assessment’ of his or her total income where he or she will be taxed based on the aggregate total of his or her income.

Individuals are taxed at either a progressive rate, ranging from 2 per cent to 17 per cent, or a flat rate of 15 per cent depending on which method of calculation provides the lower amount of tax payable. When determining the income taxable under either salaries tax or personal assessment, the individual’s allowable allowance (such as personal allowance and child allowance) and allowable deductions (such as contribution to the Hong Kong mandatory pension scheme and donations to charities) are deducted from the individual’s total income.

Also, unlike many other jurisdictions, the taxes payable by an individual (either under salaries tax or personal assessment) are not deducted at source (i.e., not deducted prior to payment to the individual by the employer). An individual is responsible for paying his or her taxes to the Hong Kong Inland Revenue Department (IRD). Every year, the Hong Kong IRD issues a notice of assessment to individuals and individuals are required to complete and file the notice of assessment to the IRD. The IRD will then calculate the amount of salaries tax payable by the individual.

Other forms of income received by individuals such as dividends, interest and distributions from trusts are not usually subject to tax in Hong Kong.

Profits tax

Profits tax is imposed on every person who is carrying on a trade, profession or business in Hong Kong in respect of the profits arising in or derived from Hong Kong from the carrying on of the trade, profession or business in Hong Kong. Therefore, profits tax is

5 Subsection 8(1), Inland Revenue Ordinance (Cap 112).
6 Subsection 14(1), Inland Revenue Ordinance (Cap 112).
often seen to be similar to corporate tax. Like salaries tax, the tax residency of the company is usually irrelevant when determining whether a company is subject to Hong Kong profits tax. However, issues such as where the directors are based and where the directors’ meetings are held are relevant factors when it comes to determining whether or not the profit is arising in or derived from Hong Kong. The company’s place of incorporation is also irrelevant when determining whether a company is subject to profits tax although it is generally assumed that a Hong Kong company will be subject to profits tax and therefore the Hong Kong IRD will send Hong Kong companies a profits tax return every year for assessing the profits tax payable by the company. The current rate of profits tax is 16.5 per cent.

A ‘person’ is defined widely to include a corporation, partnership, trustee, whether incorporated or unincorporated, or body of persons. The inclusion of ‘trustee’ but not ‘trust’ in the definition of a person and the wording of the profits tax charging provision makes it unclear whether the trustee of a trust, particularly in relation to discretionary trusts, will be subject to profits tax on the trust income because any profit generated by the trustee as the trustee of a trust belongs to the trust and not the trustee. Where the trust is a bare trust, the profit is considered as belonging to the beneficiary and therefore it is the beneficiary who will be subject to profits tax on the profit, not the trustee.

Like individuals, income in the form of dividends and interest are not usually subject to tax.

**Property tax**

Property tax is a tax imposed on the net assessable value of land and buildings in Hong Kong. Net assessable value is calculated based on the consideration received for the use of the land or building less any allowable deductions. In other words, property tax is charged on rental income received less allowable deductions. The current rate of property tax is 15 per cent.

Where the land or building is owned by a corporation and the rental income received by the corporation is subject to profits tax, the corporation can apply for exemption from property tax.

**Stamp duty**

The SDO imposes stamp duty on leases of Hong Kong immovable properties, transfer of Hong Kong immovable properties and transfer of Hong Kong stocks such as shares. The rate of stamp duty on leases depends on the length of the lease and the annual rental payable under the lease. The rate of stamp duty on the transfer of Hong Kong immovable properties depends on the value of the property transferred or the market value of the property transferred as assessed by the IRD. The rate of stamp duty on Hong Kong stocks is usually 0.1 per cent of the amount of consideration paid and 0.1 per cent of the consideration received payable by the transferee and transferor respectively.

In the past few years, as part of an effort by the Hong Kong government to cool rising property prices in Hong Kong, a number of additional stamp duties have been imposed in relation to immovable property transactions. A special stamp duty is imposed on individuals and companies that resell residential property within 36 months of purchase. The rate of

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7 Section 2, Inland Revenue Ordinance (Cap 112).
9 Section 4 and First Schedule, Stamp Duty Ordinance (Cap 117).
stamp duty depends on the length of time the property was held for before it is resold. Another stamp duty is the buyer’s stamp duty, whereby a stamp duty of 15 per cent is imposed on companies and non-Hong Kong individuals (i.e., individuals who are not Hong Kong permanent residents) purchasing Hong Kong residential properties. In addition, the *ad valorem* stamp duty imposed on individuals or companies buying residential properties on or after 23 February 2013 has, since 4 November 2016, been increased to a flat rate of 15 per cent.\(^\text{10}\) There is an exemption in that this will not apply where the purchaser is a Hong Kong permanent resident, does not own other residential properties in Hong Kong (at the time of the purchase) and acquires only one residential property under a single instrument. Where the individual purchases a second residential property and subsequently sells the first residential property within six months, the purchaser will be rebated the additional higher rate of stamp duty paid, in other words, they will only have to pay the normal rate of stamp duty instead of the higher rate of stamp duty.

**Other taxes**

Hong Kong does not have gift tax, estate duty (which was abolished in 2006) and capital gains tax. Although Hong Kong does not have capital gains tax, gains made from the trading, such as buying and selling of shares or properties, may be considered to be profit and therefore be subject to Hong Kong profits tax. Hong Kong also does not have any form of sales tax, such as goods and services tax and value added tax.

### ii Cross-border issues

Hong Kong’s territorial system of taxation means that an individual’s tax residency and domicile are usually not relevant when determining taxability and hence there is no definition for tax residency under the IRO and a lack of case law on the issue of tax residency. In relation to companies, the company’s tax residency is also not usually relevant when determining taxability. This lack of definition of tax residency under Hong Kong law may create issues when dealing with certain cross-border issues because international agreements such as double tax treaty agreements use the concept of tax residency when determining taxability. However, the Hong Kong IRD will issue a certificate of resident status to Hong Kong residents who need proof of resident status.\(^\text{11}\)

Since Hong Kong’s return to the PRC, Hong Kong has entered into double tax treaty agreements with 37 countries.\(^\text{12}\) Hong Kong has also entered into tax information exchange agreements with the United States and six Nordic jurisdictions. Hong Kong also signed a Model 2 intergovernmental agreement with the United States on 13 November 2014 to facilitate compliance with the US Foreign Account Tax Compliance Act. On 7 June 2017, Hong Kong introduced new legislation expanding the list of reportable jurisdictions for automatic exchange of financial account information from two to 75, and aims to commence the first exchanges by the end of 2018.\(^\text{13}\)

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10 Hong Kong Inland Revenue Department website (www.ird.gov.hk/eng/faq/#avd).
11 Hong Kong Inland Revenue Department website (www.ird.gov.hk/eng/tax/dta_cor.htm).
12 Hong Kong Inland Revenue Department website (www.ird.gov.hk/eng/tax/dta_inc.htm).
13 Hong Kong Inland Revenue Department website (www.ird.gov.hk/eng/tax/dta_aeoi.htm).
III SUCCESSION

In recent years, Hong Kong has seen a number of wealthy families go through the process of passing wealth from the first generation to the second generation. In a number of cases, this transfer of wealth has ended up with second generation family members going to court to settle their disputes over the distribution of the family wealth, or family members and beneficiaries challenging the validity of wills. These cases have also been widely publicised by the media. This has prompted individuals to consider the need to put in place some form of succession mechanism to ensure the smooth succession of wealth from one generation to the next and to protect the family's privacy and confidentiality.

Because of the low tax rates in Hong Kong and especially after the Hong Kong estate duty was abolished, tax planning is not usually a driving factor when it comes to estate planning for individuals who are resident in Hong Kong and whose family members are also resident in Hong Kong. For many of these individuals and their families, succession planning and wealth preservation are often the reasons for planning.

i Wills

In Hong Kong, individuals are generally free to decide how their assets are to be distributed through the use of wills since Hong Kong does not have forced heirship rules. However, the Inheritance (Provision for Family and Dependents) Ordinance allows dependants, such as the spouse, former spouse (who has not remarried), parents, offspring and other persons related to the deceased who are resident in Hong Kong and whose family members are also resident in Hong Kong. For many of these individuals and their families, succession planning and wealth preservation are often the reasons for planning.

ii Intestacy

Where an individual dies without leaving a will, his or her estate will be distributed in accordance with the Hong Kong intestacy rules set out in the Intestates' Estates Ordinance. If the deceased leaves a spouse but no issue, parent or sibling, all the assets are inherited by the spouse. If the deceased leaves a spouse with issue, then the spouse will inherit all personal chattels, HK$500,000 and half of the residue estate with the other half of the residue estate going to the issue. If the deceased leaves a spouse with no issue, then the spouse will inherit all personal chattels, HK$1 million and half of the residue estate with the other half going to parents or siblings, if the parents are not living. If the deceased leaves no spouse but issue, then the issue inherit in equal shares. If the deceased leaves no spouse and no issue, then the parents inherit in equal shares. If there are no parents, then the siblings (failing which grandparents, failing which uncles and aunts) inherit in equal shares.

iii Marital property and divorces

In addition to wanting to prevent family disputes, wealthy individuals and families are also becoming increasingly concerned about the division of assets in the case of a family member getting divorced. The Hong Kong courts have very much followed the approach of the English courts when it comes to determining how matrimonial properties are to be divided in the case of a divorce. The Hong Kong courts will start with the ‘yardstick of equality’

14 Section 3, Inheritance (Provision for Family and Dependents) Ordinance (Cap 481).
15 Section 4, Intestates’ Estates Ordinance (Cap 73).
approach, so the starting point is to assume each party is entitled to half of the matrimonial property. This approach was also taken in the recent Hong Kong case of *Kan Lai Kwan v. Poon Lok To Otto*[^15]. In relation to prenuptial agreements, Hong Kong courts stated that Hong Kong should follow the principles on prenuptial agreements proclaimed in the English case of *Radmacher v. Granatino*,[^18] which means that prenuptial agreements are not legally binding in Hong Kong but are persuasive.[^19]

The Hong Kong courts also recently adopted the test set down by the English courts in *Charman v. Charman*[^20] in determining whether trust assets should be treated as a financial resource. The Hong Kong Court of Final Appeal stated that the test to be applied is 'to decide whether a discretionary trust is a financial resource of one of the parties, the Court asks whether, if that party were to request the trustee to advance the whole or part of the capital or income of the trust to him or her, the trustee would, on the balance of probabilities, be likely to do so'.[^21] This means that assets held by a trust can be considered matrimonial property and therefore subject to division when parties divorce.

These factors combined with recent high-profile divorce cases involving wealthy families, which were widely reported by the media, have also resulted in wealthy families looking to find ways to protect their family wealth should one of the family members get divorced.

An interesting feature of Hong Kong matrimonial law is that, prior to the passing of the Marriage Reform Ordinance in 1971, concubines were legally recognised and therefore these concubines and their children also had a legal right to the estate under Hong Kong law.

Hong Kong does not have civil unions or same-sex marriages, but in recent years, there has been increasing interest in this area with certain groups lobbying for the passing of legislation to allow for same-sex marriages.

### iv Other succession issues

One issue with Hong Kong having a separate legal system from the PRC is where Hong Kong-resident individuals own assets in the PRC, such as PRC immoveable property. Because of restrictions on the ownership of PRC assets, it is often difficult if not impossible to transfer these assets into an offshore trust (even if the trust is a Hong Kong trust). This means these individuals often have to deal with the succession of their PRC assets through a separate PRC will.

### IV WEALTH STRUCTURING & REGULATION

#### i Commonly used vehicles for wealth structuring

Offshore trusts and offshore companies are commonplace when it comes to structuring wealth for Hong Kong individuals and families. Hong Kong trusts were not often used

[^18]: See *SPH v. SA* [2014] 4 HKC 271.

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because, compared with the trust law of the offshore jurisdictions, the Hong Kong trust law was considered to be outdated and not as user-friendly. However, since Hong Kong amended its trust law in December 2013, Hong Kong trusts are gaining interest.

It is also more common to establish private trust companies in these offshore jurisdictions. One reason for this is because offshore companies provide greater confidentiality since Hong Kong companies are required to file information about their shareholders and directors with the Hong Kong Companies Registry, and this information is publicly available. Offshore private trust companies were commonly used to act as the trustee of private unit trusts in trust structures established for Hong Kong estate duty planning.

Hong Kong does not have foundation law and foundations are not as commonly used as trusts for estate planning purposes. One reason for this may be because trusts have always been more widely used and recognised in Hong Kong.

### ii Hong Kong trusts

The main piece of legislation governing Hong Kong trusts is the Trustee Ordinance, which was amended in December 2013.\(^{22}\) The amendment brought in a number of significant changes to the Hong Kong trust law. There is now a statutory duty of care imposed on trustees, whereby trustees are required to exercise a level of care and skill that is reasonable in the circumstances, taking into account the trustees’ special knowledge, experience or professional status.\(^{23}\) A statutory control on trustees’ exemption was also added whereby remunerated trustees acting in a professional capacity are not allowed to exclude their liability for wilful misconduct, gross negligence or fraud.\(^{24}\) A number of provisions relating to trustees’ powers and trustees’ rights to remuneration were also amended.\(^{25}\) The new Hong Kong trust law allows the settlor to reserve the investment and asset management of the trust to himself or herself without this invalidating the trust.\(^{26}\) Foreign forced heirship rules will also not affect the validity of transfer of moveable property to trusts that are expressly governed by Hong Kong law.\(^{27}\) The Perpetuities and Accumulations Ordinance was also amended, abolishing the rules against perpetuities and excessive accumulation of income,\(^{28}\) which means non-charitable trusts governed by Hong Kong law and set up on or after 1 December 2013 are no longer required to have a perpetuities period and accumulation period. The rule against excessive accumulation of income continues to apply to Hong Kong charitable trusts.\(^{29}\)

Under existing Hong Kong legislation, it is relatively easy to set up a Hong Kong trust company. There is no requirement that the company be registered or licensed before it is permitted to act as a trustee, even if the trustee receives remuneration for acting as the trustee. In general, provided that the company’s objects allow it to act as a trustee, the company will

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\(^{22}\) Amended by the Trust Law (Amendment) Ordinance 2013.

\(^{23}\) Section 3A(1), Trustee Ordinance (Cap 29) as amended by the Trust Law (Amendment) Ordinance 2013.

\(^{24}\) Section 41W(3)(a), Trustee Ordinance (Cap 29) as amended by the Trust Law (Amendment) Ordinance 2013.

\(^{25}\) Part 3 and Part 4B, Trustee Ordinance (Cap 29) as amended by the Trust Law (Amendment) Ordinance 2013.

\(^{26}\) Section 41X, Trustee Ordinance (Cap 29) as amended by the Trust Law (Amendment) Ordinance 2013.

\(^{27}\) Section 41Y, Trustee Ordinance (Cap 29) as amended by the Trust Law (Amendment) Ordinance 2013.

\(^{28}\) Section 3A, Perpetuities and Accumulations Ordinance (Cap 257) as amended by the Trust Law (Amendment) Ordinance 2013.

\(^{29}\) Section 3B, Perpetuities and Accumulations Ordinance (Cap 257) as amended by the Trust Law (Amendment) Ordinance 2013.
be able to act as a trustee. However, there are some activities, such as acting as an executor, which a trust company will not be allowed to undertake unless it is registered as a trust company under the Trustee Ordinance.

Service providers of trusteeship services are also largely unregulated in Hong Kong when it comes to them providing trustee services in Hong Kong, unless the company is registered as a Hong Kong trust company under the Trustee Ordinance. Having said that, many of the service providers, such as the subsidiaries of the banks and independent trustee companies, have a tendency to use offshore jurisdictions when establishing trusts and are therefore regulated by the relevant authority in those offshore jurisdictions. This lack of barrier to entry into the Hong Kong trust industry may be one reason that has contributed to increasing numbers of offshore independent trustee companies setting up in Hong Kong in recent years.

Regardless of whether an offshore trust or a Hong Kong trust is used, there are no legal restrictions on the transfer of Hong Kong assets to entities such as companies and trusts. However, the transfer of certain Hong Kong assets, such as shares in Hong Kong companies and Hong Kong immovable properties, will be subject to Hong Kong stamp duty. The introduction of the additional stamp duties on the transfer of Hong Kong properties (as mentioned previously) has made it less attractive for individuals to transfer Hong Kong properties to or own them through corporate entities or trusts. The transfer of non-Hong Kong assets such as the shares in an offshore company are, in most cases, not subject to Hong Kong stamp duty or any other form of Hong Kong taxes since Hong Kong does not have gift tax. This is one of the reasons why it is common to see offshore companies being used as holding companies to hold Hong Kong assets such as shares in Hong Kong companies or Hong Kong immovable properties. As for the general taxation of trusts, please see the profits tax section above.

V CONCLUSIONS & OUTLOOK

Hong Kong has always been home to a large number of high net worth individuals and their families. Some of these families have already experienced a transfer of wealth from the first generation to the second generation, some more successfully than others. The PRC, on the other hand, has not yet experienced this transition and is therefore increasingly looking to Hong Kong and other countries for successful models, as well as hoping to learn from others’ failures. This has resulted in demand for service providers and advisers who will be able to assist these high net worth individuals and their families with succession and estate planning needs, particularly those who are able to speak Chinese.

Since the amendment of the Hong Kong Trustee Ordinance, there has been increasing interest from service providers and individuals in using Hong Kong law as the governing law of trusts. As mentioned previously, trust companies in Hong Kong are largely unregulated. Given the increased interest in and use of Hong Kong trusts, it remains to be seen whether regulations will be put in place to regulate Hong Kong trust companies.

Apart from the amendment of the Trustee Ordinance, the Hong Kong company law was also amended and the new Companies Ordinance came into effect on 3 March 2014. The new Companies Ordinance brought in a number of changes, such as the requirement that there be at least one director who is an individual in a private company, which could potentially affect the use of Hong Kong companies when structuring for wealthy individuals and their families.
Hong Kong charity law is also currently largely unregulated and is undergoing reform. The Law Reform Commission of Hong Kong issued a report in December 2013 that set out a number of recommended changes to the Hong Kong charities law, including introducing a clear statutory definition of what constitutes a charitable purpose, requiring charitable organisations that solicit public donation or have sought tax exemption to be regulated, and creating a set of specifically formulated financial reporting standard for charities.

With the new legislation and the entering of more agreements (such as double tax treaties and tax information exchanges) with other countries, Hong Kong is having to move towards more regulation and greater transparency.
I INTRODUCTION

Before the democratic transformation of Hungary, private wealth and estate planning were of minor importance. They grew in importance, however, with the advent of privatisation. In the past two decades, there have been several fundamental legislative changes intended to create a legal environment facilitating the return to the market economy. Nevertheless, legal instruments enabling effective wealth and estate planning in Hungary have not been fully available until now, and Hungary has been regarded as rather an excellent holding location, famous for its tax rules on IP licensing.

In recent years, however, Hungary has been striving to attract foreign affluent individuals by reducing personal income tax and adopting other favourable measures for private individuals (e.g., Preferential Acquisition of Shares and Hungarian Residence Government Bond schemes) that we detail below.

In March 2014, a new Civil Code, which could significantly improve the legal environment for private wealth planning, entered into force. In this respect, the most significant development of the Civil Code is the Hungarian trust, which was incorporated into the Hungarian Civil Code and is expected to be a new stimulus for the Hungarian economy.

II TAX

i Personal income tax

Hungarian tax-resident status

The rules applicable to personal income tax (PIT) are set out in the Act of CXVII of 1995 on Personal Income Tax (the Act on PIT). According to Section 3 of the Act on PIT, the following should be regarded as being resident for PIT purposes in Hungary:

a Hungarian citizens;

b EEA nationals who spend at least 183 days per calendar year (including the day of entry and the day of exit) in Hungary; and

c third-country nationals who have a permanent residence permit or stateless status in Hungary.

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1 Janos Pasztor is a senior associate heading the tax practice group at Wolf Theiss Budapest.

Also, individuals qualify as being resident in Hungary for PIT purposes if:

- their only permanent home is in Hungary;
- their centre of vital interests is in Hungary if there is no permanent home in Hungary or if Hungary is not the only country where they have a permanent home; or
- their habitual abode is in the domestic territory if there is no permanent home in Hungary, or if Hungary is not the only country where they have a permanent home and if their centre of vital interests is unknown.

For the purpose of a permanent home, any form of home may be taken into account (e.g., a house or apartment belonging to or rented by the individual, a rented furnished room, etc). However, the permanence of the home is essential; this means that the individual has arranged to have a dwelling available to him or her at all times continuously, and not occasionally for the purpose of a stay that, owing to the reasons for it, is necessarily of a short duration (e.g., business travel, educational travel). To substantiate that the individual has a permanent home in Hungary, it is usually required to have at least a rented flat for which he or she is paying utility, telephone and internet bills.

As regards the notion of centre of vital interest, the Hungarian tax authority largely follows the OECD Commentary and claims that the centre of vital interest is the country with which the personal and economic relations of the individual are closer. Thus, his or her family and social relations, occupation, political, cultural and other activities, place of business, and the place from which he or she administers his or her properties should be considered. The circumstances must be examined as a whole, but considerations based on the personal circumstances of the individual (e.g., close family relatives living in the same household) must receive special attention.

Hungarian tax residents are subject to income tax on worldwide income, regardless of whether the funds are transferred to Hungary. Non-residents are taxed on income from Hungarian sources only.

**Hungarian PIT treatment of interest, dividend income and capital gains**

We summarise the Hungarian PIT treatment of certain passive income earned by Hungarian tax residents below.

**Interest**

Hungarian-resident individuals are subject to PIT on their worldwide income, including interest income.

It may occur that the source country of the interest income imposes a withholding tax on the same income. To eliminate double taxation, the Hungarian domestic legislation grants credit for the taxes paid abroad. The maximum amount of the tax credit would be subject to certain limitations. If there is a double tax treaty in force between the two countries concerned, the relevant double tax treaty rules will apply to eliminate double taxation.3

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3 Hungary has several double tax treaties (DTTs) with countries that include the European Union, the Balkans, Iceland, Liechtenstein, Norway, San Marino and Switzerland, Belarus, Moldova, Russia, Ukraine, the countries of the Caucasus, Kazakhstan and Uzbekistan, Canada, the United States, Mexico, Brazil and Uruguay. There are DTTs in place with India, Pakistan, Vietnam, Thailand, Taipei, Hong Kong, China, Mongolia, South Korea, Japan, the Philippines, Indonesia, Malaysia, Singapore and Australia. Hungary also has DTTs with African countries, namely, South Africa, Morocco, Tunisia and Egypt. In recent © 2017 Law Business Research Ltd
Interest income of a Hungarian-resident private individual will be subject to Hungarian PIT at a rate of 15 per cent in 2017.

The Act on PIT applies a broad definition of interest income; in connection with publicly offered and traded debt securities and collective investments in transferable securities, interest shall mean the following:

\[ a \] the income paid to the private individual under the title of interest or yield, if the securities are held at a specific time prescribed as a precondition for entitlement to interest or yield; and

\[ b \] in certain cases, the capital gains achieved when securities are called, redeemed or transferred. In connection with collective investments in transferable securities, redemption shall also cover when the securities are exchanged upon the transformation or merger of the investment fund for the investment certificates of the successor fund. Gains from the transfer of collective investments in transferable securities in certain qualified exchange markets or in a market of an EU, EEA or OECD state will not qualify as interest income, but will be considered as income from capital gains for Hungarian tax law purposes.

In the event that the interest income is paid in the form of valuable assets (e.g., securities) and the Hungarian paying agent cannot withhold the relevant tax, the taxable base would be assessed in the amount of the fair market value of the asset received multiplied by 1.18.

If the interest income is received from a Hungarian paying agent, such paying agent should withhold the PIT. If the interest income is not received from a paying agent, taxes should be assessed, declared and paid to the tax authority by the private individual himself in his regular annual tax return.

Payments distributed by or on behalf of a legal person or other organisation having its seat in a low tax jurisdiction\(^4\) are subject to PIT at a 15 per cent rate and the recipient should pay health tax of 22 per cent, in addition to the PIT. Please note, however, that the legislation does not provide for any adverse tax implications in respect of interest received from controlled foreign companies\(^5\) (CFC) in the future as the new definition of the low tax jurisdiction does not cover CFCs as of 1 January 2017.

\(^4\) Low tax jurisdiction means a state that refrains from imposing CIT or if the tax rate thereof is 9 per cent or lower, unless Hungary has concluded a Double Tax Convention with such state.

\(^5\) Under Hungarian tax legislation, CFGs are foreign persons not qualifying as foreign entrepreneurs or Hungarian resident taxpayers, in which the taxpayer (either on its own, or with its related parties) – directly or indirectly – holds more than 50 per cent interest (shareholdings or voting rights) or is entitled to a share of after-tax profit exceeding 50 per cent thereof in the financial year, in which the tax equivalent to the CIT paid by the foreign legal entity is less than the difference with which the CIT that it would have paid assuming that its seat were in Hungary exceeds the tax equivalent to the CIT paid by the foreign legal entity (i.e., CIT paid by the foreign person is less than 50 per cent of the Hungarian CIT that the foreign entity should have paid in Hungary if it were a Hungarian taxpayer). The Hungarian tax legislation also regards foreign permanent establishments of a Hungarian resident taxpayer to be a CFC if in the tax year, in which the tax paid by the foreign permanent establishment is less than the difference with which – assuming that the permanent establishment was located in Hungary – the CIT that it would have paid exceeds the tax equivalent to the CIT paid by the foreign permanent establishment. The foreign legal entity
Dividend
The dividend income of a Hungarian-resident private individual is subject to PIT at a rate of 15 per cent and health tax at the rate of 14 per cent in 2017 (the latter is capped at 450,000 forints per annum).

Dividend payments distributed by or on behalf of a legal person or other organisation having its seat in a low tax jurisdiction are subject to PIT at a 15 per cent rate and the recipient should pay health tax of 22 per cent in addition to PIT.

Capital gains
Capital gains realised by a Hungarian-resident private individual will be subject to PIT at a rate of 15 per cent and health tax at a rate of 14 per cent in 2017 (the latter is capped at 450,000 forints per annum).

Capital gains arising from the sale of shares in a legal person or other organisation having its seat in a low tax jurisdiction would be subject to PIT at 15 per cent and health tax at 22 per cent.

On certain conditions, preferential PIT rules may apply to income from the ‘controlled capital market transactions’ of private individuals.

Income from ‘controlled capital market transactions’ shall be calculated as the difference between the total profit and the total loss realised on transactions during the tax year. In 2017, a 15 per cent PIT rate would apply on that income. Because of the preferential tax treatment of ‘controlled capital market transactions’, the private individual could be entitled to tax compensation with respect to losses realised from controlled capital market transactions during the tax year, during the year preceding the current tax year and in the two years preceding the current tax year. Tax ‘calculated’ for such losses could reduce the taxes calculated on gains realised by the private individual from controlled capital market transactions during the tax year, during the year preceding the current tax year and in the two years preceding the current tax year.

Furthermore, in cases of transfer of shares in a Hungarian real estate holding company as defined by the Act LXXXI of 1996 on the Corporate Income Tax and Dividend Tax, a charge to Hungarian PIT (15 per cent) arises at the foreign shareholder in respect of any income triggered on the transfer of shares in a real estate holding company unless the applicable double tax convention excludes the taxation of such capital gains in Hungary.

Income from qualified long-term investments
Preferential tax rules may apply to income from ‘qualified long-term investments’ of private individuals.

Income derived from qualified long-term investments refers to the profit the private individual realises under a long-term investment contract entered into with an investment service provider or a credit institution. Under the long-term investment contract, the private individual places an amount equal to at least 25,000 forints on his or her account for a minimum period of three (and further two) years, and the parties agree on applying the preferential taxation rules laid down by the Act on PIT. If all the conditions prescribed by law

or the foreign permanent establishment should not be considered as a CFC if it carries on a substantive economic activity supported by staff, equipment, assets and premises, as evidenced by relevant facts and circumstances.
are fulfilled and the ‘qualified long-term investment’ is held for less than three years, for the 2017 tax year a 15 per cent rate may apply, while if the investment lasts at least three years, a preferential 10 per cent rate is applicable; income from qualified long-term investments would be subject to a zero per cent rate if the investment is held for at least five years. As of 1 January 2017, under certain conditions, the above beneficiary tax rules may also extend to foreign qualified long-term investments, where the investment service provider or the credit institution is not subject to Hungarian data disclosure requirements.

ii Inheritance tax and gift tax

The inheritance of assets located in Hungary would be subject to Hungarian inheritance tax regardless of the nationality of the heirs. If the inheritance is handed over during a probate action then the tax authority assesses the inheritance tax and informs the heirs regarding the tax payable.

The base of the inheritance tax and the gift tax is the net value of the inheritance or gift, which is the market value of properties inherited or gifted less any liabilities related to the inheritance or gift.

The generally applicable inheritance and gift tax rate is 18 per cent. However, a preferential 9 per cent tax rate applies to residential properties. In the case of vehicles, the inheritance and gift tax are double the transfer tax. Special rules apply in cases of inheritance of beneficiary ownership over real estate properties or rights with pecuniary value.

Hungarian legislation provides for exemption from inheritance and gift tax in several cases, such as the following:

- **a** as of 2014, succession and gift by and to lineal relatives or a spouse is exempt from inheritance and gift tax;
- **b** if the heir is a stepchild, step-parent, foster child or foster parent of the deceased, 20 million forints from the tax base qualifies as a tax-exempt inheritance;
- **c** the inheritance and gifting of debt securities issued by a European Economic Area (EEA) Member State;
- **d** inheritance that has been granted for scientific, artistic or educational purposes; and
- **e** if the heir or recipient undertakes to build a residential property within four years after the succession or gifting and the total territory of the flats in this residential property is at least 10 per cent of the maximum build-in territory, the inheritance or gifting of the land would be exempt from inheritance or gift tax. To become eligible for this exemption, the heir or recipient should file a statement to the tax authority. The tax authority will assess after four years whether the heir or recipient has fulfilled all obligations related to the tax exemption. In case of non-compliance, the heir or recipient should pay inheritance or gift tax, plus the amount of the late payment interest.

If the heir offers any fine art, applied art or folk art creation, or museum piece, collection or a part of it that he or she has inherited to the Hungarian state, municipality or higher education institution and it has been accepted by the recipient, then the inheritance or the offered part of the inheritance is exempt from inheritance tax.

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6 Act XCIII of 1990 on Duties.
In cases of underage heirs, the inheritance tax may be payable without any late payment interest until the end of the second calendar year from the date they have reached maturity. If the underage heirs pay their inheritance tax liability in advance then the amount of tax should be decreased by 10 per cent to 70 per cent.

In case of the inheritance of the ownership of arable land or rights with pecuniary value relating to the arable land, the applicable tax rate is half (and in certain cases one-quarter) of the general tax rate.

iii Transfer tax

Transfer tax is payable upon the acquisition of real estate property, moveable property on auctions, cars and trailers, rights of pecuniary value (e.g., rights related to real estate, cars), usufruct on real estates, building structures in public places and acquisition of securities by means of contract of inheritance.

Since 2010, the acquisition of shares in a real estate holding company is also subject to real estate transfer tax (RETT), provided that the ownership of the acquirer reaches 75 per cent of the company that holds the real estate in Hungary. Under transfer tax legislation, an entity should be regarded as a real estate holding company if the value of the real estate in Hungary owned by that entity exceeds 75 per cent of the total value of the assets (excluding liquid assets, monetary claims, accruals and loans) of the entity shown on the balance sheet that was most recently formally approved. An entity should also be regarded as a real estate holding entity if it holds directly or indirectly at least 75 per cent of shares in a company that fulfils the above conditions.

The standard rate of RETT is 4 per cent of the market value of the acquired real estate. If the market value of a real estate property exceeds 1 billion forints, the rate of the RETT on the exceeding part is 2 per cent, but the RETT liability is capped at 200 million forints per real estate property.

iv Property taxes

Building tax

Local municipalities may levy tax on buildings. The maximum of the building tax is either 1,100 forints per square metre (adjusted with cumulated inflation) or 3.6 per cent of the adjusted fair market value of building.

Land tax

Land tax may be levied by local municipalities on the owner of the land. The land tax is either charged annually based on the area of land owned, at a maximum rate of 200 forints per square metre (adjusted with cumulated inflation) or based on the adjusted fair market value of the land, at a maximum of 3 per cent.

v Preferential taxation regimes

Private individuals being subject to Hungarian PIT may opt for a preferential regime to apply to their tax liabilities with regard to certain types of income designated therein (e.g., interest,

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7 Act XCIII of 1990 on Duties.
dividend, capital gains, income from controlled capital market transactions, etc) earned by
them until 30 June 2016 according to the Hungarian PIT instead of the general rules laid out
in the Act on PIT and in the Act on Tax Procedures.

This regime applies a tax rate of 10 per cent. The tax payable is equal to the income
multiplied by the tax rate. The individual who has opted for the application of this regime shall
deposit the income with a bank having its seat in a Member State of EEA and designated for
the acceptance of such deposit by the National Tax and Customs Authority of Hungary. This
bank should settle the tax liabilities from the bank account to be opened for the fulfilment of
the aforementioned tax liabilities by 30 June 2017.

According to the rules of the Preferential Acquisition of Shares (PAS) regime, under
certain circumstances no tax liability arises from the acquisition of shares or other transferable
interests in legal entities or other organisations.

In order for the PAS regime to apply, at least 10 per cent of shares in a legal entity or
other organisation should be acquired by 30 June 2017. Such acquisition should also be
reported to the National Tax and Customs Authority of Hungary until the aforementioned
deadline. Once the taxpayer has acquired such shares in the above-mentioned way, it cannot
report such shares to the tax office in order to exempt the future alienation of shares from
Hungarian CIT by applying the reported participation regime.9

The provisions on stability savings accounts (SSAs)10 were repealed on 18 January 2017.
With regard to the tax liabilities concerning deposits on SSAs opened until the 30th day
following the promulgation of Act CLXXI of 2016 on the Modification of certain Acts on
Universal and Equal Taxation and on the Exercise of Functions of Public Bodies (thus until
18 January 2017), the rules on SSAs shall apply.

vi Hungarian Residence Government Bond11

To attract new investors to finance state debt, the Hungarian government introduced the
Hungarian Residence Government Bond (LMAK) scheme in 2012, which effectively began
its operation in 2013.

In exchange for purchasing LMAKs via investor companies, third-country individuals
may obtain a residence permit in Hungary under beneficial conditions. The scheme is quite
popular; more than 1,300 third-country individuals joined the programme in 2016.

LMAKs are issued by the Hungarian state, with a nominal value of €50,000 and for
a minimum period of five years. They are issued at a discounted price and redeemed at face
value at maturity.

The minimum yield of the bonds is at least 2 per cent. The bonds can be subscribed
only by licensed investor companies. These investor companies issue their own securities that
third-country individuals or an entity that is majority owned by the third-country individual
must purchase in the amount of €300,000 when applying for the national permanent
residence permit under this special regime.

9 If a taxpayer holds at least 10 per cent of the shares of an entity for at least one year and reported the
acquisition of the shares within 75 days of the date of the acquisition to the Hungarian tax authorities, the
shares qualify as ‘reported shares’. Any capital gain arose in relation to the alienation of such reported shares
should be exempt from Hungarian corporate income tax.
If the private individual acquires the residence permit by investment, then he or she would also be regarded as being resident in Hungary for PIT purposes and may benefit from the Hungarian PIT system.

The Hungarian Debt Management Agency stopped accepting requests for LMAKS on 31 March 2017, although the provisions on LMAKS are still in force.

III  SUCCESSION

i  Hungarian succession rules

The respective rules of Hungarian succession law are set out in the Civil Code. The main rule of Hungarian succession law is that the heirs acquire the inheritance by the mere fact of the death of the deceased person. Accordingly, the heirs become the owner of the properties at the time of death; however, they are not entitled to exercise their rights relating to the inheritance (e.g., to register their ownership in the land registry) until the notary public has rendered a binding resolution on the handover of the heritage during the probate action. Therefore, the aim of the probate action is to identify the properties of the deceased person and to clarify the inheritance relationships and make a resolution regarding the succession. In the event of any dispute concerning the resolution of the notary public, each of the interested persons could challenge the resolution before the court.

Under Hungarian law, the inheritance takes place either according to a disposition of property upon death or in accordance with the statutory rules. If there is a disposition of property upon death at hand it must prevail over the statutory regime. A disposition of property upon death could cover either the entire heritage or some part of the estate of the deceased person. If the disposition of property upon death does not cover the entire heritage, the statutory regime of inheritance applies in respect of the remaining parts.

Inheritance by disposition of property upon death

In case of the disposition of property upon death, the Civil Code provides for the formal requirements and the eligible terms of such dispositions. The Civil Code distinguishes between last will, contract of succession and donation upon death.

Besides the public will that is made in the presence of a notary, the Civil Code recognises private wills (including the holographic will and other forms of last wills made in writing) and oral wills. An oral will is valid only if a danger threatening the testator with death hinders him in making a last will in writing and if two witnesses are present. The Civil Code introduced a new feature to Hungarian succession law, namely the joint will. Under Hungarian law, only spouses may make a joint will.

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12 Act V of 2013 of the Civil Code.
13 Sections 7:1 and 7:87 of the Civil Code.
14 Section 7:3 (1) of the Civil Code.
15 Section 7:3 (2) of the Civil Code.
16 Section 7:10 of the Civil Code.
17 Section 7:30 of the Civil Code.
18 Sections 7:13 to 7:17 and 7:20 of the Civil Code.
19 Sections 7:20 and 7:21 of the Civil Code.
20 Section 7:23 of the Civil Code.
In the framework of a contract of succession, the testator makes a disposition of property upon death in favour of the other contracting party, while this other party is obliged to provide either maintenance or periodic payment of any other sum or services of care to the testator.\textsuperscript{21}

The rules on reserved share represent, however, a significant limitation to the autonomy of the testator. The descendants, the spouse or the registered partner and the parents of the deceased can claim their reserved share if they inherit in the absence of any disposition of property upon death.\textsuperscript{22}

**Inheritance by law**

Under the statutory regime of succession, the estate of the deceased must be distributed among his or her relatives and spouse or registered partner in accordance with the strict order of succession set out in the Civil Code. Children and their descendants constitute the first category, followed by the parents and their descendants.\textsuperscript{23} Then comes the category of grandparents and their descendants, which is followed by the category of great-grandparents and their descendants, and finally the ancestors of the great-grandparents.\textsuperscript{24} However, the category of grandparents and their descendants may inherit only if the spouse or the registered partner could not be the heir of the deceased.\textsuperscript{25} Relatives within a category inherit in equal shares.\textsuperscript{26}

Prior to the new rules of the Civil Code, the spouse or the registered partner was only able to inherit usufruct over the estate of the deceased. Under the new rules, if at least a child or a descendant of a child is an heir, both the spouse or the registered partner inherit usufruct over the residential property and its equipment used together with the deceased and a share of the rest of the inheritance corresponding with the share of a child.\textsuperscript{27} If there is neither child nor a descendant of a child, the spouse or the registered partner inherits the residential property and its equipment that was used together with the deceased, and half of the rest of the inheritance, while the parents of the deceased inherit the other half of the rest of the inheritance.\textsuperscript{28} If there is neither child nor descendant of a child nor parent, the spouse or the registered partner inherits the entire estate.\textsuperscript{29}

If the heir is not a descendant of the deceased, there is a special regime of succession with respect to the assets the deceased inherited or received as a gift either directly or indirectly (through his or her brother or sister or any of the descendants of the aforementioned).\textsuperscript{30} In this case, only those persons who provided the asset to the deceased or whose ancestor provided

\begin{itemize}
\item \textsuperscript{21} Section 7:48 (1) of the Civil Code.
\item \textsuperscript{22} Section 7:75 of the Civil Code.
\item \textsuperscript{23} Sections 7:55 (1) and (3), 7:63 (1) and (2) of the Civil Code.
\item \textsuperscript{24} Sections 7:64 (1) and (2), 7:65 (1) and (2) and 7:66 of the Civil Code.
\item \textsuperscript{25} Section 7:64 (1) of the Civil Code.
\item \textsuperscript{26} Sections 7:55 (2), 7:63 (1), 7:64 (1), 7:65 (1) and 7:66 of the Civil Code.
\item \textsuperscript{27} Section 7:58 (1) of the Civil Code.
\item \textsuperscript{28} Section 7:60 of the Civil Code.
\item \textsuperscript{29} Section 7:61 of the Civil Code.
\item \textsuperscript{30} Section 7:67 (1) and (2) of the Civil Code.
\end{itemize}

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the asset to the deceased can inherit. The spouse or the registered partner has usufruct over the respective assets in this case.\footnote{Section 7:69 (1) of the Civil Code.} If no one can inherit the assets under this regime, the general rules of inheritance by law apply.\footnote{Section 7:68 (3) of the Civil Code.}

ii Matrimonial issues
The respective Hungarian rules of matrimonial property are set out in the Civil Code. The basic rule is that unless the spouses conclude a matrimonial property agreement, the rules of the statutory matrimonial property regime prevail.\footnote{Section 4:34 (2) of the Civil Code.}

The statutory matrimonial property regime
The rules of the statutory matrimonial property regime apply only during the life of the spouses as a couple in the same household once they have concluded a marriage.\footnote{Section 4:35 (1) of the Civil Code.} These rules no longer apply if: (1) the spouses conclude a matrimonial property agreement; (2) the court terminates the matrimonial common property during the spouses’ life as a couple; or (3) the spouses no longer live together.\footnote{Section 4:53 of the Civil Code.}

Under the statutory matrimonial property regime, the assets the spouses had before their marriage belong to their own separate estates.\footnote{Section 4:38 (1) (a) of the Civil Code.} Additionally, \textit{inter alia}, the assets inherited or received as a gift, IP rights and the surrogate of the assets belonging to the separate estate constitute the parts of the spouses’ separate estates.\footnote{Sections 4:38 (1) (b), (c) and (f) of the Civil Code.} The assets acquired during the spouses’ life as a couple constitutes common property.\footnote{Section 4:37 (1) (a) of the Civil Code.} Both of the spouses may use the common property and manage and administer these assets together.\footnote{Section 4:42 (1) and (2) of the Civil Code.} This rule has limited application in respect to shares, shareholdings and the assets necessary for the business or other profession of one of the spouses.\footnote{Section 4:43 of the Civil Code.} Under this regime, each spouse is liable to third parties for the performance and the breach of any contracts concerning any common property limited to their shares in the common property.\footnote{Section 4:49 of the Civil Code.}

Matrimonial property agreements
The Civil Code contains two types of model rules in respect of matrimonial property agreements. This means that unless a mandatory rule prohibits the derogation from these rules, the parties could agree otherwise.\footnote{Section 4:63 (2) of the Civil Code.} The spouses could limit their liability with respect to their common property towards third parties under the matrimonial property agreement if they register the agreement in the appropriate registry.\footnote{Section 4:65 (2) of the Civil Code.}
Under one model regime, both of the spouses have their own separate estates and each of them is entitled to half of the assets acquired during their life as a couple.\textsuperscript{44} Under the other model regime, both of the spouses have their own separate estates and they have to bear only the costs of the common household and the education of the children together.\textsuperscript{45} Deviation from the obligation to bear these costs is not allowed.\textsuperscript{46}

**Partners and registered partners**

The assets of partners living together outside marriage remain their own separate estates, and upon the end of their relationship as a couple, each of them can claim a part of the assets acquired during their life as a couple corresponding to the respective partner’s contribution in the acquisition of those assets.\textsuperscript{47} The partners can deviate from these rules by an agreement.\textsuperscript{48}

Although same-sex marriage is not available in Hungary, homosexual couples may register their relationship as set out in the Registered Partnership Act.\textsuperscript{49} The rules of succession and matrimonial property applicable in respect to marriage and spouses also apply to the registered partnership and registered partners.\textsuperscript{50}

**IV WEALTH STRUCTURING & REGULATION**

**i Hungarian trusts**

The Civil Code provides for new rules for Hungarian trusts and private foundations, although the latter seems to be less suitable for wealth structuring.\textsuperscript{51} Nevertheless, the introduction of the new Hungarian rules on trusts represents dramatic improvements in wealth structuring.\textsuperscript{52} While the Civil Code contains the rules on the relationship between the settlor, the trustee and the beneficiary, the Trustees Act provides for the regulatory framework for providing such services.

**The relationship between the settlor, the trustee and the beneficiary**

The Civil Code sets out the rules on trusts within the rules of contract law. The Civil Code provides that the parties are free to deviate from the rules of contract law regarding their rights and obligations, unless the statute does not allow any derogation.\textsuperscript{53} Hence, the statutory rules of trust as set out in the Civil Code are mostly model rules.\textsuperscript{54} There are five trust-specific mandatory rules where a derogation is not allowed:

\begin{itemize}
  \item [a] the trust arrangement needs to be in writing;
\end{itemize}

\textsuperscript{44} Sections 4:69 – 4:71 (2) of the Civil Code.
\textsuperscript{45} Sections 4:72 – 4:73 (2) of the Civil Code.
\textsuperscript{46} Section 4:73 (2) of the Civil Code.
\textsuperscript{47} Section 6:516 of the Civil Code.
\textsuperscript{48} Section 6:515 of the Civil Code.
\textsuperscript{49} Act XXIX of 2009 on the Registered Partnership.
\textsuperscript{50} Section 3 (1) of the Registered Partnership Act.
\textsuperscript{52} The Civil Code and Act XV of 2014 on the Trustees and the Rules of Their Activities.
\textsuperscript{53} Section 6:59 (2) of the Civil Code.
\textsuperscript{54} A Menyhei, ‘Development of the estate planning industry through the introduction of the trust in Hungary’ (2016) 22 **Trusts & Trustees** 659, 662.
the trustee should not be the sole beneficiary;
c the trust assets need to be separated from the trustee’s own assets and other trust assets;
d neither the settlor nor the beneficiary may give instructions to the trustee; and
e the term of the trust arrangement may not exceed 50 years.55

A trust arrangement could be established either by a contract between the settlor and the trustee or by a unilateral declaration of the settlor or by a testament.56

In the framework of the trust under Hungarian law, the settlor transfers the title of the property or assigns rights and claims to the trustee. The trustee is obliged to manage the transferred trust assets in his or her own name and for the benefit of the beneficiary, while the settlor shall pay a fee for the trust management to the trustee.57 The beneficiary may claim the distribution of the trust assets and their profits in accordance with the trust deed.58

Under the trust arrangement, the trustee is obliged to act for the utmost benefit of the beneficiary’s interests in accordance with the fiduciary nature of the trust.59 The trustee is liable for the trust assets as well as the performance of the obligations incurred.60 The trustee could dispose over the trust assets in accordance with the terms specified in the trust deed.61 The trustee has the right to remuneration and reimbursement in respect to the expenditures out of the trust assets.62

One of the major issues of trusts is the position of the creditors. The creditors of the trustee may not enforce any claim against the trust assets and the trust assets do not belong to the inheritance of the trustee.63 The creditors of the beneficiary may enforce claims on the trust assets only if the trustee’s obligation to transfer the trust assets to the beneficiary is due.64 The creditors of the settlor can pursue claims against the trust assets only if the settlor aimed at avoiding payment of the debts in question by setting up the trust.65

Moreover, tracing is one of the most significant issues that the law needs to address with regard to trusts. Under Hungarian law, if the trustee was in breach of the trust deed by alienating or encumbering the trust assets, the settlor and the beneficiary could claim from third parties, who were not in good faith or acquired the assets free of charge, the transfer of the assets back to the trust assets.66 The trust terminates if:
a the trust assets cease to exist;
b the trustee gives notice;
c there is no trustee with respect to the trust assets for a period exceeding three months;
d the settlor is the sole beneficiary in the event that the settlor dies;

56 Sections 6:310 (1) and 6:329 (1) and (2) of the Civil Code.
57 Section 6:310 (1) of the Civil Code.
58 Section 6:314 (1) of the Civil Code.
59 Section 6:317 (1) of the Civil Code.
60 Section 6:323 (1) of the Civil Code.
61 Section 6:318 (2) of the Civil Code.
62 Section 6:322 (2) of the Civil Code.
63 Section 6:313 (1) of the Civil Code.
64 Section 6:314 (2) of the Civil Code.
65 Section 6:120 of the Civil Code.
66 Section 6:318 (3) of the Civil Code.
The settlor gives notice with regard to a contract entered into for an indefinite period; or 50 years have passed since the establishment of the trust.

It is not sufficient grounds to terminate the trust if the settlor becomes the legal successor of the trustee. In the event that any of the settlors, the trustee or the beneficiary dies or ceases to exist, the trust would still continue to exist.

Taking account of the above model rules, it was concluded in the academic literature that the concept of trust under Hungarian law corresponds with the definition of trust as defined in the Hague Convention on the Law Applicable to Trusts and Their Recognition.

**Regulatory framework of trusts**

The Trustees Act provides specifically for licensing, notification and registration requirements.

To accept the appointment of a trustee at least twice a year or on a business scale, a licence from the National Bank of Hungary (MNB) is necessary. Such a licensed trustee could be a limited liability company, a joint stock company or the branch of an EEA undertaking. The licensed trustee needs to meet certain transparency criteria and must have registered capital of at least 70 million forints. Additionally, the licensed trustee must have financial collateral of a value corresponding to at least 20 per cent of the trust assets, but ranging from 70 million to 1.5 billion forints. The legislation also prescribes conditions with respect to the managing directors of the trustee.

In the event that the trustee accepts the appointment on an ad hoc basis and not on a business scale, the trustee is merely required to notify the MNB.

**Taxation of trusts**

As a general rule, the transfer of the assets between the settlor and the trustee is tax-neutral as it does not trigger any tax liability in Hungary: any properties (e.g., real estate, shares in a company) can be transferred into the trust without incurring any tax obligations, which may arise only when the assets and their yields are allotted to the beneficiaries.

For corporate income tax purposes, the trust assets (managed assets) are considered a corporate income taxpayer. This means that any tax benefits granted to Hungarian tax-resident entities are also available for trust assets. Therefore, trusts can be used for various purposes.

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67 Sections 6:326 (1) and (3) of the Civil Code.
68 Section 6:326 (4) of the Civil Code.
69 Section 6:326 (5) of the Civil Code.
70 The Hague Convention on the Law Applicable to Trusts and on Their Recognition (1985); A Menyhei, 'Development of the estate planning industry through the introduction of the trust in Hungary' (2016) 22 Trusts & Trustees 659, 661.
71 Section 3 (1) of the Trustees Act.
72 Section 3 (1) and 7 (2) of the Trustees Act.
73 Section 2 (1) of the Decree of the Government No. 87 of 20 March 2014 on Certain Rules on the Financial Collaterals of Trustee Undertakings.
74 Section 19 of the Trustees Act.
76 Section 17/D (2) of the Act XCIII of 1990 on Stamp Duties.
77 Section 2 (6) of the Act LXXI of 1996 on Corporate Tax and Dividend Tax.
domestic and international tax planning purposes (e.g., making use of favourable rules of holding regimes, tax-neutral company restructurings, asset transfers, eliminating related party classifications).

In cases of distribution, the managed assets must be categorised as capital and yield. If the trustee distributes the capital to a beneficiary, a gift tax liability may arise, unless the beneficiary is the settlor or the spouse or a lineal relative of the settlor. If the yield of assets is distributed to the beneficiary, the beneficiary is obliged to pay PIT in accordance with the rules applicable to dividends.78

**Fields of use**

Besides tax planning opportunities, trusts may be used for several purposes, such as:

a) maintaining and preserving family businesses combined with professional asset management expertise to be able to continue the family business successfully;

b) deviating from statutory inheritance rules as an alternative and more flexible solution to testaments (e.g., for avoiding collisions in case of cross-border scenarios);

c) protecting the estate against potential future creditors;

d) providing representation for the beneficiaries;

e) establishing joint ventures and performing share acquisitions for collateral purposes;

and

f) safeguarding business secrets.

**V CONCLUSIONS & OUTLOOK**

Based on the above developments, it is clear that Hungary has made a great leap towards being an attractive location for high net worth individuals. The legislation is designed to facilitate third-country individuals moving to Hungary under beneficial conditions and obtaining tax-resident status in Hungary benefiting from the Hungarian tax regime. The Hungarian tax environment also provides considerable opportunities for voluntary disclosures. In addition, the new Hungarian trust represents a significant improvement in terms of private wealth management and for the private wealth industry in Hungary, and could be a stimulus for the Hungarian economy.

Besides domestic legislative changes, Hungary is very much exposed to international trends, such as OECD BEPS, AEOI and EU anti-avoidance, and it has recently changed its IP box regime to be aligned with the OECD BEPS approach. In 2014, Hungary ratified the Convention on Mutual Administrative Assistance in Tax Matters along with the Protocol amending the Convention.79 Furthermore, in 2015, Hungary became a party to the Multilateral Competent Authority Agreement on Automatic Exchange of Financial Accounts.

78 Section 66 (1) (a) (ae) of the Act of CXVII of 1995 on Personal Income Tax.
Hungary

Information, 80 implemented the DAC2 Directive 81 and the 4th AML Directive. 82 Hungary is also among the signatories to the Multilateral Convention to Implement Tax Treaty Related Measures to Prevent Base Erosion and Profit Shifting (MLI) and is committed to implement the MLI minimum standards into its bilateral tax treaties. In addition, in compliance with the Council Directive (EU) 2016/1164 of 12 July 2016 laying down rules against tax avoidance practices that directly affect the functioning of the internal market (ATAD), Hungary has already modified its regulation regarding CFCs and – except for the interest limitation rules83 – it aims at transposing the other anti-avoidance measures of ATAD in 2018.

80 Act CXC of 2015 on the Promulgation of the Multilateral Competent Authority Agreement on Automatic Exchange of Financial Accounts Information. Hungary will exchange financial account information (such as data identifying the beneficiary owner, data on the assets and revenues, etc.) with the following countries: Andorra, Argentina, Australia, Austria, Belgium, Brazil, Bulgaria, Canada, Colombia, Croatia, Cyprus, Czech Republic, Denmark, Estonia, Faroe Islands, Finland, France, Germany, Gibraltar, Greece, Greenland, Guernsey, Iceland, India, Ireland, Isle of Man, Italy, Japan, Jersey, Korea, Latvia, Liechtenstein, Lithuania, Luxembourg, Malta, Mauritius, Mexico, Monaco, Netherlands, Norway, Poland, Portugal, Romania, San Marino, Seychelles, Slovak Republic, Slovenia, South Africa, Spain, Sweden, Switzerland, United Kingdom. The first exchanges are scheduled to take place in September 2017 (except for some countries, e.g., Australia, Brazil, Canada, Japan, which first intend to exchange information by September 2018).


83 As regards the interest limitation rules, Hungary intends to maintain its current thin capitalisation regime until 31 December 2023 if the European Commission acknowledges that the Hungarian thin capitalisation rules are equally effective to the interest limitation rule set out in the ATAD.
ITALY

Nicola Saccardo

I INTRODUCTION

Italy is home to individuals of considerable wealth. In particular, medium and large businesses in Italy tend to be owned and managed by Italian families who need advice on the structuring of the generational transfer of the business. Furthermore, Italy attracts foreigners that relocate to Italy under the Italian forfait tax regime for individuals moving to Italy (see Section II, iv). Italy also attracts significant investments, including those in Italian real estate, by non-resident private clients, who need advice on the structuring of the acquisition, ownership and disposal of such investments.

II TAX

i Income tax

Residents are subject to income tax on their worldwide income, including capital gains. Non-residents are subject to income only on their Italian-sourced income.

For income tax purposes, an individual is regarded as a resident of Italy if, for most of the tax period (i.e., the calendar year), he or she is registered with the Official Register of Italian residents, has his or her habitual abode in Italy, or has the main seat of his or her business and interests in Italy (similar to the Organisation for Economic Co-operation and Development (OECD) concept of a ‘centre of vital interests’).

The total taxable income of individuals is subject to income tax at progressive rates up to 43 per cent, plus local surcharges that depend on the municipality of residence.

That said, income from financial assets, as well as capital gains upon the sale of such assets, is generally taxed in the hands of individuals at a flat rate of 26 per cent (12.5 per cent on the interest and capital gains on Italian governmental bonds and bonds issued by foreign states providing for exchange of information). This favourable regime does not, however, apply to dividends and capital gains from substantial participations in companies and partnerships (in general terms, more than 20 per cent ownership) of which 58.14 per cent of their total are subject to tax at progressive rates. Nor does it apply to dividends and capital gains from participations in unlisted companies and partnerships established in blacklisted jurisdictions, which are entirely liable to tax.

1 Nicola Saccardo is a partner at Maisto e Associati.
Capital losses on financial assets can offset capital gains of the same category and can be carried forward for five years. Furthermore, an optional regime is available whereby capital gains and losses on certain financial assets are taxed on an accrual – rather than cash – basis and certain income from financial assets may be offset by these accrued capital losses.

Capital gains realised by individuals upon the sale of real estate, either owned for more than five years or inherited, are generally exempt from income tax. Furthermore, Italy does not tax capital gains realised by individuals upon the sale of assets other than financial assets and real estate (such as paintings or statues) unless such gains are realised in the context of a business or of a professional activity (or of a speculative transaction).

Resident individuals are subject to reporting obligations on foreign-held assets. Since 2013 these obligations apply also to foreign-held assets held by companies, partnerships, trusts, foundations and other entities, to the extent that the resident individual qualifies as the beneficial owner for Italian anti-money laundering purposes. The broadening of the definition of beneficial owner, due to the implementation of the EU Directive 2015/849 of 20 May 2015, has triggered the broadening of the scope of these reporting obligations. Failure to comply with these reporting obligations may result in very severe penalties.

Controlled foreign corporation (CFC) rules may apply to companies, partnerships or other entities established in jurisdictions (other than EU Member States and EEA Member States providing for exchange of information) where the nominal tax rate is lower than 50 per cent of the Italian nominal tax rate. They may apply also to companies, partnerships or other entities established outside the above jurisdictions if the CFC is controlled by an Italian resident, is subject to a foreign effective tax rate lower than 50 per cent of the effective tax rate that would have applied if the CFC were resident of Italy, and derives revenues that are, for more than 50 per cent, either passive or from intra-group services.

Italy does not have a part-year residence rule. Indeed, in any calendar year, an individual either is or is not a resident for the whole year. Consequently, if an individual moves to Italy in the second half of the calendar year, he or she will be regarded as non-resident in the year of transfer because the conditions for tax residence will not be met for most of the tax period. This feature of the Italian tax system may allow for the optimisation of the tax regime upon transfer of residence. On the other hand, if an individual moves to Italy in the first half of the calendar year, he or she will be regarded as resident for the whole year of transfer.

Finally, no exit tax is levied on individuals (the exception being for assets held in the capacity of entrepreneur).

ii Inheritance and gift tax

Inheritance and gift tax is levied on worldwide assets if the deceased or donor had his or her habitual abode in Italy on the date of demise or gift, otherwise it applies only to Italian situs assets.

In particular, transfers upon death and gifts are subject to inheritance and gift tax at the following rates and with the following exempt amounts:

- **a** 4 per cent, if the transfer is made to spouses and direct descendants or ancestors; here, the transfer is subject to tax on the value exceeding €1 million (this exempt amount applies to each beneficiary);
- **b** 6 per cent, if the transfer is made to brothers and sisters; here, the transfer is subject to tax on the value exceeding €100,000 (this exempt amount applies to each beneficiary);
6 per cent, if the transfer is made to relatives up to the fourth degree, to persons related by direct affinity as well as to persons related by collateral affinity up to the third degree; and

8 per cent, in all other cases.

Same-sex civil unions have been recently introduced under Italian civil law (same-sex marriages or civil unions executed abroad have been assimilated to Italian same-sex civil union). Such introduction has the effect of making them subject to the same tax regime (e.g., rates and exempt amount) applicable to marriages.

The rules for the calculation of the taxable base may be extremely favourable. For instance, the value of unlisted participations in companies or partnerships is generally equal to the corresponding quota of the book net equity of the company or partnership resulting from the latest balance sheet drawn up pursuant to the applicable law. The value of the Italian real estate is, in principle, equal to its fair market value, but the tax office cannot dispute the value declared if it is at least equal to the value resulting from the cadastral registers, which is generally much lower than the fair market value.

Exemptions from inheritance and gift tax may apply to assets of cultural value, while Italian governmental bonds are free from inheritance tax.

An exemption from inheritance and gift tax applies to the transfer of businesses and participations in companies and partnerships to spouses or descendants.

For participations in Italian-resident companies, the exemption is subject to the additional condition that the recipient acquires or reaches a controlling shareholding. The control must be retained for five years following the transfer, otherwise the exemption will be clawed back. The tax authorities have clarified that the exemption would apply to the transfer of a controlling shareholding in joint ownership to a spouse or descendants and may apply to the settlement of a controlling shareholding into a trust for their exclusive benefit. For instance, if an individual holding a 60 per cent participation in an Italian-resident company were to transfer a 30 per cent participation to each of his or her two children, the exemption would not apply. On the other hand, the settlement of the 60 per cent participation into a trust for the exclusive benefit of the two children would qualify for the exemption, provided that the trust was properly structured.

The application of the exemption to non-resident companies is a source of debate. According to one interpretation, the exemption is not available to non-resident companies, which would conflict with EU law, where applicable. According to a second interpretation, the exemption applies to non-resident companies irrespective of the control condition. According to a third interpretation, the exemption applies to non-resident companies under the same control condition applicable to resident companies. In a private ruling dated 2 August 2011, the tax authorities held the third interpretation to be the case.

Finally, individuals who are subject to Italian inheritance and gift tax on their worldwide assets can benefit from the Italian inheritance, estate and gift tax treaties, which may preclude the levy of more burdensome taxes in other jurisdictions. Treaties for the avoidance of double taxation on inheritance and estate tax are in force with Denmark, France, Greece, Israel, Sweden, the United Kingdom and the United States. The treaty with France also covers gift tax. For instance, a UK-domiciled or deemed domiciled individual may transfer his or her habitual abode to Italy and become immediately exposed to Italian inheritance tax on his or her worldwide estate, but, as a consequence, he or she becomes treaty protected from UK inheritance tax on non-UK-situs assets.
Wealth taxes

Italian legislation does not provide for a comprehensive wealth tax. In very general terms, wealth taxes apply at proportional rates to the following:

a  Financial assets held in Italy: foreign assets deposited with an Italian financial intermediary should be regarded as assets held in Italy for the purpose of wealth taxes provision. The annual rate is 0.2 per cent. The taxable base is calculated on the basis of the value of the assets laid down in the periodic reports issued by the Italian financial intermediary with which the assets are deposited. Current accounts are subject to tax at a fixed negligible amount.

b  Financial assets held abroad by resident individuals: the annual rate is 0.2 per cent. The taxable base depends on the type of financial asset. In general terms, the taxable base is the trading value for listed assets. In other cases, the taxable base is generally the nominal value. Current accounts are subject to tax at a fixed negligible amount.

c  Real estate located abroad held by resident individuals: the annual rate is 0.76 per cent. The taxable base is generally equal to the purchase price of the real estate, but if the real estate is located in an EU or EEA Member State providing for exchange of information, the taxable base is equal to the value resulting from foreign cadastral registers or other deemed value relevant to foreign income, wealth or transfer taxes and, in the absence of such value, is generally equal to the purchase price.

Another tax applies on the value of Italian real estate, calculated on the basis of the value resulting from the cadastral registers. Favourable tax regimes may apply to, for example, the main abode.

New forfait tax regime for individuals moving to Italy

The Budget Law 2017, which entered into force on January 1, 2017, introduced a special forfait tax regime (the substitute tax regime) for individuals who transfer their tax residence to Italy. This regime is meant to attract high net worth individuals to Italy.

The conditions for the substitute tax regime

The option for the substitute tax regime is available to individuals (whether Italian or foreign nationals) who acquire Italian tax residence. The substitute tax regime is subject to the following conditions:

a  The individual must have been non-resident of Italy for Italian tax purposes in at least nine of the 10 years prior to the first year of effect of the option.

b  The individual must opt for the aforementioned substitute tax option in the annual tax return.

The substitute tax regime

The substitute tax regime is as follows:

a  All foreign-source income and gains are subject to a substitute tax (in lieu of the levy of income tax according to general rules) equal to €100,000 per year (such income and gains are not subject to any additional taxation if remitted to Italy).

b  Foreign assets are not subject to wealth taxes.

c  Foreign assets are not subject to inheritance and gift tax.

d  Foreign assets are not subject to reporting obligations.
As an exception, foreign-source capital gains on substantial shareholdings realised in the first five years of Italian tax residence are subject to income tax according to general rules. As a consequence, during such five-year period, substantial shareholdings are subject to reporting obligations.

The individual can opt for one or more foreign states to be excluded from the scope of the substitute tax regime.

**The duration of the substitute tax regime**

The option for the substitute tax regime is effective up to a maximum period of 15 years. The option can be revoked by the individual but, if revoked, is no longer available.

**The possible extension to relatives**

The substitute tax regime can be extended to one or more qualifying family members against the payment of an annual substitute tax of €25,000 (rather than €100,000) per family member benefiting from such a regime. Therefore, if for example, two spouses transfer their tax residence to Italy and both of them wish to benefit from the substitute tax regime, the overall annual substitute tax would be €125,000.

**Optional ruling procedure**

A ruling on the application of the substitute tax regime may be requested, even prior to the transfer of tax residence to Italy, to an ad hoc office of the Italian tax authorities.

### III SUCCESSION

**Applicable law**

Italian international private law dealing with successions are laid down in EU Regulation No. 650 of 4 July 2012. The Regulation provides for the general rule whereby the law applicable to the succession as a whole will be the law of the state of habitual residence of the deceased at the date of death. In limited circumstances, the law of the state the deceased was manifestly more closely connected with at the date of death will apply. An individual can, however, opt for the succession law of the state whose nationality he or she possesses either upon the exercise of the option or upon death. In a case of multiple nationalities, the individual can choose the law of any of the states whose nationality he or she possesses. The conflict of law rules provided by the chosen law will not apply.

**Forced heirship rules and succession agreements**

Italian succession law provides for forced heirship rules.

The reserved quota of the estate, which is reserved to forced heirs and therefore cannot be freely disposed of, depends on the composition of the family of the deceased upon death. For instance, if the spouse and three children are the forced heirs, 50 per cent of the estate of the deceased is the reserved quota for the children, to be divided in equal shares. In this case, the reserved quota for the spouse is equal to 25 per cent of the estate of the deceased, while the remaining 25 per cent of the estate can be freely disposed of.

For the purposes of calculating the reserved quota, the value of the estate of the deceased is equal to the value of all the assets owned at the time of death, net of any debts, plus the value of all assets that were gifted by the deceased during his or her life.
Italian law provides for the discretionary right of the forced heirs to claim the ‘reduction’ of the transfers made during lifetime or by way of will that prejudice their reserved quota. This clawback action – ‘reduction action’ – if exercised, is aimed at making transfers in excess of the disposable quota partially or totally ineffective. The transfers will remain fully valid and effective should the forced heirs not exercise the reduction action.

Succession agreements are null and void under Italian law, so that an individual cannot waive, or in any other way dispose of, his or her rights, including forced heirship rights, under a future succession.

The ban on succession agreements has only one exception: under a family pact a business, or a qualifying participation in a company carrying on a business, can be transferred to descendants under an agreement between all the living forced heirs, whereby the forced heirs, not receiving their share of the business or of the qualifying participation, may either be granted a cash amount or other assets by the transferees, or renounce, in whole or part, their reserved quota. It is fair to say that the family pact has not been widely used.

IV WEALTH STRUCTURING & REGULATION

i Trusts

Despite the fact that Italy is a civil law jurisdiction, trusts are widely used, particularly for the purpose of governing the generational transfer of businesses. In this context, the use of trusts may also achieve the exemption from inheritance and gift tax for the transfer of a controlling shareholding (see Section II.ii, supra).

Recognition of foreign trusts

Italian civil law does not regulate trusts, but trusts regulated by foreign laws are recognised in Italy pursuant to the Hague Convention on the Law Applicable to Trusts and on their Recognition, which was ratified by Italy in 1989. Furthermore, in 2016, specific civil law provisions have been introduced to regulate trusts created for the benefit of individuals with qualifying disabilities. In any event, the settlement of assets into a trust is considered a gift from a succession law perspective, therefore it is relevant to the calculation of the value of the estate of the deceased for the purpose of calculating the reserved quota (see Section III. ii, supra).

The issue of the recognition of ‘domestic trusts’ has arisen. The far prevailing case law has taken the view that domestic trusts must be recognised to the extent that they pursue a legitimate interest, but no explicit judgment of the Supreme Court has ever been issued on this specific point.

Tax regime of trusts

Opaque trusts

Income tax provisions recognise trusts as taxable persons for corporate income tax purposes, subject to the comments below on transparent and disregarded trusts.

A trust qualifies as resident if either its seat of management (similar to the OECD’s notion of a ‘place of effective management’) or its main object (the place where the day-by-day activities mainly take place) are located in Italy for most of the tax period. Deeming rules

2 Trusts whose settlor, beneficiaries and trust property are closely connected with Italy.
may apply to trusts established in jurisdictions not providing for exchange of information. Furthermore, the tax authorities take the view that, if a trust holds only real estate and such real estate is located mainly in Italy, its main object is located in Italy, and, accordingly, the trust is resident in Italy.\(^3\)

Under the assumption that a trust, resident or otherwise, does not carry out a business activity, it may benefit from the 12.5 or 26 per cent final withholding taxes or substitute taxes on income and capital gains from financial assets that would apply to individuals (see Section II.i, supra) and from the exemption from income tax on capital gains on real estate owned for more than five years. Furthermore, anti-avoidance provisions targeting the use of business assets by shareholders or partners or the use of dummy companies or partnerships do not apply to trusts.

**Transparent trusts**

Income tax law provides for a sort of transparency regime for trusts that have ‘identified beneficiaries’. The income imputed to the identified beneficiaries qualifies as income from capital and is subject to progressive tax rates if the beneficiaries are individuals. A beneficiary qualifies as an ‘identified beneficiary’ to the extent that he or she holds a current unconditional right to claim a share of the income generated by the assets held in trust; for example, the whole or a percentage of the income of the trust or the income from certain assets held in trust.

**Disregarded trusts**

Revocable trusts are disregarded for income tax purposes so that the income from the trust assets is imputed directly to the settlor. Furthermore, the income can be imputed directly to the settlor or the beneficiaries should the overall analysis show that either the settlor or the beneficiaries have a power or de facto control or influence to manage the trust assets or dispose of either the assets held in trust or the income from such assets. In these cases, the income is subject to tax as if it were cashed directly by the settlor or the beneficiaries. In Circular No. 61 of 27 December 2010, the tax authorities provided a non-exhaustive list of examples of disregarded trusts, including trusts that can be terminated by the settlor or the beneficiaries, trusts where the beneficiaries have a right to receive advancement of capital and trusts where the settlor has the power to change the beneficiaries. Also, the power of the settlor to revoke the trustee may be one of the factors leading to the trust being disregarded by the tax authorities.\(^4\)

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3 Circular No. 48 of 6 August 2007.

4 This approach was rejected by the provincial tax court of Novara, judgment No. 73/06/13 deposited on 21 May 2013. More recently, another first degree local court (Provincial tax court of Varese, Chamber 3, judgment No. 305 of 28 May 2015) rejected the assessment of the tax authorities. In particular, the tax authorities claimed that a trust was to be disregarded on the ground that the protector had significant powers, the protector and the beneficiaries had, by way of a joint decision, the power to remove and appoint the trustee ad nutum, and the trustee was entitled to a limited remuneration. On that occasion, the court held that such elements were not sufficient to disregard the trust.
Distributions of income to the beneficiaries

The tax authorities clarified that distributions of income from resident opaque trusts are not subject to income tax in the hands of the beneficiaries since the income has already been subject to tax at the level of the trust.  

On the other hand, the income tax regime for distributions of income, including capital gains and accumulated income and capital gains, from a non-resident opaque trust with foreign-sourced income to an Italian-resident beneficiary is not clear.

The distributions of income are not relevant to income tax to the extent that the trust is either transparent or disregarded.

Inheritance and gift tax

Following the 2006 reform of inheritance and gift tax, the tax authorities hold that inheritance and gift tax will be due by the trustee at the time of the addition of the assets to the trust fund and that the applicable rate and the possible exempt amounts are calculated by making reference to the relationship between the settlor and the beneficiaries (this approach to levy inheritance and gift tax on the addition to the trust fund has been upheld, with reference to trusts created after the 2006 reform of inheritance and gift tax, by the majority decisions of the Supreme Court; in judgment No. 3886 of 25 February 2015, the Court also upheld the view of the tax authorities that, to the extent that the settlor is a beneficiary, the applicable gift tax rate is the highest 8 per cent rate). In certain instances, however, favourable inheritance and gift tax rates and exempt amounts may not be effectively benefited from. For instance, in the event of a discretionary trust having a class of beneficiaries with different degrees of family relationship with the settlor, the highest rate will apply as the capital may be wholly distributed to the family member that qualifies for the highest rate. Exemptions from inheritance and gift tax for the transfer of businesses and participations in companies and partnerships to the spouse or descendants may be feasible (see Section II.ii, supra). From an income tax perspective, the transfer of assets from the settlor to the trustee does not trigger the taxation of the latent gains and the tax basis is rolled over to the transferee.

The tax authorities have further stated that distributions to the beneficiaries will not be a taxable event for inheritance and gift tax purposes, since inheritance and gift tax was applied at the time of the addition to the trust fund was made. However, according to the Supreme Court (decisions Nos. 25478, 25479 and 25480 of 18 December 2015), to the extent that the addition to the trust fund occurred prior to the 2006 reform of inheritance and gift tax, the distributions to the beneficiaries should be a taxable event, since the addition of assets to the trust fund was not a taxable event prior to the 2006 reform.

Life insurance policies

Life insurance policies are widely used thanks to the high flexibility they grant to the policyholder, who can wholly or partly redeem the policy or change the beneficiaries at any time. From an income tax perspective, the income is not taxed until either redemption or death of the insured. In the event of redemption or death, the income is subject to a 26 per cent tax (12.5 per cent to the extent that the income on the underlying capital consists of interest and capital gains on Italian governmental bonds and bonds issued by foreign states providing for exchange of information). The income is equal to the difference between the

amount received and the premiums paid (so that the policy allows the full set-off of the underlying income, gains and losses); however, in case of death, the beneficiary is exempt from tax on the portion of the income attributable to the life risk component. Finally, transfer to the beneficiary upon the death of the insured is not **mortis causa**, since the beneficiary has a direct entitlement to the underlying capital, and, accordingly, is not subject to inheritance tax.

### iii  Gift with reservation of usufruct

The gift of bare ownership with the reservation of usufruct allows the donor, usufruct holder, to continue to enjoy the use of the asset and the income therefrom for his or her lifetime. To the extent that the asset is a shareholding the donor may also retain the voting rights. Gift tax is levied on the value of the bare ownership only. Such value is calculated on the basis of percentages provided by tax legislation and based on the age of the usufruct holder. Upon the death of the usufruct holder, the usufruct is extinguished and the bare owner becomes the full owner of the assets, but the consolidation of bare ownership with usufruct does not qualify as a **mortis causa** transfer under the Italian civil law. Therefore, it does not trigger the levy of inheritance tax.

### iv  Non-commercial partnership

The resident non-commercial partnership is widely used, particularly to hold real estate; it may be used to avoid the fragmentation of family real estate. Furthermore, the splitting of voting rights from profit participation rights may be achieved. Individuals other than family members may be prevented from acquiring an interest in the partnership and from being involved in the management of the real estate. The resident non-commercial partnership is fiscally transparent. Therefore, the beneficial regimes applicable to real estate held by individuals are preserved (e.g., the exemption from income tax on gains on real estate owned for more than five years). Furthermore, anti-avoidance provisions targeting the use of business assets by shareholders or partners or the use of dummy companies or partnerships do not apply to the resident non-commercial partnership.

### V  CONCLUSIONS & OUTLOOK

The introduction of the new Italian forfait tax regime for individuals moving to Italy (see Section II. iv, **supra**) has made Italy one of the most appealing European jurisdictions for high net worth individuals to move to. The regime has gained significant success and specific provisions have been issued to ease the granting of the entry visas for non-EU nationals.

For those outside the scope of the aforementioned new Italian forfait tax regime, the scope of reporting obligations on foreign-held assets (see above) has been broadened as a consequence of the expansion of the notion of beneficial owner by the EU Directive 2015/849 of 20 May 2015.
I INTRODUCTION

Japan has the world’s third-largest economy, having achieved remarkable economic growth after the Second World War, and private wealth management among business owners and wealthy families has become popular in Japan. However, Japan may not be such a favoured jurisdiction for private wealth management compared to others, largely owing to the significant tax burdens of personal income tax and inheritance and gift tax for wealthy individuals, and there being little room for effective tax planning to lawfully avoid these taxes. Recently, tax reforms have been made to increase the tax burden of wealthy individuals, such as establishing a new marginal tax bracket for personal income tax of taxable income exceeding ¥40 million (45 per cent) and the new ‘exit tax’ regime. On top of this, the recent enforcement attitude of the Japanese tax authority towards wealthy individuals has become very active and rigorous: the media frequently reports that wealthy individuals, e.g., business owners, who planned to avoid taxes were audited and subject to a tax bill of billions of yen as the tax authority did not respect the position taken. These examples seem to be enough to warn wealthy individuals and professional tax advisers against aggressive tax planning, setting aside the option of subsequently disputing the assessment in the courts. The Japanese government’s recent enforcement attitude is probably partially politically motivated, so that in exchange for raising the rate of the consumption tax (i.e., VAT) from 5 per cent to 8 per cent in April 2014, then from 8 per cent to 10 per cent in October 2019, to be borne by the general public, any dissatisfaction or feeling of unfairness of the general public towards the seemingly low tax burden of wealthy individuals must then be mitigated.

In such an environment, Japanese tax planning considerations for high net worth individuals would inevitably have to shift towards utilising ready-made measures offered by tax laws, rather than using creative or novel structures or techniques – presumably considered by the Japanese tax authority as deviating from the original intent of the relevant tax provision – to pursue no or little tax burden.

II TAX

i Personal income taxation

Resident individuals

Generally, Japanese resident individuals are taxed at regular progressive rates on all types of income under the Income Tax Act (Act No. 33 of 1965, as amended), subject to the
special tax rules discussed below under the Act on Special Measures Concerning Taxation (Act No. 26 of 1957, as amended). The marginal tax rate of individual income taxation is 55.945 per cent (comprised of 45 per cent national individual income tax, 0.945 per cent special reconstruction income surtax and 10 per cent local inhabitants tax) until 2037. The marginal rate applies to the portion of the taxable income exceeding ¥40 million; this new marginal rate bracket has been effective from 2015. Among others, business income and employment income (including directors’ and officers’ remuneration) are subject to the regular progressive taxation.

Special rules apply to income from financial assets, which are significant for Japanese high net worth resident individuals. Japanese resident individuals are taxed on capital gains arising from sale of securities (shares, whether private or publicly listed, and bonds for which sufficient disclosures are made) at the flat rate of 20.315 per cent, substantially lower than the 55.945 per cent marginal rate. As for dividends, if the Japanese corporation distributing the dividends is a private or non-listed corporation, Japanese resident individuals are subject to withholding tax at the rate of 20.42 per cent, and at the same time are subject to the regular progressive taxation to be reported by filing a tax return. In the case of a publicly listed corporation, they are subject to withholding tax at the rate of 20.315 per cent, and will be subject to the separate taxation at the rate of 20.315 per cent to be reported by filing a tax return; provided that, for individual shareholders who own 3 per cent or more of the total issued shares of the publicly listed corporation (typically owners or founders of the business), the treatment will substantially be the same as that for a private or non-listed Japanese corporation mentioned above.

Japanese resident individuals are subject to the Japanese anti-tax haven or controlled foreign corporation (CFC) rules. As is common with wealthy Japanese resident individuals, when he or she owns shares of a foreign corporation (e.g., as a holding company), he or she will be subject to these rules and taxed on a pro rata portion of the profits earned by the foreign corporation (i.e., to be aggregated with his or her own income), if, in general: (1) Japanese resident individuals (including non-resident individuals having certain special relationships with them) and Japanese corporations collectively own, directly or indirectly, more than 50 per cent of the foreign corporation; (2) that particular Japanese resident individual owns, directly or indirectly, 10 per cent or more of the foreign corporation; and (3) the effective tax burden in a fiscal year of the foreign corporation is less than 20 per cent (less than 30 per cent if the foreign corporation is a certain shell company or cash-box company). This CFC rule has been overhauled and tightened by the 2017 tax reform, in response to the BEPS action plan 3, and will take effect from April 2018.

Non-resident individuals

Non-resident individuals are taxed in Japan only on certain specifically enumerated types of Japanese source income. Non-resident individuals having no permanent establishment in Japan are, in general, not subject to Japanese taxation on capital gains arising from sale of shares of a Japanese corporation, unless such non-resident individual, together with certain related persons (its affiliates and related parties, etc.) as defined in Japanese tax laws and partnerships in which it is directly or indirectly a partner: (1) owns or owned 25 per cent or more of the total shares of the Japanese corporation at any time during a period of three years on or before the end of the calendar year in which the sale of such shares took place; and (2) sells 5 per cent or more of the total shares of the Japanese corporation in that calendar year. This exceptional rule is commonly referred to as the ‘25/5 rule’ in practice. If this applies,
non-resident individuals are subject to income tax at the flat rate of 15.315 per cent, to be reported by filing a tax return. Special rules apply if the Japanese corporation at issue is a certain real property holding corporation, e.g., Japanese REITs.

As for dividends, if the Japanese corporation distributing the dividends is a private or non-listed corporation, non-resident individuals having no permanent establishment in Japan are subject to withholding tax at the rate of 20.42 per cent. In the case of a publicly listed corporation, it is subject to withholding tax at the rate of 15.315 per cent; provided that, for individual shareholders who own 3 per cent or more of the total issued shares of that publicly listed corporation, the 20.42 per cent withholding tax rate will apply. This taxation is finalised only by the withholding tax, i.e., there is no need to file a tax return.

The foregoing Japanese taxation in Japan on foreign individuals having no permanent establishment in Japan can be modified by an applicable tax treaty between Japan and the country of residence of that foreign individual.

Exit tax for resident individuals

Because income taxation for non-resident individuals on financial assets is limited as compared to that for resident individuals, particularly taxation on capital gains arising from sale of shares of a Japanese corporation as discussed above, this acts as an incentive for high net worth resident individuals to exit Japan to avoid taxation on the capital gains. Popular destinations for this purpose include Singapore, Hong Kong, Switzerland, etc. In order to prevent high net worth resident individuals from doing this and so preventing the loss of Japan’s tax revenue, an ‘exit tax’ regime has been introduced effective 1 July 2015 by an amendment to the Income Tax Act. That is, in general, Japanese resident individuals owning certain financial assets (shares, bonds, derivatives, etc.) of ¥100 million or more (on a fair market value basis) will be taxed on the unrealised gains on these financial assets at the time of the exit from Japan to be a non-resident individual, as if they had sold such financial assets. While there are some exceptions, e.g., in the case of a temporary job assignment to overseas followed by re-entry to Japan within a certain period, this exit tax is now a significant deterrent for high net worth resident individuals to migrate to foreign low-tax jurisdictions.

Information reporting and disclosure requirements

The 2012 tax reform introduced a regime of ‘statement of foreign assets’, where Japanese resident individuals who have foreign assets exceeding ¥50 million (on a fair market value basis) must disclose details of their holdings in the statement of foreign assets. Similarly, the 2015 tax reform introduced a regime of statement of assets and liabilities, where individuals (resident or on-resident) who have to file a tax return and have: (1) taxable income exceeding ¥20 million to be reported; and (2) assets of which the total fair market value as of the end of a calendar year is ¥300 million or more or assets that are subject to the ‘exit tax’ regime of which the total fair market value as of the end of a calendar year is ¥100 million or more. In the statement of assets and liabilities, individuals must disclose details of their holding of assets and liabilities. Failure to submit these statements will entail a surtax of 5 per cent on top of the penalty tax rate that otherwise applies. These are intended for the Japanese tax authority to collect information on high net worth individuals to effectively enforce the relevant tax laws. These regimes are based on the Act on Submission of Statement of Overseas Wire Transfers for Purpose of Securing Proper Domestic Taxation (Act No. 110 of 1997, as amended).
Inheritance and gift taxation

Inheritance tax and gift tax are imposed based on the Inheritance Tax Act (Act No. 73 of 1950, as amended) as follows:

a. Japanese national and resident taxpayers, if they are an heir or a donee, are subject to Japanese inheritance and gift tax on worldwide (i.e., Japanese and foreign) assets that they acquired by the inheritance, bequest or gift;

b. taxpayers who are a Japanese national but are not a Japanese resident are taxed only on Japanese assets (but not on foreign assets), unless either the deceased or the heir or donee used to reside in Japan at any time during the 10-year period preceding the commencement of the inheritance, bequest or gift; and

c. taxpayers who are neither a Japanese national nor a Japanese resident are taxed also only on Japanese assets, unless the deceased used to reside in Japan at any time during the 10-year period preceding the commencement of the inheritance, bequest or gift.

This means that an attempt to avoid inheritance and gift taxation on foreign assets by becoming a non-resident or even a foreign national has become impractical, since it mandates a 'waiting period' of 10 years. Indeed, aiming to discourage such an attempt, the waiting period in the case of (b) above has been extended from five years to 10 years by the 2017 tax reform, and the 2017 tax reform has set a new 10-year waiting period in the case of (c) above.

The marginal inheritance tax rate is 55 per cent if the total value of the inherited assets succeeded to by an heir as a taxpayer exceeds ¥600 million, effective from 2015. Also, effective from 2015, standard deductions for inheritance tax were significantly reduced. This is obviously intended to expand the tax base of the inheritance tax and to increase taxation of high net worth families. The marginal tax rate of gift tax is 55 per cent if the total value of the gifted assets of a donee as a taxpayer exceeds ¥30 million; as such, gift tax can be significantly burdensome when assets of a significant value are gifted, and hence is a deterrent for succession of a business to the next generation.

The value of assets for inheritance and gift tax purposes is measured in accordance with the Asset Valuation Basic Circular of the Japanese tax authority (the Circular). Because room for creative tax planning is rather limited, a major part of the planning in practice is to try to reduce the value of the assets, taking advantage of the Circular. However, the Circular contains a general anti-avoidance provision called General Rule Paragraph 6, and this has been actively invoked by the Japanese tax authority to disallow 'creative' (in its view 'abusive') tax planning to reduce the value of the assets.

III SUCESSION

i. Overview

After the Second World War, the succession system was transformed in Japan. There are two kinds of succession: testate and intestate. In the case of intestate, the surviving spouse is always an heir. Children of the deceased are heirs of the first rank, the lineal ascendants (parents and grandparents) are heirs of the second rank, and the siblings (brothers and sisters) come the third. If there is a spouse and children, the spouse will take half the estate and the remaining half is equally divided among the children, and heirs of the second and third rank have no share in the estate. If there is a spouse but no children, the estate is divided among
the spouse who takes two-thirds of the estate and the lineal ascendants who take one-third. If the lineal ascendants have already died, the spouse takes three-quarters and the siblings take a quarter.

The share of an illegitimate child used to be half of that of a legitimate child. However, the Supreme Court declared that the relevant provision of the Civil Code of Japan (Act No. 89 of 1896 as amended) (the Civil Code) is unconstitutional and invalid and, thereafter, such discriminatory treatment was abolished.

If a prospective heir dies before the deceased, such heir's lineal descendant will become the heir (in addition, where a child's lineal descendant also dies before the deceased, such lineal descendant's lineal descendant will become the heir).

An heir will have a choice to accept or renounce succession. An heir may also accept succession with a reservation by declaring that he or she is liable for the debts of the deceased only up to the amount of the inherited estate. Renunciation or acceptance with reservation will have to be made within three months after he or she has become aware of the death of the deceased and of the fact that he or she is to succeed the estate. He or she must prepare an inventory of the estate and declare renunciation or acceptance at the family court in order to effect renunciation or acceptance with reservation. When an heir fails to renounce or accept succession with reservation within three months, he or she is deemed to have accepted the succession.

If there is no will, the estate of the deceased as well as his or her debts pass directly to the heirs. Until the estate is distributed among the heirs, it will be jointly owned by the heirs and each heir may dispose of its own share. The division of the estate will take effect retrospectively upon the death of the deceased, but the division may not affect the third party who acquires an interest in the estate before the division. Therefore, if an heir sold its share in the succeeded land to a third party before the division, such sale is valid even after the division.

If there is a will, the distribution of the estate will be effected in accordance with the will. Any person over 15 years of age is capable of making a will. A will must follow the strict formalities set forth in the Civil Code. There are three kinds of ordinary wills: (1) a will written in the testator's own hand (a holographic will); (2) a will by notarised document; and (3) a will by a sealed secret document. A will can be revoked at any time by the testator. However, certain categories of heirs (children, spouses and lineal ascendants, not including siblings) have a secured portion of the estate that they cannot be deprived of, even by will. If the lineal ascendants are the only heirs, one-third of the estate will be reserved for them and otherwise, half of the estate will be reserved.

Whether or not a lease of a flat or a house may be succeeded or not has been discussed. For example, where the deceased was living with a de facto wife, after the death of the deceased she may be evicted by the heirs, if the status as the lessee is to be inherited by the heirs. Regarding the claim of eviction from a landlord, the Supreme Court has held that a de facto wife may exercise the right of the heir against the landlord.

Whether or not an insurance payment should form part of the estate subject to succession has been also discussed. As for an insurance payment, in general, when an heir has been designated as a beneficiary of insurance, it will not be included in the estate and

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2 Decision of the Supreme Court, September 4, 2013, Minshu 67-6-1320.
3 Judgment of the Supreme Court, April 28, 1967, Minshu 21-3-780.
the designated heir may receive the insurance payment separately from the succeeded assets. Similarly, in the case of a death allowance paid by the company the deceased worked for, the beneficiary receives such allowances separately from the succeeded assets.

ii Recent Supreme Court change of rule

Under a previous judgment of the Supreme Court, the bank deposit in the estate of the deceased was automatically divided in proportion to the statutorily determined ratio of succession and belonged to the statutory successors upon the death of the deceased. However, in 2016, the Supreme Court changed its former view and held that the bank deposit in the estate of the deceased will not be automatically divided upon the death of the deceased and shall be dealt with by the division of the estate agreed or conciliated among the heirs or adjudicated by the family court.

iii Conflict of law rules

Under the Japanese conflict of law rules, in general, the succession is governed by the laws of the deceased's nationality. The execution and effect of a will shall be governed by the laws of the testator's nationality when the will is executed. However, Japan has ratified the Convention of 5 October 1961 on the Conflicts of Laws Relating to the Form of Testamentary Dispositions and pursuant to the domestic law enacted thereunder, a will will be legally valid if a will complies with: (1) the laws of country where the will is executed; (2) the laws of the country of the testator's nationality when the will is executed or the testator is dead; (3) the laws of the country of the testator's domicile when the will is executed or the testator is dead; (4) the laws of the country of the testator's habitual residence when the will is executed or the testator is dead; or (5) in the case of a will regarding immoveable property, the laws of the country where such immovable property is located.

iv Applicable changes affecting personal property

While prenuptial agreements are not very popular in Japan, a couple may execute an agreement regarding their properties (couple's property agreement) prior to the filing of their marriage notice to the authority pursuant to the Civil Code. Such agreement shall be registered at the Legal Affairs Bureau so that it may be legally claimable against their heirs or other third parties.

No legislation has been made regarding same-sex marriage and, therefore, no particular legal protection has been given to same-sex couples in Japan. Recently, some local municipalities enacted certain local regulations under which the municipality commenced to issue 'partnership certificates' to same-sex couples, although the legal effect of such certificates is not clear; arguably, a same-sex couple with such certificate might be treated the same as a de facto heterosexual couple.

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5 Judgment of the Supreme Court, 8 April 1954, Minshu 8-4-819.
6 Judgment of the Supreme Court, 19 December 2016, Hanta 1433-44.
IV WEALTH STRUCTURING & REGULATION

i Vehicles and structures

Asset holding companies

Companies and corporations are the most widely used vehicles for wealth management in Japan. Typically, two types of companies will be available: a stock company and a limited liability company. Equity-holders of these companies are responsible for the financial obligations of the companies only to the extent of the subscription price paid for the equities owned by such equity-holders. A stock company is divided into two types: public company and non-public company. The shares of public company shall be limited to transfer-unrestricted shares. Meanwhile, the shares of non-public company may include transfer-restricted shares that may not be transferred without the company’s permission. The term public or non-public as used here is a technical term, and is not equal to whether the company’s shares are publicly listed or not. A limited liability company is modelled after a US LLC and may be converted into stock company, which makes it a useful vehicle for start-up companies. When the shares in listed companies are transferred to asset holding companies, a large volume of shareholding reports or their amendment reports or extraordinary reports may be required to be filed with the financial authority and may also be subject to TOB regulations and insider trading regulations under the Financial Instruments and Exchange Act (Act No. 25 of 1948, as amended). To prevent disputes among family members in the future succession, it is recommended that the number of asset holding companies is the same as the number of family members (e.g., if there are a spouse and two children, three asset holding companies should be set up).

For high net worth individuals who own a business in the form of shares of a Japanese company operating the business (in many cases this is a publicly listed company), a Japanese asset holding company privately owned by the owner-individual is widely used. This is because dividends paid by the operating Japanese company to the holding company will be (except for a portion corresponding to interest on debts) exempt from corporation tax at the asset holding company’s level (i.e., dividend received deduction), if the asset holding company owns more than one-third of the outstanding shares of the operating Japanese company generally for six months or more prior to the record date for the relevant dividend. This effectively enables deferral of taxation at the level of the owner or individual on the dividends paid by the operating Japanese company, and he or she can avoid the 20.42 per cent withholding tax and the regular progressive taxation had he or she owned the shares directly. In addition, from a viewpoint of valuation for inheritance and gift tax purposes under the Circular, if the asset holding company is well structured so that it will not fall under a certain specified share or real property holding company, the valuation of the shares of the private asset holding company may be made by taking into consideration the share prices of some other similarly situated listed companies, without being bound solely by the market price of the underlying shares of the publicly listed operating Japanese company, which may result in a substantially lower valuation under the Circular. We should note, however, that the tax authority has recently often challenged structures using shell holding companies with a view to reducing the valuation under the Circular, by invoking the General Rule Paragraph 6 and by looking to the economic substance of such structures.

There are cases where an owner or individual has a private asset holding company that is a foreign company in some tax-favourable jurisdictions. In this case, the foremost concerns
include application of the CFC rules as tightened by the 2017 tax reform, and a permanent establishment risk in Japan (where the owner manages everything for the holding company in Japan).

**Associations and foundations**

Associations and foundations are also popular vehicles for a family’s wealth management in Japan. An association or foundation that does not intend to distribute its surplus may be established as a general-association judicial person or a general-foundation judicial person by just registering them without having to demonstrate their public purpose. They may apply for non-profit status as a public-interest-association judicial person through the office of the Prime Minister or a regional governor of prefecture, which then will establish committees consisting of private sector specialists to examine the public interest character of the applicant.

The gift or donation of an asset to public-interest-association judicial persons will generally be deductible as a qualified donation for the donor’s income or corporation tax purposes. The gift or donation of appreciated assets (e.g., shares of the operating Japanese company) by a resident individual to public-interest-association judicial persons (and certain other qualifying corporations) may be exempt from capital gains taxation subject to a specific approval of the tax authority. Public-interest judicial persons are generally not subject to corporation tax on income from non-profit public activities. As such, public-interest-association or foundation judicial persons are often used as a vehicle to own the shares of the publicly listed operating company as transferred from the owner or individual, as a stable shareholder that would prevent hostile takeovers of the operating company. Also, by doing so, the owner or individual can alienate these shares from his or her inheritance estate to reduce the future inheritance tax burden.

**Trusts**

Traditionally, trusts have been used as substitutes for bank deposits and securities investments or as vehicles for securitisation or other commercial transactions. Recently, however, they have become popular as vehicles for succession of business from the owner to its families (as substitute for a will) or for other wealth management purposes.

Trusts may be set up under the Trust Act (Act No. 108 of 2006 as amended). If the grantor entrusts its properties to a trust, such properties will not be affected by the bankruptcy of the grantor or the trustee (bankruptcy remoteness) and the trusted properties are managed and disposed of solely by the trustee pursuant to the trust certificate. By setting up the trust, the grantor acquires the trust beneficial interests and may transfer such interests to a third party more smoothly than the trusted assets such as securities or real estates.

For tax purposes, a plain-vanilla trust (defined as a ‘beneficiary-taxed trust’) is, in general, treated as a conduit, i.e., a holder of the trust’s beneficial interests will be deemed to directly own the underlying entrusted property. That is, a beneficiary-taxed trust cannot generally achieve deferral of taxation on income arising from the entrusted property, or alienation of the underlying entrusted property from the inheritance estate for tax purposes. Although there are two other types of trust, the tax regime is so strict and straightforward that there is little room for creative and effective tax planning using trust (including a beneficiary-taxed trust).
ii Anti-money laundering and other regimes

In Japan, money laundering of proceeds from certain serious crime is prohibited under the Narcotics Special Provisions Act (Act No. 94 of 1991 as amended) and the Punishment of Organised Crimes and Control of Crime Proceeds Act (Act No. 136 of 1999 as amended). Furthermore, in order to prevent money laundering and terrorist financing, the Criminal Proceeds Transfer Prevention Act (Act No. 22 of 2007 as amended, the Criminal Proceeds Act) requires that specified business operators (SBOs) such as financial institutions and real estate agents: (1) verify the counterparty of the transaction; (2) prepare and preserve records of such verification and transaction; and (3) report any suspicious transactions to the relevant authority.

In 2016, responding to the Financial Action Task Force’s (FATF) critical statement, the Criminal Proceeds Act was amended in various points, such as: (1) an amendment to the procedures for assessment of suspicious transactions; (2) SBOs’ were obliged to confirm that a new counterparty of transactions had adopted a similar level of internal anti-money laundering measures; (3) expanding SBOs’ obligations upon adopting internal anti-money laundering measures; and (4) a requirement of strict verification when making transactions with foreign PEPs (Politically Exposed Persons), etc. As a result of such amendments, anti-money laundering legislation became closer to other developed nations’ anti-money laundering regime.

While not yet enacted, it is reported that the government is planning to introduce reporting obligations for tax professionals and promoters who are involved in certain tax planning, in response to the BEPS Action Plan 12.

V CONCLUSIONS & OUTLOOK

The current direction is to tighten taxation on wealthy individuals in Japan, both as a matter of tax policy and legislation and enforcement. As to enforcement, the tax authority has recently established divisions specialising in monitoring and auditing wealthy individuals; as such, the enforcement is expected to be much more active and rigorous. On the other hand, on taxpayers’ side, the issue is not limited to tax or money – many wealthy individuals care about their reputation and so want to avoid sensational press reports that they under-reported their tax liability. This reputational risk tends to deter wealthy individuals from creative or novel tax planning at the outset, because of the press coverage that appears once they are subject to an assessment, and even if they later win in the courts, it would not necessarily lessen the damage to their reputation. Therefore, in Japanese wealth management practice, what is sought from professional tax advisers may not be technical ability or creativity, but a way of ascertaining whether the Japanese tax authority is likely to find the planned transaction as abusive or excessive tax planning.
I INTRODUCTION

In recent years Liechtenstein has continued to improve the legal framework for wealth structuring and succession planning and to adjust to international developments.

On 1 January 2011 the totally revised Liechtenstein Tax Act entered into force. With the new Act Liechtenstein introduced an attractive tax system, which complies with European law.

With a corporate tax rate of 12.5 per cent and the reduction of the effective tax rate even further through the notional interest deduction, Liechtenstein has joined the league of most tax-efficient jurisdictions by European standards. Furthermore, the taxation of legal entities as private asset structures (PAS) offers an attractive way for individuals to structure their wealth.

Liechtenstein is also an interesting jurisdiction for individuals to take residence. The top income tax rate for a resident of the capital, Vaduz, is 20 per cent. Income from assets that are subject to wealth tax is not taxed directly. Instead, tax is currently levied on a notional income of 4 per cent of the tax value of these assets. Moreover, a favourable lump-sum taxation regime is available for foreigners, and there is no inheritance or gift tax.

Liechtenstein has a long-standing tradition of private family foundations that continue to be attractive vehicles for wealth preservation and succession planning. With the latest reform of the Liechtenstein Foundation Law in 2009, a new foundation governance structure was implemented, providing for more checks and balances regarding the interests of the founder, the beneficiaries and the foundation itself, while the favourable opportunities for wealth planning have fully been preserved. The rules regarding the enforcement of forced heirship rights were amended, resulting in considerably more room for estate planning.

Liechtenstein has a long history of its own trust law. In 1926, Liechtenstein incorporated the institution of the trust, based on the English Trust Act of 1925, into national law. Since then, the Liechtenstein trust has developed into a popular vehicle for wealth structuring and succession planning.

Furthermore, with the implementation of the AIFM Directive of the European Union into national law, Liechtenstein has incorporated a new investment fund referred to as a ‘Smart Fund’, which provides another internationally recognised, tax-neutral vehicle for structuring private wealth.

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1 Markus Summer and Hasan Inetas are partners at Marxer & Partner Rechtsanwälte.
TAX

i  Taxation of trusts

Trusts managed from Liechtenstein are subject to an annual tax of 1,800 Swiss francs. No tax filings are necessary.

ii  Regular taxation of legal entities

Corporate tax rate and tax base

Legal entities that are taxable in Liechtenstein are subject to corporate tax on their net income at a rate of 12.5 per cent under regular taxation rules.\(^2\)

The net income is reduced by income from foreign permanent establishments, rental and lease income from foreign real estate, gains from selling real estate, distributions from foundations or trusts, dividends and capital gains on the sale of shares and unrealised capital gains on shareholding in companies both in Liechtenstein and abroad.\(^3\) In general, dividend income and capital gains from the sale of shares are tax-exempt. As a result, not only income and capital gains from interests in partly or wholly owned subsidiaries, but also income and capital gains from shares held as part of a securities portfolio, are in principle tax-free.

However, in 2016, a number of the OECD’s Base Erosion and Profit Shifting (BEPS) measures were implemented in the Liechtenstein Tax Act. As a result, dividend income is no longer tax exempt if: (1) the shareholding in the respective subsidiary amounts to at least 25 per cent of the capital or voting rights; and (2) the share of profits are treated as expenses deductible for tax purposes by the subsidiary.\(^4\) This means that if a Liechtenstein entity receives dividend income which for some reason is classified as tax deductible interest payment in the country where the dividend was declared, Liechtenstein will be forced to tax the dividend if the 25 per cent holding threshold is met.

Notional interest deduction

The new tax law introduced a notional interest deduction, which is currently 4 per cent of the modified equity as a deemed expense to ensure equal treatment of debt and equity.

The modified equity is calculated by deducting the following items from the net equity:

\(a\) own equity;
\(b\) shares in legal entities;
\(c\) assets not required for the company’s purposes; and
\(d\) a deduction of 6 per cent of all assets, under exclusion of items \((a)\) to \((c)\).\(^5\)

The reason for the first three deductions is that they produce tax-exempt income and capital gains and, therefore, cannot be used to create a notional interest deduction. The term ‘all assets’ refers to the balance sheet total.\(^6\) In case of 100 per cent equity funding, the effective notional interest deduction is reduced from 4 per cent to 3.76 per cent because of the deduction of 6 per cent of the total of all assets (100 per cent – 6 per cent = 94; 94 x 4 per cent = 3.76 per cent).

\(^2\) Article 61 of the Tax Act.
\(^3\) Article 48 of the Tax Act.
\(^4\) Article 15 Paragraph 2 item n of the Tax Act.
\(^5\) Article 54 of the Tax Act; Article 32 of the Tax Ordinance.
\(^6\) BuA No. 48/2014, 33.
The table below shows the effects of the notional interest deduction, assuming 100 per cent equity financing for various return-on-equity (ROE) scenarios and the resulting earnings before interest and taxation (EBIT). It is evident that the notional interest deduction can result in a substantial reduction of the effective tax rate. Obviously, the effect is higher the closer the ROE is to the 3.76 per cent effective notional interest deduction. However, even in the case of a highly profitable company yielding a 20 per cent ROE, the notional interest deduction results in a decrease of the effective tax rate from 12.5 per cent to 10.15 per cent.

<table>
<thead>
<tr>
<th>ROE</th>
<th>3.76%</th>
<th>5%</th>
<th>10%</th>
<th>15%</th>
<th>20%</th>
</tr>
</thead>
<tbody>
<tr>
<td>Equity (prior to deduction of 6% of all assets)</td>
<td>1,000,000</td>
<td>1,000,000</td>
<td>1,000,000</td>
<td>1,000,000</td>
<td>1,000,000</td>
</tr>
<tr>
<td>Equity (after deduction of 6% of all assets)</td>
<td>940,000</td>
<td>940,000</td>
<td>940,000</td>
<td>940,000</td>
<td>940,000</td>
</tr>
<tr>
<td>EBIT</td>
<td>37,600</td>
<td>50,000</td>
<td>100,000</td>
<td>150,000</td>
<td>200,000</td>
</tr>
<tr>
<td>Notional interest deduction (3.76%)</td>
<td>37,600</td>
<td>37,600</td>
<td>37,600</td>
<td>37,600</td>
<td>37,600</td>
</tr>
<tr>
<td>Profit before taxes</td>
<td>0</td>
<td>12,400</td>
<td>62,400</td>
<td>112,400</td>
<td>162,400</td>
</tr>
<tr>
<td>12.5% corporate tax</td>
<td>0</td>
<td>1,550</td>
<td>7,800</td>
<td>14,050</td>
<td>20,300</td>
</tr>
<tr>
<td>Effective tax rate</td>
<td>0</td>
<td>3.10%</td>
<td>7.80%</td>
<td>9.37%</td>
<td>10.15%</td>
</tr>
</tbody>
</table>

Since the revision of the Tax Act in December 2014, in cases of non-operating receivables from shareholders, founders, beneficiaries or related persons carrying an interest rate of less than 4 per cent, the interest rate differential must be considered in the calculation of the notional interest deduction. This additional requirement applies to non-operating receivables from related persons exclusively.7

**IP box**

In 2011, Liechtenstein introduced a notional expense, which may be deducted from any income from intellectual property (IP) rights. The notional expense amounts to 80 per cent of the respective net income. This IP box regime was approved by the EFTA Surveillance Agency (ESA) in its decision of 1 June 2011. However, in the course of the BEPS action plan, the OECD has defined new taxation standards for IP box regimes, referred to as the modified nexus approach. Like many other countries, Liechtenstein is now implementing the measures of the OECD BEPS action plan. Liechtenstein’s government therefore abolished the IP box regime after the 2016 tax year. However, taxpayers who already take advantage of the Liechtenstein IP box regime will be allowed to benefit from it until 2020.

**iii Taxation as a private asset structure**

As an alternative to regular company taxation and inspired by Luxembourg’s private asset management company, the Liechtenstein legislature devised a new tax privilege for legal entities that are only engaged in the management of their own assets and do not perform any commercial activity. A private asset structure (PAS) is only subject to the minimum corporate income tax of 1,800 Swiss francs annually without having to file any tax returns. Taxation as a PAS was approved by the EFTA Surveillance Agency as being compliant with the European competition law on 15 February 2011.

The main feature with regard to the tax privilege is the lack of commercial activity. Article 64, Paragraph 1(a) of the Tax Act exemplifies, by reference to the Asset Management

7 Article 54 Paragraph 3 of the Tax Act.
Act, what is not considered a commercial activity. This includes the acquisition, possession, management and sale of transferable securities such as bonds, stocks, money market instruments, shares in investment undertakings and derivatives.

Likewise, buying, holding and selling of precious metals, artwork and similar assets is generally possible. In its decision approving the provisions on the PAS, however, the EFTA Surveillance Authority indicates that transactions in securities when effected ‘as part of a commercial share dealing activity’ constitute economic activity. Regular and active trading of securities (and other assets) is therefore not considered permissible for a PAS unless decisions are delegated to an independent asset manager. The purchase and sale of securities as part of a long-term investment strategy is, however, allowed in any event.

As the mere exercise of ownership and the granting of benefits by the entity to its shareholders or beneficiaries are not considered commercial activities, the holding of a property does not constitute a commercial activity as long as the property is used by the PAS or its shareholders and beneficiaries and no rent is charged.

When a PAS holds shares in a subsidiary that exercises a commercial activity, neither the PAS nor its shareholders or beneficiaries are allowed to exercise any control over the management of the subsidiary through direct or indirect influence, otherwise the PAS itself will be regarded as commercially active and lose its status as a PAS.

When comparing regular taxation with PAS taxation, it turns out that in some cases there may be only a small difference in the tax burden because, even in cases of regular taxation, the income from the management of the legal entity’s own assets tends to be tax-exempt anyway.

The following table shows where PAS taxation has advantages over regular taxation:

<table>
<thead>
<tr>
<th>Investment</th>
<th>Revenues</th>
<th>Regular taxation (12.5% corporate tax)</th>
<th>Possible advantage of PAS</th>
</tr>
</thead>
<tbody>
<tr>
<td>Shares</td>
<td>Dividends</td>
<td>Tax-free</td>
<td>–</td>
</tr>
<tr>
<td></td>
<td>Realised capital gains</td>
<td>Tax-free</td>
<td>–</td>
</tr>
<tr>
<td>Bonds</td>
<td>Interest</td>
<td>Taxable if net profit exceeds the 4% notional interest deduction</td>
<td>Yes</td>
</tr>
<tr>
<td></td>
<td>Realised capital gains</td>
<td>Taxable if net profit exceeds the 4% notional interest deduction</td>
<td>Yes</td>
</tr>
<tr>
<td>Commodities (physical, e.g., gold in a safe)</td>
<td>Realised capital gains</td>
<td>Taxable if net profit exceeds the 4% notional interest deduction</td>
<td>Yes</td>
</tr>
<tr>
<td>Real estate (non-Liechtenstein)</td>
<td>Rent</td>
<td>Tax-free</td>
<td>–</td>
</tr>
<tr>
<td></td>
<td>Realised capital gains</td>
<td>Tax-free</td>
<td>–</td>
</tr>
<tr>
<td>Derivatives</td>
<td>All income</td>
<td>Taxable if net profit exceeds the 4% notional interest deduction</td>
<td>Yes</td>
</tr>
<tr>
<td>Investment funds</td>
<td>Treated as transparent; investments of the fund are treated as being held directly by the legal entity</td>
<td>Yes (except pure stock or property funds)</td>
<td></td>
</tr>
</tbody>
</table>

The table shows that a Liechtenstein legal entity that is taxed as a PAS does not have any tax advantage over a regularly taxed company if it only holds shares, or real estate outside Liechtenstein. The reason is that even under regular taxation any income or capital gains produced by these asset classes will be tax-free anyway. In the case of the other asset classes, whether taxation as a private asset structure is preferable over regular taxation depends on whether the asset classes yield more than the 4 per cent notional interest deduction applying in case of regular taxation.
Taxation of individuals

Income and wealth tax

Personal tax liability

The Liechtenstein tax regime for the taxation of individuals combines income and wealth tax. The wealth tax is based on the notional income of currently 4 per cent on the taxpayer’s assets, which is then subject to income tax in lieu of the real income from such assets (which is tax-free). There is an eight-stage scale for determining the income tax.

Individuals having their residence or habitual abode in Liechtenstein are taxable on their entire wealth and income. While residence means the place where a person lives with the intent of staying permanently, habitual abode refers to the place or area in which a person dwells not only temporarily. The Liechtenstein Tax Act considers a temporary continuous abode of more than six months as habitual abode, whereby short-term interruptions are not taken into account.

Limited tax liability applies to individuals whose residence and habitual abode is not in Liechtenstein. Such individuals are taxable in respect of their Liechtenstein wealth and income.

Subject of income tax

All income in money and money’s worth is subject to income tax such as:

- any income from self-employment;
- any income from employment relationship under private or public law;
- any income of board members, foundation council members and members of similar bodies of legal entities and trusts which they receive for their respective functions; and
- contributions received by the taxpayer as beneficiary, unless this is subject to wealth tax.8

Tax-exempt income includes income from wealth for which the taxpayer pays wealth tax, recurring benefits to the taxpayer, which are considered as taxable wealth, and income from permanent establishments abroad.

Subject of wealth tax

The entire moveable and immoveable wealth of the taxpayer is subject to wealth tax. Individuals with limited tax liability are only taxable in respect of their domestic wealth, that is real estate and permanent establishments in Liechtenstein.9

The Tax Act provides for certain exemptions from wealth tax. In particular, real estate and permanent establishments abroad are exempted from wealth tax. Taxpayers are also entitled to make certain deductions, such as reducing assets by debts and other liabilities, provided that the taxpayer is liable as principal debtor.

Trusts or foundations with Liechtenstein-resident settlors or beneficiaries

With regard to trusts, foundations and similar vehicles with Liechtenstein residents as settlors or beneficiaries the following rules apply.

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8 Article 14(2) of the Tax Act.
9 Article 6(4) of the Tax Act.
The wealth of revocable foundations, trusts and establishments with a foundation-like structure is attributed to the founder and wealth tax is paid by the founder. However, it is possible to opt for taxation at the level of the trust, foundation or similar structure instead.

In the case of irrevocable trusts, foundations and establishments with a foundation-like structure, a distinction is made between entities with determinable beneficiaries that benefit from a certain quota and entities where this is not the case.

In the case of trusts, foundations or establishments with a foundation-like structure with determinable beneficiaries entitled to a certain quota, wealth tax is levied at the level of the beneficiaries. However, the beneficiaries may apply for taxation at the level of these structures but require the consent of the body responsible for distributions. Such a structure will not become the taxpayer itself but rather must meet the wealth or personal tax liability in lieu of the beneficiaries.10

If such structures have no determinable beneficiaries entitled to a certain quota, no wealth tax is payable because the wealth cannot be attributed to any natural persons; however, if such structures are established by Liechtenstein tax residents, the set-up itself triggers a special tax as follows.

Such transfers to a discretionary structure are subject to taxation to the extent that: (1) this wealth is no longer subject to wealth tax; and (2) benefits or shares do not become liable to wealth tax.11 For example, the first prerequisite is not met if real estate abroad is transferred as this is exempted from wealth tax.

The taxation of transfers to a fiduciary structure also applies in the event of changing circumstances after the establishment of a fiduciary structure that led to a shortfall of the wealth tax liability. As a result, the conversion of a determinable benefit into a discretionary benefit also leads to taxation.12

The transferor shall pay a tax in the amount of 3.5 per cent of the wealth tax value of the contribution plus the applicable municipal surcharge. If a tax resident of Vaduz (where the municipal surcharge is 150 per cent) establishes a foundation or trust where no quota can be attributed to the beneficiaries and, therefore, the assets are no longer subject to wealth tax, the set-up is therefore taxed at a rate of 8.75 per cent. The assets will then no longer be subject to wealth tax. However, any distributions from such a foundation or trust to a beneficiary who is a Liechtenstein tax resident will be subject to income tax.

**Tax calculation**

The taxation of individuals is based on a combination of wealth and income tax: the wealth tax is integrated into the income tax by transforming a part of the wealth into an additional category of income. This transformation is based on a notional income.13 To determine the taxable base, wealth and income are calculated separately and then a notional income from the wealth is assumed. The interest rate for determining the notional income from wealth is determined annually in the Finance Act, being 4 per cent for 2017. This notional income from taxable wealth is then considered income (instead of the real income) and added to the total taxable income.

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10 Draft Bill (BuA) No. 48/2010, 75.
11 See Article 13(1) of the Tax Act.
12 BuA No. 48/2010, 83.
After basic exemptions up to 15,000 Swiss francs (and up to 22,500 Swiss francs in case of single parents within the meaning of the Family Allowance Act and up to 30,000 Swiss francs for jointly assessed married couples), taxable income (including the notional income resulting from wealth tax) is then taxed at different rates for eight income brackets, with the highest rate for the national income tax being 8 per cent. Additionally, the Liechtenstein communities may levy a municipal surcharge between 150 per cent and 250 per cent on the national tax. Currently, all Liechtenstein communities levy a surcharge between 150 per cent and 200 per cent on the national income tax, with the rate in Vaduz being 150 per cent. The top tax rate for a resident of Vaduz therefore amounts to 20 per cent and applies in the case of a non-married taxpayer without children if his or her annual income exceeds 200,000 Swiss francs.

**No inheritance or gift tax**

Inheritance tax and gift tax have been abolished in the course of the revision of the Liechtenstein Tax Act. Under the new Liechtenstein tax regime just a disclosure of donations to the fiscal authority is required. Liechtenstein-resident donors and recipients of gifts must therefore include gifts in their tax returns. The purpose of this notification is to enable comprehensibility of declarations of wealth set out in the tax returns of these individuals (i.e., the information is only declaratory). The disclosure requirement applies only to gifts, inheritances and bequests exceeding 10,000 Swiss francs.

**Lump-sum taxation**

Individuals can apply to the fiscal authority for lump-sum taxation (i.e., apply for taxation on expenditure instead of income and wealth tax). The latter does not apply to real estate in Liechtenstein, which remains subject to wealth tax.

Liechtenstein citizens are not entitled to apply for such lump-sum taxation. Another prerequisite for the application is that the individual takes residence or habitual abode in Liechtenstein for the first time or after an absence of 10 years or more from Liechtenstein. The individual must not be entitled to work in Liechtenstein but shall live on income from his or her wealth or other receipts from abroad.

The discretionary decision regarding the lump-sum taxation is up to the Liechtenstein fiscal authority. The lump-sum taxation considers the total expenditure of the taxpayer, and the tax based on the expenditure amounts to 25 per cent of the expenditure. The tax may be determined for several years depending on the regularity of the amount of the expenditure.

Individuals intending to apply for lump-sum taxation must also take into account the applicable provisions in conjunction with the permission to reside in Liechtenstein. Currently, residence permits are quite restricted, although there is a lottery open to citizens of the EEA. Furthermore, several times in the political process there have been discussions to issue more resident permits to wealthy or highly qualified foreigners but no final conclusion has been reached.

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15 See Article 33 of the Tax Act.
III SUCCESSION

Generally, under the Liechtenstein Private International Law Act all aspects of legal succession are governed by the law of citizenship of the deceased, which will be applied by the Liechtenstein courts. Foreign testators and Liechtenstein nationals living abroad may, however, choose the law of the country of their last residence instead, which offers some planning opportunities.

The enforcement of forced heirship rules against Liechtenstein trusts, foundations and other fiduciary structures has been the subject of several court cases and has consequently led to actions by the Liechtenstein legislator.

Forced heirship rules allocate a part of the assets to the disposition of the testator and another part to certain family members. Generally, contributions of assets to a foundation may be disputed by the heirs in the same way as a donation. If Liechtenstein inheritance law applies, upon request of a child, the spouse or the registered partner entitled to a compulsory portion, donations by the testator must be taken into consideration in the computation of the estate. The subject of the donation must be added to the estate. If the estate is insufficient to cover the forced heirship claims because of the transfer of assets by the deceased to a foundation, the subject of a potential challenge is not the foundation itself but the transfer of assets to the foundation.

Donations to persons not entitled to a compulsory portion that have been made more than two years prior to the donator's death are disregarded. This fairly short period also applies to contributions to a foundation, with the caveat that its commencement depends on the structure of the foundation. In particular, the period does not start before the founder's death if the assets have not really been economically transferred to the foundation prior to his or her death. Assets are not deemed entirely separated from the founder if he or she has reserved rights to revoke the foundation and to amend the foundation documents; however, it has been argued that even where the foundation documents provide a revocation right, the statute of limitations starts with the setting up of the foundation if the foundation documents refer to a third party as ultimate beneficiary in the case of a revocation. The founder is also entitled to waive such rights: upon waiver of such rights set out in the foundation documents, the two-year period shall also start. The Liechtenstein Supreme Court recently stated that a revocation right is not the only indication that the assets have not been separated from the founder, and therefore the two-year period has not started to run. Rather, any circumstances indicating the control of the foundation by the founder must be taken into account.

If the founder is not a citizen of Liechtenstein and not resident in Liechtenstein, his or her entire estate is governed by law of the country whose citizen he or she was at the

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16 Article 552 Section 38(1) of the Persons and Companies Act (PGR). This provision shall refer to Sections 785 and 951 of the Civil Code (ABGB) entitling the heirs to challenge. See BuA No. 13/2008, 122.
17 See Section 785(1) of the ABGB.
18 See BuA No. 13/2008, 122.
19 Pursuant to Section 785(3) of the ABGB, donations will also be disregarded that the testator made out of current income for charitable purposes in accordance with moral duty or consideration of decorum without diminishing the substance of property.
20 See Jakob, *Die Liechtensteinische Stiftung*, 2009, margin No. 685 with references to Germany and Switzerland.
23 Supreme Court, 7 December 2012, 03 CG.2011.93.
time of his or her death (unless the founder chose the law of the country of his or her last residence instead in a will). That law will also apply to the questions of whether there is a forced share for certain family members and whether such compulsory heirs can challenge transfers to a trust or foundation under certain circumstances. As a result, if a foreign resident has established a Liechtenstein trust or foundation, any challenge of the transfer of assets will generally be based on the law governing his or her estate, not on Liechtenstein compulsory heirship law. Accordingly, the Liechtenstein Supreme Court has allowed claims of foreign heirs in several cases based on the applicable foreign heirship law, irrespective of the fact that the Liechtenstein two-year statute of limitations had expired.

However, the newly introduced Article 29 Paragraph 5 of the Liechtenstein Private International Law Act installed another barrier to any challenges, saying that the heirs are entitled to claims for a compulsory portion only if they are entitled in the same way under the laws governing the acquisition of the assets by the foundation or trust. Therefore, disputes by persons entitled to a compulsory portion of contributions to a Liechtenstein foundation made by its foreign founder must be possible both under the applicable inheritance law and under Liechtenstein law if Liechtenstein law had been chosen as the law governing the transfer or if Liechtenstein law is applicable because the funds were transferred to the foundation as part of its stated capital. As a result, if Liechtenstein law applies to the contributions to the foundation, the Liechtenstein rules regarding the statute of limitation will be applicable.25

In practice, this means that if a foreigner establishes an irrevocable discretionary trust or a foundation in Liechtenstein (without reserving any revocation rights or equivalent powers) and chooses Liechtenstein law as the law governing the transfer of his or her assets to the foundation or trust, any claims of any compulsory heirs under the applicable inheritance law will become time-barred after the expiry of two years from the transfer of the assets to the trust or foundation.

Alternatively, a potential claim of compulsory portion will generally also be denied, if a founder makes an *inter vivos* donation to a Liechtenstein foundation and agrees that such contributions will be governed by a jurisdiction not having forced heirship rules at all.26 However, this concept has not yet been contested in court, and it seems possible that under certain circumstances a court could rule that a foundation cannot rely in good faith on such a choice of law for the transfer of assets to the foundation, if it was designed only to frustrate the rights of compulsory heirs under the applicable inheritance law.

### IV WEALTH STRUCTURING & REGULATION

The main Liechtenstein vehicles used for wealth structuring and estate planning are trusts and foundations. The following have recently been the subject of discussions or legislative efforts:

* a the checks and balances that can be incorporated in the structure of a Liechtenstein foundation to prevent any abuse (often referred to as foundation governance);
b asset protection and the protection of creditors in connection with Liechtenstein trusts and foundations; and

c the use of a Liechtenstein foundation as a private trust company instead of a trustee company owned by a financial service provider.

**Smart Fund**

In the course of the implementation of the Alternative Investment Fund Managers Directive (2011/61/EU) in Liechtenstein, a special investment vehicle was created for families. If the investor circle only consists of members of a single family then a ‘Smart Fund’ can be set up. A Liechtenstein Smart Fund is an alternative investment fund in the meaning of the Liechtenstein AIFM Act and the AIFM Ordinance.\(^{27}\) It provides an opportunity for families to create a tax-neutral, internationally recognised investment vehicle for family members only (i.e., all family members who are or have been related by marriage or registered partnership, by direct or collateral line or by inheritance).

**Foundation governance**

**Foundation types**

The Liechtenstein foundation is a legally and economically independent special-purpose fund, which is formed as a legal entity through a unilateral declaration of will by the founder.\(^{28}\) Assets transferred to a foundation become independent from the personal assets of its founder. The latest reform of the Liechtenstein Foundation Law has led to remarkable amendments. In this chapter we are focusing on the area of foundation governance as one area notably affected by this reform.\(^{29}\)

For foundation governance purposes, it is necessary to distinguish between common-benefit and private-benefit foundations. For instance, a common-benefit foundation requires a registration in the Commercial Register to acquire legal capacity. By contrast, private-benefit foundations acquire legal capacity by the declaration of establishment. While a common-benefit foundation serves entirely or predominantly common-benefit purposes, a private-benefit foundation serves entirely or predominantly private or personal purposes. If this is unclear, the foundation is treated as a common-benefit foundation.

**External foundation governance**

Common-benefit foundations are subject to supervision by the foundation supervisory authority (i.e., the Office of Justice).\(^{30}\) This authority must *ex officio* ensure that the foundation assets are managed in accordance with the purpose of the foundation. The law grants certain information rights to the authority; for example, inspection of the foundation’s books and right to information in relation to the foundation. Furthermore, the authority may apply to court to control or remove foundation bodies, to carry out special audits or to

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27 See Article 155 of the AIFM Ordinance.
28 See Article 552, Section 1 of the PGR.
30 See Article 552, Section 29 of the PGR.
cancel resolutions of the foundation council. Such measures are available for all foundation participants,\(^{31}\) including the founder, the beneficiaries, the foundation bodies and the members of these bodies.

As a rule, private-benefit foundations are not subject to supervision by the foundation supervisory authority. This can be changed if the articles of the foundation (voluntarily) provide for supervision.

**Internal foundation governance**

All foundations that are subject to supervision by the foundation supervisory authority require an auditor. The auditor that is appointed by the court must be independent from the foundation. As foundation body, the auditor is obliged to annually review the management and the use of the foundation’s assets to ascertain that they are in conformity with the purpose of the foundation, and must report to the foundation council, as well as to the foundation supervisory authority.\(^{32}\)

External foundation governance of private-benefit foundations is constrained because they are not subject to supervision by the foundation supervisory authority. For this reason mechanisms of internal foundation governance, particularly the rights granted to the beneficiaries, are of paramount importance. Beneficiaries of the foundation are entitled to inspect the foundation documents as far as their rights are concerned. Beneficiaries are also entitled to information, to reporting and accounts. Again, such rights are only available if the beneficiary's rights are affected. The law restricts the rights of the beneficiaries, for instance, in the event of abuse of such rights.\(^{33}\) Moreover, the rights may not be exercised in a manner conflicting with the interests of the foundation or other beneficiaries. In this respect, carefully balancing different interests is necessary. The above-mentioned rights are also restricted insofar as they can be denied for important reasons to protect the beneficiary.\(^{34}\)

To some extent, the interests of the founder can also be considered within the internal foundation governance: if the right of revocation has been reserved by the founder and if the founder is the ultimate beneficiary, the beneficiaries are not entitled to the information rights above.\(^{35}\)

Adjustments of the internal foundation governance can also result from the founder’s right to provide for other supervisory bodies. This will have the consequence that beneficiaries may only demand disclosure of information about the purpose and organisation of the foundation and with regard to their own rights in relation to the foundation, and may verify the accuracy of this information by inspecting the foundation deed, the supplementary foundation deed and the regulations.\(^{36}\) Obviously, this leads to restrictions for the beneficiary

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31 See Article 552, Section 3 of the PGR.
32 Upon application, the foundation supervisory authority exempts a common-benefit foundation from the obligation to have an auditor in the case of low asset value.
33 See Article 552, Section 9(2) of the PGR.
34 See BuA No. 13/2008, 65; Jakob, *Die Liechtensteinische Stiftung*, 2009, margin No. 490; Article 552, Section 9(2) of the PGR.
35 Article 552, Section 10(1) of the PGR.
36 The founder can also be a controlling body pursuant to Article 552, Section 11(2) No. 3 of the PGR.
to get information about the foundation. In practice, the beneficiary will not be able to get the names of other beneficiaries, for example. The beneficiary will therefore also not know what distributions other beneficiaries received.37

In summary, it can be stated that the Liechtenstein legislator has implemented various checks and balances. Because of a lack of mandatory supervision of private-benefit foundations by the foundation supervisory authority, information rights particularly granted to the beneficiaries are necessary to guarantee a control mechanism. On the other hand, the interests of the founder are also safeguarded by allowing several ways to exclude or limit the information rights of beneficiaries in certain cases.

ii Asset protection and protection of creditors

Asset protection and protection of creditors obviously reflect opposing interests. Needless to say, the settlor of a Liechtenstein trust or foundation seeks to protect the trust or foundation assets against third parties, but the interests of the founder or settlor are generally in conflict with the demands of third parties.

Creditors of the founder or settlor

Creditors may consider different options to enforce their claims towards the founder of a foundation or trust. First, creditors may dispute contributions of assets to the foundation in the same way as they would a gift.38 As a rule, every creditor having an enforceable claim is entitled to do so if full compensation could not be achieved by enforcement of the claim against the founder or settlor, or this could be assumed at the time of approval of the enforcement.

Under Article 75 of the Legal Remedy Code, the challenge of a transfer of assets to a foundation or trust by a creditor must be possible under both the laws of the country of residence of the debtor and the law governing the transfer. As a result, if the transfer of assets to a Liechtenstein foundation or trust is made subject to Liechtenstein law, the challenge must be permissible not only under the laws of the country of residence of a foreign settlor or founder, but also under Liechtenstein law.

Under Liechtenstein law, the dispute of the transfer of assets must refer to actions made within a period of one year before approval of the enforcement.39 The one-year period will not be required if the creditor is able to prove that the debtor’s (in the case of foundations the founder’s) actions are based on intent to defraud creditors, in which case a five-year limitation period from the transfer of the assets applies.40

Under exceptional circumstances creditors may refer to the general principle of the ban on abuse of legal right enshrined in Liechtenstein company law.41

37 See BuA No. 13/2008, 68.
38 Article 552, Section 38(1) of the PGR. Reference is particularly made to Article 65 of the Liechtenstein Legal Remedy Code (RSO); see BuA No. 13/2008, 121.
39 The burden of proof will be carried by the creditor (see Article 65(2) of the RSO).
40 See Article 74(1) of the RSO.
Furthermore, in the case of rights of revocation and amendment of the purpose reserved by the founder or settlor, creditors may attempt to attach such rights.  

**Creditors of the beneficiaries**

Another instrument for asset protection is stipulated in Article 552, Section 36 Paragraph 1 of the PGR, which contains an enforcement privilege for family foundations providing that creditors of beneficiaries will not be permitted to deprive the beneficiaries of their entitlement to a beneficial interest acquired without valuable consideration by way of enforcement or bankruptcy proceedings. Such an enforcement privilege must be included in the foundation articles. In the case of mixed family foundations, such a privilege can only be implemented to the extent it serves the purpose of the foundation. It is, however, questionable whether a beneficiary who simultaneously is also the founder will be entitled to such a privilege because in the case of the founder, the beneficial interest was arguably not acquired 'without valuable consideration' since the founder contributed the assets.

In practice, however, the meaning of the aforementioned enforcement restriction is limited. The reason is that it applies only if the beneficiaries have a sufficiently specified claim at all that could potentially be attached by the beneficiaries' creditors. In the event that discretionary beneficiaries of a foundation or trust are merely members of a class of several beneficiaries without any rights to a certain share in the trust or foundation fund, there are no enforceable claims and therefore the beneficiaries' creditors cannot attach their rights, a fact that has been confirmed by the Liechtenstein Supreme Court.

**V A LIECHTENSTEIN FOUNDATION AS A PRIVATE TRUST COMPANY**

Many families use trusts as an estate planning vehicle and for wealth preservation. Increasingly, instead of using a trustee company owned by a financial service provider, a private trust company (PTC) is appointed as a trustee. The use of a Liechtenstein foundation as such a PTC offers several key advantages.

**i A common set-up of a private trust company structure**

While using a PTC has several benefits, it begs the question who should act as the shareholder of the privately held trustee company. In most cases, the shareholder cannot be the settlor of the trust because then the shares of the PTC would be part of his or her estate, which would frustrate the estate planning purpose of the trusts. A common set-up to solve this problem has been to establish a separate purpose trust whose only purpose it is to hold the shares of the PTC.

The main drawback of this approach is that again a trustee is needed for the purpose trust holding the shares of the PTC. In most cases, a trustee company owned by a financial service company is used for this purpose. This means that the reasons for not using such

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42 See Jakob, *Die Liechtensteinische Stiftung*, 2009, margin No. 710, providing conclusive arguments against such potential enforceability.

43 See Article 552 Section 16(2) No. 6 of the PGR.

44 See Jakob, *Die Liechtensteinische Stiftung*, 2009, margin No. 713.

45 Supreme Court, 5 February 2009, 2R EX.2008.5850-17.
a company as a trustee of the family trust are still present. However, they are moved to a remoter level and are mitigated because the only assets held by the trustee company of the purpose trust are the shares in the PTC.

ii Using a Liechtenstein foundation as a PTC

Using a Liechtenstein foundation removes entirely the need for a trustee company owned by a financial service provider and at the same time reduces complexity. The structure then simply consists of a Liechtenstein foundation acting as trustee of one or more family trust.

A Liechtenstein foundation essentially is a fund endowed for a specific purpose that becomes autonomous and acquires the status of a legal person. It has no shareholders and therefore the question of who holds the foundation does not arise. Such a foundation can be established with the sole purpose to act as the trustee of one or more trusts for the benefit of a certain family.

When a Liechtenstein foundation acts as a private trust company, generally no special business licence is necessary in Liechtenstein. This was clarified recently by a submission of the Liechtenstein government to the parliament dealing with an amendment of the Trustee Act. The Liechtenstein Trustee Act deals with the regulatory framework for professional trustees and trust companies. In this submission, the Liechtenstein government clarified that a PTC does not qualify as a professional trust company and does not require a licence under the Trustee Act.

The government noted that a Liechtenstein PTC, like all other Liechtenstein companies without a special business licence, requires a member of the board who is licensed as a professional trustee or in an employment relationship with such a professional trustee. According to the Liechtenstein government, no separate regulation of the entity acting as a PTC is necessary. The government pointed out that the licensing requirement only applies to ‘professional’ trustees and that a privately held trustee company typically does not meet this criterion because it is not used with the goal of creating profits. The government also mentioned that the fact of directors charging a fee to the PTC is not harmful either. Furthermore, the government stated that even if the Liechtenstein entity charges a trustee fee to the trusts, it still does not need to be regulated because the PTC offers its services only to a closed circle of persons. The government also specifically confirmed that a Liechtenstein foundation can act as a PTC.

VI CONCLUSIONS & OUTLOOK

With the adoption of a tax law which is in compliance with European rules, and the revised foundation law, Liechtenstein has strengthened its position as an attractive jurisdiction for wealth structuring and estate planning.

In spite of a demanding environment, Liechtenstein maintained its high degree of stability and the financial system has proven to be very reliable during the last financial crisis. Reputation, healthy government finances and market access are the key factors for ongoing success. In this context, it is noteworthy that Liechtenstein remains one of the few European countries with a long-term credit rating of AAA by Standard & Poor’s Rating Services (Outlook: stable).

46 See BuA 42/2013, 40 et seq.
Chapter 26

LUXEMBOURG

Simone Retter

I INTRODUCTION

For decades Luxembourg has been a major participant in the international wealth management industry with its large private banking industry, today ranked first in the eurozone, fourth in Europe and seventh in the world.

Luxembourg has also become a home for many individuals and families with significant wealth. Since the country’s taxation reform in 2006, private individuals have taken advantage of its favourable tax regime on investment income and the absence, under certain conditions, of taxation on succession.

The Luxembourg authorities are constantly improving the legal and regulatory framework, implementing instruments and vehicles designed and available for wealth management, as well as cultivating a culture of investor protection, both of which help explain Luxembourg’s success and importance.

There are many reasons that explain Luxembourg’s position in the wealth management industry and Luxembourg’s appeal as a country of residence for high net worth individuals (HNWIs), but it is primarily the political and tax stability that is key to the emergence of the industry and that at the same time continues to safeguard the necessary conditions for its permanent successful development. Over the past 50 years, almost all Luxembourg governments have been coalition governments gathering representatives from at least two political parties. The bipolar political landscape that exists in other countries does not exist in Luxembourg, and this explains the very sustainable tax stability of Luxembourg and why tax laws are rarely changed, but only slightly amended to implement new developments or to take advantage of new market opportunities.

Luxembourg’s public debt is among the lowest in the world (20.5 per cent in 2016; it is expected to decrease in 2017) and it is one of the few countries in Europe to meet the 3 per cent budget deficit criteria.

The political stability and healthy public finances (Luxembourg is AAA-rated) contribute to a great extent to the social stability and the overall security in Luxembourg.

This political, social and tax stability together with the fact that Luxembourg is part of the EU and geographically lies in the heart of Europe is of increasing importance for wealthy families, as is the safeguard afforded by the policy of investor protection promoted by the Luxembourg authorities.

1 Simone Retter is a partner at Retter Attorneys.

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The purpose of this chapter is not to give a complete view on taxation principles for private individuals in Luxembourg but merely to address the main characteristics and issues that are important in the context of wealth management.

II TAX

i General

Luxembourg tax-resident individuals are generally taxed on their worldwide income. This means that all income deriving from Luxembourg or from abroad has to be included in the annual tax return of a Luxembourg resident. Non-residents are normally taxed on income generated in Luxembourg and on their property located in Luxembourg. There are exceptions to this rule under double taxation treaties and other provisions. Based on the double tax treaties signed by Luxembourg, residents will be considered as tax exempt in Luxembourg for income related to real estate located and taxable abroad, but the income that is taxable abroad will be considered for the determination of the tax rate applicable to the income to be taxed in Luxembourg.

Luxembourg has in force double taxation treaties (DTTs) relating to income tax with 81 countries (as of June 2017). Most provide for double taxation relief through exemption. Investment income is generally subject to tax credit rules. Since 2009 Luxembourg approved the entry into, or updated, more than 54 double taxation treaties that provide for exchange of information on request following Article 26 of the OECD Model Tax Convention. Luxembourg has not entered into any double taxation treaties relating to inheritance tax and gift tax.

By two laws of 26 March 2014 and 29 March 2013, the Luxembourg parliament adopted Council Directive 2011/16/EU of 15 February 2011 on administrative cooperation in the field of taxation, introducing the concept of automatic exchange of information for certain information and providing for an exchange of information procedure applicable under the double taxation treaties.

On 18 December 2015, the Luxembourg parliament adopted Bill No. 6858 introducing the Automatic Exchange of Information Law (the AEOI Law) by implementing Directive 2014/107/EU, dated 9 December 2014 (which amends the previous Directive 2011/16/EU). This Directive extends the existing scope of the mandatory exchange of information as introduced by the Savings Directive 2003/48/EC and amended by Directive 2014/48/EU. As a consequence, the Savings Directive 2003/48/EC was repealed with effect from 1 January 2016 (law of 23 July 2016), and the Directive 2014/48/EU was no longer implemented into Luxembourg law. However, the exchange of information under the Savings Directive relating to the year 2015 has remained in force during 2015, reportable in 2016.

The AEOI Law entered into force on 1 January 2016. As from this date, Luxembourg Reporting Financial Institutions are required to provide to the fiscal authorities of other EU Member States and jurisdictions participating in the OECD Common Reporting Standard (CRS) details of financial account information of holders who are residents of, or established in, an EU Member State and certain dependent and associated territories of EU Member States or in a jurisdiction that has introduced the CRS in its domestic law. The automatic exchange of information is effective as of 1 January 2016. By 30 June 2017, Luxembourg Reporting Financial Institutions has been required to report to the Luxembourg Tax Authorities the 2016 information on accounts. Afterwards, the Luxembourg Tax Authorities will have until 30 September 2017 to report such information to the competent foreign authorities.
In application of the law of 18 December 2015, the Grand Ducal Decree of 15 March 2016 determines the list of the participating jurisdictions and the exempt products in relation to the CRS.

Unless there is a relevant double taxation treaty applicable, tax residency is determined in domestic law by two criteria: (1) domicile; or (2) usual place of residence.

Domicile is defined as the location of the individual’s abode, in circumstances where he or she maintains and uses it (as owner, tenant, holder of a life interest, or free of charge) with a permanence that shows that he or she does not intend to stay there on a temporary basis only.

Usual place of residence is defined as the place where the individual resides, if it can be shown that he or she does not intend to stay there on a temporary basis only. The law does not fix a minimum term and, depending on the circumstances, even a stay for less than six months can qualify as a usual place of residence. A stay for more than six months automatically qualifies as a usual place of residence and the individual is considered tax-resident (the tax liability being extended to the first six months). The concept of usual place of residence is a factual one.

Double taxation treaties concluded by Luxembourg mostly follow the OECD Model Tax Convention 1977 as revised in 2014. These provide that, where an individual is a resident of both contracting states, his or her status is determined as follows:

a. he or she is deemed resident only in the state where he or she has a permanent home available. If he or she has a permanent home in both states, he or she is deemed resident in the state that is the centre of his or her personal and economic relations (centre of vital interests);

b. if the centre of his or her personal and economic relations cannot be determined, or if he or she has no permanent home available in either state, he or she is deemed resident in the state in which he or she has a habitual abode;

c. if he or she has a habitual abode in both states, or in neither of them, he or she is deemed resident in the state of which he or she is a national; or

d. if he or she is a national of both states, or neither of them, the competent authorities in the contracting state will settle the question by mutual agreement.

There is no formal exit tax for individuals acting in the course of the management of their private wealth. Leaving Luxembourg does not trigger taxation on unrealised gains. However, capital gains realised on the disposal of substantial shareholdings held in Luxembourg entities after departing from Luxembourg are taxable, if the following two conditions are met:

a. the taxpayer was resident in Luxembourg, for tax purposes, for over 15 years; and

b. the taxpayer became non-resident less than five years before the disposal.

If a person resides in Luxembourg for less than six months it is possible to qualify as a non-resident (see above).

A specific regime applies to EU officials and other EU employees. If they reside in Luxembourg to perform their duties in the service of the EU, they maintain their original domicile for income tax, wealth tax and death duty purposes (Article 13, Protocol on the Privileges and Immunities of the European Union).

The official tax year runs from 1 January to 31 December. Taxpayers must file their tax returns by 31 March in the year following the relevant tax year and make quarterly advance
payments. If a non-resident generates income in Luxembourg, he or she must in certain cases file an annual tax return. Final payments (or reimbursements) are made once the final tax assessment has been received from the tax administration.

Any individual is entitled to request a reimbursement of potentially excessive taxes withheld on salaries and pensions derived from Luxembourg if he or she only resides in Luxembourg for part of the year (décompte annuel).

On 18 December 2015, the Luxembourg parliament adopted the 2016 Budget Law, through which the step-up principle has been introduced. Any non-resident individual who becomes a Luxembourg tax resident may revalue the purchase price of securities to their market value on the day that he or she becomes a Luxembourg tax resident. This new regime only applies to substantial shareholdings and to convertible loans in which the taxpayer holds a substantial shareholding.

Married couples have to jointly file a tax return, including their children under the age of 18.

Declared partners can be jointly taxed under certain conditions and upon request.

Additionally, as from 1 January 2018, resident and non-resident married couples can opt for individual taxation (tax reform of 23 December 2016).

As of 2016, Luxembourg-resident taxpayers who have omitted to declare some of their income to evade income taxes, inheritance taxes or registration duties will be able to regularise their situation further to some conditions, such as filing a tax return with the Luxembourg tax authorities on a spontaneous basis, covering their undeclared assets and income.

As a counterpart, a 10 per cent surcharge on taxes due is applied for amended tax returns submitted in 2016 and there is a 20 per cent surcharge for returns submitted in 2017.

Luxembourg is not a tax haven and income tax rates vary from zero to 45.78 per cent with the maximum marginal rate of 45.78 per cent applicable to income above €150,000 for a single person and €300,000 for a couple taxed jointly.

Income tax rates are progressive. Since 1 January 2017 the new marginal tax rate is 42 per cent for taxable income exceeding €200,004 (class 1 and 1a) or €400,008 (class 2). The contribution to the unemployment fund is 7 per cent, increasing to 9 per cent for taxable income exceeding €150,000 (class 1 and 1a) or €300,000 (class 2). Therefore, the maximum marginal tax rates applicable in 2017 can amount up to 45.78 per cent.

In addition, a dependency contribution of 1.4 per cent is applicable, bringing the overall maximum rates to 47.18 per cent. The temporary budget balancing tax of 0.5 per cent put in place in 2015 has been abolished as from 2017.

ii Taxation of investment income

Wealth tax and interest income

For investment income purposes, Luxembourg is a very attractive country to be a resident of for the following reasons:

a  wealth tax for private individuals has been abolished since 1 January 2006; and

b  a final withholding tax of 20 per cent (10 per cent until 2016, law of 23 December 2016) applies to interest payments made by Luxembourg paying agents to (or for the immediate benefit of) residents. This withholding tax fully discharges income tax if the beneficial owner is an individual acting in the course of the management of his or her private wealth (Law of 23 December 2005, as modified).
Residents can also opt for a final 20 per cent levy if they are the beneficial owners of interest payments from paying agents established outside Luxembourg, either:

- in a Member State of the EU or the European Economic Area (EEA); or
- in a jurisdiction that has concluded an agreement with Luxembourg in connection with the Savings Directive.

In these circumstances, the 20 per cent levy is calculated in the same way as if the paying agent was resident. The option for the 20 per cent levy must cover all interest payments made during the calendar year. Finally, residents who opt for this option must file a specific return before 31 March of the year following the year in which the interest was received.

This interest income and the assets producing the income will not need to be reported in the individual's annual income tax return.

The withholding tax previously applied under the EU Council Directive 2003/48/EC on taxation of savings income in the form of interest payments (the Savings Directive) has been replaced by the automatic exchange of information (see above).

**Dividend income**

Dividend income is subject to income tax but a 50 per cent exemption is granted for dividends received from the following types of company (Article 115 (15)a of the Luxembourg Income Tax Law):

- a fully taxable resident company;
- a fully taxable limited company, which is:
  - resident in a country that has entered into a double tax treaty with Luxembourg; and
  - liable to a tax equivalent to corporate income tax in Luxembourg.

Expenses linked to such dividends are only deductible up to 50 per cent.

Currently, a withholding tax of 15 per cent (17.65 per cent if borne by the distributing company) is levied on dividends distributed by fully taxable resident companies. This tax will be credited on Luxembourg income tax or can be reduced by the application of double tax treaties or refundable under certain circumstances.

**Capital gains**

Capital gains on moveable assets are taxable if:

- they are qualified as speculative capital gains (this applies when the period between acquisition and disposal is less than six months or when the transfer precedes the acquisition);
- they are realised on the disposal of a substantial shareholding in a resident or non-resident corporation. A resident individual owns a substantial shareholding in a company if he or she (either alone or together with his or her spouse or minor children) holds or has held (directly or indirectly) more than 10 per cent of the company’s share capital within five years preceding the disposal. A resident can also dispose of a substantial shareholding if he or she acquired free of charge, within five years preceding the disposal, a shareholding that constituted a substantial shareholding in the hands of the individual he or she acquired it from (or individuals if there were successive free transactions) that were not a result of a share capital increase. The shareholding must have been held for at least five years before disposal. A shareholding is a substantial shareholding if it constitutes at least 10 per cent of the share capital of the company. The tax is calculated on the gain at the rate of 33.33 per cent.

Expenses linked to the disposal of such capital assets are deductible up to 50 per cent.
transfers within the same five-year period). In these cases the capital gain will be fully
taxed but at a rate amounting to 50 per cent of the average tax rate (the maximum tax
rate is 23.59 per cent) and will apply a tax relief of €50,000 (€100,000 for spouses or
partners jointly taxed if the capital gain is realised after a six-month holding period).
These allowances can be used once per decade only;

c no capital gains tax is due if both:
• the gain is realised more than six months after the acquisition; and
• the moveable assets do not constitute all or part of a substantial shareholding;

d for non-residents capital gains on substantial shareholdings are taxable if: (1) the shares
are disposed of within six months of the acquisition or before the acquisition. This can
occur, for example, when shares in a listed company are sold before their acquisition
(in a regulated market that authorises such activity) or (2) the taxpayer was resident
in Luxembourg for tax purposes for more than 15 years and became non-resident less
than five years before the disposal. The provisions of double tax treaties can override
the rules for non-residents (double tax treaties entered into by Luxembourg generally
allocate the right to tax capital gains on moveable assets to the shareholder’s country of
residence); and

e a taxable capital gain is the difference between the transfer price and the acquisition price
(the acquisition price includes the acquisition costs). On the transfer of a substantial
shareholding, or a speculative investment, the applicable rate must be calculated. The
average rate applicable to the total income is calculated according to progressive income
tax rates and 50 per cent of the average rate is applied to the capital gain.

Capital gains on immoveable assets, real estate and land are taxable if:
a made within the first two years after purchase (or before purchase); and
b made more than two years after purchase. The capital gain is subject to income tax at
50 per cent of the global rate (with a current maximum rate of 23.59 per cent) after:
• adjustment of the acquisition price to take account of inflation during the period
  of ownership; and
• application of any applicable allowance.

The same allowances that are available for moveable assets apply. Capital gains realised on the
principal residence of the taxpayer would be exempt.

The following additional allowances apply:
a €75,000 for capital gains realised on the disposal of real estate inherited from a direct
ascendant (that is, someone from whom a person is descended, for example, a parent
or grandparent), if it was the principal residence of the taxpayer’s parents (or spouse’s
parents); and
b capital gains derived from the sale of an individual’s principal residence are exempt
from income tax.

Non-residents are taxed in the same manner as residents in relation to immoveable assets
located in Luxembourg.

Non-residents are subject to the same taxes as residents when buying assets and other
property located in Luxembourg. Both residents and non-residents pay a 6 per cent transfer
tax on real estate located in Luxembourg. There is a 3 per cent surcharge on real estate located
in the City of Luxembourg, and a 1 per cent transcription tax.
**Royalties**

For non-residents, royalties that are not linked to a permanent establishment in Luxembourg owned by a non-resident taxpayer and paid to a non-resident are not subject to withholding tax in Luxembourg, nor are they taxable by assessment.

For residents, royalties are subject to Luxembourg income tax for individuals.

### III SUCCESSION

#### i General

Luxembourg estate laws have mostly been implemented by the Napoleonic Code and are still today very similar to French estate law. For the determination of the law applicable, Luxembourg applies the last-domicile criteria for moveable assets and the law of situs for real estate.


For EU residents the situation has substantially improved since the adoption on 4 July 2012 by the European Council of Regulation (EU) No. 650/2012 on jurisdiction, applicable law, recognition and enforcement of decisions and acceptance and enforcement of authentic instruments in matters of succession and on the creation of a European Certificate of Succession (the Succession Regulation).

The Succession Regulation, which does not need to be implemented into national domestic law of the Member States, entered into force on 16 August 2012 and will have a direct effect on death situations occurring on and after 17 August 2015.

Under the Succession Regulation, citizens will be able to choose whether the law applicable to their succession should be that of their habitual residence or that of their nationality. In the absence of a designation of the law of nationality, the law applicable to a given succession will be the law of the habitual residence of the deceased.

The Succession Regulation will ensure that a given succession will be treated coherently under a single law and by one single authority and that a mutual recognition of decisions relating to that succession will be implemented throughout the EU. The applicable legal system will rule the entirety of the inheritance ('principle of the unity of succession').

Regulation (EU) No. 650/2012 is not applicable:

- to taxes and customs;
- to the status of natural persons, and the legal capacity of natural persons; or
- to questions relating to matrimonial law.

Luxembourg is a civil law country and as such has strong forced heirship rules. Under Luxembourg law only the children benefit from the protection of forced heirship rules. The spouse would not be a compulsory protected heir and can be excluded by virtue of a will.

Third parties or family members may only benefit from gifts or legacies if the assets fall into the scope of the free portion of the deceased. From a legal point of view, all gifts, even those executed abroad, and all contractual arrangements executed to the benefit of a third party (like insurance policies) will be reintegrated fictively in the mass of assets as of the day...
of death for the purpose of the calculation of the free reserve. The same would apply to assets structured in companies, foundations and trust structures. In cases of violation of a statutory reserve, the forced heirs may claim for reduction of the gifts.

### ii Taxation of successions and gifts

Inheritance tax (IHT) is levied on the total net estate left by a Luxembourg resident person valued on the day of the death except for:

- real estate located abroad; and
- moveable assets located abroad and taxed abroad by virtue of the citizenship of the deceased person.

When determining whether IHT is due on the deceased’s estate, Luxembourg considers whether the deceased was domiciled in Luxembourg at the date of his or her death. This can lead to conflict with the tests of other countries, which may use the residence or citizenship of the deceased, when determining whether the estate is liable to IHT.

IHT rates vary between zero per cent and 48 per cent (including surcharge), depending on the amount transferred and the relationship between the parties.

Exemptions of IHT apply in the following cases:

- on the portion those in the direct bloodline are entitled to under the intestacy rules;
- succession between spouses and partners bound by a partnership agreement registered for more than three years, with common children;
- succession between spouses married under the universal community regime, where it is expressly stipulated that the surviving spouse will receive all the community assets at the death of the other spouse (Articles 1094 and 1527, Civil Code);
- succession between spouses or partners bound by a partnership agreement registered for more than three years, where, on the death of the deceased:
  - the surviving spouse or partner receives a life interest (usufruct) in an asset, periodic payment or pension; and
  - the deceased’s children of a first marriage or partnership (or their descendants) receive the ownership of the asset or must pay the periodic payment of the pension;
- estates not exceeding a value of €1,250; and
- real estate situated outside Luxembourg.

The last domicile of the deceased is the decisive factor in establishing whether or not Luxembourg IHT applies.

Luxembourg levies a death transfer tax on the value of real estate located in Luxembourg held by non-residents at the date of their death. The death transfer tax rates vary between zero per cent and 48 per cent, depending on the amount transferred and the family relationship between the deceased and the heirs. Resident and non-resident heirs can be liable for death transfer tax on immovable property located in Luxembourg, if the deceased was non-resident.

Since the Law of 18 December 2009, the tax regime of estates where the deceased was a non-resident of Luxembourg has been aligned with the tax regime applicable to estates where the deceased was a resident of Luxembourg. As a result, the above exemptions and allowances apply identically in both cases.

For the determination of the taxable base the following assets are deemed to be aggregated:
gifts made by the deceased in the year preceding the death, unless gift tax has been paid;
other assets received by a third party without tax pursuant to a contractual arrangement (e.g., life insurance); and
moveable goods received on real estate sold by the deceased to the heirs within three months preceding the death if the deceased has reserved a right of usufruct.

The rates of IHT are as follows:
zero per cent on the forced heirship entitlement of those in the direct bloodline;
2.5 per cent on the portion exceeding the forced heirship entitlement of those in the direct bloodline (5 per cent on the portion exceeding the freely disposable portion);
5 per cent on property transferred between spouses and partners bound by a partnership agreement registered for more than three years, without children in common. In addition, a lump-sum deduction of €38,000 is granted to the surviving spouse or partner in this case;
6 per cent on property transferred between siblings, on the portion they are entitled to under the intestacy rules (15 per cent on the surplus (i.e., the portion exceeding their entitlement under the intestacy rules));
9 per cent on property transferred between uncles and aunts, and nephews and nieces (and between the adopting and the adopted, in a simple adoption), on the portion they are entitled to under the intestacy rules (15 per cent on the surplus);
10 per cent on property transferred between grand-uncles and grand-aunts, and great-nephews and great-nieces (and between adopted and adopting descendants, in a simple adoption), on the portion they are entitled to under the intestacy rules (15 per cent on the surplus); and
15 per cent on property transferred between unrelated persons.

In addition, a progressive surcharge (from 10 per cent to 220 per cent) is levied, depending on the value of inheritance. For example, the amount of tax is increased by:
10 per cent for estates with a value between €10,000 and €20,000; and
220 per cent for estates whose value exceeds €1.75 million, bringing IHT rates to a maximum of 48 per cent.

Gift taxes are levied on the fair market value of the gift transferred. Gift tax rates vary according to the relationship between the parties. Gifts have to be passed by notarial deed according to the Civil Code and as such are subject to a gift tax. Rates vary from 1.8 per cent to 14.4 per cent.

Rates of gift tax, including the surcharge, are as follows:
between 1.8 per cent and 2.4 per cent on gifts to those in the direct bloodline, depending on whether or not the gift is recoverable;
4.8 per cent on gifts between spouses and partners bound by a partnership agreement registered for more than three years;
6 per cent on gifts between siblings;
4.8 per cent on gifts made to certain public institutions, foundations and not-for-profit associations (the same rate applies in the case of inheritance);
8.4 per cent on gifts between uncles and aunts, and nephews and nieces;
Luxembourg

9.6 per cent on gifts between great-uncles and great-aunts, and great-nephews and
great-nieces; and
14.4 per cent on gifts between unrelated persons.

The rate is reduced by 50 per cent on gifts made under a marriage contract or with a view to
marriage.

No gift tax applies on:
a tangible assets transferred by hand are not subject to gift tax (unless the donor dies
during the year of making the gift, in which case the gift must be included in the
estate), as they are not registered;
b gifts executed by notarial deed in a foreign country. The law of the country where the
gift is received (locus regit actum) governs the tax treatment of the gift; and
c gifts made to scholarship foundations designed for universities and academic public
institutions (the same rate applies for inheritance) as well as, under certain conditions,
some other public foundations.

iii Legal regime

There are two types of succession: intestate and by will. In the absence of any testamentary
provision, the intestacy rules apply.

The designation of the beneficiaries under the devolution rules depends upon the legal
order in which these beneficiaries rank among themselves and in relation to the surviving
spouse. This order is determined by: the degree of relationship; and the lineage of inheritance.

The legal devolution system provides for a hierarchy of heirs and provides for several
rules (proximity, order and representation).

The hierarchy of heirs will be the following:
a the descendant (legitimate, natural, adopted);
b the surviving spouse;
c the privileged ascendants and collaterals (father, mother, brother, sister and their
descendants);
d the ascendants other than mother and father;
e the other collaterals; and
f the state.

The descendants are forced heirs. They exclude all the others, except the surviving spouse.
If a child has predeceased his or her parents then the descendant of that child comes in
representation of that child into the estate of the parent.

Where the surviving spouse has no children, the surviving spouse inherits all
the estate and excludes all other heirs (except if divorced or excluded by application of
a testamentary provision).

Where there are children present, the surviving spouse is entitled to a child portion
(without being lower than a quarter of the estate) or the usufruct on the main residence.

Children receive a portion of the deceased’s estate under a forced heirship regime
(Article 913, Civil Code). The amount of the forced heirship depends on the number of
children:
a one child: 50 per cent, leaving 50 per cent freely disposable;
b two children: one third each, leaving one third freely disposable; and
(c three or more children: 75 per cent divided equally, leaving 25 per cent freely disposable.

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If there are forced heirs, legacies and gifts can only be made on the freely disposable portion. When calculating the forced heirship, the following are taken into account:

- the assets that the deceased owned at death; and
- gifts made during the deceased's lifetime. These are valued as at the date of the deceased's death but taking into account their condition on the date of donation.

If the gifts granted by the deceased exceed the freely disposable portion, a forced heir who has been deprived of his or her rights can initiate an action for a reduction of these gifts. Under Luxembourg law, such a reduction must be granted. There are two types of reduction:

- if the gift has been made to a third party who is not an heir to the estate, the reduction will be in kind, meaning that the forced heir is, in principle, entitled to claim back the gift; and
- if the gift has been made to an heir of the estate, the reduction will be en moins prenant, meaning that the heirship will be reduced in proportion to the value of the gift received. If the value of the gift exceeds his or her entitlement as an heir, he or she will have to compensate the forced heir in cash.

The forced heirship regime cannot be avoided by holding assets through an offshore company, a trust or foundation, or in joint names. Only the deceased’s children (and not the spouse) are forced heirs. Only forced heirs can claim for a reduction of the gift, not their creditors.

Estate planning tools, testamentary provisions, gifts, corporate structures, insurance policies, proxies, joint bank accounts, fiduciary agreements, foundations and trusts are acceptable to the extent that they do not infringe forced heirship rules.

Except for the rules applicable on forced heirship and provision applicable to the surviving spouse, the heirs cannot normally challenge the intestacy rules. However, a challenge to these rules may be possible under certain conditions.

It is not essential for the owner of assets in Luxembourg to make a will, if he or she agrees to his or her estate passing under the intestacy rules. However, an individual must make a will to take advantage of the free portion of the estate or to protect the surviving spouse's interests.

Normally, a will set up by a Luxembourg resident would be subject to Luxembourg law. Under the EU Succession Regulation (also known as Brussels IV), discussed above, a foreign national can make a will governed by the law of his nationality (see Section III.i, supra).

A will that has been validly executed abroad under a foreign law can be recognised in Luxembourg under the Hague Testamentary Dispositions Convention.

There are three forms of testamentary provisions:

- handwritten (holographic) will (Article 970, Civil Code). This must be entirely handwritten, signed and dated by the testator;
- notary deed (Articles 971 to 975, Civil Code). This must be executed before two notaries or one notary assisted by two witnesses. Normally, a notary public takes a record of the testamentary provisions as dictated by the testator. The notary then reads the testamentary provisions to the testator and the will is signed by:
  - the testator and the notaries, if the will was executed before two notaries; or
  - the notary and the witnesses, if the will was executed before a notary and two witnesses; and
Testamentary contracts (except in marriage contracts) and inheritance agreements (*pacte sur succession future*), by which a person waives or grants a right in relation to assets of a future estate, are, in principle, invalid (with the following exceptions: certain provisions included in donation deeds are valid, and insurance contracts are valid).

The deceased’s estate vests in the heirs on his or her death (Civil Code). The legal heirs automatically become co-owners on the death of the deceased. However, the heirs can:

- accept the estate;
- accept or refuse the estate after reviewing the estate inventory, showing its assets and liabilities (with three months to review the inventory and 40 days to accept or refuse); or
- refuse the estate.

As the heirs benefit from the rights of joint owners, they can sell their share in an asset to another heir or to a third party (Article 815, Civil Code). A person cannot be forced to stay in a joint-possession situation.

Before determining the assets and liabilities of an estate, any assets that were common to the spouses under a matrimonial regime must be liquidated.

There are two types of marital regime:

- the legal regime. This is the regime applicable if there is no marital contract. The assets and debts are owned in common (apart from those assets and debts acquired before the marriage or which are inherited or received as gifts); and
- the conventional regime entered into by notary deed. This can provide for adaptations to:
  - the legal regime (e.g., by providing that assets and debts acquired before the marriage are common to both spouses or by providing for a universal community regime, meaning that all assets are owned in common between the spouses); and
  - the separate ownership regime (each spouse retains sole ownership of the assets they acquired before and after entering into the marriage).

The Law of 9 July 2004 grants legal rights to cohabitants (including those of the same sex) if they declare the partnership with their local authority. This has the benefit of, for example, protection in relation to common property and tax advantages. If a declaration has been made, a partnership grants to the partners similar legal rights to those of married couples.

The surviving partners only inherit from the dead partner if a will has been made.

If the two partners are bound by a partnership of more than three years and if the dead partners had descendants or common children with the surviving partner, the inheritance tax rate is zero per cent.

If the two partners are bound by a partnership of more than three years and if the dead partner did not have descendants or common children with the surviving partner, the inheritance tax rate is 5 per cent (for inheritance tax purposes, a lump-sum deduction of €38,000 is applicable for the surviving partner).

The deadline for filing the IHT tax return depends on where the deceased died.
IV WEALTH STRUCTURING AND REGULATION

Luxembourg legal tools used in wealth structuring are numerous and can address almost every need. They range from corporate structures and partnerships to contractual instruments such as insurance policies and fiduciary agreements, and to civil law instruments such as donations, wills and matrimonial agreements. Luxembourg has signed a large number of HCCH conventions relating to international private law issues.

i Structuring for estate planning reasons:
As a majority of estates are exempt from IHT no advance estate planning is necessary in most cases. For the remaining cases where IHT would be applicable, donation by hand of cash amounts, securities or shares in Luxembourg or foreign companies, as well as insurance policy structures, would be used. Given the fact that Luxembourg law generally invalidates inheritance agreements by which a person waives or grants a right in relation to assets of a future estate, structuring for succession purposes has to be used with caution.

Luxembourg has enacted a law on fiduciary agreements that are contracts under which a fiduciary (trustee) that, subject to the obligations determined by the parties, the fiduciary becomes the owner of assets (Article 5, Law of 27 July 2003). The assets under a fiduciary contract are separated from the fiduciary’s personal assets and can only be claimed by creditors who have rights over them. The fiduciary assets are not included in the fiduciary’s personal estate on bankruptcy or liquidation, and the fiduciary must account for the fiduciary assets separately from his or her personal assets.

Luxembourg has ratified the HCCH Convention on the Law Applicable to Trusts and on their Recognition 1985 (Hague Trusts Convention) (Law of 27 July 2003). At present, Luxembourg does not have its own trust legislation but trusts validly set up under foreign legislation can be administered in Luxembourg and are recognised under the conditions provided for by the Hague Trusts Convention. In that respect claims can be filed against a trustee or trust assets in Luxembourg by a spouse, a civil partner of a settlor or a beneficiary or a heir.

In June 2013, the Luxembourg government has adopted a draft law on the creation of a private wealth foundation. This draft law, if adopted, will allow Luxembourg to offer a new legal vehicle benefiting from having legal personality, as distinct from the personality of its founder or its beneficiaries, a legal entity that is the subject of rights and liabilities and duly represented by its board of directors. The draft law contains strict rules on governance, provides for a balance between the protection of the settlor’s interest and the beneficiaries’ interest. The draft law contains state-of-the-art provisions on Financial Action Task Force compliancy rules and is at the same time very protective of the private client in respect of information available to third parties.

The private wealth foundation will be a legal vehicle exclusively dedicated to private clients and private wealth. The private wealth foundation will have an ordinary tax regime and should normally benefit from the various tax treaties concluded by Luxembourg. The draft law also clarifies issues on indirect taxation such as gift taxes and estate taxes.

ii Structuring for tax planning reasons
Luxembourg has no ‘controlled foreign corporation’ legislation applicable to individuals (subject to implementation of the Anti-Tax Avoidance Directive). With appropriate structuring the tax impact can be optimised on investment income by structuring the assets
of the client: (1) in a private asset management company; (2) by structuring substantial shareholdings in financial holding companies; or (3) by holding a portfolio of bankable assets through capitalising investment funds.

V CONCLUSIONS & OUTLOOK

The Luxembourg government has committed to continue with its strategy to make Luxembourg a major international centre in the field of wealth management. The recent law on family office activities, as well as the draft law on the private wealth foundation, clearly demonstrates this aim.

A main international topic in 2017 remains the fight against tax fraud and the pressure on those financial centres that are viewed as being only partially compliant or are considered to be offshore financial centres. The recent Panama Papers issue clearly highlights the importance for financial centres to be globally compliant. The implementation of the automatic exchange of information applicable since 1 January 2016 will assure Luxembourg of its place in the future landscape of the wealth management industry, as this industry, worldwide, moves towards greater transparency and private clients move to overall tax compliancy. For the compliant private client it will enhance the attractiveness of Luxembourg as an internationally recognised, secure and truly compliant financial centre.

Another international topic in 2017 will be the sustainability of domestic banking secrecy laws. Along with the move to greater transparency the role for these laws will also change, becoming of even greater importance to the private client as the gatekeeper to the private sphere and to overall security for wealthy families. The implementation by the government of a tax amnesty law to be applied in the tax years 2016 and 2017 again puts the issue of the sustainability of domestic banking secrecy law in the spotlight.
I INTRODUCTION

Malaysia is experiencing a year of challenges in 2017 as the nation moves towards Vision 2020, an ideal high-income developed economy set out in the Sixth Malaysia Plan 1991, and continues to be beleaguered by political turbulence and the global drop in crude oil and gas prices, revenue from which has traditionally been the stalwart of the Malaysian economy. Despite uncertainties in the global economy and slowdown in the economies of major trading partners, in the 2017 Budget themed ‘Ensuring Unity and Economic Growth, Inclusive Prudent Spending, Wellbeing of the Rakyat’ tabled on 21 October 2016, Malaysia’s targeted growth trajectory for 2017 is set at an admirable 4–5 per cent as compared to forecast global growth of 3.4 per cent. In addition, the government is expected to achieve a fiscal deficit target of 3 per cent of GDP in 2017 (reduced from 3.1 per cent in 2016).

This year further marks the third year of implementation of the goods and services tax that was first introduced on 1 April 2015 to address issues such as a narrow tax base and overdependence on oil and gas revenue, which has invariably exposed Malaysia’s economy to a precarious position subject to the volatility of oil and gas prices.

In the interim, the lucrativeness of Malaysia as a jurisdiction attractive to private wealth is relatively measured. While the Asia-Pacific region continues to record a robust high net worth individual (HNWI) population and healthy wealth growth rates (at 9.4 per cent and 9.9 per cent respectively) amid a decreased growth rate for the global climate in 2016, Malaysia experienced a relatively modest growth of HNWIs between 2013 and 2014, and the population of recorded a 3 per cent increase in 2016 compared to a 15 per cent decline in 2015 according to the Knight Frank’s Wealth Report 2017, and is anticipated to drive 0.2 per cent of global HMWI wealth growth through 2025.

1 DP Naban is a senior partner, SM Shanmugam is a partner, Ashley Lee Si Han is a senior associate and Heng Jia is an associate (Christine Lay Kei Een is a pupil) at Lee Hishammuddin Allen & Gledhill.
4 Country Note – Malaysia, extract from the Economic Outlook for Southeast Asia, China and India, 2014: Beyond the Middle-Income Trap (http://dx.doi.org/10.1787/saeo-2014-en) (available for download).
7 Figure 6 of the World Wealth Report 2016 (www.knightfrank.com/wealthreport) (available for download).
Nonetheless, with the introduction of new legislation and concurrent efforts to bolster Labuan’s status as an international business and financial centre, Malaysia continues to position itself to cater to the growing volume of private clients in the region. The 2017 Budget also contains a host of balanced measures to support Malaysia’s goal to achieve advanced and high-income status and to surpass the US$15,000 threshold of a high-income economy by 2020.8

II TAX

i Personal taxation

Malaysia’s taxation is principally governed by the Malaysian Income Tax Act 1967 (MITA). While the MITA lays out the fundamentals of personal income tax, there are other developments and case law in relation to personal income tax in Malaysia that should be taken into account in ascertaining the Malaysian taxation regime as a whole. Similar to other jurisdictions, such as Singapore, the scope of taxation in Malaysia is based on a territorial system.9

An individual in Malaysia is liable to income tax if he or she has income accruing in or derived from Malaysia (Malaysia-sourced income) or received in Malaysia from outside Malaysia (foreign-sourced income) for a year of assessment, for income in relation to banking, insurance, and sea or air transport businesses. Otherwise, all foreign-sourced income is exempt from tax.

The residence status10 of an individual is also an important factor in determining how an individual will be taxed, as a resident individual is taxed on both income accruing in or derived from Malaysia and foreign-sourced income, while a non-resident individual is only taxed on income accruing in or derived from Malaysia.

Pursuant to the 2016 Budget, the prime minister increased the tax rate for income earners of 600,001 ringgit to 1 million ringgit from 25 per cent to 26 per cent and for income earners of 1 million ringgit and above, from 25 per cent to 28 per cent.11

As stated earlier, the law imposes income tax on profits derived in two circumstances: Malaysia-sourced income and foreign-sourced income in relation to banking, shipping, insurance, and sea or air transport businesses. However, Malaysian law does not provide any definition of ‘income’. Nonetheless, the MITA categorises income into a number of classes.12

Business income

Business income includes any gains derived from a trade, profession or vocation. In ascertaining whether the gains are derived from a trade, profession or vocation, one should look at the relevant case law (including countries with taxation laws that are pari materia to Malaysia) as the MITA does not provide any statutory definitions.

10 Section 7 and Schedule 1 of the Income Tax Act 1967.
Trade
In determining whether an individual is carrying on a trade, one should consider the following factors (commonly known as the six badges of trade):

- **a** the subject matter;
- **b** period of ownership;
- **c** frequency of transactions;
- **d** supplementary work on or in connection with the asset realised to enhance marketability;
- **e** organisation set up to dispose of goods; and
- **f** motive for transaction.\(^{13}\)

Profession
Profession is also not defined in the Act. Case law has defined ‘profession’ to involve ‘the idea of an occupation requiring either purely intellectual skill, or if any manual skill, as in painting and sculpture, or surgery, skill controlled by the intellectual skill of the operator, as distinguished from an occupation that is substantially the production, or the sale, or arrangement for the production or sale of commodities’.\(^{14}\)

Vocation
This word is also not defined in the MITA. Therefore, we look to case law for guidance on its definition. For instance, the case of *Patridge v. Mallandaine* [(HL) 2 TC 179] held that persons who attend races, engaging themselves in systematic bets, are involved in a vocation.

An individual engaged in a business that falls under any of the above categories is subject to income tax on gains obtained thereof. Similarly, other gains arising from the running of a business, such as rental income and interest income, are also taxable.

Employment income
Employment income is any gain derived from employment. Section 2 of the MITA defines employment as any situation where the relationship of ‘master and servant’ subsists, or any appointment or office, whether public or not and whether or not that relationship subsists, for which remuneration is payable.\(^{15}\)

A fundamental principle of Malaysian income tax is that for income to be taxable as employment income it must be in respect of having or exercising an employment.\(^{16}\) The law in relation to employment income is quite clear in that one can clearly say that an individual who has a master and servant relationship or is remunerated for holding an appointment or office clearly falls under this category.

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\(^{13}\) See the Radcliff Commission final report in 1954, United Kingdom.

\(^{14}\) *CIR v. Masse* [(CA) 12 TC 41].

\(^{15}\) Section 2 of the Income Tax Act 1967.

\(^{16}\) *McMillan v. Guest* (24 TC 190).
ii  Gift
The Malaysian parliament has not specifically made laws to govern gifts. In general, gifts are not income and, hence, not taxable. Nonetheless, one should look at whether the gift is made voluntarily and whether it is connected to a business or employment. In short, the character of the gift would depend on the motive of the giver.17

iii  Succession
There is no inheritance tax in Malaysia. Hence, property transferred by a predecessor to a successor in the context of effecting succession will not be taxed. Generally, capital gains are not taxed in Malaysia, except for gains derived from the disposal of real property or shares in a real property company (real property gains tax). Real property includes any land and any interest, option or right over such land in Malaysia.18 The rate for real property gains tax for individuals is between zero per cent (if the property is held for more than five years) and 30 per cent (if the property is disposed of within three years). For individuals who are not citizens or permanent residents,19 the rate applicable is 5 per cent (if the property is held for more than five years) and 30 per cent (if the property is disposed of within five years).20

iv  Cross-border developments
With the worldwide focus on globalisation and the fact that cross-border transactions are becoming increasingly simpler to administer, international business operations and the use of international wealth structures by wealthy families or individuals are gaining popularity. In this regard, tax implications are inevitable.

Akin to many other countries, Malaysia operates a territorial scope of taxation. The same income from a cross-border transaction may be taxed in two or more countries depending on determination of residency and permanent establishment. In this circumstance, double tax agreements (DTAs) entered into with various countries accommodate and deal with the tax conflicts.

As such, in Malaysia, when the same income has been subject to tax in two or more countries, the MITA allows the minister to declare arrangements that afford relief or credit, with the view of reducing the incidence of double taxation.21 For countries that have signed a DTA with Malaysia, taxpayers are accorded bilateral credit.22 The relief is given by way of statutory order in the Government Gazette. For countries that do not enter into a DTA, taxpayers could resort to unilateral credit.23

In this context, one frequently asked question is that in the event of conflict, does the treaty or domestic law take precedence? In general, this is very much dependent on each respective country’s view on international law. In countries such as the United States, treaties

19 See Section 2 of the Real Property Gains Tax Act 1976, on definition on ‘permanent resident’.
22 See: Paragraph 16 of Schedule 3 of the Income Tax Act 1967. Bilateral credit means credit in respect of foreign tax which, by virtue of any arrangements having effect under Section 132, is to be allowed as a credit against Malaysian tax.
have the same footing as domestic law.\textsuperscript{24} By comparison, in Malaysia, by virtue of Section 132(1)(b) of the MITA, which reads, ‘…not withstanding anything in any written law’, these legislated words clearly give DTA precedence over domestic law.\textsuperscript{25} This principle has been well established and confirmed by Malaysian courts on several occasions.\textsuperscript{26}

To further foster cross-border transactions, specific provisions have recently been enacted to provide for tax information exchange arrangements and mutual administrative assistance arrangement.\textsuperscript{27} Treaty countries would exchange information and cooperate to eliminate tax avoidance.

III SUCCESSION

i Introduction

Benjamin Franklin once said: ‘In this world, nothing is certain except death and taxes.’ Of the two, death, though certain, cannot be predicted as to when it will happen. It is, therefore, important to ensure that one’s estate is well planned in advance.

The law of succession is an important law that regulates the inheritance and entitlement of properties both moveable and immovable and even trusts and debts in the event of death. There are three main legislations in this area – the Wills Act 1959, the Probate and Administration Act 1959 and the Distribution Act 1958.

The law of succession is influenced by English common law,\textsuperscript{28} owing to the fact that Malaysia was a colony of the British Empire prior to its independence on 31 August 1957.

ii Key changes and applicable changes affecting personal property

The major change to the Malaysian law of succession was made in 1997, when the Distribution Act 1958 was amended\textsuperscript{29} in terms of the procedure for intestate distribution. The amendment to the Distribution Act 1958, among others, recognised equality between genders (i.e., husband and wife) and also improved the rights of parents of an intestate deceased.\textsuperscript{30}

iii Cross-border developments

Although Malaysia is part of the Association of Southeast Asian Nations (ASEAN), there has been a lack of movement to introduce cross-border law of succession between Member States similar to that done by the European Union in 2015.\textsuperscript{31}

The closest resemblance to cross-border law of succession can be seen among Commonwealth Member States, of which Malaysia is a member. In cases where grants


\textsuperscript{28} Section 3 of the Civil Law Act 1956 (Revised 1972).

\textsuperscript{29} See: Distribution (Amendment) Act 1997.

\textsuperscript{30} Section 6 of the Distribution (Amendment) Act 1997.

\textsuperscript{31} See: EU Law 650/2012 (Brussels IV Regulation).
of representation are issued in the courts of competent jurisdiction in a Commonwealth Member State, the same can be resealed in courts of equal level at other Commonwealth member states or vice versa.\textsuperscript{32}

As it stands, of the 10 Member States of ASEAN, only three (i.e., Malaysia, Singapore and Brunei Darussalam) are members of the Commonwealth. There is no legislation to allow the re-sealing of a Malaysian grant of representation in non-Commonwealth Member States such as Thailand, Indonesia and the Philippines. In an era of globalisation, the time has come for ASEAN countries to look into harmonising laws of succession.

\section*{IV WEALTH STRUCTURING & REGULATION}

\subsection*{I Common vehicles for wealth structuring}

It was commonly perceived that only the wealthy would plan their wealth and finance. However, as time passed, and through education and awareness, many now realise the importance of planning their wealth and finance in advance.

The common vehicles or ‘instruments’ used in wealth, financial and estate planning are wills, codicils, trusts, foundations and charitable remainder trusts. In particular, wills and trusts are instruments that have proven effective in succession planning. HNWIs commonly use the combined package of trusts, foundation and charities in managing their wealth, with the goal of having their wealth to last over a few generations.

\subsection*{Legal treatment}

Over the years, Malaysian courts have revamped and expedited the process of obtaining a grant of representation. Malaysian courts generally dispose uncontested applications for a grant of representation in under three months from the date of filing.\textsuperscript{33}

There are several advantages in making a will. The main advantages are that it only takes effect after the death of the testator, hence, leaving the testator in total and complete control of his or her personal assets during his or her lifetime, and the person has control over the manner in which his or her estate is distributed after death.\textsuperscript{34} In this regard, a valid will must comply with the requirements under the Wills Act 1959. For example, a will must be in writing and signed by the testator in front of two witnesses.\textsuperscript{35} There can only be one will at any given time and the latest will revokes all former wills, codicils and testamentary documents. A will is also an effective tool to ensure that beneficiaries are sufficiently protected. For example, against trustees who may have the intention to delay distribution of assets.\textsuperscript{36}

Trust instruments,\textsuperscript{37} on the other hand, bypass the need for court processes (i.e., a grant of representation) but the effect of a trust is that the settlor will have to part with his or her assets from the time of formation of the trust, thus effectively putting him or her out

\begin{itemize}
  \item Section 52 of the Probate and Administration Act 1959 (Revised 1972).
  \item See: Speech by The Right Honourable Tun Arifin Bin Zakaria, Chief Justice of Malaysia at the opening of the legal year 2016 at paragraph 50.
  \item As per the effect of Section 18 of the Wills Act 1959 (Revised 1988).
  \item Section 5 of the Wills Act 1959 (Revised 1988) and Chenna Gounder Kandasamy v Angamah Sunappan [2016] 7 CLJ 914.
  \item See Liong Siew Keng & Ors v Ho Soon Cheng [2016] 6 CLJ 761.
  \item As defined in Parameshiri Devi & Anor v Pure Life Society [1971] 1 MLJ 142.
\end{itemize}
of control of his or her own assets during his or her lifetime. Trust instruments also cater for very specific subject matters and may not be a viable replacement for a will in terms of testamentary disposition of assets. A trust instrument is a good supplement to a will.

Charities and foundations, while getting more popular by the day in countries such as the United States, have yet to gain any real form of traction in Malaysia. In particular, the benefits of setting up a foundation – a hybrid of a trust and a company – that is able to tap into both the benefits of trusts and the advantages of being a corporate body, have not attracted the attention of individuals in Malaysia, with the exception of those HNWIs as a form of asset protection and wealth management.

Though Malaysia has the necessary foundation law\textsuperscript{38} to offer private foundations as a vehicle for the protection of assets and estate planning, many have not seized this opportunity, perhaps because of a lack of awareness or high set-up costs. Just like wills and trusts, the public need to be educated and introduced to these two vehicles and when costs of setting up are reduced, perhaps we will see more resorting to foundations and charities for asset protection and estate planning.

Wills are, by far, the most basic instrument to fall back on for estate planning and wealth management after death.

**Tax treatment**

The principles of English trust law are instrumental in moulding the Malaysian law of trusts. Today, it is primarily governed by the Trustees Act 1949 and the Civil Law Act 1956,\textsuperscript{39} which still allow for the applicability of the common law of England, rules of equity and statutes of general application, subject to qualifications.

From a taxation perspective, Section 61(2) of the MITA provides that the income of the trust body of a trust shall be assessed and taxed separately from the income of a beneficiary from any source in relation to the trust.\textsuperscript{40} In other words, this necessitates that income tax can only be charged once, either in the hands of the trustee or the beneficiary when it is paid out to the latter.

For a trust body, any source forming part of the property of the trust, any source of a trustee of the trust, being a source of his or hers by virtue of specific provisions of the MITA and any income from any such source, save that gains arising from the realisation of investments from unit trusts, shall be treated as income of the trust body of the trust.\textsuperscript{41}

For a beneficiary to a trust, subject to qualifications, he or she will be subject to tax on his or her share of income. It is noted, however, that in relation to sources of income of a beneficiary to said trust, it may comprise the following:

\begin{itemize}
  \item[a] ordinary source from the trust;\textsuperscript{42} and
  \item[b] further sources,\textsuperscript{43} defined under the relevant provisions as the amount of excess from the difference between statutory income from the beneficiary’s ordinary source in
\end{itemize}

\textsuperscript{38} See the Labuan Foundations Act 2010.
\textsuperscript{39} Section 3 of the Civil Law Act 1956.
\textsuperscript{40} Section 61(2) of the Income Tax Act 1967.
\textsuperscript{41} Section 61(1)(b) of the Income Tax Act 1967.
\textsuperscript{42} Section 61(1)(c) of the Income Tax Act 1967.
\textsuperscript{43} Section 61(5) of the Income Tax Act 1967.
relation to the trust and the total income from all sums received in Malaysia from the
trust body in the basis year, together with all sums received from outside Malaysia in
any year and remitted to Malaysia in the basis year.

On top of that, a trust body is regarded as resident for the basis year for a year of assessment
if any trustee member of that body is resident for that basis year. In certain circumstances,
the trust body in question shall not be regarded as resident in Malaysia for that basis year if:

a. the trust was created outside Malaysia by a person or persons who were not citizens;
b. the income of the trust body for that basis year is wholly derived from outside Malaysia;
c. the trust is administered for the whole of the basis year outside Malaysia; or

d. at least half of the number of the member trustees are not resident in Malaysia for the
   basis year.

For a beneficiary, residency status is regulated by Sections 7 and 8 of the MITA.

The residence status of a trust is pertinent for the following reasons:

a. a further source of a non-resident individual derived from sources outside Malaysia is
   exempt from income tax when remitted into Malaysia; and

b. if the trust body is resident for the basis year in question:
   • the amount payable in respect of any annuity for the basis year shall be deemed to be
     derived from Malaysia whether or not the trust body has any total income for that year of
     assessment; and
   • in ascertaining the total income of the trust body for that year of assessment that amount
     shall be deducted in a specific manner stipulated by the relevant provisions.

In terms of tax rates, the applicable tax rate in respect of a trust body is fixed at a rate of
25 per cent for the year of assessment 2014, and 24 per cent for subsequent years. This can be
contrasted with the applicable tax rate for resident individuals, which stretches across a range
of zero per cent to 28 per cent, depending on the income bracket, or that of a non-resident
individual, which is fixed at 28 per cent. With the comparative tax rates in mind, the setting
up of trusts in Malaysia may be a viable option for private clients.

In line with Malaysia’s efforts to brand itself as an Islamic investment hub, from the
year of assessment 2007 to year of assessment 2020, exemptions are accorded to resident
companies in Malaysia in respect of payment of income tax for statutory income derived
from a business of providing fund management services to foreign investors or to local
investors in Malaysia in respect of funds managed in accordance with sharia or Islamic
principles.

In Malaysia, the law governing charities is not entrenched in any specific act and
instead comprises an array of Malaysian legislation, including the Companies Act 1965 and
the Societies Act 1966, and case law.

46 Section 63(3) of the Income Tax Act 1967.
49 Income Tax (Exemption) (No. 6) Order 2008 (PU (A) 255/2008).
The terms ‘charity’ or ‘charitable institution’ are not expressly defined in the MITA. Rather, Section 44(6) of the MITA accords deductions at specific rates for gifts of money made to an organisation or institution \(^{50}\) approved by the relevant authorities. This deduction is read in line with Paragraph 13 Schedule 6 of the MITA, which accords tax exemption to institutions, organisations or fund approved for the purposes of Section 44(6) or religious institutions, organisations or funds that are not operated or conducted primarily for profit and that are established in Malaysia exclusively for the purposes of religious worship or the advancement of religion. In short, an organisation, institution or fund that obtained approval from the relevant authorities under Section 44(6) \(^{51}\) will automatically \(^{52}\) be eligible for tax exemption.

On the other hand, with effect from the year of assessment 2017 and subsequent years of assessment, ‘fund’ is now defined under the MITA to mean ‘a fund administered and augmented by an institution or organisation in Malaysia for the sole purpose of carrying out the objectives for which the fund is established or held and that fund is not established or held primarily for profit’ \(^{53}\).

Further, it is noted that an approved organisation, institution or fund may also carry out businesses whereby the business is carried on in the course of the actual carrying out of the primary purpose of the institution, organisation or fund, or the work in connection with the business is mainly carried on by persons for whose benefit the institution, organisation or fund was established. \(^{54}\)

The MITA allows such an approved organisation, institution or fund to apply no more than 25 per cent of its accumulated funds as at the beginning of the basis period for the year of assessment for the carrying on of or participation in a business, provided that its profits shall be used solely for charitable purposes or for the primary purpose for which the institution, organisation or fund was established, or to carry out charitable activities outside Malaysia with the prior consent of the Minister. \(^{55}\)

It is also noted that with effect from the year of assessment 2017, a registered religious institution or organisation established in Malaysia exclusively for the purpose of religious worship or the advancement of religion and is not operated or conducted primarily for profit is exempt from payment of tax in respect of its gross income derived from all sources and is exempted from furnishing a return under Section 77 of the MITA. \(^{56}\)

While internal guidelines and rulings by the Malaysian Inland Revenue Board have no legal effect, \(^{57}\) it is worth noting that the Malaysian Inland Revenue Board issued a guideline in which it stipulated that at least 50 per cent of the income and donation received must be spent yearly in carrying out the objectives of the institution, organisation or fund, and failure to meet this condition will result in withdrawal of the exempt status. \(^{58}\)

\(^{50}\) Section 44(7) of the Income Tax Act 1967, which defines ‘institution’ and ‘organisation’ respectively.


\(^{52}\) See: Public Ruling of the Malaysian Inland Revenue Board (Public Ruling No. 1/2015).

\(^{53}\) See Finance Act 2017

\(^{54}\) Section 44(7B) of the Income Tax Act 1967.

\(^{55}\) Section 44(7A) of the Income Tax Act 1967.

\(^{56}\) See Income Tax (Exemption) Order 2017 (PU (A) 52/2017)


\(^{58}\) See the IRB’s Guidelines for Application of Approval under Subsection 44(6) of the Income Tax Act 1967.
From the wording of the legislation as well as the position adopted by the Malaysian Inland Revenue Board in its Public Ruling, it appears that these businesses would not jeopardise the tax exemption enjoyed under paragraph 13 Schedule 6 unless the approved organisation, institution or fund applies more than 25 per cent of its funds for the business in question, does not use the profits or income derived solely for charitable purposes or for the primary purpose for which the institution, organisation or fund was established, or carries out charitable activities outside Malaysia without prior consent of the Minister.

Therefore, the requirement for approval, as well as limitations in terms of the nature of business and the utilisation of profits derived, should very well be taken into consideration when weighing the merits of a charitable institution or organisation or fund as a wealth-structuring vehicle.

In Malaysia, the establishment of a limited liability partnership (LLP) is governed by the Limited Liability Partnerships Act 2012. Unlike conventional partnerships under the Partnership Act 1961, under which individual partners are subject to income tax, an LLP is treated as a separate taxable person for the purposes of the MITA. Its residence status is accorded for under Section 8(1A) of the MITA and the MITA stipulates that for an LLP the responsibility for carrying out all acts required to be done by or on behalf of a LLP lies jointly and severally with either the compliance officer appointed among the partners or if no such person is appointed, any one or all of the partners.

With effect from year of assessment 2017, for an LLP resident in Malaysia which has a total contribution of capital (whether in cash or in kind), the chargeable income for the first 500,000 ringgit would be 18 per cent and for every ringgit exceeding 500,000, the tax rate would be 25 per cent for year of assessment 2015, and 24 per cent for subsequent years. It is noted that this provision does not apply if 50 per cent of the capital contribution (cash or in kind) is directly or indirectly contributed by a company, 50 per cent of the paid up capital of the ordinary shares of the company is indirectly owned by the LLP, or 50 per cent of the capital contribution and 50 per cent of the paid up capital is directly or indirectly owned by another company.

Further, subject to restrictions, a registered LLP is exempted from payment of income tax in respect of the amount of chargeable income derived from the carrying on of a business in the basis period for a year of assessment in respect of years of assessment 2007 and 2008.

It is also pertinent to note that where a partnership or company converts to an LLP, for the year of assessment in which the conversion occurs, every partner shall continue to be personally assessable and chargeable to tax for that year of assessment and for any previous year of assessment before the conversion in like manner and to the like amount, as the company would have been taxed prior to the conversion.

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60 See qualification at Section 44(7B) of the Income Tax Act 1967.
61 Ibid.
62 See definition under Section 3 of the Limited Liability Partnerships Act 2012.
65 Under the the Limited Liability Partnership Act 2012.
66 See Income Tax (Exemption) (No. 2) Order 2017 (PU (A) 117/2017).
67 Subsections 75B(3) and (4) of the Income Tax Act 1967.
The Labuan perspective

The Federal Territory of Labuan, a federal territory of Malaysia best known as an offshore financial centre, offers attractive alternatives in its bid to attract investors. With a sound and robust regulatory framework in place, some of its key highlights are as follows.

The existence and constituents of a Labuan trust is governed by the Labuan Trusts Act 1996. Under the Act, income derived from trust property in respect of a Labuan trust is subject to the Labuan Business Activity Tax Act 1990,68 which imposes tax at a lower rate of 3 per cent for Labuan trading activity,69 or non-chargeable for non-trading activity.70 Alternatively, taxpayers may elect to be charged to tax 20,000 ringgit71 or to be charged to tax in accordance with the MITA.72

It is noted, however, that the rate of 3 per cent will only be applicable to trust property that does not include Malaysian property, and generally, trust property excludes Malaysian property,73 unless prior consent of the authorities is obtained or the trust in question is for charitable purposes. Where the trust property in question includes Malaysian property, income from the trust property is subject to the MITA.74

Further, affairs pertaining to a Labuan trust enjoy legislative protection in terms of higher levels of secrecy with strict disclosure laws, and leave from the court is necessary if any details in any court proceedings are to be divulged.75

Where a Labuan trust is validly created, the courts do not vary or set it aside. In addition, the courts do not recognise the validity of any claim against the trust property in question pursuant to the laws of a foreign jurisdiction unless in specific circumstances,76 or if it is proven that the trust is fraudulent.77 The unenforceability of claims of a foreign jurisdiction may be a factor to be taken into account in considering the viability of a Labuan trust.

The accession of the Labuan Financial Services and Securities Act 2010 further establishes a more comprehensive framework in relation to private funds management in Labuan. The Act governs the requirements on an establishment of a private fund in Labuan, including the requirement for notice for private funds,78 as well as the appointment, duties and other aspects pertaining to private trust companies in Labuan to increase its appeal, with regard to the provision of wealth management facilities, and attract more private investors.

A recent development of Labuan legislation brings in place the Labuan Foundations Act 2010, which allows for the establishment of a Labuan foundation. The founder and beneficiary of a Labuan foundation may be resident or non-resident.79 For Labuan foundations, not unlike the Labuan Trusts Act 1996, the income derived from any property...
which is not Malaysian property is subject to the Labuan Business Activity Tax Act 1990.\textsuperscript{80} Again, there are restrictions in place in relation to the property of a Labuan foundation that governs the applicable tax laws\textsuperscript{81} and secrecy and confidentiality provisions in place.\textsuperscript{82}

In addition, not unlike the Limited Liability Partnerships Act 2012, a Labuan LLP under the Labuan Limited Partnerships and Labuan Limited Liability Partnerships Act 2010 accords a separate legal personality in respect of Labuan LLPs,\textsuperscript{83} which is a taxable Labuan entity for tax purposes, and precludes members from personal liability save to the extent of their own investments.\textsuperscript{84}

\textbf{ii Regulation}

There may be people who abuse these vehicles, meant for genuine asset protection and estate planning, as means of laundering monies gained from illegal activities or worse, to finance acts of terrorism both locally and globally. This is more so with the ever-increasing global threat of terrorism from terrorist organisations using their ill-gotten gains to perform acts of terrorism on a global front.\textsuperscript{85}

It is apt that, in line with the various recommendations by the Financial Action Task Force,\textsuperscript{86} Malaysia has the necessary legislation in place to counter these illegal activities. Malaysia’s primary anti-money laundering regulation is the Anti-Money Laundering, Anti-Terrorism Financing and Proceeds of Unlawful Activities Act 2001 (AMLATFA).

The AMLATFA came into operation on 15 January 2002 as a legislation to, \textit{inter alia}, provide for the offence of money laundering, the measures to be taken for the prevention of money laundering and to provide for the forfeiture of property involved in or derived from money laundering, proceeds of an unlawful activity and instrumentalities of an offence, and incidental matters.

This is further supplemented by Section 114 of the MITA, which provides for the criminal offence of tax evasion – a ‘serious offence’ as defined under AMLATFA. Although AMLATFA came into operation in early 2002, it is pertinent to note that the Act is applicable to any serious offence, foreign serious offence or unlawful activity whether committed before or after the commencement date and applies to any property situated in or outside Malaysia.\textsuperscript{87} In other words, the Acts covers a wide range of activities\textsuperscript{88} and have far-reaching implications that may transcend time or territorial limitations.

Other anti-money laundering regulations include the Malaysian Anti-Corruption Commission Act 2009, which established the Malaysian Anti-Corruption Commission, an independent and accountable anti-corruption body tasked with, among others, detecting

\begin{itemize}
  \item \textsuperscript{80} Section 6(3) of the Labuan Foundations Act 2010.
  \item \textsuperscript{81} Section 5(2), 6(2) of the Labuan Foundations Act 2010.
  \item \textsuperscript{82} Sections 62 to 64, 71 and 73 of the Labuan Foundations Act 2010.
  \item \textsuperscript{83} Section 55 of the Labuan Limited Partnerships and Labuan Limited Liability Partnerships Act 2010.
  \item \textsuperscript{84} Sections 55 and 56 of the Labuan Limited Partnerships and Labuan Limited Liability Partnerships Act 2010.
  \item \textsuperscript{86} See: Amongst others, FATF 2001 recommendations, FATF 2012 recommendations, FATF 40 recommendations.
  \item \textsuperscript{87} Section 2(1) and (2) of the AMLATFA.
  \item \textsuperscript{88} Section 4(1) of the AMLATFA.
\end{itemize}
and investigating any suspected offences under the MACCA 2009. With these regulations in force, Malaysia is well placed to ensure that vehicles meant for genuine asset protection, estate planning and wealth management are not used for the wrong reasons.89

V CONCLUSIONS & OUTLOOK

Presently, while North America remains the key hub for ultra high net worth individuals (UHNWI), Asia is poised to be a strong contender with an anticipated increase of growth by 91 per cent.90

Nationally, notwithstanding global economic uncertainty, the commitment of the Malaysian government to strengthen the economy could be seen from the Budget 2017, wherein various tax incentives and exemptions have been introduced to sustain the growth of the Malaysian economy, which is anticipated to achieve a growth between 4 per cent and 5 per cent in 2017. The government's effort to diversify its sources of revenue has also contributed to sustained economic growth despite recent decline in oil prices by almost 50 per cent. In fact, in the first half of 2017, the Malaysian ringgit is one of the currencies that experienced tremendous growth in Asia. It is also notable that despite uncertainties to the political climate in Malaysia, the number of UHNWI Malaysians increased by 3 per cent last year.91 In fact, the government taken initiative to launch a series of discourse in line with the recently announced 2050 National Transformation (TN 50) initiative to improve the state of the Malaysian economy and propel the nation's economic growth.

In light of the above, it could be seen that the economic growth of Malaysia and its attractiveness to foreign investors remains optimistic for the time being.

89 See: Minister says Malaysia has adopted comprehensive framework that criminalises terrorism financing (http://www.themalaymailonline.com/malaysia/article/minister-says-malaysia-has-adopted-comprehensive-framework-that-criminalise#sthash.3hjr0aaL.dpuf).
91 See: Ultra rich Malaysians up 3pc last year, wealth report shows (http://www.themalaymailonline.com/malaysia/article/ultra-rich-malaysians-up-3pc-last-year-wealth-report-shows#1ZE9y27hIYQbWigQ.99).
I INTRODUCTION

Malta is an onshore high-tax jurisdiction for individuals who are both domiciled and resident in Malta. The top rate of income tax is at 35 per cent. However, British influence meant that Malta inherited the remittance basis of taxation. Under this system non-domiciliary high net worth individuals and investors can benefit by becoming residents of Malta and being taxed only on income arising in or remitted to Malta. Capital gains arising outside of Malta even if remitted to Malta are also exempt from tax in the hands of resident permit holders.

Malta introduced a residence programme in 1988 through the adoption of the Malta Permanent Residence Scheme that was designed in order to attract high net worth individuals. This immediately placed Malta on the map as an attractive destination for high net worth individuals. This residence programme has evolved throughout the years and is now in the form of the Malta Global Residence Programme for non-EU individuals and the Malta Residence Programme for EU, EEA or Swiss individuals. These residence programmes attract, among others, retirees, authors, artists, intellectuals and international consultants or simply persons seeking to establish an alternative residence that suits their lifestyle and tax profile. The requirements to obtain and retain residence in Malta are a minimum annual tax of €15,000 covering the main applicant and dependants on the same application, a residential address (no need to buy a property but even renting out a property is sufficient), and paying tax on a remittance basis of taxation at the advantageous tax rate of 15 per cent.

Strengthening Malta’s attractiveness for high net worth individuals in 2014 the Government of Malta introduced the Malta Citizenship by Investment Programme as the first EU-approved citizenship programme. Citizenship obtained under this programme grants the rights of full citizenship for life and can be passed on to future generations by descent. Maltese citizenship grants access to all investment opportunities in Malta and throughout the European Union open to Maltese and European Union citizens.

Other attractive features that make Malta popular with individuals of significant wealth for investment purposes but also personal planning are Malta’s geographical location (right in the centre of the Mediterranean), climate and highly trained workforce. The Republic of Malta enjoys a stable political climate and a bipartisan political scene that is largely convergent on issues of national and economic importance. Malta has weathered the financial crises well

1 Jean-Philippe Chetcuti is the managing partner and Priscilla Mifsud Parker is a partner at Chetcuti Cauchi Advocates. The information in this chapter is correct as of 2016.
and shared the limelight with Germany as the only two states maintaining economic growth in the eurozone. Malta’s banks have been ranked among the top five soundest banks in the world.

Malta has been a member of the European Union since 2004, part of Schengen since 2007 and part of the eurozone since 2008. The Maltese economy is currently generating perfect opportunities for investors who would like to locate their interests in Malta. Various measures were introduced in the 2015 Malta Budget. Deficit is expected to reduce to 2.1 per cent of the GDP in 2014 and down to 1.6 per cent of the GDP in 2015. GDP is expected to increase by 4.9 per cent over 2013. The number of people registering for work has decreased to 13.7 per cent.

Malta provides a wide range of investment vehicles available whereby wealth management is supported by legal infrastructure and regulatory framework in that various asset management solutions can be sought for private client matters whereby the system offers individuals the possibility of minimal tax leakage both on a corporate and on a personal level. This is also backed up by a strong banking infrastructure, a solid jurisprudence on foundations and a codified trusts law based on the Jersey model. Private clients are therefore spoilt for choice in terms of what vehicles to use for their wealth and estate planning purposes in a pleasant and safe environment with no language barriers. Maltese and English are the two main languages, however, the use of Italian, French, Spanish and German is widespread.

II TAX

Domicile and residence are the determining factors in establishing whether and in what manner a person is taxable in Malta. An individual who is resident and domiciled in Malta is taxable in Malta on a worldwide basis, that is to say on all income and capital gains wherever these are derived and whether or not these are remitted to Malta.

If a person establishes his or her residence in Malta but is not also domiciled therein, he or she would be subject to tax on a source and remittance basis and would therefore be liable to tax on:

a income and taxable capital gains arising in Malta (e.g., on local bank interest, employment income and gains made on the transfer of immoveable property situated in Malta);  
b foreign-source income that is remitted to or used in Malta (e.g., on foreign investment income paid directly into a Maltese bank account or that, although not paid directly into Malta, is eventually remitted to Malta or used to pay expenses in Malta).

Capital gains arising outside Malta are exempt from tax in Malta whether or not these are remitted to or used in Malta.

The term ‘resident’ is not clearly defined in the Malta Income Tax Acts. However, there are indications in the law that may assist in determining who may be considered to be resident in Malta for tax purposes.

A person is considered tax resident in Malta by law if he or she is not a temporary resident, that is to say if he or she is not in Malta for some temporary purpose without any intent to establish his or her residence therein, and has not actually resided in Malta at one or more times for a period equal in the whole to six months in the preceding calendar year.

The type of income tax levied on an individual depends on the type of tax status applicable to the individual. If an individual simply takes up ordinary residence in Malta,
the progressive tax rates (0–35 per cent) would apply. If, in addition to taking up residence, an individual has been granted special tax status under one of the applicable programmes mentioned above, then the flat rate of taxation (15 per cent) would apply on foreign-source income that is remitted to or used in Malta, provided that the applicable requirements are complied with. The individual is required to own or rent property to be occupied as his or her principal place of residence worldwide and may not spend more than 183 days in any other single jurisdiction in any calendar year.

When purchasing a property, its value must be at least €275,000, and €220,000 when the property is in the south of Malta or Gozo. When renting a property, the values are set at €9,600 per annum for immovable property in Malta and €8,750 per annum for immovable property in Gozo or the south of Malta. Such property may not be let or sublet.

Malta tax legislation also caters for highly skilled individuals who are specifically covered by the Highly Qualified Persons Rules. Under these rules, non-domiciled individuals employed by a company operating in the financial services, gaming and aviation sectors that holds a licence or recognition by the Malta Financial Services Authority (MFSA), the Malta Gaming Authority (MGA) or an Air Operator’s Certificate respectively, receive beneficial tax treatment. The rules entitle the individuals employed in ‘eligible offices’ to apply a flat rate of taxation of 15 per cent on their employment income, which should be of at least €82,353 per annum (adjusted annually in line with the Retail Price Index), up to a maximum income of €5 million. The flat rate of tax applies for a consecutive period of five years for European Economic Area and Swiss nationals and for a consecutive period of four years for third-country nationals. Individuals who already have a qualifying contract of employment in an eligible office two years before the entry into force of the scheme may benefit from the 15 per cent tax rate for the remaining years out of the total period permitted by the scheme.

The law also provides for a flat 15 per cent tax rate in respect of employment income for eligible offices in the digital games and audiovisual industry, whereby the income derived should amount to at least €45,000. This option applies for a consecutive period of no more than three years commencing from the year preceding the first year of assessment in which that person is first liable to tax under the provisions of this law, provided that Malta Enterprise may extend the option by one year for any person whose employment commences after the 31 August of a particular year.

A similar regime, Qualified Employment in Aviation, was introduced for eligible offices in the aviation industry, with effect from year of assessment 2017. Non-domiciled individuals occupying certain posts, such as flight operations manager, aviation systems developer or key aviation specialists, earning a salary of at least €45,000 annually shall be entitled to benefit from a 15 per cent flat rate of tax on such income.

### Recent developments

The Budget Implementation Measures 2016 continued the trend of previous budgets to reduce personal taxation. The tax-free allowance has been increased from €8,500 to €9,100 for single taxpayers, from €11,900 to €12,700 for married taxpayers filing a joint tax return and from €9,800 to €10,500 for taxpayers benefitting from the parent rates.

Other important developments were the following:

- the double tax treaty between Mauritius and Malta came into effect on 23 April 2015;
c the double tax treaty between Moldova and Malta came into effect on 17 June 2015; and

d the double tax treaty between Malta and Curaçao was signed on 18 November 2015, but has not yet entered into force.

ii Developments relating to personal taxation for individuals both in relation to gift and succession taxes

Inheritance tax, gift tax and wealth tax do not apply in Malta and there is only a stamp duty tax applicable on transfers of immoveable property. Transfers of property inherited after 24 November 1992 are subject to a 12 per cent final tax on the difference between the transfer value of the property and its acquisition value.

iii Issues relating to cross-border structuring

Double tax relief

Malta has entered into approximately 70 double taxation agreements and the list is always increasing. Their impact is very positive in that they encourage the growth of trade between two countries and remove the incidence of double taxation and reduce withholding taxes for payments from one country to another. The OECD had issued a positive peer review for the Malta tax framework in July 2013.

Before the 1994 amendments, double tax relief was only available in Malta under the domestic provisions of the Income Tax Act if the foreign tax had been suffered in a country with which Malta has a double tax treaty or in respect of British Commonwealth income tax.

Unilateral relief

Malta allows relief from double taxation on a unilateral basis where overseas tax is suffered on income received from a country with which Malta does not have a tax treaty. The overseas tax suffered is allowed as a credit against the tax chargeable in Malta on the gross amount. The credit shall not exceed the total tax liability in Malta on the receipt.

Unilateral relief for underlying tax suffered is available where the taxpayer is a Maltese company that holds more than 10 per cent of the voting power of the overseas company paying the dividend.

When claiming unilateral relief, the recipient of the income must prove the following to the satisfaction of the Commissioner:

\( a \) that the income arose from overseas;

\( b \) that the income suffered overseas tax; and

\( c \) the amount of that tax.

iv Regulatory issues relevant to high net worth individuals generally or that impact the general market of private wealth services

The tax regime applicable to the transfer of immoveable property situated in Malta encompassed a combination of the 12 per cent final withholding tax regime levied on the property transfer value introduced in 2006 and in certain instances, income tax of 35 per cent (or progressive rates in the case of individuals) on the gain derived from the property transfer.

The Malta 2015 budget brought amendments to the applicable rate for the final withholding tax whereby 8 per cent instead of 12 per cent is being levied on the value of the property except in the following instances where the following different rates are applicable:
a 5 per cent of the transfer value in cases where the property being transferred does not form part of a project and the property is transferred within five years from the date of acquisition;
b 10 per cent of the transfer value in the case of properties acquired prior to 1st January 2004 and for which transfer a promise of sale has not been presented to the Commissioner before 17 November 2014;
c 2 per cent of the transfer value in the case of property transferred, which, immediately before the transfer was owned by an individual or two co-owners who had declared in the deed of acquisition that such property had been acquired for the purpose of establishing therein or constructing thereon his or their sole ordinary residence and the transfer is not made within three years of the date of acquisition;
d 5 per cent of the transfer value for transfers of property situated in Valletta and other urban conservation areas outside Valletta, which were acquired before 31 December 2018 and where such property has been restored or rehabilitated and works are certified by the Malta Environment and Planning authority before 31 December 2018. Such transfer must not be made more than five years from 31 December 2018; and
e 7 per cent in the case of restored property where a notice of promise of sale has not been given prior to 17 November 2014.

One should also give due regard to the fact that it will no longer be possible to opt out of the final tax system and therefore to be taxed on the profit. Furthermore, no deduction of expenses will be allowed when one seeks to arrive at the transfer value. The new implementations do not affect the exemptions that are already in place in relation to the sale of one’s own residence, donations as prescribed, assignments during separation and divorce and intra-group transfers.

v Issues impacting entrepreneurs as holders of active business interests at the proprietor level

The implementation of the Standard for Automatic Exchange of Financial Accounting Information will surely have an impact on entrepreneurs and their businesses. The Common Reporting Standard (CRS), which was implemented as from 1 January 2016, is a multilateral agreement aimed at preventing tax evasion and fraud through the automatic exchange of information that would occur automatically once a year. The treaties empower financial authorities to monitor bank accounts (including offshore countries) whereby the banks would be required to disclose who the ultimate beneficial owner even if owned via fiduciary structures. Malta has pledged to exchange information by September 2017 and is part of the early adopters group.

The financial institutions that are required to report under the CRS are:

a banks and custodians;
b brokers;
c certain collective investment vehicles;
d certain insurance companies; and
e trustees fall under the category of custodians and will have the obligation to report accounts that are held through trusts that they administer.
III SUCCESSION

i Introduction to succession

Maltese succession law, as in other civil law jurisdictions, entails the notion of forced heirship, whereby certain persons at law are entitled to receive the legitimate portion as a reserved portion calculated against the entirety of the estate of the deceased.

Chapter 16 of the Laws of Malta, the Maltese Civil Code, regulates testamentary succession and the drawing up of wills. Barring these rules on forced heirship, any person may bequeath any of his or her property in accordance with his or her discretion. In any case, a testator may bequeath by singular title, that is, as a legacy, or by universal title, that is, the person or persons appointed would succeed to the deceased in all capacities as heirs. By and large, wills are cumulative, provided that the testator does not expressly or tacitly revoke previous wills by drawing a further will in which certain clauses challenge previous ones.

With respect to intestate succession, the applicability of the rules on forced heirship holds that the persons entitled to receive in virtue of the law would be the heirs. Where the deceased has descendants and a surviving spouse, these persons are entitled to receive the inheritance; where the deceased dies without issue, the ascendants of the testator are entitled to receive the inheritance. The Civil Code further provides for those situations where there are no descendants, surviving spouse or ascendants to receive, in which case the inheritance shall devolve upon the government of Malta. These rules would also apply when no person entitled to receive accepts the inheritance; hence, no one to claim the right over the inheritance.

It is worth highlighting the fact that the civil legal approach prevails throughout the Maltese legal system and the rules on forced heirship apply even with respect to trusts and foundations. For this reason, rightful heirs may attack transactions made in relation to the trust and the foundation; namely, a settlement of property and an endowment respectively, where it may be proven that the effect thereof prejudices the entitlement of the reserved portion.

Under Maltese succession law (prevalent also in other civil law jurisdictions), persons entitled to receive by law may accept the inheritance conditionally. Strictly speaking, such persons would be accepting the inheritance through the benefit of inventory; the testamentary executor would draw up a list of all the assets and liabilities that belonged to the testator and the rightful heir would be given a peremptory time frame within which to decide whether to accept or refuse the inheritance.

ii Key legislative or case law changes affecting succession

Key changes affecting succession

The recent coming into force of Regulation (EU) No. 650/2012 of the European Parliament and of the Council of 4 July 2012 (the Succession Regulation) saw significant changes affecting succession – particularly cross-border succession – being introduced into the law. The Succession Regulation regulates jurisdiction, applicable law, recognition and enforcement of decisions, and acceptance and enforcement of authentic instruments in matters of succession. It also introduces the European Certificate of Succession. In this regard, a new chapter entitled ‘Of Cross-Border Successions’ was introduced to the Maltese Civil Code by virtue of Act No. XVI of 2015.2

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2 Title III, Sub-Title III, Chapter VIII of the Civil Code.
New legal provisions were also enacted within the Notarial Profession and Notarial Archives Act\(^3\) governing the European Certificate of Succession.\(^4\) Amendments were also made to the Public Registry Act\(^5\) to regulate the registration within or removal of European Certificates of Succession from the Public Registry.\(^6\)

**Case law affecting succession**

With respect to judgments delivered by Maltese law, the recurring issues are generally linked to the consent of the testator and division of property. On consent of the testator, the courts have taken a consistent approach in which invalidating a will is unequivocally the exception. Many a time, the court rules against the plaintiff for failing to produce sufficiently conclusive evidence that establishes the vitiation of the testator’s consent on the basis of coercion and, or duress. Any room for doubt has always directed the court to uphold the deceased’s will as valid on the basis that the testator’s will and intention cannot be positively challenged.

The court has also addressed matters concerning the testamentary executor who would be appointed by the deceased by virtue of his will for the better execution of all his dispositions. The testamentary executor, upon being confirmed by the Court of Voluntary Jurisdiction, is fundamentally responsible for the administration and liquidation of the estate of the testator and ensuring that the testator’s dispositions are fulfilled at law and given in full effect, while exercising any and all acts necessary for the preservation of the estate.\(^7\)

### iii Relevant cross-border developments

**Conflict of law rules**

The Civil Code contemplates situations in which wills are made outside of Malta. In these cases, a will shall have effect in Malta provided that it is made in the form prescribed by the law of the place in which the will is made.\(^8\) Having said that, the validity of any such will would have to be determined in accordance with the law the place in which the will is made.

**The Succession Regulation**

The Succession Regulation gave rise to the need for amendments to Malta’s laws on succession.

The provisions of the Regulation that have direct effect in participating EU Member States became applicable to cross-border successions from 17 August 2015, and are intended to simplify matters post-death in instances where the assets of the testator are located in more than one jurisdiction. The Regulation attempts to provide legal certainty and enable a faster and easier resolution of cross-border succession by establishing one applicable law and one court to govern the entire estate.

In this regard, cross-border succession refers to instances where the deceased held property or assets in more than one country, the deceased had his or her last habitual residence in a country other than the country of which he or she was a national, the deceased made a

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\(^3\) Chapter 55 of the Laws of Malta.
\(^4\) Article 2(1) (2) (k), Article 50 (1)(p) of the Notarial Profession and Notarial Archives Act.
\(^5\) Chapter 56 of the Laws of Malta.
\(^6\) Article 34 A of the Public Registry Act.
\(^8\) Ibid. Article 682.
disposition of property upon death in a country other than the country of which he or she was a national, or the beneficiaries of the succession are habitually resident or nationals in more than one country.9

By means of the Succession Regulation, cross-border successions may be facilitated on the basis of four grounds, namely that:

\[ a \] a citizen is able to choose whether the law applicable to his or her succession should be that of his or her habitual residence or that of his or her nationality. On failure to make any decision, the law of the deceased’s habitual residence would apply;

\[ b \] a particular succession may be tackled under a single law and its competent authority or authorities;

\[ c \] judicial proceedings and conflicting judicial decisions are avoided; and

\[ d \] mutual recognition and enforcement of judgments in the EU is guaranteed.10

Essentially, the Regulation offers three possible routes to the testator:

\[ a \] The Regulation introduces the principle of the last habitual residence as a default position. In this regard, the default law applicable to succession would be the law of the state where the deceased had his or her habitual residence at the time of his or her death.

\[ b \] The Regulation provides an exception that in cases where circumstances are such as to show that at time of death, the deceased had a manifestly closer connection with another state, the prevailing law governing the succession will be of that state.

\[ c \] The Regulation introduces an option for testators to choose to apply the law of the country of his or her nationality to regulate his or her will, either at time of making the choice or at time of death. This particular limited choice of law must be made expressly or implicitly by way of a testamentary disposition.

In practice, this would mean that any person who has Maltese nationality or has his or her habitual residence in Malta, may decide to have his or her succession regulated by Maltese law, irrespective of the fact that he or she may or will have assets in other jurisdictions, and whether the assets are moveable or immoveable.

The legal concept of ‘habitual residence’ introduced by virtue of the Regulation, as distinct from the concept of ‘domicile’, makes the Regulation innovative. Whereas domicile generally refers to the country intended by the individual as his or her permanent home, habitual residence is the place where the person ordinarily resides with a certain degree of continuity; for example, for professional or economic reasons. Interestingly, the Regulation leaves the interpretation of ‘last habitual residence’ open as it fails to provide a definition of the term. Having said this, the preamble to the Regulation stipulates that the competent authority, in Malta’s case, the Civil Court (First Hall),11 shall make an overall assessment of the circumstances of the life of the deceased during the years preceding the death and at the time of death, taking into account all relevant factual elements, in particular, the duration and regularity of the deceased’s presence in the state concerned and the conditions and the reasons for that presence.12 The habitual residence should reveal a close and stable connection.

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9 Article 958A of the Civil Code.
11 Article 958C. (1) of the Civil Code.
12 EU Regulation Preamble Recital No. 23 et seq.
The Regulation also recognises that determining the habitual residence of the testator may be difficult. In this regard, it provides that in cases where it is shown that the deceased maintained a closer and stable connection with the Member State of origin, in which the centre of interests of the family and social life are located, then the deceased would be considered to still have his or her habitual residence in said state of origin.

Notwithstanding the above, the substantive domestic rules on succession will remain unaltered. As a result, rules on entitlement over inheritance, property law and family law, as well as applicable tax in relation to succession, will continue to apply in any case.

**Concluding matters**

It appears that the harmonisation of certain succession matters within a cross-border context will ease many practical issues that commonly arise by reason of the diversity of rules concerning succession matters in Member States. The idea behind this is to improve the procedure as well as facilitate the liquidation of the estate through the laws of one jurisdiction based on the principle of ‘universality of succession’, resulting from the ever-growing reality of free movement of persons within the EU.

**iv  Applicable changes affecting personal property**

**Matrimonial rules**

Under the Civil Code, the law regulates matrimonial regimes; establishing community of acquests as the default regime.\(^{13}\) However, this does not mean that spouses are obliged to establish the community of acquests throughout their marriage;\(^{14}\) prior to contracting marriage, the prospective spouses may opt out of this regime by means of a prenuptial agreement whereas after marriage, authorisation is required by the court prior to contracting a post-nuptial agreement. Maltese law allows spouses to choose from three matrimonial regimes, (1) community of acquests; (2) community of residue under separate administration (CORSA); and (3) separation of assets, also known as paraphernal property.

As regards the right to the reserved portion, whether spouses choose to opt for a community of acquests, as the most benevolent option, or for the separation of estate, such right remains an entitlement not only in favour of the deceased’s descendants but also to the surviving spouse with whom a marriage contract has been entered into. However, disposal and alienation of assets belonging to the community of acquests would be regulated by the law as there applies such rule as requiring consent from both spouses where an act of extraordinary administration is to be carried out. By the term ‘act of extraordinary administration’ the law includes the giving of security; partitioning of property; alienation of immoveable property or real rights thereon; certain donations and so on.

After the demise of one of the spouses, the right to the reserved portion applies indiscriminately whether the assets belonging to the deceased were paraphernal or co-owned with the surviving spouse.

\(^{13}\) Article 1316.
\(^{14}\) Ibid. Article 1317.
Civil unions

The Civil Unions Act\textsuperscript{15} regulates civil unions and provides that, when registered, said civil unions shall for all intents and purposes have the corresponding effects and consequences in law of civil marriage contracted under the same Act.\textsuperscript{16} The law requires every person intending to contract into a civil union to fulfil all the requirements that would be necessary if one were to enter into marriage.\textsuperscript{17}

In view of the above-mentioned considerations, the law on succession does not distinguish between a civil marriage and a civil union on the basis that Chapter 530 specifically requires that the same legal effects and consequences in civil marriage apply \textit{mutatis mutandis}.

Conclusively the legal obligations and rights emerging from the Civil Code on succession are applied without distinction in the eyes of the law as to whether the spouses are of same or opposite sex. \textit{Inter vivos}, all of the rules with respect to extraordinary acts of administration shall be adhered to by the spouses who have contracted a civil union inasmuch as spouses who contracted a civil marriage do. Likewise, the demise of one of the partners in a civil union will \textit{ipso jure} give rise to the same legal implications, rights and obligations as the demise of one of the spouse in a civil marriage would do. Therefore, the surviving spouse or the surviving partner are deemed to be equal in the eyes of the law in terms of their rights over the deceased's inheritance; likewise, the children thereof would benefit from the same rights irrespective of whether they are the biological children or adopted children thereof because Act XIII of 2004 has already abolished any such unequal treatment.

IV WEALTH STRUCTURING & REGULATION

Malta is quickly becoming a compelling alternative in the area of wealth management thanks to the wide range of investment vehicles on offer coupled with its tax efficiency. Malta allows investors to protect their assets through the use of funds, companies, trusts and foundations in a secure EU jurisdiction that is well regulated and yet flexible at the same time, accommodating the most complex of structures. An efficient tax regime results in minimal tax leakage at both entity or structure level and the personal level. The country has an excellent legal infrastructure supported by highly qualified and experienced professionals and a track record for innovative, customised solutions. The country also has a strong banking infrastructure that can cater to all levels of wealth.

i Companies and partnerships

Companies and partnerships are the entities most commonly used in wealth structuring.

ii Trusts and foundations

Malta is unusual in that although it is a civil law jurisdiction, it caters for the setting up of both trusts and foundations. While trusts are more familiar to persons from common law jurisdictions, the concept of foundations may be more familiar to persons from civil law

\begin{footnotesize}
\textsuperscript{15} Chapter 530 of the Laws of Malta.
\textsuperscript{16} Article 4 (1) of the Civil Unions Act.
\textsuperscript{17} Ibid. Article 3(1).
\end{footnotesize}
jurisdictions that are not familiar with the concept of a trust or have introduced it recently and therefore the concept is still in its infancy and jurisprudence minimal. Both trusts and foundations are valuable arrangements for both asset protection and succession planning.

Trusts in Malta are regulated by the Trusts and Trustees Act (the Act) that was, to a large extent, modelled on the Trust (Jersey) Law 1984. Malta has ratified the Hague Convention on Trusts and on their Recognition, and as a result, Malta distinguishes between Maltese Law Trusts that are entirely regulated by the Trusts and Trustees Act and Foreign law Trusts that may be set up and regulated by any law whatsoever and are recognised by Maltese law subject to certain conditions laid down in the Convention being satisfied.

iii Investment funds
Malta has become a well-established domicile for collective investment schemes. The jurisdiction is particularly well known for its well-developed hedge fund infrastructure, but Malta also caters for a number of private wealth oriented fund structures. Growth in the sector has been very steady, bolstered by a dynamic and approachable regulator and a legal environment that provides a useful mixture of clarity and flexibility. The Professional Investor Fund has become a ‘go-to’ choice for small, relatively closely held funds that require sophisticated structural arrangements, and continues to be a popular choice even after the introduction of the new Alternative Investment Fund Managers Directive.

V TAX & REGULATORY

i Companies
All companies registered in Malta are deemed to be ordinarily resident and domiciled in Malta and are thus taxable on a worldwide basis at the corporate income tax rate of 35 per cent. However, certain distributions to shareholders would entitle them to a refund of all or part of the tax paid at company level considerably lowering the effective tax rate. Income from qualifying participations may furthermore be completely exempt in Malta at the level of the company. Malta has an extensive double tax treaty network and unilateral double taxation relief mechanisms that ensure relief from double taxation in most cases.

ii Partnerships
Recent developments in relation to the taxation of partnerships means that all partnerships, whether *en nom collective* or *en commandite*, the capital of which is divided into shares or otherwise may now elect to be treated as companies. Where they do not elect to be treated as companies, partnerships are tax transparent in that the partnership itself does not pay tax but the partners must include their share of partnership profits in their tax returns and pay tax accordingly at the applicable tax rates (progressive rates if partner is an individual, 35 per cent if a company).

iii Trusts
Where at least one of the trustees of a trust is tax resident in Malta, income and capital gains attributable to the trust are subject to tax in Malta. However, there are situations where legislation deems all income attributable to a trust to have been derived directly by the beneficiaries of the trust and thus insofar as no income has been attributed to the trust, no
tax would be due in Malta. The criteria examined for the purposes of transparency are the nature of the trust property, source of income or gains accruing to or derived by the trust and whether beneficiaries are persons who are resident, ordinarily resident or domiciled in Malta.

iv  Foundations

As a default position, foundations are treated as companies that are ordinarily resident and domiciled in Malta, thus taxable on a worldwide basis, however, the administrators of a foundation may by notice in writing to the Commissioner of Inland Revenue irrevocably elect that a foundation be treated as a trust.

v  Funds

The tax treatment of funds in Malta hinges upon the classification of funds as prescribed or non-prescribed funds. A non-prescribed fund is one that holds more than 15 per cent of its assets outside of Malta and such fund is only taxed upon gains made from the disposal of immoveable property in Malta. A prescribed fund on the other hand is taxed in Malta on its profits at the rate of 35 per cent.

vi  Applicable anti-money laundering regime and other key aspects of regulation of service providers dealing with private wealth

Malta has distinguished itself as a serious and extremely adaptable jurisdiction in the field of private client servicing. Trustees, fiduciaries, investment service providers, funds, company services providers, are among the providers that offer relevant services which require regulation.

These service providers are regulated by the Malta Financial Services Authority, (MFSA) and have to abide by an Anti-Money Laundering (AML) regime. As an EU Member State, Malta has an obligation to implement all directives including those relating to AML. These service providers are therefore also supervised and regulated by the Financial Intelligence Analysis Unit (FIAU) from an AML perspective. The applicable legal regime encompasses the enforcement of various laws, directives and regulations being mainly:

c  the Prevention of Money Laundering Act, Chapter 373 – 1994 (PMLA); and

d  the Prevention of Money Laundering and Funding of Terrorism Regulations, Subsidiary Legislation 373.01 – 2008 (PMLFTR).

All these focus around the subject of Anti-Money Laundering (AML) and Funding of Terrorism (FT). The main legislative authority that obliges service providers to abide by an adequate AML regime is the PMLFTR, based upon the third AML Directive.

Additionally, the PMLFTR allows the FIAU to lay out rules and procedures for subject persons to abide by in their ordinary course of business, namely the Implementing Procedures (issued on 20 May 2011), which in turn provide a supplementary outline to the various legislative acts, clarifying the applicable regime and expanding on the following issues.

Adequate due diligence needs to be established. The norm is to undergo normal customer due diligence, comprising of various obligations, such as identification and verification of beneficial owners, acquisition of dependable information about the client in general, and ascertaining of the good standing of character of same.
This can be scaled down or intensified, through the implementation of simplified or enhanced due diligence, always in accordance with the necessity of the particular circumstances of each individual client. Explicit provisions are laid down in this regard, in all the procedures identified above.

Record keeping, reporting, data protection and other measures are other requirements imposed upon service providers for transactions carried out for their clients.

Another essential requirement upon service providers is that of implementing effective systems and training in observing compliance with all the rules and regulations indicated above.

In terms of developments in this area, the fourth AML Directive (European Parliament and Council Directive 2015/849/EU – 20 May 2015) will provide for key changes in the AML regime. Among the key changes there are the risk-based approaches and transparency measures. The Directive will need to be implemented in Maltese legislation by the 26 June 2017.

VI CONCLUSIONS & OUTLOOK

Throughout Malta’s history as a tax-efficient jurisdiction, it has acquired a reputation for being a well-regulated yet client-oriented country in which to do business. The tax regime is tried and tested and clients have the benefit of a jurisdiction with over 20 years of experience in this regard. Malta has sought to attract serious, responsible businesses and has moved away from the mere setting up of brass plate companies to advising on and implementing complex structures and transactions. Notwithstanding its successes, Malta constantly evolves and adapts to meet the needs of businesses and industries and to comply with international best practice and standards. It continues to present tax initiatives as well as regulatory flexibility to enhance Malta’s reputation as the jurisdiction of choice particularly in the financial services sector and maintains a drive to expand its already extensive double tax treaty network.

Malta has survived the worst effects of the international financial crisis, as a result of the Maltese core banks’ prudent approach to maintaining a healthy balance sheet and robust capitalisation. The banks also fund themselves largely from the domestic retail deposit market, lend locally and hold securities issued in Malta. Growth in economic activity is being reflected in the labour market, with employment expanding and the unemployment rate declining.

In 2014, the economy and the labour market continued to perform well and the outlook for 2015–2016 is favourable. Despite the challenging external environment and the high import orientation, Malta’s exports continued to outpace imports and the net external position is expected to have improved over the past year. Economic and employment growth are projected to continue to outpace the euro area average in 2015–2016.

A peer review carried out by the OECD found Malta to be in full conformity with the international transparency standards and exchange of information requirements for tax purposes. The Maltese authorities have taken a series of steps to deliver a fair tax system by fighting tax fraud, evasion and avoidance and are likely to follow the lead taken by the OECD and EU in this regard in particular with reference to the BEPS project. Malta continues to comply with OECD standards and has joined the group of ‘early adopters’ of the OECD Common Reporting Standard.

There is no indication of taxes on wealth or property being introduced at this stage.
I  INTRODUCTION

Mexico, the world’s 15th largest economy in the world in terms of GDP, has encountered new challenges following the 2016 United States presidential election, particularly the devaluation of the Mexican peso and the possible renegotiation of NAFTA.

Uncertainty with respect to possible reforms in the United States, Mexico’s most important business partner, and its impact on Mexican economy have not become a constraint for attracting foreign investments; however, on migration-related diplomatic topics, both countries have become more distant.

Following the tax reforms introduced in 2014 by the executive branch of Mexico’s federal government, important national sectors are still facing an ongoing shifting process derived from such reforms. Private investments in the oil sector are in a maturing process; however, oil dependence in Mexico’s economy remains strong.

Mexico, a member of the Organisation for Economic Co-operation and Development (OECD) since 1994, remains one of the world’s most important emerging market economies, and has become an attractive destination for international investments within the Latin American region, which has led to the existence of an important number of wealthy individuals within an environment of unequal distribution of wealth. According to the OECD’s latest Economic Survey on Mexico, the country’s economic potential has been hindered by important challenges such as high levels of poverty, extensive informality and insufficient educational achievement.

Since the second half of the 1990s, Mexico has taken a more active approach to become an attractive investment spot by broadening its double taxation treaty network, and tax authorities are playing an active role in renegotiating current tax treaties with several countries.

Taxation in Mexico is founded on a series of laws and regulations that are in constant flux. The major tax reform of 2014, which derived in the enactment of a new Income Tax Law, had an important impact on individuals, by incorporating new tax brackets up to a 35 per cent tax rate from the previous limit of 30 per cent and imposing taxation to gains obtained from the sale of publicly traded shares (until 2013 these were generally tax-exempt) and dividends received from both national and international companies at a rate of 10 per cent.

1 Alfredo Sánchez Torrado and Roberto Padilla Ordaz are partners at Chevez Ruiz Zamarrripa y Cia, SC.
Inequality of income has, historically, been a problem for Mexican society. The authorities have constantly focused on developing policies for establishing additional taxes to the already captive taxpayers, while the informal economy keeps growing as a response to the lack of formal employment that could provide the means of support for a significant number of Mexican households. Such inequality derives from the existence of a very big number of high net worth individuals in Mexico who hold investments abroad.

A major concern of wealthy individuals, not only in Mexico but worldwide, is the current trend of tax administrations to execute information-exchange agreements intended to provide additional elements for exercising audit faculties with respect to capital placed in investment structures abroad. Mexican tax authorities, along with foreign tax administrations, are playing an active role in response to the US Foreign Account Tax Compliance Act regulations, the OECD Base Erosion and Profit Shifting (BEPS) action plan and the Common Reporting Standard of the OECD.

Mexico’s initial response to BEPS has resulted in incorporating in its legislation the obligation for taxpayers to comply with filing informative returns according to the OECD action plan: master file, local file and country-by-country report. These returns must be filed by the end of 2017 at the latest, with respect to transactions executed between related parties in tax year 2016.

An outcome of the 2014 tax reform was the elimination of the option for income tax payment on a no-name basis. This payment alternative was applicable to Mexican-resident individuals for income obtained from investments held overseas and represented a secure method of tax compliance under a confidentiality scheme.

In 2017, a temporary tax incentive programme for capital repatriation was enacted. This programme requires the payment of income tax due on investments held overseas as of 31 December 2016 and taxpayers that adopted such benefit are obliged to return to Mexico funds by 19 October 2017. The benefit of this programme consists of a reduced income tax rate of 8 per cent conditioned to a minimum two-year holding period in specific types of investments authorised by the Mexican tax authorities. Additionally, those taxpayers who elect to apply such repatriation programme are relieved from the formal obligations that were not timely complied with.

Tax authorities continue to focus on gathering information with respect to inbound transactions conducted by taxpayers. Several tax provisions oblige individuals and corporations to constantly inform of specific transactions targeted as part of aggressive tax planning or with the intention of detecting money laundering. Additionally, tax audits conducted by the Mexican tax authorities are focused on validating the substance of transactions. In 2017, the Mexican tax authorities launched a campaign of massive electronic audits.

Owing to the regulations that have recently been enacted, additional administrative resources must be invested by taxpayers so as not to fall into default with any of the obligations established therein, in addition to the fact that more complex requirements for issuing electronic invoices have to be dealt with.

The presidential succession in 2018 is creating expectation and uncertainty in certain sectors of Mexican economy and consequently its impact in taxation. At time of writing, no candidates have been officially been proclaimed in what is expected to be a very competitive election race.

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3 The original text of the Decree established as the initial due date 19 July 2017; however, a three-month extension was published in the Official Gazette on 17 July 2017.
Overall, taxation in Mexico for private wealth is constantly changing, and tax authorities are playing an active role not only in verifying whether individuals’ tax obligations are duly being complied with, but also in promoting actions to reach agreements on a broad exchange of information and obliging taxpayers to keep providing information on their transactions.

II TAX
Domestic legislation establishes that Mexican-resident individuals are subject to income tax with respect to their worldwide income.

An individual is deemed resident in Mexico if his or her dwelling is located within the country. If such individual holds property in Mexico and in another country, the Mexican residence would be afforded if his or her main centre of interest (the place where more than 50 per cent of its overall income is obtained) is located in Mexico.4

Mexican resident individuals are subject to a progressive tax rate on their annual income. The maximum tax rate of 35 per cent introduced in the 2014 tax reform is still in effect.

Depending on the type of activities conducted by individuals, miscellaneous formal obligations may have to be complied with.5

Individuals are obliged to file an annual tax return on 30 April, following year-end; however, depending on the type of income received, advance income tax returns may have to be filed before the Mexican tax authorities during the ongoing tax year. Mexican tax legislation provides that the tax year runs from 1 January to 31 December.

Several items of income are fully or partially income tax-exempt. Until 2013, individuals were fully exempt on gains derived from the sale of dwellings, to the extent that in the five previous tax years no other sale of dwellings was carried out. Since 2014 such sales are partially exempt for an amount of approximately US$220,000 (considering 2017 figures).

A major impact on individuals resulting from the most recent tax reform is a limit on the amount of personal deductions that could offset taxable income, such as medical expenses, additional contributions to private pension funds and interests on mortgages for acquisition of dwellings. The annual limit of personal deductions corresponds to the lower of approximately US$7,500 (considering 2017 figures) or 15 per cent of the individual’s annual taxable income. An exception for people with physical disabilities (according to the Federal Labour Law) was incorporated in order for them not to consider the aforementioned threshold. Additionally, since 2016, contributions to savings and retirement plans were excluded from such general threshold; however, a specific deductibility limit for such type of contributions is applicable.

Most tax-exempt items of income must be reported to the Mexican tax authorities to maintain such status, otherwise they are deemed taxable income.

i Taxation on real estate
Individuals are subject to income tax on gains derived from the sale of immoveable property. The tax basis of immoveable property is subject to restatement by Mexican inflation and subject to depreciation rules (except for land).

5 2017 Mexican Income Tax Law.
The Income Tax Law provides a tax computation procedure for individuals that results in having two types of gains, determined based on the number of years of their investment holding period. The first basket is taxed as part of taxpayers’ ordinary income, while the second basket is taxed at their previous five-year effective tax rate following the procedure established for such purposes.

Gains obtained from immoveable property deemed as ordinary income are subject to the annual progressive rate (maximum rate of 35 per cent), and in the case of sale transactions they are conducted before a notary public, who is then responsible for computing and remitting the corresponding tax to the authorities.

Local taxes apply to the acquiring party of immoveable property. State and municipal legislation may vary; however, property taxes normally range between 2 per cent to 5 per cent, which is habitually applicable to the greater out of cadastral value, according to each state’s records, appraisal value or transaction value.

ii Taxation of gains of publicly traded securities

The tax exemption regime for gains obtained by individuals and non-residents derived from the sale of shares through the stock exchange was repealed by the 2014 tax reform.

Since 2014, individuals and non-residents in certain cases are obliged to pay income tax at a rate of 10 per cent over gains derived from the sale of securities through authorised stock exchanges or recognised derivative markets.

Specifically, this new regime is applicable to shares issued by Mexican companies, or where the value stems more than 50 per cent from Mexican real estate, and securities that represent them such as American depository receipts; foreign shares that are listed on the Mexican stock exchange through its international quotation system; securities that represent indexes such as ETFs or TRACs, which are sold on the Mexican Stock Exchange and equity financial derivative transactions referred to shares listed on the Mexican Stock Exchange or referred to indexes on such shares that are realised in the Mexican market.

Mexican financial intermediaries must conduct the computation of gains or losses derived from sale transactions. Mexican-resident individuals are entitled to offset losses against gains from the sale of securities.

Losses obtained from the sale of shares can only be offset against gains obtained from the sale of shares. A 10-year period is established for carrying forward losses obtained by taxpayers.

At year-end, Mexican financial intermediaries are obliged to provide Mexican-resident individuals with the details of the annual computation of gains or losses obtained during each calendar year. If a final gain is obtained, Mexican-resident individuals are obliged to remit to the tax authorities the 10 per cent income tax jointly with their annual tax return. The annual tax return for individuals is due to be filed on 30 April of the following year.

Non-residents can apply tax treaty benefits based on their tax residence. Mexico has an extensive network of tax treaties and exchange of information agreements.

There are some exceptions to which the 10 per cent rate does not apply, such as publicly traded securities that were acquired or sold in private transactions (the 10 per cent tax regime is applicable in cases where shares sold do not represent more than 1 per cent of the issuer’s overall stock) and sales conducted by a person or group that within a 24-month period sells more than 10 per cent of an issuer’s stock or its control, as defined in the Stock Market Law.
iii Taxation on dividends

Until 2013, Mexican legislation established an integrated profit distribution system in which profits were taxed at the level of the distributing entity, and no additional taxation was imposed on the recipients of such dividends.

As a result of the 2014 government’s tax reform, individuals and non-residents are subject to an additional 10 per cent income tax on dividends received from profits generated in 2014 and the following years. Such income tax must be withheld by the distributing entity and remitted to the tax authorities.

Mexican-resident entities are required to maintain separate records of profits generated until 2013 and of profits generated starting 2014 for the purposes of determining whether the additional 10 per cent income tax withholding is applicable or not in case any distribution to individuals or non-residents is conducted.

Additionally, Mexican-resident individuals are subject to the additional 10 per cent tax on dividends received from non-resident entities, which must be paid in the month following such in which they receive profits.

In certain cases, tax treaties can reduce or eliminate the 10 per cent rate on dividends paid by Mexican-resident corporations.

iv Preferential tax regime rules

Mexican residents holding investments in foreign vehicles are obliged to determine whether income arising from such investment is subject to a preferential tax regime.

Under Mexican legislation, and from a general approach, income is subject to a preferential tax regime when it is not subject to taxation abroad or is subject to income tax lower than 75 per cent of the income tax that would have been triggered and paid in Mexico, even when such situation derives from the application of special regulations, tax refunds, tax credit or any other procedure.

Income obtained from entities or foreign transparent legal vehicles is deemed as subject to a preferential tax regime, except when such vehicle conducts entrepreneurial activities and its passive income represents 20 per cent or more of its overall income.

An exception for not considering that income is subject to a preferential tax regime is established by the Mexican Income Tax Law for such cases where a Mexican resident does not exert control (directly or through a third party) in the management of foreign entities or legal vehicles to such a degree that could decide the moment of profit distribution. The Mexican Income Tax Law assumes that the Mexican resident exerts control; thus, proof to the contrary must be obtained in such applicable cases.

Income subject to a preferential tax regime is taxed at the level of the Mexican-resident investor at the moment in which such income is generated, regardless of whether it has been distributed to such investor.

Mexican-resident individuals and entities are obliged to comply with filing an informative return in case they obtain income subject to a preferential tax regime, conduct transactions through foreign transparent legal vehicles or obtain income arising from any territory established on the black list of the Mexican Income Tax Law transitory provisions. In 2017, a more complex informative tax return was required to be filed as the Mexican tax authorities introduced a new official form enforcing taxpayers to provide information in a more detailed manner.
Failure to comply with such informative return or providing incomplete information is a criminal offence. Administrative rules\(^6\) provide relief on specific cases for not filing the informative return, specifically if income is derived from a country that has entered into a broad exchange of information agreement with Mexico.

v Gifts
Gifts in Mexico are tax-exempt in the following cases:
\textit{a} gifts between spouses or those received by descendants from their lineal ascendants;
\textit{b} gifts received by ascendants from their lineal descendants, to the extent goods that received are not sold or given to other lineal descendants in any degree; or
\textit{c} other gifts that do not exceed an approximate amount of US$4,500 (considering 2017 figures). For the excess amount thereof, income tax must be paid.

A donee must consider the tax basis of goods received in relation to the donors immediately before they granted such goods as a gift. The acquisition date of goods received must also correspond to the acquisition date of donors.

However, in cases where income tax is paid on a gift transaction, the acquisition cost would correspond to the appraisal value considered for computing such tax and the acquisition date on which the tax is paid.

The donee has to declare the amount of gifts received in his or her annual tax return in order not to lose the exemption.

III SUCCESION
Successions do not give rise to a taxable event provided the recipient of the deceased’s estate reports this situation in his or her annual tax return. If such report is not made, the transferred estate is taxable.

Non-residents are not exempt from tax on real estate and shares that have a source of wealth located in Mexico. Transfer of such assets would be subject to taxation according to the corresponding provisions.

Contrary to what occurs in other jurisdictions, Mexican legislation does not include an estate tax. Notwithstanding this, certain property taxes may be triggered depending on the local legislation of each state and municipality.

No forced heirship regime exists in Mexico; however, upon intestacy, succession rules would be applicable in any of the following cases:\(^7\)
\textit{a} the deceased left no will, or the will is void;
\textit{b} the will does not provide for the entirety of the estate;
\textit{c} conditions established to heirs are not complied with; or
\textit{d} beneficiaries renounce the will.

If the succession rules are required, descendants, spouses and ascendants, among others, are considered as heirs in different amounts and according to specific rules. In case of any dispute, the civil courts will decide according to the civil legislation applicable.

\(^6\) 2017 Miscellaneous Tax Resolution.
\(^7\) Federal Civil Code.
It is not essential to have a will executed under Mexican law. In general terms Mexican legislation recognises any will executed and formalised in a foreign jurisdiction, to the extent it is valid in such jurisdiction and is not against Mexican law.

Mexican and foreign residents can make wills in Mexico. Even though there are several types of wills in Mexico, the most common is the ‘public open will’, which is executed before a Mexican notary public in the presence of a witness and is formalised in a public deed.

Under Mexican legislation, the beneficiaries of a will are entitled to decline or transfer their rights under such will in favour of other persons.

The Federal Civil Code provides specific situations in which wills may be contested for specific cases in which they are deemed void pursuant to the corresponding provisions.

An executor manages the deceased's estate and handles the disposal of the assets of the estate. Such executor could be appointed in the will or could be elected by the beneficiaries.

In general terms, the executor of the estate should make an inventory of all the assets of the estate and manage such assets until their distribution to the beneficiaries.

In addition, the executor is obliged to file the annual estimated tax returns of the estate. Alternatively, the beneficiaries could opt to recognise the taxable income corresponding to their share of the estate.

IV WEALTH STRUCTURING & REGULATION

Tax wealth structuring in Mexico has been focused primarily on estate planning and preserving confidentiality.

A very common vehicle used in wealth structuring is the Mexican trust or fideicomiso, which is a commercial contract governed by the Mexican General Law of Negotiable Instruments and Credit Operations.

Such law includes several mandatory provisions, but also allows fideicomisos to include other legal contractual provisions, making them one of the most flexible types of contracts in Mexico, enabling them to be used for different purposes.

i Fideicomiso

In general terms, a fideicomiso consists of three parties: settlor; trustee and beneficiary. The settlor is the individual or entity that transfers title or management of certain assets and rights to the trustee. The trustee is the party that holds the assets in trust and has the responsibility of performing and complying the purposes and goals of the fideicomiso. Finally, the beneficiary is the party that is designated to benefit from the assets and rights contributed to the fideicomiso, whether by using and enjoying the assets or rights, or by receiving income from such assets or rights, among others. Under Mexican law, the beneficiary can be the settlor itself.

Even though legal title over the assets and rights is actually transferred to the trustee (which means the trustee is the legal owner of such assets and rights), such legal title is limited, since the trustee cannot dispose for his own benefit of the assets and rights transferred to it, as it holds title under a fiduciary capacity. Thus, Mexican legislation requires trustees to keep separate accounting books and records for assets and rights held in trust.

In general terms, only a Mexican bank or other qualified and regulated financial institution may act as trustee in a fideicomiso. Trustees are required to exercise good faith and shall use diligent and professional efforts to promote and protect the best interests of the assets and rights in trust.
Regardless of the purpose for which a fideicomiso is created, it shall either be revocable or irrevocable. The first case occurs when the settlor reserves for himself or herself the right to revoke or modify the agreement (i.e., settlor maintains the legal ability to ‘reacquire’ the assets and rights from the trustee). In the second case, the settlor cannot revoke the agreement, at least until the settlor has fulfilled his or her obligations.

From a tax perspective, when asset contributions are made to a fideicomiso in which settlors reserve the right to reacquire such assets, no sale is deemed to exist at that moment. Tax is triggered when such reacquisition right is lost or when a third party is appointed as beneficiary of the trust.

Depending on the purposes of the fideicomiso, the trustee may require either constant or specific supervision and direction, or simply certain assistance in satisfying the fideicomiso’s purposes. This is accomplished by a governing body working in the form of a committee, which is called the technical committee. The committee’s duties can be as specific or as broad as determined by the parties creating the fideicomiso.

Fideicomisos are normally created for a specific period, and in terms of law they cannot exceed 50 years; although, under certain specific cases the term can be extended.

Fideicomisos can terminate for several reasons, such as the fideicomiso reaching its purpose; such purpose becoming impossible to satisfy; by agreement of the settlor, trustee and beneficiary; when revoked by the settlor; among other cases. Upon expiration, and unless otherwise provided by the fideicomiso agreement, the assets and rights in trust will be transferred to the settlor or to the beneficiary, as the case may be.

While the three persons that are part of this agreement have legal personality, the fideicomiso itself does not have any legal personality; this means that there is no new legal person formed under the contract, but rather the trustee acts on behalf of the parties. Thus, fideicomisos are not deemed to hold the capacity of a ‘resident’ vehicle.

Therefore, all income received for any activities carried out by the fideicomiso is not taxable to the trustee but taxable for the beneficiary, as the activities are being carried out on behalf of the parties of the fideicomiso.

Mexican legislation provides a specific tax treatment for fideicomisos through which entrepreneurial activities are carried out. Mexican fiduciary institutions are obliged to compute a tax profit or tax loss derived from activities conducted thereof and report them to the fideicomiso’s beneficiaries, who are obliged to consider as part of its annual taxable income the tax result in the corresponding participation; therefore, such type of fideicomisos are pass-through vehicles. Losses generated in fideicomisos are not shifted to the beneficiaries, as they can only be offset against income generated in such vehicle.

In addition, fiduciary institutions are obliged to file advance and final tax payments on behalf of the fideicomiso’s beneficiaries, who are entitled to claim credit for the portion of those payments that corresponds to their participation.

ii  Foreign investment structures

Investment structures held overseas are commonly implemented by high net worth Mexican resident individuals.

Overseas structures are commonly established with estate planning and confidentiality purposes. Mexican tax authorities are constantly striving to obtain information about Mexican individuals and their investments abroad.
As a result of this, Mexican resident individuals and companies are investing important resources in complying with all informative obligations enacted by Congress and regulated by the Mexican tax authorities.

### iii Anti-money laundering regulations

The Anti-Money Laundering statute became effective in July 2013, which from a general overview requires financial and non-financial institutions to report ‘vulnerable’ transactions.

A series of vulnerable transactions must be reported such as gambling or betting games, issuance of credit or prepaid cards not issued by financial institutions, lending activities not conducted by financial intermediaries, sale of jewellery or watches, sale of new or used vehicles, armoured services and acquisitions on behalf of third parties.

Each vulnerable activity must be reported in case the transaction thereof exceeds the amounts established for each case within the period of time provided thereof.

The Mexican government created a special Financial Intelligence Unit that is responsible for receiving all the reports that must be filed according to the anti-money laundering statute and administrative rules and is responsible for analysing them in order to detect transactions linked to money laundering.

Non-compliance with anti-money laundering reports leads to penalties from the tax authorities. Providing false information is deemed a criminal offence punishable by jail.

### iv Reporting obligation on ‘relevant’ transactions

The 2014 tax reform introduced a new provision to the Federal Fiscal Code that obliges taxpayers to report ‘relevant’ transactions determined by the tax authorities through administrative rules.

Upon issuance of the corresponding tax form, which must be used for reporting purposes, a series of transactions required to be reported were disclosed. Among such transactions are the following:

- financial derivative transactions;
- financial transactions involving coupon strips;
- change in an entity’s shareholders;
- sale of shares;
- change of residence to Mexico;
- sale of intangible assets;
- financing transactions;
- accrued interests in long-term financing; and
- financial assets contributed to fideicomisos.

Taxpayers are relieved of reporting such transactions if their aggregate amount in a tax year is lower than 60 million pesos. This exception is not applicable to financial institutions.

This new obligation is part of the current trend of the Mexican tax administration for gathering information on transactions conducted by taxpayers in order to provide additional elements for conducting tax audits that might result in an increase in tax collection from both individuals and legal entities.

On November 2016, the Supreme Court of Justice established that the provision of the Federal Fiscal Code containing the obligation to report such relevant transactions infringes the fundamental rights of legality and juridical certainty. The overall effect of such ruling results in taxpayers being obliged to inform relevant transactions until the applicable rules
are amended. In response to this, the Mexican tax authorities issued a press release informing that through the Ministry of Finance, a tax reform initiative would be submitted in order to remedy the constitutional defects of such provision.

v Exchange of information agreements

As a G20 and OECD member country, Mexico has actively participated with other OECD countries in the development of new standards for the exchange of financial information in a more expeditious manner.

Mexican authorities have shown a keen interest in acquiring information on overseas investments of Mexican residents by being part of the Early Adopters Group (EAG) for adopting the Common Reporting Standard (CRS), which is the standard in automatic exchange of information between tax authorities developed by the OECD.

Mexican tax authorities, acting as signees of the Multilateral Competent Authorities Agreement, have sent a clear message on their position on challenging tax evasion by enabling the exchange of information in an automatic standardised manner.

It is expected that Mexico will conduct its first automatic exchange of information under the new standard in September 2017, jointly with the rest of the EAG members.

V CONCLUSIONS & OUTLOOK

The ongoing ambitious tax collection policy of the tax authorities has been supported by tax reforms in Mexico that have resulted in an increase in the federal government's revenue derived from tax collection and have enabled Mexican tax authorities to gather more information on transactions conducted both by corporations and individuals in Mexico and abroad. Validating substance of transactions is a common practice in the tax authorities' audit trends, and taxpayers if their counterparties do not provide evidence that suffices the tax authorities demand to prove the actual existence of transactions.

As part of a global trend, tax policies are being focused on gathering information of each country's tax residents with respect to assets and investments held overseas in a more efficient, standardised and automated manner. Fiscal secrecy appears to be the central topic to be challenged by tax administrations worldwide, through a scheme of unparalleled international cooperation, which will actively begin in 2017.

Jurisdictions that in the past were considered traditionally secretive are currently adopting a more open position for exchanging information with foreign governments. Mexican tax authorities are currently executing exchange information agreements that will allow them to exercise their audit faculties on investments held by Mexican resident individuals.

Mexican high net worth individuals have been constantly concerned about the confidentiality of their investments both in Mexico and overseas. The current trend of tax administrations seems challenging and more scrutiny is expected. The five-year statute of limitation of the Mexican tax authorities’ audit faculties has led an important number of Mexican investors to follow a voluntary tax regularisation programme with respect to such investments; however, more complex investment structures should be expected to try to achieve privacy and confidentiality for Mexican investors.

The 2017 temporary programme for capital repatriation has led certain high net worth individuals to withdraw from complex overseas investment structures, as automatic exchange
of information among tax administrations worldwide has become an important concern to certain individuals who are not willing to run any possible risk, having as a downside the loss of confidentiality, which has frequently been the major concern for investors.

Several external factors are still having a major adverse effect on foreign currency exchange rates with respect to the Mexican peso, and will certainly encourage investors to seek alternatives for hedging their position, considering that Mexican-resident individuals are obliged to recognise as part of their taxable income unrealised foreign exchange gains generated in each tax year.

The presidential succession process that will soon begin in Mexico will have an impact on the economic scenario of the country and in foreign investment policies of key players, in addition to the impact on foreign exchange rates with respect to the Mexican peso.

The following years will be important in knowing the actions the tax authorities might follow once the exchange of information between governments is conducted in a more automated manner.
NEW ZEALAND

Geoffrey Cone and Claudia Shan

I  INTRODUCTION

New Zealand is a member country of the Organisation for Economic Co-operation and Development (OECD) and a member of the Commonwealth of Nations. It has a well-developed infrastructure and is regularly cited as one of the least corrupt countries in the world. In 2016 New Zealand was ranked as the least corrupt country in the world alongside Denmark in Transparency International’s Corruption Perceptions Index.

It has a relatively small population for its size (it covers 268,680 square kilometres, and has a coastline of 15,134 kilometres; compared with the United Kingdom, which covers 244,820 square kilometres with a coastline of 7,918 kilometres. To further the comparison, the United Kingdom has a population of 65.6 million and New Zealand 4.8 million.) These comparisons influence many essential characteristics of the country, including a low level of regulation, stability, and as an attractive, if remote, place to live. New Zealand’s significance in wealth planning arises because of its attractiveness as a migratory destination, and as a centre for international wealth and succession planning. Of particular interest are the absence of most kinds of capital gains, estate or gift taxes, and the incorporation into statutory law of a variety of structures that do not tax overseas sourced income when utilised by non-resident persons.

II  TAX

There is no estate tax or inheritance tax in New Zealand. Gift tax has been abolished. As there are no capital transfers or accumulation taxes in New Zealand, there is no need to employ tax planning that takes into account capital tax protection.

The principal taxes in New Zealand are direct in nature: an across-the-board corporate rate of 28 per cent and a progressive individual rate of up to 33 per cent apply. An indirect tax is levied on the provision of goods and services, and is charged at a rate of 15 per cent.

New Zealand enjoys the following beneficial features for wealth planning purposes:

a  it is a member of the OECD group of countries;

b  it is a domestic taxpaying jurisdiction;

c  it is a party to numerous double taxation treaties and taxation information exchange agreements; and

1  Geoffrey Cone is the founding partner and Claudia Shan is a partner and head of legal and international compliance at Cone Marshall Limited. The writers would like to acknowledge the assistance of James Gribbin, solicitor.
it has comprehensive anti-money laundering legislation, and is a founding member of the Financial Action Task Force (FATF).

**Tax treaties**

New Zealand tax treaties generally follow the standard OECD model. Currently, New Zealand is party to 39 double tax agreements, which are summarised in the following table. New Zealand is also a signatory to 11 tax information exchange agreements.

New Zealand is a signatory to the OECD Convention on Mutual Administrative Assistance in Tax Matters, which came into force for the purposes of New Zealand domestic law on 1 March 2014.

In June 2014, the New Zealand government signed an intergovernmental agreement (based on a Model 1A type) with the United States for the implementation of the Foreign Account Tax Compliance Act (FATCA).

The New Zealand government implemented the OECD Common Reporting Standards (CRS) on 1 July 2017.

The CRS is a system for the automatic exchange of information (AEOI) between countries about the source and beneficial ownership of financial investments. New Zealand will only provide financial account information to the 58 countries that it has deemed to be reportable jurisdictions (the list is subject to change annually).

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<th>Country of residence</th>
<th>Interest (per cent)</th>
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<th>Dividends (per cent)</th>
<th>Royalties (per cent)</th>
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<td>10</td>
<td>0 or 15</td>
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<td>10</td>
</tr>
</tbody>
</table>
### ii Liability for tax in New Zealand

New Zealand tax residents are taxed on their worldwide income. An individual is resident for tax purposes if he or she has a permanent place of abode in New Zealand, or is personally present in New Zealand for one or more periods exceeding 183 days in the aggregate of any 12-month period. The income of non-residents is also subject to income tax if it is derived from a New Zealand source, although the operation of a double tax agreement may limit liability. Employment income is taxable on a gross basis and no deductions are permitted for expenditure incurred in deriving employment income. Employers withhold tax from salary and wage payments under the pay-as-you-earn system. Self-employed individuals pay tax on a net basis and are allowed deductions for expenditure incurred to obtain their income. As mentioned, there is no capital gains tax in New Zealand; however, care must be taken not to buy and sell property within a short period of time or in such a way that a pattern of regular trading activity is established, thereby making any gains taxable under the residential land withholding tax regime or as business income.

### iii Overseas income

In New Zealand, an investment that produces overseas income is called a foreign investment fund (FIF). There are three broad categories of FIFs: foreign companies, foreign superannuation schemes and foreign life assurance policies. FIF income is taxed as it accrues, not on distribution to the owner of the FIF. The FIF rules do not apply where an individual has total FIF interests worth less than NZ$50,000 in a particular tax year.

Controlled foreign companies (CFCs) are a subset of FIFs. A CFC is a foreign company that is controlled by five or fewer New Zealand residents (note that there are various de facto controls that can enable a foreign company to be treated as a CFC).

<table>
<thead>
<tr>
<th>Country of residence</th>
<th>Interest (per cent)</th>
<th>Interest paid to associated persons (per cent)</th>
<th>Dividends (per cent)</th>
<th>Royalties (per cent)</th>
<th>Copyright (cultural) royalties (per cent)</th>
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<td>15 (min)</td>
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</tbody>
</table>
tests for control, and the basic de jure standard is that a holding of greater than 50 per cent of the shares on issue will be deemed to be a controlling interest), or that is at least 40 per cent owned by a single New Zealand resident, where no one foreign resident has a higher individual holding. The FIF rules do not apply to an interest of 10 per cent or greater in a CFC. In such cases the CFC rules come into play.

There are seven methods of calculating FIF income, one of which must be applied to calculate the income of the holder of an assessable FIF interest (i.e., one which is worth NZ$50,000 or more in the tax year in question, and is not subject to the CFC rules). The relevant methods are:

a. the attributable FIF income method;
b. the comparative value method;
c. the deemed rate of return method;
d. the fair dividend rate method;
e. the cost method;
f. the branch equivalent method; and
g. the accounting profits method.

There is a consistency rule that requires a person to use the same income calculation method if the person has two or more attributing FIF interests.

The different methods are complex and advice must be taken before determining which method of calculation is to be used. However, in a broad sense the calculations will be made on the basis of reference to the gains or losses overall and not to income derived or distributed. When insufficient information is available to calculate income derived precisely, a deemed rate of return is applied.

An active income exemption applies generally to all interests of 10 per cent or greater in a foreign company. This exemption comes into effect where the active business income test is satisfied. If 95 per cent or more of the income of the CFC or FIF in question is derived from an active business enterprise (as opposed to passive sources of income such as interest, dividends, and royalties), then there will be no attribution of income to the New Zealand resident holder of that FIF or CFC interest, irrespective of the fact that it might otherwise be considered to be an attributing interest.

Dividends paid to resident persons by foreign companies are generally exempt from tax in New Zealand. Foreign dividend income will, however, be assessable in the hands of a resident individual if the attributable FIF income method is used, or if the individual is subject to an exemption from the FIF rules (including the scenario where the CFC rules apply). Resident companies will be taxed on their foreign dividend income only where the dividend is paid on fixed-rate shares, or where a deduction is granted in respect of the dividend in the jurisdiction of tax residency of the foreign company paying the dividend.

iv Credits for tax paid in another jurisdiction

New Zealand taxpayers may claim credits for tax paid in other jurisdictions, even where there is no double tax agreement in place. For the credit to apply, the tax in question must be of substantially the same nature as New Zealand income tax.
III  SUCCESSION

i  Intestacy rules

New Zealand’s intestacy rules are regulated by the Administration Act 1969. The property of the intestate deceased is vested in the Public Trustee, and devolves according to the provisions of the Act: in the first instance, to any surviving spouse, children or dependants; in their absence to the parents of the intestate; failing which, the brothers and sisters of the deceased inherit in equal shares. If there are no brothers or sisters, then the property passes first to the grandparents, and in their absence, to the uncles or aunts of the intestate. In the event that none of the heirs identified by the Act are in existence, then the assets are deemed to be \textit{bona vacantia}, and pass to the government.

ii  Wills

New Zealand’s domestic law of wills is based on the English model, as is the underlying principle of complete freedom of testamentary disposition. A person must be 18 years of age before he or she can make a will. A will is subject to certain formalities in wording and in witnessing. A will must be in writing and generally be in a specific format, and words of formality are required. There must be at least two witnesses who are in the presence of the person who makes the will and those persons must subscribe their full names, addresses and occupations. Each page of the will must be signed by the testator or testatrix and also by the witnesses.

iii  Forced heirship

New Zealand recognises the principle of testamentary freedom, and therefore does not have a forced heirship regime. There are, however, several important exceptions to the principle of testamentary freedom. In addition to the standard common law avenues that may be pursued to challenge the validity of a will (lack of testamentary capacity, duress, etc.), there are two statutory mechanisms that allow for courts to intervene and alter the division of an estate as stipulated in the relevant testamentary instrument. The Law Reform (Testamentary Promises) Act 1949 provides for the recognition of promises made by a testator during his or her lifetime to make provision for a person in his or her will, and the satisfaction of that promise from the estate where no provision has been made for the person in question. The Family Protection Act 1955 allows the court to make orders mandating departure from the disposition of assets stipulated in a will where inadequate provision has been made for persons to whom the testator owed a moral obligation of financial support.

\textit{Forced heirship planning}

New Zealand may be a useful planning jurisdiction in relation to countries that do have forced heirship regimes. Because of the primacy of the doctrine of testamentary freedom, New Zealand law does not recognise the concept of forced heirship. Consequently, there is no corresponding legal category into which a foreign court order based on that concept could be translated. Even in the case where one of the statutory mechanisms for the recognition of foreign judgments, such as those available under the Judicature Act 1908 or the Reciprocal Enforcement of Judgments Act 1934, is applicable, it would be difficult to sustain an action for the enforcement of a foreign judgment, as the New Zealand-resident respondent would usually hold the assets at issue pursuant to some kind of trust.
Asset protection planning

New Zealand has no specific asset protection law. However, the laws that cover insolvency and liquidation can effectively provide an asset protection structure.

Use of trusts

The Trusts Bill (the Bill) is currently before Parliament and aims to modernise and clarify the Trustee Act 1956. There are some unique features of New Zealand trust law that the Bill will add or build upon, including the ability to have special trust advisers, investment advisers and managers, with wide discretionary powers and the ability to add and remove beneficiaries. A protector or investment manager, who again need not be a New Zealand resident, can be given relevant advisory and discretionary powers. New Zealand is not a signatory to The Hague Convention on the Law Applicable to Trusts and on their Recognition, and some aspects of New Zealand trust law are not compatible with this Convention. New Zealand trusts currently have a maximum trust period of 80 years and the Bill aims to extend this to 125 years.

Marital property rights

Marital property, known in New Zealand as relationship property, is regulated by the Property (Relationship) Act 1976. Relationship property claims may be brought by persons who are married or persons who have lived in a permanent relationship. There is no difference whether the relationship is a homosexual or heterosexual relationship. Broadly, all property obtained during the relationship is divided equally. In respect of property that is brought into the relationship, an assessment will be made of any contributions the other party has made to the property after it was introduced.

Divorce

Divorce in New Zealand is known as dissolution of marriage. In New Zealand divorce may be obtained on a no-fault basis on grounds of separation for two years. Dissolution of marriage may be obtained by the parties without recourse to legal counsel. An application for dissolution may be made unilaterally or jointly by the parties.

Adoption

Under New Zealand law adoption must be approved by the family court and may be carried out by any persons over 20 years of age. Adopted children enjoy the same succession rights as any biological children of the adopted family.

Life insurance strategies

Except in a business context, premiums paid for insurance policies are not tax-deductible in New Zealand. There are, therefore, limited opportunities for insurance planning. In general, the tax treatment of insurance payments in New Zealand depends on what the payment is compensating; insurance for loss of capital assets is non-taxable, but income-replacement insurance may be taxed. Therefore, the receipt of a death benefit will generally be non-taxable.

Business succession

Most New Zealand businesses are held in partnership or in closely held private companies. Company constitutions and partnership agreements almost always contain provisions that
provide for business succession between shareholders. Commonly, these set out a mode of pre-emption on a notice of sale or the death of a partner or equity owner, which enable that person's share to be valued and disposed of to the continuing owners. Regardless of whether there are such provisions contained in the rules of the holding entity, in conventional family companies the interest of the outgoing shareholder or partner is valued and the acquisition price for that share is fixed as a debt repayable upon demand, in some cases carrying interest. In the case where the debt is owing to an individual, this debt is often forgiven on that debtor's death by will. An alternative method of disposition of business succession is via a trust. The shares or participation in the company or partnership are held by a trustee, who may distribute those shares to a family member or members at dates agreed by or fixed by the settlor or other members of the family.

xi  Use of offshore companies

Offshore companies have not featured prominently in New Zealand-based planning strategies for some time, because of the introduction of New Zealand's CFC and FIF rules in the late 1980s and early 1990s. Where offshore companies are utilised, they are generally held by overseas entities such as foreign trustees, individuals or foundations. It remains to be seen whether the changes made to New Zealand's international tax regime during recent years will result in a resurgence of the use of offshore companies held directly by New Zealand entities.

xii  Pre-immigration planning

Pre-immigration planning usually involves the establishment of trusts or foreign companies, or both. It is unwise for a New Zealand resident to be holding substantial investment assets outside New Zealand because of the adverse tax and other planning and reporting rules within New Zealand. Failure to plan will reduce flexibility in the future should the individual or members of his or her family wish to leave New Zealand. Therefore, any gifts or transfers of property should be made before a potential donor becomes tax-resident or domiciled in New Zealand. Ideally, a family management company should be established outside New Zealand, which will hold the assets to be invested and managed overseas. This company should be owned and controlled by a foreign trustee under a foreign trust to avoid any CFC issues or domestic tax issues in New Zealand. Capital and income that is to be utilised to settle the family in New Zealand and provide the family with a reasonable standard of living should be repatriated to New Zealand and maintained in a separate domestic structure. The overseas structure should be used to enhance and develop the family’s long-term investment wealth, with resort to such funds being used for New Zealand purposes only in exceptional cases.

xiii  Post-immigration planning

Provided a New Zealand resident has been absent from New Zealand for more than 10 years, he or she may obtain the benefit of the transitional residence rules upon re-establishing residence in New Zealand. Those rules exempt a person who is to become a resident in New Zealand from taxation of all income, except that derived from active business enterprises in New Zealand, and the provision of services overseas, for a period of 48 months from the date of establishing tax residency. Accordingly, a returning resident may safely plan to return to New Zealand and, before the expiration of the relevant period, leave New Zealand for another jurisdiction. Alternatively, he or she may utilise the transitional period to set up legitimate overseas structures that will reduce future New Zealand taxation liability.
New Zealand

xiv Mobility planning – generally
New Zealand tax residency is lost after spending more than 325 days in any 12-month period outside the country; however, the maintenance of enduring ties with New Zealand, in particular the retention of a permanent place of abode, may result in tax residency being deemed to have continued. Once tax residency has been lost, the expatriated person will only be liable to tax on income derived from a New Zealand source.

xv Mobility planning – trailing residency or domicile
Expatriation from New Zealand for tax purposes is achieved by losing tax residency. There are no significant departure issues in New Zealand.

xvi Exit or expatriation tax
There are no expatriation rules or penalties in New Zealand.

IV WEALTH STRUCTURING & REGULATION
i Trusts
New Zealand trust law is derived from English trust law. For a variety of fiscal reasons, the trust is commonplace in New Zealand. New Zealand trust jurisprudence is robust and well understood by lawyers, judges and accountants.

The New Zealand foreign trust has been a part of New Zealand’s legislative framework since 16 December 1988. It is a simple and logical structure; the result of a deliberate policy of the New Zealand government. The New Zealand exempt trust offers non-residents of New Zealand all the advantages of a conventional tax-free structure within a well-regulated jurisdiction. Features of a New Zealand foreign trust are as follows:

a a trustee holds the trust assets for the persons described in the trust deed as beneficiaries;
b a trust deed describes an equitable and contractual relationship between persons, which is regulated only by the courts;
c the trust is registered with the New Zealand Inland Revenue Department (information is not publicly available);
d a trustee may be a natural person, company or a limited partnership. The trust may have any number of trustees;
e a New Zealand trust may hold property, trade or operate a business;
f a custodial or principal trustee must be a New Zealand resident to be trustee of an exempt trust;
g a trust can be terminated at any time; and
h the trust may operate for a maximum of 80 years.

Trusts occupy a particularly favourable position in the New Zealand tax regime. Provided that the assets of the trust are contributed by a non-resident settlor, and none of the trust property consists of New Zealand-situated assets, then in the vast majority of cases the income derived from the holding of those assets can be received by the New Zealand-resident trustee, and distributed to non-resident beneficiaries, without any liability to tax arising in New Zealand.

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Apart from the residential land withholding tax that applies to non-residents or entities controlled by non-residents who purchase residential property located in New Zealand, there is no capital gains tax in New Zealand. Any capital increase in the value of the trust's assets is, therefore, not taxable.

ii Limited partnership

Limited partnerships were introduced into New Zealand law by legislation enacted in March 2008. A limited partnership comprises at least one limited partner, and a general partner who is the manager of the limited partnership. The limited partner may not, subject to minor exceptions, take part in any management activity. In return, the limited partner enjoys the protection of limited liability in respect of the debts and liabilities of the partnership. The partners may be natural or legal persons, and need not be New Zealand residents. However, requirements that a partnership should have at least one general partner that is either a New Zealand incorporated company, a New Zealand resident person or a New Zealand unlimited partnership have come into effect on 1 September 2014. The partners may or may not have a participation in the capital of the limited partnership, although the limited partner would usually be granted an equity interest in the partnership in return for contributing the capital used to establish the partnership.

A limited partnership, as distinct from a general partnership, is treated in New Zealand as having a separate legal personality. It is registered in the same way as a company with the New Zealand Companies Registry. The public information in the Companies Registry comprises the name of the limited partnership, details of its registered office and the identity of the general partner. The identity of the limited partner is protected as confidential information in terms of the legislation. The partnership agreement is a private document and is not registered in the Companies Office.

Limited partnerships are transparent for tax purposes. In other words, in determining their liabilities under the Income Tax Act, the Inland Revenue Department of New Zealand will attribute the partnership's income, expenses, tax credits, rebates, gains and losses to the underlying partners in proportion to their partnership interests.

The limited partnership can be particularly useful in offshore wealth planning. The partnership will generally be recognised as a separate legal entity under foreign law, and therefore can be useful in mitigating the problems associated with the lack of recognition of trusts in certain jurisdictions. A foreign trust could act as the limited partner of the partnership, with 100 per cent of the partnership interests being held by the trust. The income generated by the partnership assets would therefore flow through to the trust in its entirety, and would be eligible for all of the benefits enjoyed by foreign trusts under New Zealand law. The identity of the limited partner would also be confidential, and could only be disclosed in a limited number of circumstances.

iii Foreign investment zero-rate portfolio investment entities

New rules have been introduced for the taxation of collective investment vehicles resident in New Zealand, or portfolio investment entities (PIEs). These rules are aimed at making New Zealand more attractive as a jurisdiction for funds administration.

The major problem with the taxation of PIEs under the previous regime was that foreign-resident investors in PIEs were taxed fully on the income attributed to them,
irrespective of the fact that the PIE may have derived that income entirely from sources outside New Zealand. This was in contradiction to the basic policy of the New Zealand tax base that non-residents should only be taxed on New Zealand-sourced income.

The new rules provide the opportunity for a PIE to elect to be treated as a foreign investor zero-rated (FIZR) PIE (for tax purposes), which allows foreign investors to be taxed at a rate of zero per cent on the foreign-sourced income they derive through the FIZR structure.

An entity must meet the general criteria for becoming a PIE before it can elect to be treated as a FIZR. In very simple terms the general criteria are:

a the entity must make investments on behalf of one or more investor classes, one of which must have not less than 20 members, none of whom owns or controls 20 per cent or more of the interests in that investor class;
b the entity, which may be a company or a unit trust, must be resident in New Zealand; and
c the holdings of the entity must comprise at least 90 per cent passive income-generating assets.

The New Zealand administrator of the PIE will be either a New Zealand trustee or the directors of a PIE company. In the case of a company, it is suggested that a separate company administrator be appointed.

If it is treated as a FIZR for tax purposes, the PIE may attribute its income to its investors at a rate of zero per cent if the following two conditions are fulfilled:
a the income of the entity is entirely foreign-sourced; and
b the investors are notified foreign investors (NFIs).

NFIs are non-New Zealand-resident investors. They may be natural persons, or any other legal entity, including a New Zealand exempt trust. The NFI must provide the FIZR PIE with the personal information of the NFI, which will be held by the administrator of the FIZR PIE. The NFI must also certify that it is a recommended investor.

The PIE must file a tax return each year and prepare accounts. These accounts need not be audited or publicly filed.

iv New Zealand’s anti-money laundering regime

The Anti-Money Laundering and Countering Financing of Terrorism Act 2009 (the Act) was fully implemented on 30 June 2013 and imposes several obligations on reporting entities. An amendment to the Act is currently before Parliament to extend the core obligations to real estate agents, lawyers, accountants, conveyancers, the New Zealand Racing Board, and some high-value dealers. Entities that fall within the definition of reporting entities need to take the following steps to be compliant:
a a written risk assessment of the money laundering and financing of terrorism that could be expected in the course of business;
b an anti-money laundering and countering financing of terrorism programme that includes procedures to detect, deter, manage and mitigate money laundering and the financing of terrorism;
c a compliance officer appointed to administer and maintain the programme (above);
d customer due diligence processes based on the risk assessment, including customer identification and verification of identity; and
e suspicious transaction reporting, auditing and annual reporting systems and processes.

The Act takes a risk-based approach to compliance. Reporting entities (within the limits set by the Act and regulations) have some flexibility to determine the way in which they meet their obligations based on their risk assessment.

There are several supervisory bodies that regulate the application of the Act. They are:
a the Financial Markets Authority;
b the Reserve Bank of New Zealand; and
c the Department of Internal Affairs.

V CONCLUSIONS & OUTLOOK

As mentioned, New Zealand has a lightly regulated economy. It has recently passed tax reforms, considered in the body of this chapter, that make its taxation system simpler, as well as reducing income tax rates. This has resulted in an increase in high net worth families and individuals moving to New Zealand.

New Zealand is also overhauling the financial advisory system. Recent financial market reforms include changes to the regulation of capital raisings, and to how financial products and services are created, promoted and sold.

The financial crisis has not affected New Zealand’s banking system, although a moderate slowdown occurred in the economy following the 2008 crisis. New Zealand has, however, not been significantly affected by this downturn. As a founding member of both bodies, New Zealand is fully compliant with FATF and OECD standards and is known as a transparent and safe jurisdiction. As the taxation system in New Zealand is simple, and the government runs a surplus, there is no foreseeable need to change the tax system for fiscal reasons. New Zealand has a voluntary taxation system and the absence of wealth and most capital taxes makes it an attractive place to live and invest.
Chapter 31

POLAND

Sławomir Łuczak

I  INTRODUCTION

Poland is a neutral jurisdiction to individuals of significant wealth, which means that Poland provides neither positive nor negative regulations for the wealthiest individuals. On the one hand, the lack of such taxes as wealth tax and exit tax, tax exemption for closed-end funds and relatively low tax rates makes Poland an attractive place to keep personal wealth. On the other hand, Poland conforms with current global trends aimed at closing the remaining loopholes in its tax system through the introduction of various regulations such as controlled foreign corporation (CFC) rules, general anti-abuse rules (GAAR), new transfer pricing documentation requirements and taxation of joint-stock partnerships. It is significant that Poland participates in the Base Erosion and Profit Shifting (BEPS) project and implements the Council Directive 2014/107/EU of 9 December 2014 amending Directive 2011/16/EU as regards the mandatory automatic exchange of information in the field of taxation. Poland has signed many double tax treaties (more than 80 conventions) and international agreements on the exchange of information on tax matters. These act as a deterrent to individuals who intend to keep their wealth in Poland.

II  TAX

There are two types of tax obligation in Poland: unlimited and limited. Unlimited tax obligation is constituted when individuals with their place of residence in Poland are taxed on their worldwide income, regardless of where the income is earned. The limited tax obligation arises when individuals do not have a place of residence in Poland, and they are taxed solely on their income derived from Polish sources. It should be stressed that from 2017 the Polish legislator has extended a list of circumstances in which the income of non-residents is deemed to be generated in Poland. The extended list includes: (1) any kinds of operation undertaken in Poland, including operation of a foreign facility located in Poland; (2) a property located in Poland or rights to such a property, including sales thereof in its entirety or part, or sales of any rights to such a property; (3) securities and derivative financial instruments not being securities allowed for public trading in Poland within the regulated stock exchange market, including those obtained through sales of such securities or instruments and exercising rights stemming from them; (4) the deed of ownership transfer of shares in a company, the whole of entitlements and obligations in a company not being a legal person or deeds of participation

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1 Sławomir Łuczak is a partner at Sołtysiński Kawecki & Szlęzak. The author would like to gratefully acknowledge the contribution of Karolina Gotfryd to this chapter.
in an investment fund or a collective investment scheme where at least 50 per cent of the value of assets, directly or indirectly, constitute properties located in Poland or rights to such properties; and (5) regulated titles due, including left for disposal, paid or deducted by natural persons, legal persons or organisational units not having a legal entity, with residence, registered office or management in Poland, irrespective of the place where the agreement was concluded or where the service is delivered.

A progressive income tax scale that is widely used in other EU countries, such as France, Sweden and the Netherlands, is applied to individuals in Poland. Tax rates vary depending on income earned, defined as: ‘the total revenue minus tax deductible costs, earned in a given taxable year’. The Polish tax bands are relatively low: 18 per cent and 32 per cent. Poland is in ninth position in the ranking of progressive tax rates in EU countries regarding higher tax rates (32 per cent), and in 14th position concerning lower tax rates (18 per cent). Nevertheless, according to statistics, only approximately 3 per cent of taxpayers pay the higher tax band of 32 per cent. Most wealthy taxpayers optimise their profits using regulations intended for natural persons conducting business activity. These individuals are taxed according to the tax scale; however, at their request, they may tax their income at a 19 per cent flat rate, which is dedicated to natural persons conducting a business activity. It may be assumed that the most affluent Polish taxpayers are self-employed in Poland for tax purposes.

The richest Poles often derive their income from capital gains (dividends, interests, profit on the sale of shares), which are not covered by social security contributions, and it is taxed with a 19 per cent flat-rate tax (whereas in Germany and Ireland it is 25 per cent and in Scandinavian countries it is more than 30 per cent). Income from capital gains is not counted in the overall income.

In many countries, high tax rates are connected with a high tax-free personal allowance; however, this is not the case in Poland, where the tax-free amount is the lowest of all EU countries (approximately €750). It is worth stressing that the Polish Constitutional Tribunal recently issued a judgment (Case No. K 21/14) in which it stated that the level of tax-free amount is unconstitutional insofar as it does not provide a correction mechanism for the tax-free amount to ensure a minimum standard for living. Hence, from 2017 the tax-free allowance for low earners has been increased to 6,600 zlotys. In cases of earnings higher than 6,600 zlotys the allowance is decreasing depending on the income. Where yearly earnings exceed 127,000 zlotys the personal allowance is not applicable at all.

A taxpayer’s personal and family situation may be taken into account in the tax system, especially in relation to income tax, in the form of reliefs and tax exemptions.

Poland, like most other EU countries, provides various tax credits, such as an internet tax credit, a tax credit for an individual retirement security account and a tax credit for charitable donations. Since the Polish tax system is in favour of families in many tax respects, a large part of tax credits concern a taxpayer’s personal situation. Therefore, Polish income tax provides a child tax credit, joint taxation (with children) of single parents and joint taxation.

5 K Święch, Pozycja rodziny w polskim prawie podatkowym, Warsaw 2013, page 133.
of spouses, the aim of which is to ensure a family has a reduced financial burden. At this point it should be noted that the preferential treatment of families also appears in gift and inheritance tax, where the immediate family members of the testator are exempted from tax.

As of 1 January 2015, numerous amendments to the Polish Personal Income Tax Act relating to cross-border structuring entered into force, such as the introduction of CFC rules, new transfer pricing documentation requirements and comprehensive regulations regarding the provision of information on interest payments, implementing Directive 2014/48/EU of 24 March 2014. The above changes aim to close loopholes in the Polish tax system.

From an individual taxpayer's perspective, the most crucial change is the introduction of CFC rules that revolutionise international tax planning and optimisation. The Polish legislator's aim was to tax income derived by Polish tax residents from foreign companies when such income is not taxed in the company's country of residence or the tax is too low (lower than 14.25 per cent). Under new provisions, an additional income tax (19 per cent) is imposed on shareholders holding at least a 25 per cent direct or indirect holding in entities deriving their revenues mainly (more than 50 per cent) from passive income (i.e., dividends, interests, royalties, share disposals). CFC rules also affect taxpayers who are shareholders of entities that have a seat or place of management in a tax haven. Polish taxpayers who own CFCs will also need to keep a register of qualifying foreign entities and a record of transactions occurring in the foreign entities, and file a special annual return in Poland.

As for transfer pricing documentation, new provisions impose new requirements on taxpayers conducting related party transactions, which means more comprehensive information on related party transactions should be disclosed to the tax authorities. Under these new provisions, taxpayers are obliged to prepare more extensive transfer pricing documentation (in particular, local files are expanded). According to the new provisions, taxpayers whose annual revenues and expenses exceed €20 million in the preceding financial year are also obliged to provide master file documentation that includes, among others, the group's capital structure, TP policy and detailed information on intellectual property. Additionally, the biggest Polish taxpayers with consolidated revenues exceeding €750 million are obliged to provide country–country reporting. It should be stressed that some changes in transfer pricing provisions are favourable for taxpayers whose revenues and expenses do not exceed €2 million in a given year, as they do not need to prepare transfer pricing documentation.

As already mentioned above, Polish tax law provides for neither wealth tax nor exit tax, and there is no indication that the Polish legislator will introduce these taxes in the near future.

III SUCCESSION

The Polish law of succession is mainly regulated in the Polish Civil Code. However, specified provisions regarding the law of succession are also found in other statutory laws (e.g., banking law, labour law and the Code of Commercial Companies). The right to inherit is protected by the Polish Constitution, which states that everyone has the right of succession and this right is equally protected by the law.
The law of succession is based on legal principles, namely testamentary freedom and the protection of relationships between family members.  

The right to succession may result from two sources: the will or the statute (the Polish Civil Code). It should be noted that a will takes precedence over the statutory inheritance. A testate succession occurs when a testator (a person with full legal capacity) expresses his last will through one of three forms of will. The first is the simplest: the will should be written entirely by the hand of the testator, who must sign and date it. The second may be made in the form of a notarial deed. The third is to make a will by declaring its content orally before a local government officer in the presence of two witnesses.

Statutory succession should be applied when no (valid) testament exists or the persons who were appointed as heirs in the testament disclaimed the testament or are unable to become heirs. There are four groups of heirs under Polish succession law. The range of these entities is determined by family ties, such as blood ties, marriage or adoption.

In the first group, the surviving spouse and descendants will inherit. Here, the principle that children and a spouse inherit in equal parts applies; however, the spouse's share cannot be less than one-quarter of the entire estate. In the second group, in the absence of descendants, the spouse and deceased's parents will inherit. In this case, the inheritance attributable to the spouse must correspond to half of the deceased's estate. If the deceased's parents have died, the inheritance attributable to this parent goes to the testator's siblings or, if the deceased's siblings have died, their children. The third group of heirs is entitled to the succession solely when there are no heirs in the first two groups. This category includes the deceased's grandparents or, if they are also deceased, their children. The fourth group consists of children of the deceased person's spouse whose parents were not alive when the estate was opened. Last of all, the municipality in which the decedent last resided will inherit, or, if the deceased's residence cannot be determined or is located abroad, the State Treasury.

Here, it should be indicated that the sequence of the inheritance and the range of the entities entitled to the succession presented above is a result of amendments to Polish succession law from 2009. So far, provisions in scope of statutory succession have been rigorous and have prevented grandparents and their descendants from succession. Another key change is the testator's stepchildren's entitlement to the succession; however, they inherit only when their parents have passed away. The amendment was designed to strengthen family ties and limit the municipality's and State Treasury's access to the succession in a situation where a member of the testator's family is still alive.

It is noteworthy that heirs may either accept succession without the limitation of liability for debts (simple acceptance), or accept succession with the limitation of such liability (acceptance with benefit of inventory). Alternatively, heirs may reject the inheritance within a time limit of six months from the day when they became aware of their title to inherit. Until 2015, when no statement of intent was submitted within the prescribed time limit, heirs were deemed to have accepted the inheritance and were liable for debts without any limit. Such a state of affairs was deemed socially unfair. Therefore, since 18 October 2015, provisions concerning liability for debts under succession have been changed to be analogous with the latest European codifications. According to the new regulation, if heirs do not do anything
within a time limit of six months from the day they become aware of their title to inherit, their liability for debts will be limited to the assets of inheritance (acceptance with benefit of inventory).

A testator may appoint an executor to ensure that all the testamentary provisions will be properly conducted; however, the executor cannot be treated as a fiduciary or a trustee.

Polish law forbids mutual wills and contracts of inheritance, with the only exception to this rule being a contract of renunciation of inheritance, in which a person who belongs to one of the classes of statutory heirs renounces his or her statutory inheritance after the testator’s death.

There have been no changes affecting personal property, such as developments on prenuptial agreements and same-sex marriages. Same-sex marriages are illegal in Poland; therefore, people in a same-sex relationship are not subject to intestate succession. However, there are no obstacles to prevent either party in such a relationship from drawing up a will that decides who will receive a party’s estate. It should be noted that Polish succession law protects the closest relatives of a deceased person by forced share. Only descendants, a surviving spouse, and the deceased’s parents have the right to a statutory portion.

Nevertheless, a person in a same-sex relationship can receive the right to a tenancy from the deceased partner. This was confirmed by the Supreme Court in its resolution (Case No. III CZP 65/12) of 28 November 2012, in which it was held that the person of the same sex who is connected through emotional, physical and economic ties with the tenant may receive the right to the tenancy from the deceased partner just as a wife or a cohabiting partner.

Prenuptial agreements do not change the rules for passing on inheritance, including the intestate succession rules, which are binding when the testator does not draw up a will. This means that spouses who have concluded a prenuptial agreement inherit from each other according to succession law principles. This agreement may affect the seizure of assets of the inherited wealth only (there is no succession of the couple’s property, only the individual property of the deceased spouse).

Natural persons are the only taxpayers of inheritance tax. Inheritance tax is imposed on acquisitions as a result of inheritance of property (moveable and immoveable) located in Poland, and property rights exercised in Poland, including money. Tax is also applied to the acquisition of property located outside Poland and rights exercised abroad if at the time of the deceased’s death, the beneficiary was a Polish national or had a permanent place of residence in Poland. If neither the deceased nor the beneficiary were Polish citizens or had permanent residence in Poland at the moment of death, inheritance tax is not levied.

Payers of inheritance tax are grouped into three categories depending on their relationship with the testator. The first group consists of the spouse, descendants (children, grandchildren, etc.), ascendants (parents, grandparents, etc.), sons-in-law, daughters-in-law, siblings, stepfathers, stepmothers and parents-in-law. The second includes descendants of siblings (nieces, nephews, etc.), siblings’ spouses, siblings of spouses, the spouse's siblings' spouses, other descendants' spouses' siblings of parents (aunties, uncles, etc.) and stepchildren’s descendants and spouses. Finally, the third group includes other acquiring parties, including unrelated parties.

Determining the base and the rate of Polish inheritance tax depends on the specific tax group the testator belongs to and on the minimum tax-exempt amount. Currently, tax-exempt amounts are as follows: for acquirers from tax group 1: 9,637 zlotys; for tax group 2: 7,276 zlotys; and for tax group 3: 4,902 zlotys. Tax on inheritance applies to the acquisition of ownership of assets over the tax-free amount.
The table below presents the rates of Polish inheritance tax:

<table>
<thead>
<tr>
<th>Taxable base</th>
<th>Tax scale</th>
</tr>
</thead>
<tbody>
<tr>
<td>Above Up to</td>
<td></td>
</tr>
<tr>
<td>(1) from acquirers in group I</td>
<td></td>
</tr>
<tr>
<td>– 10,278 zlotys</td>
<td>3%</td>
</tr>
<tr>
<td>10,278 zlotys – 20,556 zlotys</td>
<td>308.30 zlotys plus 5% of the surplus over 10,278 zlotys</td>
</tr>
<tr>
<td>20,556 zlotys –</td>
<td>822.20 zlotys plus 7% of the surplus over 20,556 zlotys</td>
</tr>
<tr>
<td>(2) from acquirers in group II</td>
<td></td>
</tr>
<tr>
<td>– 10,278 zlotys</td>
<td>7%</td>
</tr>
<tr>
<td>10,278 zlotys – 20,556 zlotys</td>
<td>719.50 zlotys plus 9% of the surplus over 10,278 zlotys</td>
</tr>
<tr>
<td>20,556 zlotys –</td>
<td>1,644.00 zlotys plus 12% of the surplus over 20,556 zlotys</td>
</tr>
<tr>
<td>(3) from acquirers in group III</td>
<td></td>
</tr>
<tr>
<td>– 10,278 zlotys</td>
<td>12%</td>
</tr>
<tr>
<td>10,278 zlotys – 20,556 zlotys</td>
<td>1,233.40 zlotys plus 16% of the surplus over 10,278 zlotys</td>
</tr>
<tr>
<td>20,556 zlotys –</td>
<td>2,877.90 zlotys plus 20% of the surplus over PLN 20,556 zlotys</td>
</tr>
</tbody>
</table>

The taxpayer has 14 days from the day the decision of the revenue office determining the tax rate (unless it was collected earlier by the notary) has been delivered to pay the inheritance tax.

Poland is unique among tax jurisdictions across the world for exempting the testator’s immediate family members from inheritance tax. This is aimed at accumulating the family’s wealth across generations, and therefore the provisions of inheritance tax give preference to the family. The beneficiaries need to report the acquisition to the competent head of their tax office within six months of the day the tax obligation has arisen.

IV WEALTH STRUCTURING & REGULATION

For wealth structuring, Polish taxpayers commonly use regulations and structures available in Poland and as well as in foreign countries. However, trusts and private foundations are unknown to the Polish legal system, and therefore they are not widely exercised in Poland. This is not the case, however, for the wealthiest taxpayers, who willingly benefit from foreign foundations and trusts located in countries that provide these regulations, such as the United Kingdom, the Netherlands and Luxembourg.

Until 2017 optimisation structures in Poland have been established by using closed-end funds. However, from January 2017 the taxation of investment funds has been changed. The new provisions have repealed the existing regulations constituting a basis for exemption from corporate income tax for Polish closed-end investments funds (CIF) and foreign collective investment institution of a closed type.

In practice, this means that profits of these funds derived from participation in Polish or foreign tax partnership; from interest on loans granted to such entities; from interest on equity contributions to such entities; from donations and fully and partially free-of-charge performances of such entities; from securities issued by these entities and from the sale of participation in such entities are subject to the standard income tax of 19 per cent.

Above-mentioned exclusions from the CIT exemption aim at the elimination of tax optimisation schemes involving Polish CIF, which has been a part of the chain of tax transparent vehicles, including Luxembourg special limited partnership, (SCSp).
However, it should be noted that some types of CIF income is still exempt within specific exemption and considering the above exclusions, e.g., income from real property directly owned by CIF.

Polish open-end funds and special open-end funds (not applying the policies of closed-end funds) may benefit from full tax exemption without any limitations.

As for funds from the European Union or European Economic Area there is CIT exemption for them when: (1) they are subject to income tax in the state where they have their registered office on all of their income, wherever obtained; (2) the only subject of their activity is collective investment of funds raised through a public offering of participation units in securities and money-market instruments; (3) they operate pursuant to a licence from the competent financial market regulator in the state where they have their registered office; (4) their activity is subject to direct supervision by the competent financial market regulator of the state where they have their registered office; (5) they have a depository holding the fund’s assets; and (6) they are managed by entities operating pursuant to a licence from the competent financial market regulator of the state where such entities have their registered office.

The above eligibility for CIT exemption will only be applicable in cases when foreign funds operate in a country with which Poland has concluded a double tax treaty or other international agreement allowing Polish tax authorities to receive tax information from the tax authorities of the investment funds.

The CIT exemption is not applicable to collective investment undertakings when: (1) they operate in the form of a closed-type collective investment undertaking or are an open-type collective investment undertaking operating under the investment rules and restrictions applicable to closed-type collective investment undertakings; and (2) under their founding documents their participation units are not offered through a public offering or admitted to regulated trading or an alternative trading system and can also be acquired by natural persons only if they make a one-time acquisition of participation units of no less than €40,000.

Until 2014, the use of a joint stock partnership was possible for tax optimisation purposes; however, the Polish legislator became aware of this well-known trend and decided that joint-stock partnerships are subject to corporate income tax. Imposing corporate income tax on joint-stock partnerships that were tax-transparent forced taxpayers to find other ways to find tax optimisations. Limited partnerships (LPs) turned out to be an effective alternative. An LP is a very popular form of conducting business as it enables the partners’ liability to be limited and is not subject to corporate income tax. It should be clarified that LPs are entities without a legal personality and they are created by two types of partner: a partner whose liability for the company’s obligations is unlimited and who conducts the company’s affairs and represents it in all issues before third parties; or a partner with limited liability who is obliged to a fixed amount, which does not need to reflect the partner’s contribution to the LP.

To connect benefits from limited liability (not only for tax arrears purposes) with the tax advantages resulting from the tax transparency of partnerships, it is worth considering the establishment of a hybrid company, such as a limited liability company limited partnership.7

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The general partner in this entity is a limited liability company that conducts the company’s affairs and represents it, and, therefore, its liability is unlimited (in practice, it will be limited exclusively to the company’s assets because of its legal nature). A limited partner is a natural person who can also be a shareholder of a general partner.

Tax burden optimisation for income tax is carried out through an appropriate profit distribution between general and limited partners. To achieve a measurable benefit in the tax law area, profit distribution should be done in a way that the profit of the general partner is considerably lower than the profit of the limited liability partner (e.g., unlimited liability partner – 1 per cent and limited liability partner – 99 per cent).

This interesting hybrid is a type of partnership that is neither a taxpayer of corporate income tax nor personal income tax. This means the partners in a limited partnership (natural persons) should pay personal income tax. The taxpayer’s income from participating in a partnership is determined proportionally to the right to a share in the partnership’s profit. This income is cumulated with general income subject to the progressive tax rate. The taxable person may tax its income from non-agricultural activity according to the linear rate of personal income tax at 19 per cent.

As for a limited liability company, it is a capital company and, therefore, it is double taxed, which means that taxes are paid both by the company (19 per cent on income earned) and the shareholders (19 per cent from dividends); hence, why a general partner’s profit should be reduced to the minimum.

While discussing different ways of tax optimisation, issues regarding the general anti-avoidance rule in Poland should not be omitted. The fate of this clause in Poland seemed to be tortuous, but eventually the Polish government enacted a GAAR, which came into force on 15 July 2016. The general anti-avoidance rule was created as a new tool that the tax authorities may apply to reclassify business operations where a taxpayer was demonstrated to have obtained substantial tax profits through tax-avoidance strategies. Achieving ‘tax benefit’ through artificial arrangements prejudices the possibility of applying the anti-abuse rule. The term ‘tax benefit’ should be understood as ‘reducing, avoiding or postponing the taxpayer’s tax liability, creating a tax payment surplus or an entitlement to a tax refund, or increasing the amount of tax payments surplus or tax refund’. To decide whether a legal arrangement is artificial or not, various factors should be taken into account, such as excessively complex transactions. It should be noted that when a taxpayer obtains a ‘tax benefit’ that does not exceed 100,000 zlotys in a given settlement period, the GAAR will not be applied.

The clause allows the tax authorities to ignore artificial legal arrangements, which means taxpayers may be obliged to pay the avoided tax with default interest and become exposed to criminal fiscal liability. To protect taxpayers from the tax authorities’ discretionary powers, the Council for Tax Avoidance Matters, a collegiate body independent of the tax authorities, was created. The Council issues non-binding opinions on whether the GAAR

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8 GAAR was originally introduced in the 2003 Tax Ordinance Act and this provision continued to be applied until May 2004 when the Polish Constitutional Court held that the GAAR provision was unlawful because it did not meet the constitutional requirements of appropriate legislation and repealed this rule. Since then, the Polish tax law system did not have a general anti-avoidance rule until this year; however, some attempts in the past were made to introduce this clause with regard to closing remaining loopholes in Polish tax law.
should be applied in a given case or not, at the request of the taxpayer or the competent authority. Moreover, the taxpayer may apply to the Minister of Finance to issue an opinion, which disallows the application of the GAAR. The cost of this opinion is 20,000 zlotys.

The Polish GAAR is applicable as *lex generalis* to other specific anti-avoidance rules. The Polish Ministry of Finance states that the GAAR should be applied only as a last resort when other measures (i.e., specific anti-abuse rules) fail.

It is noteworthy that from May 2017 the Polish Ministry of Finance has been publishing a series of documents, including a warning about the possibility of applying GAAR to certain aggressive tax optimisation schemes. The Ministry warns in its statements against application of the tax optimisation using a closed-end investment funds and bonds purchased as part of a group of affiliates; tax capital groups (PGK) and the structures with use of foreign companies.


The definition of ‘money laundering’ in Polish law is wide, as it covers not only funds from an illegal activity but also legal funds that are ‘hidden’ from taxation.


In the provisions of the Act, it may find information such as: the definitions of ‘obliged entities’ and ‘beneficial owner’; competent authorities responsible for counteracting money laundering and financing terrorism; obliged entities’ responsibilities; principles for providing information to the General Inspector; the procedure for suspending transactions and blocking accounts; specific restrictive measures against persons, groups and entities; controlling obliged entities; protecting and disclosing collected data; and pecuniary penalties and penal provisions.

Besides credit and financial institutions, obliged entities are: auditors, external accountants, tax advisers, notaries, and other independent legal professionals such as attorneys and legal advisers. The personal scope of this Act also covers an entrepreneur (both natural and legal person) conducting a transaction exceeding the equivalent of €15,000 who is obliged to register such transaction. This obligation also occurs when a transaction is carried out by more than one single operation but the circumstances indicate that they are linked and that they were divided into operations of less value with the intent of avoiding the registration requirement.

The Act on counteracting money laundering sets out several duties of obliged entities, which include registering any transaction exceeding €15,000, keeping specified records, carrying out ongoing analyses of conducted transactions, conducting risk assessment for money laundering, and financing terrorism and applying financial security measures.
Poland is not a member of the Financial Action Task Force (FATF); however, it is involved in the group’s activities. Poland not only replies to the questionnaires sent by FATF’s experts, but also participates in the meetings of the working parties (i.e., FATF and MONEYVAL).  

V CONCLUSIONS & OUTLOOK

It may be assumed that there is a regressive tax regime in Poland, as taxes for the most affluent people are lower than in other Western countries, whereas for the poorest, they are higher. Poland does not have a national tax policy for the richest individuals; most wealthy Poles have their wealth taxed outside the territory of Poland in countries that provide more advantageous tax treatment, such as Luxembourg, Cyprus and the Netherlands. Poland has begun its battle to prevent tax avoidance and tax evasion through introducing numerous regulations designed to combat this negative phenomenon. It would not be an exaggeration to say that Poland is becoming a less tax-friendly country, which consciously limits the possibility of tax optimisation.

For several years, there has been a trend in Europe to close remaining loopholes in national tax law to prevent aggressive tax planning, tax avoidance and tax evasion: from the flagship project of the OECD – BEPS to the work carried out by the Commission in the area of Anti-Avoidance Package and domestic regulations of particular countries.

The Ministry of Finance has not conducted an analysis concerning the estimation of the scale of BEPS from the results of Supreme Chamber of Control’s report. So far, the BEPS action plan has had little influence on Polish domestic tax law.

Nevertheless, significant changes have been made in Polish tax law recently. As of 1 January 2015, numerous amendments to the Polish Personal Income Tax Act have entered into force. Changes include the introduction of CFC rules, strengthening thin-capitalisation rules and the introduction of a number of new transfer pricing documentation requirements. However, only the transfer pricing provisions reflect the OECD’s recommendations provided for in the BEPS project and they remain in line with the guidelines included in the Final Report of Action 13.

In contrast, the BEPS project has had a huge impact on Polish tax treaty law. In its answer to the letter of 8 February 2016 concerning the impact of BEPS on treaty policy, the Polish Ministry of Finance stated that the Ministry is actively engaging in the BEPS project, which has been assessed as an important initiative to prevent the loss of tax revenues at national and international levels. This approach would seem to be supported by the actions taken by the Polish Ministry of Finance.

11 Information provided in the article: Czy najbogatsi Polacy odprowadzają dochody do rajów podatkowych?, available on the website: www.totalmoney.pl/artykuly/173464,konta-osobiste,czy-najbogatsi-polacy-odprowadzaja-dochody-do-rajow-podatkowych,1,1.
13 A response to the request for access to the public information lodged by the author to the Polish Ministry of Finance on 8 February 2016 (PK.2.824.16.2016).
During the period 2012–15, Poland concluded seven new double tax treaties, eight protocols amending double tax conventions and 15 agreements on the exchange of information on tax matters. According to the Polish Ministry of Finance, the main objectives of the above-mentioned are to limit the use of double tax treaties; to reduce opportunities for aggressive tax planning; to strengthen control mechanisms through an effective exchange of tax information; and to extend the list of types of income generated in a state where it will be covered by a credit method and it will be taxable in that state. The Polish Ministry of Finance stated that it recommends implementing selected solutions of the BEPS Action Plan. The Polish Ministry of Finance will propose new BEPS provisions concerning the principal purpose test (PPT); permanent establishment with the anti-avoidance rule; the tie-breaker rule; or hybrid entities to its treaty partners. Because of the wide scope of work undertaken in the BEPS Project, the analysis evaluating proposed measures that should be introduced into the Polish tax system or in double tax treaties concluded by Poland are still in hand.

The Ministry of Finance explained that Poland is a member of the Developing a Multilateral Instrument to Modify Bilateral Tax Treaties OECD *ad hoc* group that developed during the course of the BEPS project, and whose objective is to speedily and consistently implement the proposal of new treaty provisions using the multilateral instrument. The Polish Ministry of Finance sees this initiative as an extremely important and effective means of combating tax avoidance and tax fraud and, therefore, Poland volunteered to participate in this group in April 2015. As a result, on 7 June 2017 Poland became a signatory to the Multilateral Convention to implement tax-treaty-related measures to prevent BEPS (MLI). Poland has reported 78 out of 89 double tax treaties to subject to the MLI. Given the fact that the MLI has been recently signed, it may take some time to conclude the final scope of double tax treaties and the scope of their amendments. At this moment, it is too early to see or to predict the effectiveness of the above-mentioned measures.

The OECD places emphasis not only on the BEPS project, but also on the automatic exchange of tax information between Member States. According to the OECD’s plans, by the end of September 2017 at least 45 jurisdictions (i.e., the Early Adopters Group), including Poland, will exchange information about the bank accounts of individuals. On 4 April 2017 a new Act on the exchange of tax information with other states came into force which adapts Polish law to the requirements of the Council Directive 2014/107/EU of 9 December 2014 amending Directive 2011/16/EU as regards the mandatory automatic exchange of information in the field of taxation. The Act’s main purpose is to bring together issues concerning the exchange of tax information in a single Act, including the implementation of automatic exchange of information on tax matters, also in respect of individual tax rulings at cross-border level and the Advance Pricing Agreement. The Act specifies, among others the principles of mandatory automatic exchange of information in the field of taxation; the disclosure obligations of financial institutions regarding the exchange of information on bank accounts; the scope of exchanged information; the procedure for the notification; rules concerning reporting obligations; and the principles of due diligence of the financial institutions that are obliged to report.
The Act also provides regulations enabling the automatic exchange of tax information with third countries (outside the EU) under the Common Reporting Standard (CRS) procedure. It should be stressed that Poland concluded a separate agreement on the exchange of tax information with the United States (the Foreign Account Tax Compliance Act – FATCA). FATCA entered into force as of 1 December 2015 and its main aim is to impose an obligation on Polish financial institutions to obtain and exchange information with the tax authorities about US residents and citizens in Poland.
I INTRODUCTION

Historically not a target country for wealthy individuals, Portugal has implemented structural reforms in recent years that have made the country one of the best all-round jurisdictions for high net worth individuals to relocate to.

Much of this success is down to the special programmes introduced to attract individual investors – the Golden Residence Permit Regime (allowing for free movement within the Schengen and the possibility to apply for Portuguese nationality) and the Special Tax Regime for Non-Habitual Residents – and the absence of wealth tax, gift and inheritance taxation on transfers between spouses, descendants or ascendants, exit tax, free remittance of funds and international trends (e.g., increase of fiscal pressure in some specific countries, tightening of access to traditional target countries, new global standards on automatic exchange of information). In addition, there is, of course, the reduced cost of living, public safety, healthcare system and climate, among other factors.

Recent progresses in defining the tax regime applicable to the trusts and other fiduciary structures (a grey area until recently), also contributed to placing the country on the map of private wealth planning and foreign trust owners.

II TAX

i Personal income tax

An individual is liable to personal income tax (IRS) if he or she shall be deemed to be considered a resident in Portuguese territory or, if not, if he or she derives income from Portuguese sources. Generally, a person is deemed to be considered tax-resident subject to unlimited taxation if, in the year to which the income relates, he or she:

a stays there more than 183 days, whether these days are consecutive or not, in any 12-month period commencing or ending in the year concerned; or
b has at his or her own disposal a dwelling place in such conditions that it may be inferred that there is the intention to keep and occupy it as a habitual abode.

Portuguese tax residents are subject to IRS on their worldwide income, on an unlimited liability basis. Non-resident individuals are subject to tax on the income obtained within Portuguese territory.

José Pedroso de Melo is a managing associate at SRS Advogados.
For IRS purposes, income is divided into six categories: A (employment income); B (business and professional income); E (investment income); F (real estate income); G (capital gains); and H (pensions).

Employment income, business and professional income capital gains from the sale of property and pensions are subject to a progressive income tax rate of up to 48 per cent. A surcharge applies to the part of the income exceeding €80,000, as follows: 2.5 per cent on the part of income exceeding €80,000 up to €250,000; 5 per cent on the part of income exceeding €250,000.

Investment income (such as dividends, royalties and interests), real estate income and capital gains derived from the disposal of securities (such as shares, bonds, etc.) are subject to taxation at an autonomous final rate of 28 per cent.

Among others, the following tax benefits may apply if certain conditions are met:

- income distributed by venture capital funds to individual unit holders is subject to a reduced final 10 per cent withholding tax, if not derived within the scope of a commercial, industrial or agricultural activity; and
- income regarding insurance and life assurance policies and pension funds schemes may be partially excluded from taxation whenever the amount of premiums, sums or contributions paid in the first half of the term of the contracts represents at least 35 per cent of the total.

ii Special tax regime for non-habitual residents

With the aim of attracting high net worth professionals, entrepreneurs and pensioners, Portugal has implemented an attractive tax regime for foreign individuals who wish to establish permanent or temporary residence in Portugal: The Non-Habitual Residents Tax Regime (NHR).

The major advantage of the NHR, and the one that makes it extremely attractive compared with similar regimes adopted in other European countries, consists of the introduction of a 10-year period during which Portuguese-source income received by individuals developing a high value-added activity is subject to a reduced flat tax rate, and foreign-source income, namely pensions, capital gains or business profits, may be fully exempt from tax, irrespective of remittance.

Specifically, with regard to foreign-source income, the regime provides for a tax exemption if certain requirements regarding the type of income and taxation in the source state are met. These conditions are as follows:

- Employment income – The exemption will apply to foreign-source income if this is taxed in the source state in accordance with a double tax treaty entered into between Portugal and that state, or, if no tax treaty has been entered into between both states, the income is taxed in the source state and is not considered to arise in Portuguese territory according to the domestic criteria.

- Profits, interest, income from immovable property, capital gains, business and professional income arising from high value-added activities that are of a scientific, artistic or technical nature, and royalties – The exemption will apply if the income or gains can be subject to tax in the other state under a tax treaty entered into between Portugal and that state. Alternatively, if no tax treaty has been entered into between Portugal and the source state, the exemption applies if, pursuant to the rules of the OECD model tax convention, interpreted in accordance with Portugal’s observations
and reservations, the income or gains can be taxed in the source state, and provided
that the income is not deemed to be sourced either in a blacklisted jurisdiction or in
Portugal.

c  Pensions – The exemption will apply if the foreign-source pension income is subject
to tax in the source state in accordance with a tax treaty entered into between Portugal
and that state or, alternatively, if the income is not considered to arise in Portuguese
territory. Under this provision, both public and private pensions (other than pensions
for public service) may benefit from total exemption from tax. This means that such
pensions will not be subject to tax either in Portugal or in their state of origin in relation
to a number of jurisdictions, including, for example, Austria, Belgium, China, France,
Finland, Germany, Russia, Sweden and the UK. In some other states, this provision
may grant a total exemption for private pensions only.

An individual is eligible to register as a non-habitual resident (up until 31 March of the year
subsequent to the one in which he or she became a tax resident) if:

\[ a \] he or she qualifies as a Portuguese tax resident pursuant to the Portuguese personal
income tax code;

\[ b \] he or she has not been resident in Portuguese territory in the five previous years; and

\[ c \] he or she is able to present a foreign certificate of residence establishing that he or she
has been subject to effective taxation abroad prior to his or her arrival in Portugal.

iii  Inheritance and gift tax

The tax rate levied on gifts and inheritance is 10 per cent. A surcharge of 0.8 per cent of the
taxable property value may be imposed on gifts or inheritance as far as they consist of real
estate located within Portuguese territory.

However, there is no taxation on gifts or inheritance on assets not physically or legally
located in Portugal at the time of death or donation, or transfers in favour of a spouse,
descendants or ascendants.

iv  Wealth tax

There is no wealth tax in Portugal. However, the identification number of bank accounts held
abroad must be disclosed in the annual income tax return.

v  Other taxes

The property transfer tax is levied on the onerous transfer of immoveable property. The tax is
payable by the acquirer, whether individual or company, resident or non-resident. The taxable
amount corresponds to the higher of the contracted value or the tax patrimonial value.

The tax due is assessed as described above at the following tax rates:

\[ a \] rural property – 5 per cent;

\[ b \] urban property and other acquisitions – 6.5 per cent;

\[ c \] urban property for residential purposes – progressive tax rates (ranging from zero per
cent to 8 per cent); and

\[ d \] rural or urban property when the acquirer is domiciled in a blacklisted jurisdiction –
10 per cent.
Local property tax is levied annually on immovable property located within each municipality. The tax is payable on the taxable value by the owner of the property as of 31 December of each year, to be paid in two instalments in the following year.

The taxable value of urban property corresponds to the tax patrimonial value inscribed in the Tax Registry and is determined by reference to correcting coefficients.

The IMI (property tax) rates are:

- a rural property – 0.8 per cent;
- b urban property – 0.3 per cent to 0.45 per cent; and
- c rural or urban property when the owner is domiciled in a blacklisted jurisdiction – 7.5 per cent.

A new ‘addition’ to the local property tax has been recently introduced by the budgetary law for 2017. The addition to IMI is levied on urban properties for dwelling purposes owned by individuals or companies, but individuals will not be taxed if the taxable value of its properties does not exceed €600,000. The tax rate is of 0.4 per cent in cases of properties owned by companies and 0.7 per cent for properties owned by individuals (increased to 1 per cent for the amount of taxable value exceeding €1 million). In contrast to this measure, the stamp duty levied on residential property with a taxable value higher than €1 million has been abolished.

vi Taxation of trusts

Specific rules on the taxation of trusts and other fiduciary structures were newly introduced in the Portuguese personal income tax and stamp duty law in 2014 (in force since 2015).

Until then, all transactions involving trusts and other autonomous legal entities were simply deemed to be made with those entities – the legal owners of the trust’s assets – rather than with the beneficiaries. Any contribution made by the settlor or founder to a trust, or to a foundation or ansslalt (provided that no shares should be attributable for consideration) would simply be deemed as a transfer for free. The same would succeed in the case of a distribution made to a beneficiary.

In this context, trustees and other fiduciary owners would also be potentially liable to tax regarding income deemed obtained within the Portuguese territory (notably rentals deriving from real estate located herein or dividends of shares in Portuguese companies).

With the IRS reform, the taxation of trusts and other fiduciary structures has been finally defined in a totally diverse direction, in a way that recognises the tax existence of such structures, different from its settlors and beneficiaries.

The regime is now based on the following:

- a the income accumulated in the trust during its lifetime is not subject to tax at the level of the settlor or beneficiaries, unless CFC rules should apply;
- b in the moment of eventual distributions made during the lifetime of the structure, either to settlor or to the beneficiaries, is considered as capital income for the full amount distributed (irrespective of its nature of capital or income) and subject to a 28 per cent flat rate (that may be aggravated to 35 per cent in cases where the income is deemed obtained in a blacklisted territory);
- c in the moment of the liquidation, revocation or termination of the structure, as follows:
  • if paid to the settlor or founder, qualifying as capital gains, being the taxable income equal to the difference between the amounts delivered to the trusts and the amounts received as it happens with common corporations, and subject to a
28 per cent rate (aggravated to 35 per cent in cases where the income is deemed to have been obtained in a blacklisted territory); and

- if paid to the beneficiary(ies), deemed as transfer for free (donation or inheritance) subject to stamp duty (flat rate of 10 per cent), even if, according to the territoriality principle laid down in the Stamp Duty Code, only the assets located within the Portuguese territory would be subject to tax.

vii Controlled foreign companies

Controlled foreign companies (CFC) rules were introduced in the 1990s, aiming to combat international tax evasion, notably by means of accumulation of profits in low-taxation territories. Basically, CFC rules provide for the inclusion in the taxable income of the resident companies and individuals that control foreign legal entities that are deemed domiciled in a blacklisted jurisdiction, the undistributed passive income received by such entities.

A relevant control shall be deemed to exist where the Portuguese-resident taxpayer holds, either directly or indirectly, a corporate interest equal to or exceeding 25 per cent of the shares, voting rights or equity rights of the foreign entity or its financial assets, albeit via an agent, nominee, trustee or other intermediary.

viii Double taxation treaties

In addition to Portuguese domestic arrangements that provide relief from international double taxation, Portugal has entered into double taxation treaties with 79 countries to prevent double taxation, 74 of which are already in force.

Under these treaties, withholding tax rates on outbound dividend, interest and royalty payments are reduced wherever the beneficial owner of the income derived from Portugal is a tax resident of the other contracting state.

ix The US Foreign Account Tax Compliance Act

Law 82-B/2014 of 31 December 2014, which enacted the Portuguese budget law for 2015, approved a special financial information reporting regime, aimed at establishing the terms of the information exchange under the Foreign Account Tax Compliance Act (FATCA) agreement between the Portuguese and US tax authorities, including identification of the reporting entities, definition of reportable accounts, due diligence process for reportable accounts, information to be reported, timetable for reporting and penalties for non-compliance with the required information.

On 6 August 2015, the Portuguese Republic and the United States of America concluded an agreement to improve international tax compliance and implement FATCA, which entered into force on 10 August 2016, after the fulfilment of its constitutional requirements.

III SUCCESSION

i General features

The Portuguese succession laws have remained fairly unchanged over the years, partly owing to cultural reasons, as succession is deemed a right of the family members of the deceased in respect of a continuum principle (where possession is retained by the family). No changes are envisaged in the coming years.
As in most civil law jurisdictions, the Portuguese succession legal framework is complex and characterised by strong limits to the right of free disposition *mortis causa* of one’s property. Effectively, Portuguese succession law stipulates a forced heirship regime to protect the spouse, descendants and ascendants, ensuring these heirs from one-third to two-thirds of the deceased’s total assets.

The portion of the inheritance (deceased’s estate) that is reserved for the legal heirs is generally safeguarded and cannot be affected by will or even (in most cases) by donations prior to death, as the assets could be reintegrated in the inheritance.

A distinctive feature about Portuguese succession is that the Portuguese regime only applies if Portuguese law is considered to be the personal law of the deceased at the time of death or will, independent of the location of the assets comprising the inheritance, both moveable and immovable (universal succession).

For this purpose, Portuguese private international law stipulates that the deceased’s personal law is considered to be the law of his or her nationality at the time of death or at the time of the celebration of the will, being of utmost relevance for the determination of the law applicable to the succession and all its regulatory aspects of distribution and administration of the assets comprising the inheritance, and for the determination of the capacity for and the interpretation of the will.

As mentioned before, the Portuguese succession regime did not keep pace with regulation and social changes related to marital status, being largely irrelevant for succession purposes *de facto* unions or civil partnerships and matrimonial property schemes adopted or prenuptial agreements, as none of these situations can affect the reserved portion or change the hierarchy of heirship.

### Wills

In Portugal, the most common forms of will are the public will (which is drawn up by a notary and archived in the notary’s books, although remaining strictly confidential) and the private will (which is handwritten by the testator and its conformity with form requirements is then verified by a notary who issues the validation instrument).

Any of the said wills are freely revoked, with special requirements applicable to the public will, which need to be done by a public (i.e., not confidential) deed.

Portuguese law states that any will would be valid in Portugal if the material requirements of Portuguese law are met, the disposition does not offend or limit the reserved portion of the legal heirs and if it is compliant with the laws of at least one of the following jurisdictions:

- the place where the will was concluded;
- the personal law of the testator at the moment of the declaration;
- the personal law of the testator at the moment of death; or
- the jurisdiction to which the local conflict-of-law rules refer.

Although not as common as any of the said wills, it is also possible to conclude an international will, according to the Convention providing a Uniform Law on the Form of an International Will, concluded in Washington, DC on 26 October 1973.

Finally, according to Portuguese law – and as far as it is the applicable law – it is important to note the disposition by will of the deceased’s assets as the limit stated regarding the rights and the reserved portion of the inheritance of the legal heirs.
IV WEALTH STRUCTURING & REGULATION

As seen, the Portuguese succession regime is very strict and, therefore, there are not many legal possibilities for estate planning. In addition, as most transfers on death are exempt from inheritance tax, and taxes levied on wealth are nearly non-existent in Portugal, no advance tax planning is necessary in most cases.

That being said, there are still some situations that may justify the structure of some legal entities (as private limited corporations or public limited companies) or civil entities. In some cases, and for some specific and mostly altruistic purposes, it could also be justified to create a foundation, although in this case the creation and the activity of the foundation is subject to administrative approval and regulation.

i Trusts

As a classic civil law jurisdiction, Portugal does not regulate trusts or recognise the existence of trusts regulated by foreign law, and does not even refer to such entities, with a few exceptional situations:

a to allow the incorporation of offshore trusts within the scope of Madeira International Business Centre and regulate the corresponding tax effects;

b in the context of the tax treaties entered into with the USA and Canada, acknowledging the trusts as possible resident entities in such states, strictly for the purposes of the application of the treaty dispositions, under certain circumstances;

c for anti-abuse purposes, to consider attributable to a Portuguese tax-resident individual the income obtained by entities domiciled in blacklisted territories irrespective of the distribution, in cases where the rights over the income are handled through a fiduciary entity; and

d to qualify the income arising from the distributions, liquidation, revocation or termination of the trust.

One consequence of this legal vacuum is that a Portuguese settlor who sets up a trust must respect Portuguese mandatory heirship rules. Any infringement of these rules can be challenged by the heirs of the settlor, and the assets transferred to the trust may be reduced accordingly.

ii Life insurance policies

As Portugal has become a very popular retirement location for foreigners, life insurance is proving to be an attractive wealth-planning tool, thanks to the flexibility granted to the policyholder (allowing for partly redeeming the policies, changing the beneficiaries and, in some cases, intervening in the management of the portfolio), high level of assets protection, and the very advantageous tax regime. From an income tax perspective, taxation of income generated in an individual’s life insurance is deferred and should only be taxed in the event of redemption, early payment, or maturity of the policy. Tax could only be levied on the net income generated by life insurance. The Portuguese personal income tax law establishes that provided that at least 35 per cent of the insurance premiums contractually due were paid during the first half of the contract’s lifetime:
only four-fifths of the income received is subject to personal income tax (meaning an effective tax rate of 22.4 per cent) if the payments are made under contracts that have been in force for more than five years and less than eight years; and

only two-fifths of the income received is subject to personal income tax (meaning an effective tax rate of 11.2 per cent) if the payments are made under contracts that have been in force for more than eight years.

V CONCLUSIONS & OUTLOOK

As a result of the tax reforms and programmes undertaken within the past few years and other factors relating to economic, social and life-style aspects, Portugal is currently an extremely appealing country for wealthy individuals to have a foothold in, competing in this respect with other countries traditionally chosen for wealth-planning purposes. The NHR represented a major step forward, allowing for those who become tax-resident in Portugal and are accepted as non-habitual residents the opportunity to receive qualifying income tax-free both in Portugal and in the country of source under proper planning.

Although some recent developments in the political context have introduced some considerable uncertainty, whose effects were felt in the increase of the taxation of land and real estates, it is not expected that there will be any relevant shift in the commitment of the main political forces to ongoing reforms of the tax and labour regimes, and to the strengthening of the current path of growth.

At the same time the number of foreign wealthy people moving to Portugal increases, Portuguese wealthy families are progressively more aware of the need of a proper estate planning and estate and business protection, in this way contributing to the growth of private client’s business.

The recent abolition of bearer securities (including shares) in the context of the international recommendations to fight money laundering and the financing of terrorism poses new important challenges in terms of estate planning and estate protection, as such, Portuguese families have begun to look to trusts and other fiduciary structures in spite of their irrelevance for inheritance purposes.
I INTRODUCTION

In recent years, Russia has made an incredible breakthrough from the point of view of personal wealth development. Nowadays, the main goals of wealthy Russians are good management of the family property, safe transferring of wealth through generations, asset protection and confidentiality.

The current political situation with sanctions being imposed on particular individuals and companies, and developments in Russian tax and civil legislation have led to the increase in localisation tendencies since more wealthy Russians have expressed an interest in moving their businesses to the Russian jurisdiction. At the same time Russian people continue to use foreign instruments, such as trusts and foundations, in their estate planning rather than domestic instruments. The trends in Russia are in keeping with the worldwide trend of strengthening the framework for combating tax evasion and global transparency. It is clear that the tax planning landscape is changing and that wealthy individuals with close ties to Russia are under pressure from the changes to Russian legislation and international trends and should determine what they might need to revise in their current operations and in planning future activity.

The above conditions gave rise to the development of wealth management services in Russia. Historically, wealthy Russians preferred a high level of self-involvement in asset management and worked a lot with foreign banks, family offices and investment agencies abroad. But we see today that in Russia such services have also started to be rendered by private and state Russian banks, and by emerging private wealth management offices.

II TAX

Russian legislation sets forth three levels of taxation: federal, regional and local. Currently, the following taxes are applicable to individuals: personal income tax (PIT) is among the federal taxes; regional taxes include transport tax; while local taxes include land tax and individual property tax.

Russia taxes the worldwide income of its tax residents (individuals who stayed in Russia for more than 183 calendar days within 12 consecutive months) and Russian-sourced income of non-residents for tax purposes.

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1 Maxim Alekseyev is a senior partner, Kira Egorova is of counsel, Elena Novikova is of counsel and Ekaterina Vasina is an associate at ALRUD Law Firm.
Personal taxation

Personal income tax

Incomes of individuals are subject to PIT.

Individual tax residents should pay a rate of 13 per cent (general rate) on all income received worldwide (salaries, other remunerations, dividends, sale of property, etc.).

Non-residents pay PIT at a 30 per cent rate (except for certain types of employment remunerations taxable at a 13 per cent) and at a 15 per cent rate for dividends.

The 35 per cent rate applies to the certain types of income received by residents, such as interest on bank deposits exceeding certain limits; prizes and winnings received within promotional campaigns for goods, works or services where the relevant income exceeds 4,000 roubles; and certain others.

The PIT is levied on the total income of the taxpayer, but in some cases relevant deductions, allowances and exemptions may be enjoyed.

Capital gains

Capital gains are subject to PIT as general income, taxable at the 13 per cent rate.

Income from the sale of real estate, which has been held for more than five years, is also exempted from PIT. The five-year property holding period is not applicable if the real estate was acquired before 2015, was received as a gift, inheritance and in some other cases (the holding period required for the exemption will still be three years). If the holding period is less than three or five years, the resident may decrease the income derived from the sale of the property by the relevant expenses (allowances).

Sale of securities is subject to special rules. Generally, the taxable base is the proceeds from sale less documented costs. Income from the sale of certain securities may be tax exempted.

Taxation of donations and inheritance

There are no special taxes for donations and inheritance, so PIT is applicable in some cases with the following exemptions:

a. gifts (in cash and in kind) from other individuals are not taxable except for gifted real estate, vehicles and shares;

b. any gifts between close family members (spouses, parents and children, grandparents and grandchildren) are tax exempt; and

c. inheritance is generally exempted from PIT except for royalties, which are taxed as ordinary income at the 13 per cent rate for Russian tax residents.

Taxation of individual property

Individuals (residents and non-residents) are subject to transport tax pertaining to owned vehicles registered in Russia. Moreover, individuals are also obliged to pay land tax on land plots in possession.

Before 2015 individuals were obliged to pay individual property tax on the inventory value of real estate registered in Russia, which was lower than the market price of the real estate.

With effect from 1 January 2015, the property tax for individuals is calculated on the cadastral value of real estate, which is almost equivalent to market value.
The transition period lasts from 2015–19. During this period the tax amount will be calculated using special coefficients, which should ensure a gradual increase of the tax amount for the holders of property.

ii ‘De-offshorisation’ of the Russian economy

The Russian government, in its Key Guidelines on Russian tax policy for 2014–16, announced the need for the implementation of rules that create an effective mechanism to prevent Russian businesses from misusing low-tax jurisdictions and receiving unjustified tax benefits. Following this tax initiative, the Russian tax law was subject to significant changes during 2014–16.

One of the key developments is the adoption of the De-offshorisation Law, the key aspects of which are outlined below.

It has also been noted that in the development of these initiatives, to ensure a smooth transition period to new regulatory requirements, opportunities such as voluntary declaration of assets and bank accounts or deposits have been provided to businesses. This ‘amnesty campaign’ was held from 1 July 2015 to 30 June 2016, and during it declarants had the right to disclose certain types of assets belonging to them as of the end of 2014 that were still in their possession at the date of submission of the special declaration, and receive release of criminal, administrative and tax offences liabilities under certain type of violations.

Moreover, the Russian tax legislation was amended by the regulations offering opportunities for the tax residents, who receive income upon liquidation of foreign companies and structures without incorporation of a legal entity, including trusts. Such income (except for cash distributions) is tax exempt in case the company or structure is liquidated prior to 1 January 2018 and the tax resident filed the necessary supporting documentation specified in the legislation.

‘Beneficial ownership’ concept

For the purposes of the application of double tax treaties (DTT) the beneficial owner of income is defined as a person (or entity) who by virtue of the direct or indirect participation in the foreign entity, or control over the entity, or by virtue of other circumstances has the right to independently use or dispose of the received income. Moreover, the beneficial owner of income is a person (or entity) who authorised the other person to dispose of the received income on behalf of the entity.

Current Russian tax practice provides for the following criteria under which an entity cannot be regarded as a beneficial owner of income:

- the entity has narrow powers to use and enjoy the received income;
- the entity exercises intermediary functions with respect to the income for the benefit of another entity or person and does not undertake any other business functions or risks; and
- the entity directly or indirectly transfers received income (fully or partially) to another entity (or person), which would not enjoy a tax benefit under a DTT if it received the income directly.

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2 Federal Law No. 376-FZ on amendments to Part I and Part II of Russian Tax Code (regarding taxation of profits of the controlled foreign companies and incomes of foreign organisations) of 24 November 2014.
The above provisions of the Russian tax law are largely based on the guidance provided for in the official Commentary to the Articles of the OECD Model Tax Convention, which applies the ‘substance over form’ approach to the beneficial owner of income concept.

In respect of the above-mentioned changes, the Russian tax authorities started actively to apply the ‘beneficial ownership’ concept to challenge the application of DTT benefits for cross-border payments.

**Taxation of capital gains from the indirect transfer of Russian real estate**

The De-offshorisation Law stipulates that income derived from sale of shares in foreign organisations whose assets consist of more than 50 per cent of immoveable property located in the territory of Russia should be taxed in Russia (currently at a rate of 20 per cent).

Moreover, the De-offshorisation Law requires foreign organisations (structures established in any form other than a legal entity) that own immoveable property in Russia to provide annually, along with property tax returns, information regarding their stakeholders (shareholders, founders, beneficiaries, trustees, etc), provided their share in a foreign organisation exceeds 5 per cent.

**‘Tax residency’ concept**

The De-offshorisation Law introduced into Russian legislation the concept of tax residency for companies. The foreign company may be recognised as a Russian tax resident if it is managed from Russia.

Recognition of a foreign organisation as a Russian tax resident will result in taxation of its worldwide income in Russia and an obligation to comply with other requirements and rules provided by the Russian tax law.

**Controlled foreign company (CFC) rules**

A CFC is defined as a foreign organisation (or foreign structure established in any form other than a legal entity) that is not a Russian tax resident, but controlled by a Russian tax resident (controlling person).

In this connection, Russian tax residents are required to notify the Russian tax authorities of the following:

- direct or indirect participation in foreign companies if the share exceeds 10 per cent;
- the establishment of foreign structures in any form other than a legal entity; and
- CFCs in respect of which Russian tax residents exercise control.

In accordance with the CFC rules, undistributed profits of CFCs may be taxed in Russia in the hands of the controlling person, being a Russian tax resident, at a rate of 13 per cent (if the controlling person is an individual) or at a rate of 20 per cent (if the controlling person is an entity).

**iii Exchange of information**

Besides the De-offshorisation Law, other important initiatives allowing Russian tax authorities to use different instruments of information exchange have been launched in recent years, such as:
The publication in 2014 of a Model Agreement on Exchange of Information on Tax Matters as a basis for the conclusion of bilateral agreements with offshore jurisdictions (the Russian Model of Tax Information Exchange Agreement – TIEA).

The ratification of the OECD Convention on Mutual Administrative Assistance on Tax Matters, which came into force on 1 July 2015.

The signing on 12 May 2016 of the OECD’s Common Reporting Standard multilateral competent authority agreement with a provision to start financial information exchange for 2017 in 2018.

iv Restrictions for public officials

Since 2013, the Russian government has adopted several federal laws that impose certain restrictions related to public officers possessing foreign assets.

The restrictions are imposed on a large group of public officers, including members of federal and regional parliaments, municipal officials, heads of regional and federal authorities, their deputies, judges, other officials and officers in state corporations (companies), funds and other organisations established by Russia and appointed by the president, government or the General Prosecutor, and certain employees of organisations established by Russia, where those employees are involved in decision-making on matters concerning the sovereignty and national security of Russia.

Public officers, their spouses and children under 18 are not entitled to:

- open and hold a foreign bank account (deposits);
- keep funds in foreign banks; or
- hold or use foreign financial instruments.

v Currency regulation: foreign accounts of individuals

The Law on Currency Regulation sets a number of limitations and obligations with respect to the use of foreign bank accounts by Russian currency residents.

Thus, a Russian citizen is not considered to be a currency resident after one year of living abroad without visiting Russia.

Residents, except for state officials, can freely open foreign accounts. However, residents must notify Russian tax authorities about opening, closing or changing details of their foreign accounts within one month, and annually submit reports on the movement of funds via their foreign bank accounts.

Residents can receive into their foreign accounts only those types of funds that are expressly allowed by law. The law contains the limited list of such transactions.

Over the last few years the list of funds that may be transferred to a resident’s foreign bank account was expanded. Particularly from now on resident individuals are allowed to receive into accounts opened with banks in OECD or FATF countries income from non-residents from the transferring of funds and securities into trust management conducted by the non-resident, and to receive funds obtained as the result of disposal of foreign-listed securities (the latter being effective from 1 January 2018).

Residents can freely spend funds from their foreign bank accounts, except for transactions related to the transfer of property and provision of services in Russia.

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4 Opened in banks of states that are members of OECD or FATF.
The fine for violation of these rules is up to 100 per cent of the amount of the illegal currency transaction.

III SUCCESSION

Russian law applies to those inheritance relations in which the last permanent place of residence of a testator was in Russia or the testator's real estate property is located in Russia, provided an international agreement does not state otherwise.

Russian law provides for two types of succession: by will and by operation of law.\(^5\) In cases of succession by operation of law, all legal heirs who are called upon to inherit in compliance with the succession priority shall inherit in equal shares. Heirs of the next line of the priority will succeed only if there are no heirs of the previous line. The order of succession may be changed by composing a will. In general, foreign wills are recognised as valid in Russia if they are made in accordance with the legal provisions of the country where the testator had his or her last place of residence when making the will, or its form is in compliance with the requirements of the place of execution of the will or Russian law.

Composition of a will grants the testator the freedom of disposal of his or her property at his or her own discretion and in any proportion. However, certain mandatory rules of Russian law cannot be changed in any way by a will (forced heirship rules\(^6\) or share of a spouse with regard to joint property).\(^7\)

Forced heirship rules provide that the minors or disabled children of the testator, his or her disabled spouse and parents, as well as disabled dependants of the testator in some cases, irrespective of the provisions of the will, shall inherit no less than half of a share such a person would be entitled to in the event of inheritance by law (that is in the absence of a will). The above persons shall be entitled to claim the obligatory share from the part of the property subject to inheritance that is not stated in the will. If such property is not enough to satisfy the claims of the forced heirs, they are entitled to claim their obligatory share even from the property inherited by will.

The only option to withdraw from succession any heirs entitled to the compulsory share is to execute \textit{inter vivos} transactions, such as making donations or establishing a trust or foundation in respect of the property that overrules legal succession of the property.

One more specific aspect of Russian inheritance law is that a testator's spouse is entitled to a spouse's share of property held jointly with the testator (half of the joint property). This half of the joint property is not included in the inheritance and fully belongs to the surviving spouse. The other half is included in the estate and is divided between heirs (the surviving spouse can also be included in the list of heirs). This rule applies even if a will provides otherwise.

To come into possession of the estate, the heirs should submit an application to the notary at the place of the testator's last place of residence or at the place of real estate location in the Russian Federation (depending on circumstances) no later than six months after the testator's death.

\(^5\) Article 1111 of the RF Civil Code.
\(^6\) Article 1149 of the RF Civil Code.
\(^7\) Article 1150 of the RF Civil Code.
The notary shall issue a certificate of succession right to those heirs who come into possession of the estate. It should be noted that such a certificate is usually issued by the notary upon the expiry of the six-month period after the testator’s death, except where the heirs may be clearly identified and where no disputes between the heirs are expected to arise.

Despite the fact that Russian civil legislation was undergoing large-scale reform, succession law had not faced any fundamental changes for a long time. Then, in July 2017 the Russian Parliament introduced succession funds adopting amendments to the Civil Code.

According to the amendments, succession funds may be established by a notary public in accordance with the testament of the deceased person within three business days of the death of the testator. The respective testament should include the rules for the management of succession fund, which cannot be amended after the establishment of such a fund (an exception is made for certain unexpected circumstances). The rules should include the provisions on the election of management bodies, on the transfer of succession fund’s property (in full or in part) to certain determined or determinable persons (beneficiaries), and storage and disclosure of the succession fund’s documentation.

In addition, these amendments elaborated the rules of fiduciary management of inheritance: they include mandatory assessment of inheritance prior its transfer to fiduciary management and the provisions on the control of fiduciary management by notary public as well as requirements of the fiduciary manager.

The respective amendments will come into force on 1 September 2018.

There have not been any recent major developments affecting personal property in Russia. In this regard, certain basic aspects of Russian matrimonial law are described below.

In general, the Family Code recognises joint property rights as the legal property regime of spouses. Joint property includes any property gained by the spouses during their marriage, irrespective of in whose name it was gained or by whom such monetary funds were contributed.

Where there is an intention to dispose of joint property, the relevant spouse shall receive the consent of the other spouse for such a disposal.

In Russia, only an officially registered marriage has the legal consequences mentioned above. From the point of view of Russian family law, cohabitation has no legal standing. Registration of same-sex marriage is not permitted.

Spouses are free to change the joint property regime to a separate property regime by entering into a matrimonial agreement. However, certain restrictions shall be observed: the Family Code provides that the court can find a matrimonial agreement invalid fully or in part upon the demand of one of the spouses, provided the terms of the matrimonial agreement place this spouse in a highly unfavourable situation.

The matrimonial agreement can be concluded before or after the state registration of a marriage. The formal requirements for the validity of matrimonial agreements concluded in Russia are that such agreements shall be executed in written form and certified by the notary public.

Where a separate property regime has been established under a matrimonial agreement, property is no longer the joint property of the spouses and, therefore, the consent of the other spouse for the conclusion of a transaction with the separate property of the spouse is not required. Moreover, following changes to the joint property regime under a matrimonial agreement, in cases of inheritance, a surviving spouse is not entitled to claim a half share in
joint property. Nevertheless, the surviving spouse is still entitled to inherit on other grounds (if mentioned in a will or, in the absence of a will, by operation of law as an heir of the first order – provided that the spouse is not deprived of the inheritance by the testator).

IV WEALTH STRUCTURING & REGULATION

Russian legislation does not recognise the concept of the ‘trust’. However, at the time of writing, Russian legislation does not hinder its citizens and residents from transferring assets to foreign trusts whether as the settlor, beneficiary or protector, etc., of such structures. Transferring assets to such a structure breaks the ownership of the assets and they will then be considered to be owned not by the settlor of the structure but by the third parties (e.g., the trustees). In such cases, Russian succession law is not applicable.

The transfer of assets to trusts is not regarded as a taxable event. Income received from trusts as a general rule is subject to PIT at the rate of 13 per cent.

At the beginning of 2016, the tax legislation was amended by the provision allowing amounts that are not deemed to be distributed from the profit of the structure, including trusts, to be exempt from taxation. This exemption is provided for the value of the property (including cash) or property rights, which were previously contributed to the structure by the recipient of trust distribution or by his or her close relatives. However, the Russian Tax Code states that if the structure has any undistributed profit, any distributions within the amount of such profit will be treated as distribution of profit regardless of how it is documented and taxed.

When Russian citizens and residents intend to transfer their property to foreign trusts, certain precautions should be observed. Considering the absence of the concepts of trusts in Russia, Russian citizens and residents cannot transfer their Russian assets directly to a trust but only through a foreign company.

Moreover, Russian matrimonial law provides that the transfer of assets being the joint property of spouses to a trust requires the consent of the other spouse for such action; otherwise, such a transfer may be disputed through a court order as a violation of Russian family law.

Furthermore, despite the absence of the relevant court practice in Russia, to avoid possible disputes between heirs, the forced heirs should be included as beneficiaries of the relevant structure. Alternatively, a person transferring assets to a trust or foundation may otherwise ensure that the compulsory shares of the forced heirs will be satisfied from other assets directly possessed by the deceased and not transferred to the trust.

In the context of wealth structuring, it is important to note that the Russian citizen shall inform the Russian state authorities about the fact that he or she has another citizenship or residence permit or other valid document confirming the right of permanent residence in a foreign country. The notification may be submitted in person, by a representative (authorised by law as well as by the power of attorney) or via the federal postal service. Failure to perform this duty entails an administrative or criminal liability (depending on the nature of the violation). The administrative liability occurs in cases of late filing or provision of incomplete or deliberately false information and entails a fine in the amount of 500 to 1,000 roubles.8 Failure to provide notification at all entails a criminal liability with one of the following

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8 Article 19.8 (3) of the Russian Code of Administrative Offences.
consequences: a fine of up to 200,000 roubles; a fine of the amount of the wages or other income of the convicted person for a period up to one year; or the obligation to perform compulsory works for up to 400 hours.9

Pursuant to the amendments, these changes are not applicable to persons residing outside Russia (i.e., those without registered abode in Russia and living abroad).

In addition, we would like to bring your attention to the requirements of the Law on civil registry acts, which provides for an obligation to inform Russian state bodies about civil registry acts committed with respect to the Russian citizen outside the territory of the Russian Federation, as well as for the operation of a unified state register of civil acts (the Register) and transmission of books on civil acts into electronic form.

In accordance with the provisions of the Law on civil registry acts, the citizen of the Russian Federation, with respect to whom a civil act was registered outside the territory of the Russian Federation, should submit information about such registration to the civil registry located at his or her abode in the Russian Federation or Russian consulate. Information should be submitted within one month of such registration starting from 1 January 2018. The provisions are quite recent and currently do not clarify whether it is necessary to submit information about such acts registered before 1 January 2018 and do not establish any liability for the failure to submit such information. However, we cannot exclude the possibility that such liability will be established by adoption of additional legal acts in future.

This information should be stored in the Register, which will compile all information about civil acts registered with respect to Russian citizens outside the territory of the Russian Federation, as well as all civil acts registered in the territory of the Russian Federation. The Register should be operated by the federal tax service, which, among other state authorities, would be able to request information from the Register.

In Russia, services connected with wealth management are generally provided by legal entities and banks. In accordance with the existing anti-money laundering rules, service providers are obliged to perform know-your-customer procedures, including obtaining the information on the ultimate beneficiaries where the client is a legal entity.

The definition of a beneficial owner was introduced in Russian legislation in 2013 for the first time ever. The law defines the beneficial owner as an individual who directly or indirectly (with assistance of third parties) holds more than 25 per cent of assets of a client or has the option to control its actions.

According to new changes in the federal Law on Countering Money Laundering and Terrorism Financing, legal entities (with some minor exceptions) have to take all possible measures to identify their beneficiary owners. To do so, a legal entity has a right to request information from its founders, participants and controlling entities or persons, and such entities or persons are obliged to provide all available information. In addition, the legal entity should appoint an officer, who will be responsible for the storage and annual update of such information (usually a general director or chief accountant). Non-compliance with this requirement leads to the risk of administrative liability of a legal entity in the form of a fine of up to 500,000 roubles.

In addition, financial organisations10 have to take all possible and reasonable measures to identify the beneficial owner of a client.

9 Article 330 (2) of the Russian Criminal Code.
10 Credit institutions, professional participants in the securities market; insurance and leasing companies; the federal mail organisation; management companies of investment funds and private pension funds;
Where the beneficial owner is not identified, the client’s chief executive officer may be recognised as the beneficial owner.

Also, banks, law firms and some other organisations are obliged to report to the Russian Federal Financial Monitoring Service on certain transactions or finance operations concluded or made by the client if such transactions or operations fall under thresholds established by law.

V CONCLUSIONS & OUTLOOK

In summary, it is necessary to say that wealth is always accompanied by many responsibilities, such as the obligations to manage complicated local and international assets, invest wisely and protect one’s family. The area of Russian private wealth is one of the fastest growing in the world.

Despite the established practice of using foreign instruments, Russians show a tendency to use Russian instruments in their cross-border estate planning. However, the practice of using the Russian instruments is not completely formed and only the future will show how recent legislative changes are of effectiveness and attractiveness for the private clients.

Also, it shall be noted that the general tendency in the latest legislative amendments is towards increasing state control. An integral part of this process is the tightening of tax regulations.

Russia is not trying to reinvent the wheel; on the contrary, where prospective measures are successfully implemented in other jurisdictions around the world, the foreign experience of these rules is analysed by Russian governmental experts drafting new laws. Hence, foreign investors will mostly see rules that they are already familiar with from their experience of sophisticated jurisdictions, such as the EU countries or the United States.

However, the latest changes to Russian tax law will inevitably affect artificial structures whereby ‘letter box’ companies located in jurisdictions with favourable tax regimes are used, without a sound business purpose, only to obtain tax benefits. At the same time, robust structures are unlikely to be affected if they are used by foreign companies that have proper substance, genuine business purpose and are managed from the jurisdiction of their residence.

In light of these changes, new structures should be developed carefully. Moreover, existing structures should be reviewed as soon as possible to determine whether reorganisation is necessary to minimise the possible negative effects of the anticipated measures on information exchange.

Thus, Russian law and practice is changing and is moving in a direction with global trends – restraining the aggressive use or abuse of tax benefits stated in DTTS and increasing global transparency and tax control – and as a result, it is expected that Russia will accede to the OECD Base Erosion and Profit Shifting plan.
I  INTRODUCTION

Singapore’s gross domestic product per capita based on purchasing power parity is the world’s third-highest.2 Singapore was established as a free port and today is the world’s busiest port. Changi Airport is a major air hub. Singapore has a balanced economy in manufacturing, services, trade and tourism. The country is the fourth-leading financial centre (according to the Global Financial Centres Index as well as the International Financial Centres Development Index). Singapore is also a member of the Trans-Pacific Partnership, which is the largest regional trade agreement to date, between 12 countries that are also members of the Asia-Pacific Economic Cooperation (APEC).

Singapore is said to have the world’s fastest growth in numbers of ultra-high net worth individuals (i.e., those who have at least US$30 million in assets).3 In the five years preceding 2014, industry assets under management have expanded at a 14 per cent compound annual growth rate. As at the end of 2014, total assets managed by Singapore-based asset managers grew by 30 per cent to S$2.359 trillion, with approximately 81 per cent of total assets under management (AUM) sourced from outside Singapore.4 Of the total AUM, approximately 54 per cent was sourced from the Asia-Pacific, 19 per cent from Europe and 18 per cent from North America, demonstrating Singapore’s role in serving regional and international investors. The Asia-Pacific region continued to be a key investment destination for Singapore-based asset managers, accounting for approximately 68 per cent of total AUM – about the same as in 2013. Within the Asia-Pacific, 41 per cent of AUM was invested in ASEAN. Singapore is also a regional hub for a growing pool of institutional investors: in 2014, La Caisse de dépôt et placement du Québec set up an office in Singapore, joining the Investment Company of the People’s Republic of China, Norges Bank Investment Management and the Swiss National Bank. In 2015, the Korean National Pension Service also set up an office in Singapore.5

1  Chua Yee Hoong is a partner at KhattarWong LLP, a member of Withers KhattarWong. The information in this chapter is correct as of 2016.
3  ‘Singapore to see world’s fastest growth of super rich individuals: Knight Frank Survey’ published on 5 March 2015 by The Straits Times: www.straitstimes.com/business/singapore-to-see-worlds-fastest-growth-of-super-rich-individuals-knight-frank-survey.
5  See Note 4.
To further grow the fund management industry and attract fund management activities in Singapore, certain existing tax incentives have been refined and extended for a further five years until 31 March 2009. Goods and services tax concessions have also been introduced, further incentivising and attracting funds to be managed from Singapore. In recognition of the importance of venture capital activity in supporting entrepreneurship, the Budget 2015 introduces a 5 per cent concessional tax rate accorded to approved venture capital fund management companies managing Section 13H funds on their specified income.

Singapore continues to be ranked number one worldwide for the ease of doing business. Another contributing attribute to Singapore’s competitiveness is that it has entered into comprehensive avoidance of double taxation treaties with 80 countries, including most of the Asia-Pacific region, India, China and major European economies.

II TAX

i Personal income taxation

Unlike some countries, Singapore does not impose worldwide taxation. The basic principle is that income tax is payable on Singapore-source income, and on any foreign-source income received in Singapore. Essentially, source of income is the primary basis of taxation rather than residence or domicile.

There is no capital gains tax. Furthermore, individuals are exempt on any and all foreign-source income received in Singapore. Taken together, this means that all remittances by individuals of foreign-source income and capital are tax-free. There is also no estate duty (inheritance tax).

Income tax would apply to individuals who are employed (or operate an unincorporated business) in Singapore. Singapore-source returns on investments (e.g., rental income from local property) are taxable, but certain categories (e.g., bank interest, dividends) are exempt. Starting from Year of Assessment 2017, marginal individual income tax rates top out at 22 per cent. The effective rate on the first S$320,000 of an individual’s taxable income is 13.9 per cent, and the top rate of 22 per cent only applies to the top slice of taxable income over S$320,000.

ii Capital gains tax

There is no capital gains tax in Singapore.

iii Gifts and succession taxes

There is no inheritance tax or estate duty. There is no gift tax regime per se in Singapore. There is also no stamp duty on the transfer by assent of immoveable properties and shares to...
beneficiaries in accordance with a deceased person's will or intestacy laws. There are, however, *ad valorem* stamp duties on the conveyance, assignment or transfer of company shares\(^9\) at 0.2 per cent and immoveable property in Singapore at up to 3 per cent.

Over and above *ad valorem* duties, as part of the government's measures to curb property speculation and cool property prices, additional buyer's stamp duties have been introduced as follows:

- **a** For foreign nationals and entities buying any residential properties: 15 per cent.
- **b** For Singapore permanent residents buying their first residential property: 5 per cent.
- **c** For Singapore permanent residents buying their second and subsequent residential property: 10 per cent.
- **d** For Singapore citizens buying their first residential property: nil.
- **e** Singapore citizens buying their second residential property: 7 per cent.
- **f** Singapore citizens buying their third and subsequent residential property: 10 per cent.

However, these nationals will be afforded the same stamp duty treatment as Singapore citizens, pursuant to Free Trade Agreements that have been entered with Singapore:

- **a** nationals and permanent residents of Switzerland;
- **b** nationals of Liechtenstein;
- **c** nationals of Norway;
- **d** nationals of Iceland; and
- **e** nationals of the United States.

**iv  Goods and services tax**

Goods and services tax (GST) is the consumption tax in Singapore. Currently, the standard rate of GST is 7 per cent.

**v  Property tax**

Property tax is imposed on immoveable properties in Singapore. It is computed by applying the applicable tax rate on the 'annual value' of the property. The annual value of a property is generally derived based on the estimated annual rent that it can fetch if it were rented out (i.e., hypothetical rent). The annual value is determined in the same manner regardless of whether the property is owner-occupied, rented out or vacant. In the case of vacant land, for example, in the case where a building has been demolished, the annual value is determined to be 5 per cent of the market value of the land.

With the implementation of progressive tax rates on residential properties since 2010, which was further enhanced in 2013, property tax on residential properties has been refashioned as a form of wealth tax in Singapore. Prior to that, property tax was levied on residential properties at a flat rate. Non-residential properties (including commercial and industrial properties) continue to be taxed at a single tax rate.

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9 Generally, these refer to shares of companies for which share transfer instruments need to be executed. Stamp duties are effectively not chargeable in respect of the trading of securities which are transferrable by book-entry, (e.g., listed shares).
vi Customs duty

Customs duty is primarily levied on four categories of goods: motor vehicles, tobacco, fuel and alcohol.

III SUCCESSION

The statutory rule for intestate succession is that:

- the distribution of the moveable property of the deceased is regulated by the law of the country in which he was domiciled at the time of his death; and
- for immoveable property located in Singapore, the intestate estate will be regulated by the Intestate Succession Act, regardless of where the deceased person was domiciled at the time of his death.

The Intestate Succession Act sets out the distribution rules: where a person dies leaving a spouse and children, the spouse will be entitled to half share, and the children the remaining half. ‘Child’ is defined to mean a legitimate child. The Intestate Succession Act has thus far not been interpreted to recognise ‘spouse’ as including partners in civil partnerships or same-sex marriages.

Formal validity of testamentary succession is governed by the Wills Act 1996. Under the Wills Act, a will is considered to be properly executed if its execution conforms to the internal law in force in:

- the territory where it was executed;
- the territory where the testator was domiciled at the time:
  - when the will was executed; or
  - of his or her death;
- the territory where the testator habitually resided at either of the times referred to in (b); or
- the state of which the testator was a national at either of the times referred to in (b).

Generally, probate or letters of administration are required by various institutions (for example, banks, the land registry) to deal with the assets of the deceased. The proving of wills in the Singapore court is done by way of an application for grant of probate. Foreign grants of probate or letters of administration granted by a court of probate in any part of the Commonwealth and Hong Kong may be sealed in Singapore with the seal of the Singapore Family Justice Courts.

Generally, it is not possible for beneficiaries to challenge the adequacy of their provision under the intestacy rules. However, if the deceased was domiciled in Singapore at the time of death, it may be possible for certain family members (such as the spouse, unmarried daughter, infant son, disabled children) to apply to court for reasonable provision, as the court thinks fit, to be made out of the deceased's net estate for their maintenance. The purpose of this application is not meant to displace the intestacy rules, but rather to obtain reasonable maintenance during the applicant's lifetime. Factors that would be considered include:

- whether the deceased made adequate provisions during his or her lifetime;
- whether, prior to his or her death, the deceased was making a substantial contribution to the applicant other than for payment for work or services rendered;
- whether there is any source of past, present, or future capital or income for the applicant;
- the conduct of the applicant to the deceased and vice versa; and
other circumstances relevant or material in relation to the applicant and the persons interested in the estate.

Singapore has comprehensive specialist Family Justice Courts that deal with matters concerning probate, succession, mental capacity, adoption, guardianship and family matters. The purpose of the Family Justice Courts is to bring all family-related work under a specialised body of courts to better serve litigants and frame disputes from the perspective of families and the individuals within, and provide better support for families to resolve disputes.

IV WEALTH STRUCTURING & REGULATION

i Trusts

The law of trusts in Singapore has the same roots as the law of trusts in England and fundamentally still follows these principles. The Application of English Law Act, enacted in 1993, provides that ‘the common law of England (including the principles and rules of equity) so far as it was part of the law of Singapore immediately before 12 November 1993, shall continue to be part of the law of Singapore.’

Other relevant statutes concerning trustees and trusts in the private client context are the:

a Trustees Act 2005. This concerns the general power of investment, statutory duty of care and other duties and powers of the trustees (including personal representatives where the context permits).

b Trust Companies Act. This concerns trust business licensing regime regulated by the Monetary Authority of Singapore. The Trust Companies Act and its subsidiary legislation regulate the following business activities:

- the provision of services for the creation of express trusts;
- acting as trustee in relation to express trusts;
- arranging for any person to act as trustee in relation to an express trust; and
- the provision of trust.

The trust business licence regulatory framework has been introduced for about a decade now. There are currently 53 holders of trust business licences in Singapore.10

Settlor reserved power trusts are formally recognised: the Trustees Act provides that no trust or settlement of any property on trust shall be invalid by reason only of the person creating the trust or making the settlement reserving to himself any or all powers of investment or asset management functions under the trust or settlement.

Non-charitable purpose trusts generally are not valid. However, there are certain English exceptions (for example, the care of particular animals, the maintenance of specific graves and monuments and so on) which may possibly be valid in Singapore. There is also a known exception in relation to local customs (testamentary trust to perform Sinchew rites).

The statutory perpetuity period is 100 years. Following reforms to trust law in 2004, income arising from a settlement or disposition of property may be accumulated for the duration of the settlement or disposition, subject to the terms of the settlement or disposition to the contrary.

Cases concerning trust assets are typically fact specific. In *Anna Wee v. Ng Li-Ann Genevieve (sole executrix of the estate of Ng Hock Seng) and another* [2013] SGCA 36, the settlor and the claimant were married for 12 years before they were divorced and the decree nisi was made absolute. The claimant came from a wealthy family. Her claim was that she had thought the settlor had little or no assets and therefore did not ask for division of matrimonial assets. Two years after their divorce, the settlor died. On his death, the claimant discovered that the settlor had amassed a sizeable fortune, which was primarily kept in two offshore trusts. The beneficiaries of the first trust were the settlor’s two children from his marriage with the claimant, and Ng, his daughter from an earlier marriage. The beneficiaries of the second trust were Ng and the trustees of the first trust. However the settlor was specifically excluded from benefitting under both trusts. The claimant brought both a claim of fraudulent misrepresentation against the settlor’s estate, and a claim of unjust enrichment against the trustee of two offshore trusts.

Both claims were dismissed in the High Court and subsequently in the Court of Appeal. On the first claim, the Court of Appeal agreed with the High Court’s finding of fact that there was no expressed misrepresentation or active attempts to conceal assets during the settlor’s lifetime. Rather it was the claimant’s own perception and conclusion that the settlor was a ‘man of straw’. Even if the settlor had made a fraudulent misrepresentation, the claimant did not rely on it and there is therefore no need to consider whether she has suffered loss. Given that there was no fraudulent misrepresentation on the settlor’s part, that being the threshold question, the Court of Appeal held that the claim for unjust enrichment against the trustee cannot succeed.

In another case, during divorce proceedings, the wife made a claim of division of matrimonial assets over an Australian property that was acquired prior to the marriage and placed into a trust in respect of which the husband’s parents are unit-holders. It was inconclusive as to whether the husband had funded the purchase of the property during the course of the marriage. However, the court recognised that *prima facie* there was a trust over the property, and found that because the husband did not deliberately put the property out of the reach of the wife, the property did not form part of matrimonial assets (*BF v. BG* [2006] SGHC upheld in *BG v. BF* [2007] 3 SLR(R) 233).

In *Marie Eileen Guin v. Arun Guin* [1994] SGHC 157, during the course of his marriage, the husband created a discretionary trust for Australian tax purposes. On divorce, the husband claimed, among other things, that he lost control over the settled assets and therefore the assets should not be included as matrimonial assets. The judgment did not comment on the law on whether losing control over assets would preclude the trust assets from being part of matrimonial assets. Instead, the court decided this point on a finding of fact that the husband was unlikely to have lost control because he was a savvy and tenacious businessman. As such, trust assets were taken into consideration in the division of matrimonial assets.

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11 Section 32(1), Civil Law Act (Cap. 43).
12 Section 31(1), Civil Law Act (Cap. 43).
In *AQT v. AQU* [2011] SGHC 138, the husband set up a trust mere months after filing for divorce. It was held that the assets used to set up the trust need not be notionally included in the pool of matrimonial assets, since the terms of the trust showed that it was intended for the children’s benefit, which is consistent with the aims of the matrimonial partnership.

In contrast, in the case of *TQ v. TR* [2009] SGCA, the husband set up an irrevocable trust in Mauritius for the benefit of the children of the marriage after a decree nisi was granted. Rather than setting aside the trust, the Court of Appeal regarded this as ‘a naked attempt’ by the husband to present the wife and the court with a *fait accompli* in respect of the issues of maintenance of the wife and their children, and the distribution of the matrimonial assets. The husband was ordered to pay a sum equivalent to that in the trust into an account in a Singapore bank, which could be used by either of the parents for the benefit of the children.

**ii Charities, international charitable organisations, qualifying grant makers**

Charitable purpose trusts are recognised in Singapore. Charities could be set up in the form of a trust, company or society.

Charities are defined as ‘any institution that is established for charitable purposes and is subject to the control of the High Court in exercise of the Court’s jurisdiction with respect to charities’ (Charities Act). Although the term ‘charitable purposes’ is not specifically defined in statute, four broad categories are generally recognised:

- *a* the relief of poverty;
- *b* the advancement of education;
- *c* the advancement of religion; and
- *d* other charitable purposes that help and benefit the community that do not fall into any of the above categories.

Charitable purposes for the benefit of the community can include:

- *a* the advancement of health;
- *b* the advancement of citizenship or community development;
- *c* the advancement of arts, heritage or science;
- *d* the advancement of environmental protection or improvement;
- *e* the relief of those in need by reason of youth, age, ill-health, disability, financial hardship or other disadvantages;
- *f* the advancement of animal welfare; and
- *g* the advancement of sports, where the sport advances health through physical skill and exertion.

Charities are primarily regulated by the Charities Act. The governing board members of a charity must apply for registration within three months of the charity’s establishment. The Commissioner of Charities (COC) keeps the register of charities. A registered charity is exempt from Singapore income tax and qualifies for property tax exemption on premises that it owns and uses for charitable purposes.

Organisations with international charitable aspirations could consider the International Charitable Organisation scheme for charity registration. Separately, the Economic Development Board administers the international non-profit organisation (INPO) scheme.
Intergovernmental organisations such as the World Intellectual Property Office (WIPO) and the United Nations Development Programme (UNDP) have established regional presences in Singapore.\textsuperscript{13}

Grant making by itself is not a charitable purpose. However, grant making in advancement of one of the recognised heads of charitable purposes is considered by the Commissioner of Charities to be a charitable purpose.\textsuperscript{14} Such organisations could consider the qualifying grant maker scheme which provides for a lighter touch registration regime, given that such grant makers are founded by private or institutional money rather than through public solicitation which would require more regulatory safeguards.

Donation benefits are limited to donations to institutions of a public character (IPCs) for local charitable purposes. Donations to IPCs are tax deductible against the donor’s statutory income.

To encourage charitable giving locally, a liberal deduction of 2.5 times is currently available (until 31 December 2018).

Under the Public Art Incentive Scheme, donations of sculptures or work of art for public display to the National Heritage Board or its approved recipients may also qualify for tax deduction.

In 2016, a pilot business and IPC partnership scheme was introduced. From 1 July 2016 till the end of 2018, businesses that send their employees to volunteer and provide services to institutions of a public character (IPCs), including secondments, will receive a 250 per cent tax deduction on associated cost incurred, subject to the receiving IPC’s agreement. This deduction will be subject to a yearly cap of S$250,000 per business and S$50,000 per IPC.

\textbf{iii Capacity}

There is no statute or enacted law in Singapore that fixes the age of majority across the board. The age of majority, under common law, is 21 years. However, several statutes fix the age of persons under which the particular statute or law is applicable (for example, under the Civil Law Act, a minor who has reached 18 years can enter into certain contracts and bring or defend a legal action in his own name, as if he were of full age).

In the case of an adult who loses capacity: an application in court can be made for a deputy or deputies to be appointed in respect of a person who has lost capacity. Alternatively, one can draw up and register a valid lasting power of attorney registered in Singapore while one still has capacity. The lasting power of attorney appoints a donee who can act under specific terms as provided in the lasting power of attorney when the donor loses capacity. Only lasting powers of attorney registered in Singapore will be recognised for Singapore purposes. A new legal framework is being proposed in 2016 to introduce professional donees and deputies.

\textbf{iv Working in Singapore}

Foreign professionals, managers, executives and technicians live and work on a non-permanent basis in Singapore under work passes. Depending on the income level of the pass holder, the individual may sponsor dependant’s passes for his or her parents, spouse and children to live in Singapore. The Ministry of Manpower (MOM) has implemented and further

\textsuperscript{13} See: www.edb.gov.sg/content/edb/en/industries/industries/international-non-profit-organisation.html.

enhanced the Fair Consideration Framework to ensure that firms give fair consideration to Singaporeans in their hiring practices; apart from job advertisement requirements for Singaporean professionals, managers and executives (PME), the MOM will also increase scrutiny of EP applications for selected firms who have a weaker Singaporean core of PMEs relative to others in their industry.

v Obtaining permanent residence in Singapore

A direct means of obtaining permanent residence in Singapore is through the global investor programme (GIP). The GIP applicant could choose from three options: option A – invest at least S$2.5 million in a new business entity or expansion of an existing business operation or; option B – invest at least S$2.5 million in one or more GIP-approved fund (up to a maximum of three funds); or option FO – invest at least S$2.5 million in a Singapore-based single family office with AUM of at least S$200 million. To qualify for options A or B, the applicant must have a substantial business record and a successful entrepreneurial background whose business turnover is a minimum of S$50 million per annum in the year immediately before the application and an average of S$50 million in the three years immediately before the application. A five-year investment or business plan with milestones to be achieved needs to be submitted for option A. The approved list of sectors in which the applicant can invest is wide ranging (e.g., consumer business, education, precision engineering, professional services, art galleries, family office and financial services). To qualify for option FO, the applicant needs to have at least five years of entrepreneurial, investment or management experience and an individual or direct family net worth of at least S$400 million.

vi Anti-money laundering and counter-terrorism financing

Money laundering is the process of converting income that was obtained by criminal or illegitimate means to give the appearance of having come from a legal or legitimate source. Terrorism financing refers to the process of hiding funds to sponsor or facilitate terrorist activity. Singapore is a member of the Financial Action Task Force (FATF) – the global standard-setting body to combat money laundering and terrorist financing. As a member country, Singapore has introduced laws to prevent money laundering and terrorist financing.

Financial institutions are required to comply with the notices issued by the Monetary Authority of Singapore (MAS) on anti-money laundering and counter-terrorism financing. In April 2015, the MAS issued revised notices that introduced key changes that are benchmarked against international best practices and the latest recommendations from FATF. The key changes are:\(^{15}\)

- requiring more comprehensive money laundering and terrorism financing risk assessment;
- elaborating on steps to identify and verify beneficial ownership of companies, limited liability partnerships and trusts;
- introducing a new category of politically exposed persons (PEPs); and
- additional requirements for cross-border wire transfers exceeding S$1,500.

As a Member State of the United Nations (UN), Singapore is also committed to implementing the UN Security Council Resolutions (UNSCRs). Among other measures,

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the UNSCRs may impose targeted financial sanctions against specific individuals and entities identified by the UN Security Council (or relevant UN Committees) as contributing to a particular threat to, or breach of, international peace and security. For instance, there are UNSCRs issued to address risks of proliferation of weapons of mass destruction emanating from Iran and the Democratic People’s Republic of Korea. Broadly, MAS regulations require financial institutions to:

- immediately freeze funds, other financial assets or economic resources of designated individuals and entities;
- not enter into financial transactions or provide financial assistance or services in relation to:
  - designated individuals, entities or items; or
  - proliferation and nuclear, or other sanctioned activities; and
- inform MAS of any fact or information relating to the funds, other financial assets or economic resources owned or controlled, directly or indirectly, by a designated individual or entity.\(^\text{16}\)

vii Exchange of information and the Common Reporting Standard

Exchange of information upon request already exists bilaterally between Singapore and its tax treaty partners’ competent authority.

In addition, Singapore has committed to implementing the OECD Standard for Automatic Exchange of Financial Account Information in Tax Matters, also known as the Common Reporting Standard (CRS) by 2018. The main difference between exchange of information under the tax treaties and the CRS is that the implementation of the latter will introduce automatic, unsolicited, yearly exchange of information between Singapore and the countries with whom it will enter into international tax compliance agreements.

In July 2016, regulations were proposed by the Ministry of Finance, the Inland Revenue Authority of Singapore and the Monetary Authority of Singapore to implement the CRS with effect from 1 January 2017. As at the time of writing, public consultation and feedback is being sought on the proposed regulations, with the expectation that the regulations will be enacted soon.

V CONCLUSIONS & OUTLOOK

Singapore intends to remain competitive and attuned to global trends and challenges with continued investment into long-term infrastructure plans, including the development of Changi Airport T5, which is expected to grow passenger handling to 140 million per year,\(^\text{17}\) and the Singapore–Kuala Lumpur High Speed Rail Project, which aims to cut travelling time between the two cities to a mere 90 minutes.\(^\text{18}\) Although Singapore’s private wealth management industry will face additional regulatory compliance with the implementation of CRS, with the ease of doing business in Singapore and incentives granted to the financial sector, Singapore’s private wealth management industry is expected to continue to grow.

\(^{17}\) See: www.straitstimes.com/singapore/changi-airports-t5-will-be-10-times-as-big-as-vivocity.
I INTRODUCTION

The Spanish tax network follows the same standard principles as the main jurisdictions of continental Europe. Marginal tax rates on income are high, but capital gains taxation is more moderate. There is also a wealth tax for passive savings beyond a certain figure. Finally, in some regions there is an aggressive inheritance and gift tax policy.

Investors from all over the world invest in Spain, and cross-border taxation is designed following standard European terms. Spain has signed 98 double tax relief treaties that follow the OECD model, and older treaties are being renewed. A new tax treaty with the US is still pending full ratification, as at the time of writing. There are also three inheritance tax treaties in force in Spain.

Spain is not an attractive jurisdiction for wealth from a tax perspective. Having said that, there are significant differences in taxation in the different regions of the country. Therefore, the city of residence within Spain will also be an important factor in determining the total tax burden. There are still a lot of safe tax planning structures that can mitigate or protect wealth from this formally aggressive environment. There are important tax-saving advantages for business-oriented wealth, and there are some basic tax planning ideas that can reduce the tax burden for passive wealth.

Trusts and other similar fiduciary agreements are not accepted \textit{inter vivos} in Spain. Spanish law applies forced heirship restrictions only to Spanish nationals. However, with the new EU ruling for the harmonisation of inheritance law within Europe, the country of residence prevails if there is no will that sets nationality as a preference.

Overall it can be said that the Spanish tax environment for wealth is formally aggressive and complex, following conventional standards, but there is scope for legitimate planning.

The Spanish tax administration is highly dependent on computer systems and the internet, and companies now only deal with tax compliance via the internet.\footnote{The gateway for tax information, compliance and other tax services is www.agenciatributaria.es.}

In the past years, and owing to the government effort to comply with EU deficit limitations, the administration has frequently changed some of the relevant tax laws to improve collection. Nevertheless, the general tax framework has not changed.

A new, important tax reform was introduced on 1 January 2015. The reform reduced the nominal tax rates for individuals (both the standard rate and the capital gains and savings income tax rate), introduced several tax advantages for lower-end taxpayers, and included a variety of benefit limitations and anti-avoidance measures.

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1 Pablo Alarcón is the founding partner of Alarcón Espinosa Abogados.
2 The gateway for tax information, compliance and other tax services is www.agenciatributaria.es.
Among the new measures that may have an impact on individual wealth tax planning are the following:

- a new exit tax for individuals with significant holding interests in companies or qualified funds (UCITS) in Spain that leave the jurisdiction to become tax-resident elsewhere;
- a more restrictive definition of the controlled foreign corporation (CFC) rules, which will make it more difficult and tax-expensive to hold and control foreign companies that conduct no trade and have no substance, even within the EU;
- old coefficients that reduced the tax on part of the nominal capital gains because of inflation have been removed so there are no longer inflation correction coefficients for gains;
- the tax reduction for irregular income has been lowered from 40 to 30 per cent;
- redundancy compensation paid to employees (above a minimum level of €180,000) is taxed. Prior to mid-2015, such payments were tax-exempt up to the legal maximum; and
- non-resident standard tax rates have been reduced for EU residents from 24 to 19 per cent.

Some further changes are commented upon below. Important changes that were due to be made to inheritance and gift tax and wealth tax have been postponed but will likely come sooner rather than later.

II TAX

i Personal taxation

Spain's official tax year runs from 1 January to 31 December. An individual will be tax-resident in the country for full year periods. Income tax returns must be filed by 30 June in the year following the tax year.

Under income tax law, individuals are tax-resident in Spain if they have lived in Spain for more than 183 days in any calendar year; and most of their income or wealth, or both, is generated from Spanish sources (this is presumed to be the case if their spouses or descendants are habitually resident in Spain).

Spanish tax residents are liable to Spanish taxation on a worldwide basis. There is no concept of domicile in Spanish tax law, and Spanish nationality has no tax relevance.

Personal taxation for tax residents

Personal income tax forms the backbone of Spain's tax system, and it mainly falls on salary income. A standard withholding tax procedure collects taxes from payroll and other sources of income.

After several years with marginal rates beyond 50 per cent, marginal rates for 2016 and onwards have now been set at 45 per cent. However, the different regions are able to reduce or increase the rate via tax credits.

Capital gains and savings income are taxed at a marginal rate of 23 per cent since 2016. Capital gains can be compensated against losses, and the latter can be carried forward for four years. In the case of real estate, the gain in the sale of one's residence is tax-exempt if the proceeds are reinvested in another property to be used as the primary residence. Individuals over 65 years old selling their residence will not pay capital gains tax so do not need to reinvest proceeds.
A special tax on gains from lotteries applies at a rate of 20 per cent. There is no capital gain tax burden on inheritance. Beneficiaries of an estate will receive the assets up to market value, and will only pay inheritance tax.

High-ranking executives and other professionals can reduce a small part of their tax burden with certain limited payments in kind, and in some circumstances can also reduce up to 30 per cent of the tax on deferred bonuses that has been vested for more than two years. However, these benefits are all capped and will never imply a significant tax saving.

For passive wealth, the basic strategy is the deferral of taxes. Investment in UCITS has a favourable tax treatment since the sale and reinvestment of proceeds from one fund to another will not trigger tax and the capital gain is deferred until the funds are withdrawn or invested in other assets. This tax deferral requires a Spanish trading entity to deal with this reinvestment process and to report to the tax authorities.

Wealthy families can also hold their own investment companies (SICAVs) following the UCITS model, and can reinvest proceeds within the entity with only a 1 per cent tax on profits or gains realised. Other financial products, such as savings insurance policies or life annuities, can be structured in tax-efficient ways. The SICAV regime may be changed soon to limit the abuse of these collective investment vehicles by individual and family investors.

Spanish tax residents must declare and pay wealth tax, which is levied on the value of worldwide net wealth exceeding €300,000 for a personal home and possessions and €750,000 on other assets. Madrid is the only region not subject to this tax. The marginal rate, depending on the region, will be between 2.5 and 2.7 per cent above €10.7 million.

This can be a significant yearly burden for wealthy taxpayers. However, private wealth that is included in a family company is not subject to wealth tax; thus, most family businesses are structured in a way so that investments fall under the same umbrella as the active business. For passive wealth, there is a general limitation of combined tax (income tax plus wealth tax) that cannot exceed 60 per cent of total income (excluding capital gains) for the year. The best strategy is, therefore, not to live on income but on the returns of investment capital. Following this strategy, wealth tax can be reduced to a minimum rate of 20 per cent of the standard tax bill.

As a result of this and other tax-saving strategies, wealth tax does not collect much money, and only professionals and top executives are being hit by this levy, which was created in 1977 in a totally different economic environment. It has an obsolete framework, tax rates are very high compared with market interest rates in the past years and it is highly criticised by most technical commentators.

**Personal taxation for non-tax residents**

Non-tax residents are only taxed on Spanish-sourced income. The standard rate is 24 per cent (for EU residents the rate is 19 per cent), and the rate for interests, dividends and capital gains, provided that no treaty is applicable, is 21 per cent (for EU residents the rate is 19 per cent).

In most circumstances, taxation of non-resident individuals in Spain is ruled by one of the tax treaties that Spain has signed, which mostly follow the OECD model.

An interesting tax regime is available for non-resident individuals coming to Spain. According to this regime, such individuals are taxed as if they were non-resident on their Spanish-sourced income and foreign labour income as well as non-resident rates of tax. The relevant individuals should have labour agreements in place that are applicable in Spain. Individuals benefiting from this regime are still deemed to be tax-resident in Spain. The
regime applies for a maximum of €600,000 per year and for five years plus the remainder of
the year in which the individual arrived in Spain. This special regime is no longer available
for incoming sportspeople and performers.

A new exit tax that has been introduced in Spain follows principles similar to those
found in the French and German exit tax regimes. It has been adapted to the requirements
set by the European Court of Justice not to create conflict with the principle of freedom of
movement of persons within the EU.

There are pre-immigration tax planning ideas that could reduce or even eliminate the
yearly tax burden of incoming individuals living on passive income.

Non-residents are also subject to Spanish wealth tax on their personal assets that are
located in Spain or that can be exercised in Spain. For instance, if they own a property in a
region that levies wealth tax, they will pay such tax provided that the value of the property
exceeds the minimum exemption threshold of €750,000.

There is no wealth tax for corporations, so an easy way to circumvent this issue in the
case of large property investments is to carry out such transaction through a foreign company.

ii  Gift and succession taxes

In Spain, gift and inheritance tax is on beneficiaries and not on the gift or estate level.

Spanish tax residents (based on the same principles as above) will be liable on all gifts
or benefits received from inheritance, regardless of the location of the assets or the residence
of the deceased. Non-tax-resident individuals will only be liable to Spanish inheritance and
gift taxation for Spanish-situated assets.

There are no general tax-free allowances. Special and limited allowances are applied to
the mortis causa transfer of the home or the mortis causa transfer of wealth to minors.

There are very important differences regarding the effective taxation of gifts and
inheritance for first-degree transfers of wealth, meaning spouse, parents and grandparents to
siblings and grandchildren, and vice versa.

In regions such as Catalonia, La Rioja, Madrid, Navarra or the Basque region, there is
a very significant tax reduction on first-degree transfers of wealth, both inter vivos or mortis
causa. This tax advantage is also applicable to beneficiaries resident within the European
Union.

The tax saving of this benefit can be substantial, since the marginal tax rate goes up to
34 per cent for transfers above €680,000.

In certain circumstances, transfers of family business within the family in any region
can benefit from a 95 per cent tax reduction, because the family is not obliged to sell or
mortgage the business to be able to pay a tax bill. The beneficiary must continue the business
(or retain the shares) for at least 10 more years (five years in some regions).

For transfers to nephews, nieces or cousins, the rate can jump to 50 per cent, and for
third parties it can go to up to 68 per cent. As such, in the case of inheritance falling outside
the immediate family, it is paramount to study other alternatives that could reduce the tax
bill.

Each beneficiary is liable for inheritance or gift tax on the value of the share of the estate
received according to his or her personal circumstances.

For tax purposes, there is no significant difference between gifting assets during one’s
lifetime or by will; both are taxed on the same principles. However, it should be remembered
that a gift in kind (for instance, a property) will also trigger capital gains taxation on the donor, while for *mortis causa* there is no capital gain taxation, although the assets are received by beneficiaries with a step-up to market value.

There is a municipal capital gains tax on the transfer of real property located in Spain, which is also payable on death and on lifetime gifts. This municipal capital gains tax is based on the cadastral value of the land and the length of time that the property was held by the transferor. This tax is deducted from the tax basis of inheritance and gift tax.

Finally, it should be noted that trusts are an alien concept to the Spanish legal system. Spain has not even signed the Hague Convention for the Recognition of Trust Consequences. The tax authorities have adopted a very negative stance on trusts, with the exception of plain trust wills.

The most common approach taken by the Spanish tax authority is to ignore the trust and deem the assets to be still in the hands of the grantor or settlor, even in the case of irrevocable trusts. Plain trust wills that are wound up together with the distribution of the estate are deemed normal wills.

In any other situation, the Spanish tax consequences are unpredictable; therefore, it is of paramount importance to review the case if there are Spanish assets involved or if Spanish tax residents are beneficiaries to a foreign trust.

The complex and uncoordinated inheritance tax framework that exists throughout Spain is under review, as at the time of writing. It is likely that a minimum coordinated tax rate will be set for all regions, and that each region will set its own rules regarding this, although never allowing the total tax burden to fall below the minimum coordinated rate.

### iii Issues relating to cross-border structuring

In terms of cross-border structuring, two situations merit some thought. First, pre-immigration planning is necessary for wealthy non-Spanish tax residents coming to Spain. Considering the personal situation of such person and the nature of his or her wealth, several pre-immigration steps could be taken to create a safe tax structure under which he or she would be able to live in Spain with a limited tax burden. As previously mentioned, the key is living on returns of capital instead of income.

Second, investors in Spain, and especially in real estate property, can be misled by offers of cheap offshore structures that are no longer viable. If the property is worth enough, there are legitimate ways to mitigate future capital gains tax on the sale of the property and legally avoid Spanish inheritance tax risk, such as holding the property through a double corporate structure with the main holding company being a non-Spanish resident company.

### iv Regulatory issues relevant to high net worth individuals

Most of the highest net worth individuals or families are the first or the second generation of a family business, and most high net worth individuals have their own close personal advisers. These are very often tax experts, and at the higher end they often have a family office to deal with investment issues outside of the family company. Private banks and special units of retail banks also often manage most of the investments of high net worth individuals and families.

As previously mentioned, an important part of the financial investments of wealthy families is wrapped up in SICAVs, which are collective investment vehicles in listed securities that only pay 1 per cent tax on net income. The use of SICAVs by such wealthy families will probably be limited in the near future.
Independent financial advisers are also a reality in the Spanish market, but are not as widespread as they are in other countries because of the regulatory requirements and compliance burdens involved in obtaining and retaining a licence.

It must be highlighted also that the tax authorities are intensifying tax inspections of high net wealth individuals and families (including top sportspersons and entertainers) and are challenging the aggressive tax planning strategies that some of them have in place.

v Issues affecting entrepreneurs

In Spain, as in most of Europe, wealth that is invested in a family business will generally be protected; it will not be subject to wealth tax, and profits will not be taxed unless they are distributed.

A simple holding company would avoid double taxation of profits within the group, and profits can be reinvested without further taxation until they are paid out to individual investors.

III SUCCESSION

In Spain, forced heirship regulations apply only to Spanish nationals. However, with the new EU ruling for the harmonisation of inheritance law within Europe, the country of residence prevails if there is no will that sets nationality as a preference. Hence it can be paramount for a foreign permanent resident to formalise such will since otherwise he or she could be caught by forced heirship provisions of Spanish inheritance law.

Under the forced heirship regime, two-thirds of a person’s total assets must be distributed between the forced heirs (direct descendants, direct ascendants (if there are no descendants), spouse).\(^3\) Out of this two-thirds with restrictions, one-third of the estate must be distributed equally among the forced heirs, and the remaining third can be used to improve the conditions of any of them. The spouse has the right to receive a life interest (usufruct) in the assets comprising the compulsory one-third share received by the descendants under the forced heirship regime.

One-third of a person’s estate can be freely distributed by will.

There are some regions where the forced heirship regime does not apply or is modified, such as Navarra (where there is no forced heirship regime), the Basque region and Catalonia (where there are specific rules than can partly override the forced heirship regime). If the deceased is a Spanish national from outside the above-mentioned regions, the forced heirship regime cannot be avoided. The general rule is that the forced heirship regime applies to all distributed assets, regardless of the beneficiary’s residence.

The forced heirs can waive the right to receive their share, or propose a different distribution of the assets subject to the other forced heirs’ rights under the regime.

For Spanish nationals, matrimonial law will be the law of the first residence of the couple. Non-Spanish nationals will be ruled by the law of nationality and, if this is not definitive, the law of the residence of the couple.

The economic terms of nuptial and prenuptial agreements for the administration of the family are generally accepted by the Spanish courts if they follow the principles of the law of the jurisdiction in which the couple lives.

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\(^3\) Each category precludes those subsequent from receiving a share of the deceased’s estate.
IV WEALTH STRUCTURING & REGULATION

As previously mentioned, trusts are not recognised in Spain, and their effects cannot be imported into Spain.

From a tax perspective, if a trust is operating with Spanish assets, the tax authorities will probably ignore the trust and allocate the assets to the grantor or settlor even in the case of irrevocable trusts. However, there are no clear and uniform criteria from the tax authorities in this regard; therefore, trusts should not be used for tax structuring purposes in Spain.

Regarding family law, claims against trust assets by the spouse or civil partner of a settlor or beneficiary on the dissolution of a marriage or partnership must be filed in another jurisdiction, as Spain does not recognise trusts.

Private foundations are also not possible in Spain. All foundations should have an object of public benefit and should be supervised by the relevant public authority. Foundations are the typical legal form of charities in Spain.

Foreign private foundations are also ignored by the tax authorities except when they are the substitute for a will, in which case they could be treated as such.

Partnerships are recognised and treated as tax-transparent vehicles. They are frequently used for handling shared property and for international business ventures. Family partnerships are also common in family businesses with multi-jurisdictional partners.

However, the most common vehicle for all business purposes in Spain, including family businesses, is the limited liability company (SL). The limited liability company follows the general principles of companies with shares in which voting rights are linked to shareholding percentage. They can be used directly as business entities or as holding entities owning the shares of a group of companies.

A holding company acting as head of a group of subsidiaries is also common practice. This structure permits an easier formation of voting majorities for the whole group, and at the same time helps reinvestment of profits all over the group through the holding company and thus defer taxation of such profits at the level of the shareholders.

If the business group also holds interests in foreign companies, it can also be established as a foreign securities holding company (ETVE), which is a special tax status for entities with qualified foreign shareholdings that can provide tax advantages to its shareholders on foreign dividends or foreign portfolio gains.

In Spain, there are strict anti-money laundering provisions following EU directives and international guidelines. All practitioners, bankers, attorneys, notaries and authorised wealth managers are bound by strict compliance regulations, and are thus obliged to keep records of clients’ identities and activities, including the source of their wealth.

There is also an obligation to report to the Bank of Spain any operation that could be suspicious of involving money laundering, with the exception of matters protected by lawyer–client privilege when defending a client before the courts.

V CONCLUSIONS & OUTLOOK

For several reasons that are unrelated to tax, Spain has been an attractive country in which to live or to invest in real estate property. Taxes in Spain have been high, following European standards, for the last 20 years, but there has always been scope for legitimate tax planning that has mitigated the Spanish tax burden for well-advised incoming residents or investors.
The extraordinary tax situation that existed in Spain in the past few years – with the high notional tax rates that applied to most taxable income during 2012, 2013 and 2014 – has changed since 2015, when there was a reduction in tax rates (an average reduction of 7 per cent on marginal rates) that has had an impact on most taxpayers.

However, the benefits that have been gained from the reduction in the notional tax rates have to some extent been offset by the introduction of several important reductions in the tax benefits that were available before and with a more aggressive wording of the anti-avoidance provisions, both of which have created a more complex landscape for tax planning in Spain.

Tax collection efforts focus more on both domestic and multinational large corporations that have used and abused the tax law with very aggressive tax-leveraged structures and extreme transfer pricing policies. Corporation tax has recently been subject to a variety of measures to reduce the list of tax-deductible expenses, and there have also been significant reductions in most of the tax credits that have been available to date.

Under a tax amnesty that took place in 2012, individuals holding non-declared assets could disclose these assets subject to a very low tax payment of 10 per cent calculated on the yield or gain obtained on such assets during the past four years. However, non-compliant wealthy individuals living in Spain may have a difficult time in future years. Exchange of information and cooperation agreements for international tax collection (CRS) are now a reality and it is futile to hide wealth abroad or to ignore unpleasant tax laws. Spain has signed a Foreign Account Tax Compliance Act agreement (FATCA) with the US for the automatic exchange of information on tax-resident individuals or US citizens and foreign financial investments.

Tax residents in Spain must disclose all foreign assets to the tax authority every year; failing to do so could give rise to a tax crime that is punishable with up to six years in prison and a penalty beyond the value of the hidden asset.

Overall, Spain follows the trend of the conventional jurisdictions of Europe, where taxes on the generation of wealth are significant but where living on passive income can be subject to efficient tax planning.
Chapter 36

SWITZERLAND

Mark Barmes, Frédéric Neukomm and Heini Rüdisühl\(^1\)

I   INTRODUCTION

Switzerland has long been an attractive destination for wealthy individuals and families. Many reasons can be advanced for this: neutrality and political stability; its status as a safe haven; its central location within Europe; its reputation for high service standards; its role as a key player in the custody and management of private wealth; and its system of taxation and bank secrecy.

Since the turn of the century and the growth of globalisation, Switzerland has been faced with a new world order and accelerating internal and external demands for change. Recurrent incidents of data theft in banks, the well-publicised litigation in the United States involving UBS, the financial crisis and ever-increasing multilateral demands for automatic exchange of information have contributed to produce a breathtaking rate of change.

In this context, the Swiss government has at times seemed overwhelmed. The current uncertainty created by the multiple changes under consideration or being negotiated is probably the predominant reason. However, if one pauses to look at all that has and will be done by 2018, it is notable that the quintessential Swiss characteristics of democracy, negotiation and healthy obstinacy are producing answers to the uncertainties.

In particular, now that the switch to exchange of information in tax matters has been accepted globally, there are encouraging signs that Switzerland remains a destination of choice for wealthy individuals and for the custody of private wealth. Switzerland’s status as a safe haven now holds centre stage. This seems largely due to the significant efforts of the government to assemble the framework, tools and skills to manage private wealth in a transparent digital economy, without losing sight of the individual or respect for the rule of law.

II   TAX

i   The federal tax system

Switzerland is a federal state consisting of 26 cantons. Income tax is levied at the federal, cantonal and municipal levels, while wealth tax and gift and estate tax are levied at the cantonal and municipal levels only. The cantons are competent to assess and collect most direct taxes, including federal income tax.

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1 Mark Barmes, Frédéric Neukomm and Heini Rüdisühl are partners in the private client practice group at Lenz & Staehelin.
The rules for assessment of income and wealth are widely harmonised by federal law. Consequently, the cantons impose cantonal tax using the same basis as for the federal tax, except for certain minor rules (e.g., social deductions). The cantons are competent to set their tax rates, and the municipalities generally set their tax rate by reference to the cantonal tax rate.2

Switzerland is not a low-tax jurisdiction for ordinary taxpayers. Switzerland may, nevertheless, be fiscally attractive for high net worth individuals because it offers low tax rates in certain municipalities, an exemption from capital gains on moveable assets and reduced taxation of dividends.

The other advantages are the well-established ruling practice that allows individuals and businesses alike to discuss in advance the tax treatment of certain transactions or structures and the lump sum tax regime for foreigners who do not engage in any gainful activity.

ii Personal taxation

Income tax

Switzerland taxes Swiss residents on their worldwide income except for income derived from a foreign trade or business or real estate located abroad. Non-residents are taxable if they own businesses or real property in Switzerland, or if they receive employment income from a Swiss employer or director fees from a Swiss company.

Capital gains exemptions

Capital gains on moveable assets such as shares in companies or works of art are not taxed if the gain results from the sale of private assets as opposed to business assets. Business assets are assets that are related to a business located in Switzerland.3

Capital gains on real property located in Switzerland are exempt from federal income tax if the property is part of an individual's non-business or private assets. Such gains are subject to a cantonal and municipal property gains tax. The applicable tax rate varies greatly depending on the canton and on the duration of the holding of the property. Rates generally vary between zero per cent for very long holding periods and 30 per cent, but can be as high as 60 per cent in the case of a short holding period.

2 Tax rates are generally progressive. The maximum federal tax rate is 11.5 per cent, and maximum cantonal and municipal tax rates vary between 7.1 per cent (canton of Schwyz) and 34.3 per cent (canton of Geneva). The overall income tax rate can thus be comprised between 18.6 and 45.8 per cent. Similarly, the maximum wealth tax rates vary between 0.1 per cent (canton of Schwyz) and 1 per cent (canton of Geneva). The tax rates are generally higher in the French-speaking part of Switzerland and in the urban areas (Zurich, Basel, Bern, Lausanne, Geneva).

3 The concept of business has, however, been interpreted extensively by the cantonal tax administrations and the Swiss Supreme Court. They consider an independent business activity may exist where a taxpayer acts in a professional manner, for instance, by systematically trading in securities. This extensive interpretation led to uncertainty, and safe-haven rules have been published by the Swiss Federal Tax Administration.
**Dividend taxation**
Dividends from qualifying participations of at least 10 per cent are more favourably taxed. For federal income tax, a 40 per cent tax relief is granted for participations held as private assets so that only 60 per cent of the dividend income is subject to taxation. The incentives granted at cantonal level vary from canton to canton.4

**Wealth tax**
Cantons and municipalities levy wealth taxes on worldwide net assets,5 except for real estate abroad. The majority of the cantons apply progressive tax rates and maximum rates vary between 0.1 and 1 per cent.6 In the cantons that have high wealth tax rates, wealth tax can have a significant impact on the overall tax burden, and tax structuring or pre-entry tax planning is sometimes advisable.

**Lump sum**
The ‘lump sum’ or ‘flat’ tax system in Switzerland opens the possibility for foreign citizens resident in Switzerland to pay their taxes based on a lump sum, subject to certain minimum criteria.

Foreign citizens who come to live in Switzerland for the first time (or after an absence of 10 years) and who do not engage in any gainful activity in Switzerland may, upon request, be taxed on a lump sum basis for cantonal and communal income, net wealth and federal income tax purposes. A limited professional activity can be carried on outside Switzerland.

Under the lump sum arrangement, tax is levied on the basis of a deemed income based on the annual living expenses incurred in Switzerland and abroad by the taxpayer and his or her family.7

The tax due on the agreed tax base is calculated on the basis of the ordinary income and net wealth tax rates applicable to that agreed tax base.

In any event, the tax due must not be less than the taxes determined in a ‘control calculation’ under which certain specific Swiss-sourced items (e.g., income and wealth from real estate situated in Switzerland or securities issued by companies domiciled in Switzerland) are aggregated. The ultimate tax payable is the higher amount determined by the control calculation and the agreed flat tax. The lump sum tax system applies only to income and net wealth tax, not to inheritance taxes.

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4 Most cantons apply a relief similar or comparable to the federal tax relief, but certain cantons apply a reduced tax rate on the dividend income with a reduction that can be as high as 75 per cent (canton of Schwyz) and result in a tax rate on the dividend income of 8.8 per cent (canton of Schwyz).

5 Market value of the assets minus debt.

6 Certain cantons allow further deductions. Recently, certain cantons have also introduced a ‘wealth tax shield’ to reduce the wealth tax payable by individuals who have a proportionally low taxable income.

7 At present, such annual expenditure figure may not be less than seven times the annual rent paid for the main accommodation occupied by the taxpayer and his or her family, or, if the taxpayer owns his or her own accommodation, seven times the deemed rental value of that property.

In practice, the actual tax basis is determined by an advance ruling from the tax administration of the canton in which the individual wishes to take up residence. In the majority of cantons there is a practical minimum tax base (threshold) or an amount of tax, even if the expenses as determined above are less than this amount.
The lump sum tax system has been subject to political discussion in the past, and the canton of Zurich and four other cantons abolished the lump sum tax system for cantonal and municipal taxes, while other cantons tightened their conditions. Under the new federal legislation, the minimum amount of taxable income is calculated by multiplying the rental value of the real estate owned by the taxpayer (respectively the rent paid) by seven, with a minimum tax base for federal tax of 400,000 Swiss francs. An initiative from left-wing parties calling for the abolition of the system was rejected by 69 per cent of the Swiss voters in 2014. Following this vote, political discussions came to an end and the system is not challenged any more.

**Withholding tax**

Switzerland applies a withholding tax of 35 per cent on dividends, interest from bonds issued by Swiss residents and interest paid by Swiss banks. This tax is fully refunded to residents who declare their income in their tax return, and can also be partially or totally refunded to foreign residents subject to international tax treaties. Because of this withholding tax, tax planning is often needed for foreign-resident individuals who wish to incorporate holding structures in Switzerland.

**iii Gift and estate tax**

At the federal level, there is no gift and estate tax, but at the cantonal level, gift and estate tax is levied by most cantons, with the exception of the canton of Schwyz. Tax jurisdiction normally lies with the canton of the last domicile of the deceased, respectively the donor. Where the deceased has his or her final domicile in Switzerland, the entire worldwide estate, with the exception of foreign real property and assets belonging to a foreign permanent establishment, is subject to Swiss estate tax. Swiss real property and Swiss businesses that are the subject matter of a gift or a bequest can give rise to Swiss gift and estate tax even if the donor or the deceased was not Swiss domiciled.

The scope of the gift and estate tax varies greatly among cantons. The surviving spouse is exempt from estate and gift taxes in all cantons. All cantons, except Vaud, Neuchâtel and Lucerne, exempt gifts and bequests between parents and direct descendants. The tax rates on gifts and bequests, which are generally progressive, vary greatly depending on the relationship between the parties and the canton. The tax rate may be as high as 55 per cent in the event of a gift or bequest to an unrelated person.

An initiative by left-wing parties calling for the introduction of a 20 per cent federal gift and estate tax on estates and gifts worth more than 2 million Swiss francs was rejected by 70 per cent of the Swiss voters on 14 June 2015.

**iv Exchange of information, withholding tax on banking assets and FATCA**

Until March 2009, Switzerland’s treaty network did not provide for exchange of information to internationally agreed standards, as information exchange was generally limited to exchange for the purposes of the application of the treaty. In some treaties with OECD and EU Member States, Switzerland also provided for exchange of information in cases of tax fraud and acts of similar gravity. Subsequent requests for administrative assistance from the US Internal Revenue Service (IRS) directed against clients of UBS and Credit Suisse were based on a provision of this nature. These requests from the IRS led to several court cases and the Federal Tribunal ultimately confirmed that group requests are permitted under the 1996 treaty with the United States provided that the facts were described in sufficient...
detail so as to provide grounds for suspicion of tax fraud and enable the identification of the taxpayers involved. This decision had a considerable impact, and banks participating in the US programme aiming at regularising the past have been entering into settlements and delivering certain information to the IRS.

On 13 March 2009, the international standard on information exchange for tax purposes was adopted by Switzerland, and the country has moved rapidly to update its bilateral treaties.\(^8\)

On 14 June 2013, the Federal Council declared that it would contribute actively to the development of a global standard for the automatic exchange of information, commonly known as the Common Reporting Standard (CRS), within the framework of the OECD. The requirements to be contained in the standard were that there should be one global standard applicable to all financial centres, that the exchanged information should be used solely for the agreed purpose, that it should be exchanged reciprocally and that the beneficial owners of structures should be identified. On 21 May 2014, the Federal Council adopted draft negotiation mandates for introducing the new standard to be issued by the OECD with partner states and to incorporate, where appropriate, issues of regularisation of the past and market access for Swiss financial institutions.

On 27 May 2015, Switzerland and the EU signed an agreement regarding the introduction of the CRS.

On 17 September 2015, the Federal Council submitted the agreement, together with a dispatch, to Parliament for approval. It has been approved on 17 June 2016 by the Federal Assembly. Since then, the European Savings Tax, as it used to be applied in Switzerland, was abolished.

Parallel to this, work continued on introducing the legal basis and statutory framework (law, ordinance and directive) to implement the CRS in Swiss law.

Switzerland and foreign partner states and territories will exchange information automatically based on the Multilateral Competent Authority Agreement on the Automatic Exchange of Financial Account Information (MCAA). The MCAA in turn is based on the OECD/Council of Europe Convention on Mutual Administrative Assistance in Tax Matters (administrative assistance convention). Both the administrative assistance convention and the MCAA were adopted by Parliament in December 2015 together with the Federal Act on the International Automatic Exchange of Information on Tax Matters (AEIA). The referendum deadline expired on 9 April 2016 without a referendum being called, which signifies that the CRS will enter into force between Switzerland and those countries with which Switzerland has concluded a bilateral agreement in time on 1 January 2017 (first collection of account data). First exchange of data will be in calendar year 2018.

At the time of writing, it is expected that the framework for the automatic exchange of financial account information will be in place for the 27 EU Member States and Iceland, Norway, Guernsey, Jersey, the Isle of Man, Japan, Canada and the Republic of Korea.

Following the enactment of the Foreign Account Tax Compliance Act (FATCA), Switzerland decided to implement Model 2, which means that Swiss financial institutions will disclose account details directly to the IRS with the consent of the US clients. The agreement between the United States of America and Switzerland for Cooperation to Facilitate the Implementation of FATCA was signed on 14 February 2013, and Swiss implementing legislation entered into force on 30 June 2014. Therefore, it was somewhat surprising that,

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\(^8\) As of 1 July 2017, there were 52 treaties with the international standard in force.
on 21 May 2014, the Federal Council announced its proposal for a further draft mandate for negotiations with the US to switch to Model 1 and automatic exchange of information. This mandate was adopted by the Federal Council on 8 October 2014. It is our understanding that the negotiations are ongoing and that the date when the new agreement with the US will be signed is not determined yet. In the meantime, the first reporting deadlines for the 2014, 2015 and 2016 tax years have passed. The implementation seems to have been very smooth for such a complicated exercise.

The competent authorities of Switzerland and the United States signed an agreement on 19 February 2016 in Bern and on 29 February 2016 in Washington. This agreement contains an exception clause for accounts held by lawyers or notaries and was included in the FATCA Agreement. As a result of this exception, the clients of lawyers or notaries will no longer have to be identified, and therefore, the professional confidentiality of lawyers and notaries will be maintained under Swiss law.

### III SUCCESSION

The Swiss inheritance law system is based upon the idea that the community of heirs (community) steps into the deceased’s shoes immediately upon his or her death.\(^9\) The assets and liabilities of the deceased vest automatically in the community, the heirs becoming joint owners of the deceased’s estate and joint debtors of the deceased’s debts. The appointment of a testamentary executor (through testamentary provision) or of an official administrator (through a court decision) is possible, but such person will not be considered to be the owner of the assets of the estate, but merely as limiting the heirs’ possession of such assets until partition.

Even though Switzerland recognises testamentary freedom to a certain extent, Swiss successions are based upon a system of statutory devolution of the estate (in the absence of a will) allowing the testator to modify such system to a certain extent by will, but also limiting testamentary freedom by protecting some of the statutory heirs with forced heirship rights. The primary heirs are the descendants,\(^10\) together with the surviving spouse or registered partner.\(^11\) In the presence of descendants, the surviving spouse or registered partner is entitled to 50 per cent of the estate (the descendants having to share the other 50 per cent per capita). In the absence of descendants, the parents (or their descendants)\(^12\) will be heirs (if there is a surviving spouse or registered partner, the latter will be entitled to 75 per cent of the estate).\(^13\)

Some of the statutory heirs are protected by forced heirship rights. Descendants are entitled to a compulsory share of 75 per cent of their intestate entitlement;\(^14\) a surviving spouse or registered partner and parents are protected up to 50 per cent of their intestate share;\(^15\)

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9 Article 560 of the Swiss Civil Code (SCC); ‘le mort saisit le vivant’.
10 Article 457(1) of the SCC.
11 Article 462(1) of the SCC.
12 Article 458 of the SCC.
13 Article 462(2) of the SCC.
14 Article 471(1) of the SCC.
15 Article 471(2–3) of the SCC.
other statutory heirs are not protected. The portion of the estate that is not encompassed by the compulsory shares can be freely disposed of by the testator and is usually called the freely disposable share.\textsuperscript{16}

Forced heirship rights may also protect the heirs against \textit{inter vivos} acts, in particular revocable transfers and transfers made within five years of the time of death, as well as transfers made with the object of depriving the heirs of their protected rights.\textsuperscript{17}

The heirs may leave the infringing testamentary provision or \textit{inter vivos} transfer unchallenged. The protection merely entitles them to claim their rights (either by asserting a claim against the will or against the holder of the assets within a certain time limit and provided that certain conditions are met) or to oppose the delivery of assets held by the community to the person benefiting from a testamentary provision.\textsuperscript{18}

By testamentary provision, the testator may designate given persons as heirs,\textsuperscript{19} entitle others to legacies,\textsuperscript{20} appoint an executor,\textsuperscript{21} set up a foundation,\textsuperscript{22} or request an heir or a legatee to do something.\textsuperscript{23} The question of whether a testamentary trust could validly be set up within the framework of a succession governed by Swiss inheritance law is disputed, even if the current trend seems to be favouring such a possibility.\textsuperscript{24}

Besides the unilateral will, which has (under Swiss domestic law) to be written entirely by hand or executed in front of a notary public (and, to a very limited extent, can be made orally),\textsuperscript{25} Swiss inheritance law also recognises the possibility of entering into inheritance agreements (to be executed before a notary public). By such an agreement, it is possible for a testator to obtain, for example, the consent of a protected heir to a waiver of his or her full compulsory share (either gratuitously or in exchange for some compensation).

Swiss inheritance law has been largely unchanged since the entry into force, in 1912, of the SCC; however, with the entry into force, in 2007, of the Federal Act on Registered Partnership, the registered partner has been granted the same rights in inheritance law matters as the surviving spouse.\textsuperscript{26} Further, Article 492a of the SCC, introduced in 2013, allows a testator to determine the destination of any assets remaining out of the share of a durably incapacitated heir of the testator without risk of infringing the incapacitated heir’s compulsory share.

Finally, the Swiss government has drafted a reform to modernise the existing inheritance law in a comprehensive way. The reform could enter into force in 2019 or later. At the heart of

\begin{enumerate}
\item Article 470 of the SCC. In the presence of a surviving spouse or registered partner and of descendants, the compulsory share of the surviving spouse or registered partner will amount to 25 per cent of the estate (50 per cent of 50 per cent) and the compulsory share of the descendants will globally amount to 37.5 per cent of the estate (50 per cent of 75 per cent); the freely disposable share will in such cases amount to 37.5 per cent of the estate.
\item Article 522 et seq. of the SCC.
\item Article 533 of the SCC.
\item Article 483 of the SCC.
\item Article 484 of the SCC.
\item Article 517 of the SCC.
\item Article 493 of the SCC.
\item Article 482 of the SCC.
\item Article 498 et seq. of the SCC.
\item Articles 462 and 471 of the SCC.
\end{enumerate}
the reform are the forced heirship rights rules, with the primary objective to limit their scope and increase the testator’s freedom. The reform should essentially reduce the compulsory share of the descendants (entitled to a compulsory share of 50 per cent of their intestate entitlement under the draft reform), of the surviving spouse or registered partner (protected up to 25 per cent of their intestate share according to the draft reform) and of the parents (their compulsory share is abolished under the draft reform). The reform also aims at easing the transfer of businesses, and promoting donations to charitable institutions. The draft reform bill also provides protection to unmarried couples by allowing forced maintenance claims by domestic partners, provided they have lived at least three years in a relationship with the deceased and made a significant contribution. The surviving partner must further need the maintenance award in order to ensure his or her existence and the amount awarded must be reasonable to expect from the heirs in view of their financial situation. This maintenance award is also granted to people who have lived as a minor for at least five years in a household with the deceased, if the deceased provided financial support to him or her and would have continued to do so if he or she were still alive.

Even though not directly classed as inheritance law, it is important to mention that a revision of the rules on adult protection entered into force in 2013.27

The Swiss conflict of laws rules seek to ensure, as far as possible, the principle of unity of succession. With this objective in mind, the foremost connecting factor in inheritance matters is the place where the deceased had his or her final domicile.28

The Swiss courts generally have jurisdiction and apply Swiss law to the whole estate of a person whose final domicile was in Switzerland.29 Some exceptions exist, in particular, in relation to real estate located in countries claiming to have exclusive jurisdiction over immoveable assets;30 the devolution of the estate of Swiss nationals domiciled outside Switzerland who make the appropriate election;31 or assets located in Switzerland, where no foreign authority deals with them.32

Further, Swiss conflict of laws rules enable foreigners (who do not have Swiss nationality at the date of death) with final domicile in Switzerland to submit the devolution of their estate to their national law.33 This avoids the application of Swiss law, notably possible limitations on the creation of testamentary trusts and forced heirship rights.

27 The revision introduced new planning tools in relation to incapacitated persons. In particular, Articles 360 to 369 of the SCC now provide for the ‘advance care directive’ (mandat pour cause d’inaptitude), enabling a person with capacity to instruct a natural person or legal entity to take responsibility for his or her personal care or the management of his or her assets, or to act as his or her legal agent in the event that he or she is no longer capable of judgement. Articles 370 to 373 of the SCC foresee the possibility for a person with capacity to specify in a patient decree which medical procedures he or she agrees or does not agree to in the event that he or she is no longer capable of judgement.
28 Within the Swiss meaning (see Article 20 of the Swiss Private International Law Act (SPILA) for a definition of domicile: ‘the place where a person resides with the intention of settling’), which is closer to the English notion of permanent residence than to the English notion of domicile.
29 Articles 86(1) and 90(1) of SPILA.
30 Article 86(2) of SPILA.
31 Article 87(2) of SPILA.
32 Articles 87(1) and 88 of SPILA.
33 Article 90(2) of SPILA.
As regards persons with their final domicile outside Switzerland, Swiss law looks to the law designated by the rules of conflicts of the deceased’s final domicile. In the overall context of conflict of laws rules, one should note that the new European Succession Regulation, which governs and harmonises all conflict of laws aspects of cross-border successions in the Member States of the EU as from 17 August 2015, has a significant impact on estate planning and settlement processes for Swiss resident individuals or Swiss nationals who have their last habitual residence in the EU, have left assets in the EU, or have elected the law of a Member State of the EU to govern their succession. The Regulation essentially establishes the principles that one single court has jurisdiction to rule on the succession as a whole and that the law of the state where the deceased had his or her last habitual residence also governs the whole of his or her succession. It contains further significant innovations, such as the possibility to elect the law of the state of which a person is a national to govern the succession (professio iuris) and a provision favouring the recognition of inheritance agreements. Switzerland is obviously not bound by the Regulation. Yet, considering its close relations with the EU, one may reasonably expect that these new rules should impact cross-border succession planning involving EU Member States bound by the Regulation.

In the event that the deceased was married or bound by a registered partnership, the patrimonial relations between the spouses or registered partners first have to be liquidated to establish what is part of the deceased’s estate.

In this regard, even if marriage or registered partnerships generally have very limited effects on the powers of each spouse or registered partner to dispose of his or her assets during the marriage, some rules governing liquidation will need to be taken into account at the end of the marriage or registered partnership.

If the spouses have not entered into any matrimonial agreement, the ordinary Swiss property regime of participation in acquired property (ordinary regime) applies. In this case, each spouse will be entitled to a monetary claim against the other, amounting to half the net value of the assets acquired for consideration during the marriage (in particular, earnings from work and business assets, but not including assets owned prior to marriage or received through gift or inheritance thereafter).

By matrimonial agreement, spouses can adopt one of two other property regimes (the segregation of assets regime and the community property regime), or modify (to a limited extent) the ordinary regime. Rules are very similar as regards registered partners, except that the default regime is the segregation of assets regime.

In the event that the ordinary regime applies (which is the case for the vast majority of married couples in Switzerland), spouses remain to a very large extent free to deal with their assets as they wish. This being said, to avoid a situation where one spouse could deprive the other of his or her expectancies to half the net value of the assets acquired for consideration during the marriage, Swiss law contains protective provisions allowing – provided certain conditions are met – the taking into account of assets given away by a spouse without

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34 Article 91(1) of SPIA.
35 Swiss law admits renvoi both in the form of remission and of transmission.
37 With the notable exception of the United Kingdom, Ireland and Denmark.
38 Articles 181 and 196 et seq. of the SCC.
39 Article 18 et seq. of the Federal Act on Registered Partnership.
40 Article 201(1) of the SCC.
consideration in the calculation of the other spouse’s entitlements at the time the regime is liquidated.\textsuperscript{41} If the assets at that time are not sufficient to cover the spouse’s claim, it might even be possible in certain cases for the assigned spouse to claim assets from the person having received or benefited from the assets.\textsuperscript{42} According to a recent Federal Tribunal decision, this clawback mechanism may be applicable to trusts set up by one of the spouses, and may even entitle the other spouse to obtain a freezing of the trust assets.

In international situations, it should be noted that Swiss matrimonial law will apply to the patrimonial relationships between spouses and registered partners who are domiciled in Switzerland, unless they have chosen another applicable law (among their national laws) or are bound by a matrimonial contract.\textsuperscript{43} At the level of the EU the Council adopted in 2016 two regulations implementing enhanced cooperation in the area of jurisdiction, applicable law and the recognition and enforcement of decisions on the property regimes.\textsuperscript{44} The regulations cover on the one hand matrimonial property regimes and on the other hand property consequences of registered partnerships. The regulations will apply as from 29 January 2019 with regard to the participating EU Member States.

\section*{IV \hspace{1em} WEALTH STRUCTURING AND REGULATION}

In Switzerland, one must always distinguish between domestic and international situations.

In purely domestic planning, the use of vehicles is less common except for the very wealthy and for foreign investments. For example, when investing in foreign real estate, local advice may guide the investor towards a company, trust or foundation.

For the many foreigners who hold assets in Swiss banks, it is common that they might select either a trust or foundation, perhaps associated with a company that holds the banking relationship. This is – by some margin – the most significant market segment for the private wealth management sector in Switzerland.

One of the key features of present-day Switzerland is that, except for charitable structures, the trust or foundation that is used will not be Swiss. In this context, Switzerland has ratified and introduced the Hague Trusts Convention\textsuperscript{45} into law, thereby providing the basis for recognising trusts (as defined in the Convention) in Switzerland.

This has created a hospitable environment for trustees who wish to act as a trustee in or from Switzerland. Foreign foundations will be recognised and may be used but, as with companies, care must be taken to manage the potential tax consequences.

Both the private foundation or the trust will help the client administer his or her personal wealth and business assets efficiently and effectively during his or her lifetime and through to the next generations. In practice, the private foundation and the trust are not so different in

\begin{itemize}
  \item Articles 208 and 214 of the SCC.
  \item Article 220 of the SCC.
  \item Articles 52 to 55 of SPIILA. This results in a change of the law applicable to the patrimonial relationships at the time the spouses or registered partners move to Switzerland, and this with retroactive effect to the beginning of the marriage (Article 55(1) of SPIILA). In the absence of an agreement to the contrary, this means that the ordinary regime applies to newly arrived married couples (and the segregation of assets regime to registered partners).
\end{itemize}

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their effects. They do, however, differ significantly in their structure and management. Unlike a trust, a foundation is an incorporated body that will come into existence upon the deposit or registration of its constitutional documents.

The key advantages of both vehicles are clear. A foundation is a vehicle created to exercise ownership and management rights. The appeal of the foundation is that, in the same way as a company, it possesses separate legal personality and operates like a company, but it does not have any shares. The foundation can also fulfil the same purposes as a trust with respect to asset protection and estate planning.

A discretionary trust’s main features are its capacity to protect assets and its capacity to provide a flexible arrangement for the distribution of income and capital among a wide range of beneficiaries. The great merit of the discretionary trust is its flexibility and, therefore, capacity to adapt to changing family circumstances, taxes and regulation.

The most appropriate structure will be dictated by several factors including how comfortable the client feels with either one.

i  Taxation

**Trusts**

Swiss tax laws do not have specific rules regarding trusts, but the cantonal and federal tax authorities have issued administrative regulations regarding the taxation of trusts. Under these rules there is no taxation of a trust as such, or of the trustee in connection with the trust’s assets. Therefore, taxes, if any, are levied at the level of the settlor of a trust or at the level of the beneficiaries. For purposes of taxation, the authorities differentiate between revocable trusts, irrevocable discretionary trusts and irrevocable fixed interest trusts. Trusts may easily be considered revocable under the rules in place. Revocable trusts are disregarded for Swiss tax purposes. Irrevocable discretionary trusts are recognised unless they have been settled by a settlor who was a Swiss tax resident at the time of the establishment of the trust and they are hence often used as a component of pre-entry tax planning.

**Foundations**

As foundations have legal personality, foundations are themselves subject to profit tax and capital tax to the extent they are resident in Switzerland for tax purposes. Although foundations may be subject to a separate regime of taxation, as a holding company or a mixed company if the conditions are fulfilled, tax rules applicable to foundations established in Switzerland are a clear obstacle to the use of Swiss foundations in an asset-structuring context. Foundations whose assets are applied for charitable purposes are exempt from taxes and are hence often used in Switzerland.

ii  Applicable anti-money laundering regime

The Swiss Anti-Money Laundering Act (AMLA)\(^{46}\) applies to all financial intermediaries who, on a professional basis, accept assets belonging to third parties.

Trustees and directors of foundations or offshore companies who conduct their business in Switzerland, regardless of the law governing the trust or foundation or the location of the

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\(^{46}\) Federal Act of 10 October 1997 on combating money laundering and terrorist financing in the financial sector.
Switzerland

As mentioned earlier, Switzerland is a committed partner to the task of elaborating international standards. It was the co-chair of the working group tasked with the latest revision of the Financial Action Task Force (FATF) recommendations approved in 2012. The AMLA was subsequently amended, in particular, with the introduction of serious tax offences as offences giving rise to money laundering.

The Swiss Association of Trust Companies (SATC) was established in 2007. Its purpose is to engage in the development of trustee activities in Switzerland and to help ensure a high level of quality, integrity and adherence to professional and ethical standards in trust businesses in Switzerland. The SATC imposes certain requirements on its members.

The Swiss financial regulatory framework is undergoing further important structural changes. Historically, only banks, insurance companies, financial intermediaries active in the field of collective investment schemes (e.g., fund management companies), securities dealers and stock exchanges have been subject to a licensing obligation in Switzerland. Asset managers, except in limited cases when acting as the manager of a Swiss fund, were not required to be licensed unless the asset managers had custody of client assets. In the fund sector, Swiss managers of non-Swiss funds are now subject to a licensing requirement. This legal reform was embodied in a revision of the Federal Act on collective investment schemes, driven by the EU’s Alternative Investment Fund Managers Directive. Such revision entered into force on 1 March 2013. Further, Swiss and foreign asset managers of Swiss pension funds must be duly supervised.

In addition, on 27 June 2014, the Federal Department of Finance submitted the draft Federal Act on Financial Services as well as the draft Federal Act on Financial Institutions to a consultation process that ended on 17 October 2014.

The objective of the Federal Act on Financial Services is to provide for a new legal framework on the provision of financial services in Switzerland, including when such services are provided on a cross-border basis into Switzerland. The main features of the draft Federal Act on Financial Services are the rules of conduct (e.g., suitability or appropriateness tests), which are largely inspired by EU standards, in particular the Markets in Financial Instruments Directive. The draft provides for a new registration requirement applicable to non-Swiss financial services providers who render services in Switzerland on a cross-border basis. The objective of the draft Federal Act on Financial Institutions is to provide for a new legal framework governing the supervision of all financial institutions, with the exception of banks and insurance companies that remain regulated by specific legislation tailored to their needs. A key alignment with international standards is the introduction of a prudential supervision over independent asset managers and trustees. This prudential supervision is based on a ‘two-tier supervisory regime’, where FINMA is responsible for licensing the independent

47 The FATF is an inter-governmental body that sets standards, and develops and promotes policies to combat money laundering and terrorist financing.


49 Its members must have adequate professional indemnity coverage and minimum educational and professional experience thresholds for senior managers acting within Switzerland. A further requirement is that all members of the SATC have adopted adequate internal processes and controls, such as the four eyes principle, meaning that trustee decisions require the approval of at least two qualified trust officers.
asset managers and trustees, with a right to impose sanctions and set minimum requirements, including as to corporate governance, but where the ongoing (day-to-day) supervision is delegated to privately organised and FINMA-licensed supervisory organisations. This system benefits from a wide consent within the Swiss financial industry and is a positive element of the new legislation.

The draft Federal Act on Financial Services as well as the draft Federal Act on Financial Institutions were submitted by the Swiss Federal Council to the Swiss Parliament on 4 November 2015, after a consultation process in 2015. The Council of States as first chamber of the Swiss Parliament debated the new laws on 11 December 2016. As a result of the debates in the Council of States, a number of amendments have been made to the drafts initially submitted by the Swiss Federal Council. On this basis, the two draft acts have been submitted to the National Council (as second chamber of the Swiss Parliament to approve the new laws).

The reconciliations of the differences between the versions of the Council of States and the version of the National Council should take place in winter 2017 or spring 2018.

It is expected that both the Federal Act on Financial Services and the Federal Act on Financial Institutions will enter into force at the earliest in January 2019.

Further and independently from the consultation process of the draft Federal Act on Financial Services and the draft Federal Act on Financial Institutions, the Banking Ordinance was modified. The reliefs which were incorporated aim at accelerating the development of the fintechs within the Swiss financial market.

V CONCLUSIONS AND OUTLOOK

As can be seen from the above, Switzerland is undergoing rapid and profound change.

In 2009, Switzerland adopted the OECD international standard for the exchange of information under tax treaties, a move heralded as the end of banking secrecy and tax avoidance for people holding undeclared funds in Swiss banks.

In late 2012, the government announced the details of its white money strategy and identified the areas of asset management, pension funds and capital markets as those with significant growth potential. To help in this regard, the government plans to base its financial market policy on strengthening competitiveness, combating abuses and improving the framework, with quality, stability and integrity as its key objectives.

Since then, the US programme and related settlements, FATCA implementation, AEOI involving the EU and the rest of the world, amendments to AMLA and the major revision of the law on financial services and institutions as well as a clear Fintech strategy, give hope that Switzerland has bedded down its framework for the era of transparency.

In the short to medium term, the uncertainty that accompanies change and the complexity and cost that goes hand-in-hand with such profound changes is affecting the whole wealth-management industry. The government’s ambition to close Switzerland to undeclared funds and develop a strong financial services sector is clear.

At different times, the features that make Switzerland attractive have had varying importance. It should be clear to all concerned that Switzerland will be less secretive in the future. It is certainly not a tax-neutral jurisdiction, but there are still many reasons why it remains the home of individuals of significant wealth and a key player in the custody and management of private wealth. In the current environment it appears that Switzerland’s status as a safe haven has retaken centre stage.
I INTRODUCTION

In line with Ukraine’s efforts to create a single economic and social space with the European Union (EU), Ukrainian legislation is undergoing fundamental changes aimed at harmonisation with that of the EU law. Concurrently with the ratification of the EU Association Agreement by Ukraine and all 28 Member States of the EU (with the Netherlands being the last to ratify on 1 June 2017), which is expected to enter into full force on 1 September 2017, substantial reforms of Ukrainian laws and regulations in tax, corporate and banking spheres are taking place. This is creating new incentives both for Ukrainian businesses in Europe and for foreign investors in Ukraine.

On 11 June 2017, the decision of the Council of the European Union to introduce a visa-free regime for Ukrainian citizens to travel to Schengen Zone member states became effective. A visa-free regime allows holders of Ukrainian biometric travel passports to travel without a visa to almost all EU Member States, for no more than 90 days during any 180-day period. The visa waiver approved by the EU also covers four countries that are not members of the EU, namely Norway, Iceland, Liechtenstein and Switzerland, but excludes the United Kingdom and Ireland as they are not part of Schengen arrangements.

One of the most significant steps in the anti-money laundering direction has been the establishment in 2015 of the Ukrainian National Anti-corruption Bureau (UNAB) and National Agency on Corruption Prevention (NACP). A Specialised Anticorruption Court is also anticipated as the final stage of anti-corruption and judicial reforms in Ukraine.

An electronic declaration system for politically exposed persons (PEPs) and persons authorised to perform state or local government functions was successfully launched at the end of 2016.

In line with recent global trends, Ukraine is seeking to increase transparency and accountability within its business structures. As part of this process, Ukraine has introduced a public register of ultimate beneficial owners (UBOs) of corporate bodies. Furthermore, in line with the global deoffshorisation drive, Ukraine has joined the Inclusive Framework on OECD Base Erosion and Profit Shifting (BEPS) project, which provides for the implementation of the minimum four BEPS standards. In 2016, the President of Ukraine issued a decree establishing a working group for the preparation of draft laws on counteracting the reduction of the tax base and the transfer of profits abroad. At time of publication, the list of draft laws to improve procedures for control over transfer pricing and transfer of income abroad, introduce rules for controlled foreign companies (CFC), counteract

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1 Alina Plyushch is a counsel and Dmytro Riabikin is an associate at Sayenko Kharenko.
aggressive tax planning, and liberalise currency control regulations in Ukraine were prepared, but no significant movements have yet been made to implement these draft laws. However, Ukrainian fiscal authorities and the country’s banking regulator are still advocating adoption of anti-BEPS measures (even beyond the minimum standard, including introduction of the CFC regime) as well as implementation of the OECD Common Reporting Standard (CRS) for automatic exchange of information. In addition, in 2017, Ukraine and the USA signed an Intergovernmental Agreement Implementing the Foreign Account Tax Compliance Act (FATCA).

In 2017, the National Bank of Ukraine (NBU) considerably liberalised Ukrainian currency regulations by undertaking steps to improve conditions for conducting foreign economic activity by Ukrainian individuals and business entities.

Another substantial factor influencing Ukrainian legal reforms is the Extended Fund Facility (EFF) between Ukraine and the International Monetary Fund (IMF), approved on 11 March 2015 by the IMF Executive Board. In accordance with the EFF, Ukraine is obliged to implement a number of fiscal, economic and legislative measures under IMF supervision. In compliance with the EFF, significant changes were introduced to regulation of the banking and energy sectors, anti-money laundering regime, the fight against corruption and investor protection. These reforms seek to introduce recognised international standards (including those of the IMF, the EU and Financial Action Task Force (FATF)) in these areas.

In recent years, Ukrainian businessmen have been primarily focused on effective wealth protection and management mechanisms. The ongoing conflict in the Eastern Ukrainian regions of Donetsk and Luhansk and substantial levels of corruption continue to make wealth preservation and protection the number one priority.

II  TAX

Taxation of individuals in Ukraine depends on tax residence, source and type of income.

i  Tax residency

The Tax Code of Ukraine (the Tax Code) provides the following residency tests to determine an individual’s tax residency: (1) residence (permanent residence in Ukraine for a period exceeding 183 days in a calendar year); (2) centre of vital interests (close economic and personal ties); and (3) citizenship.

Registration of an individual as an entrepreneur in Ukraine is also sufficient to recognise this individual as a Ukrainian tax resident. In addition, an individual may voluntarily accept to become a tax resident in Ukraine in accordance with the procedures set out in the Tax Code.

Despite the above rules, in practice the main test to determine tax residency regularly applied by Ukrainian tax authorities is the number of days spent by an individual in Ukraine in a calendar year.

For the purposes of the Tax Code, any person who fails to qualify as a Ukrainian tax resident is considered a non-resident of Ukraine for tax purposes.

ii  Source of income

Tax residents of Ukraine pay tax on their aggregate worldwide income. Non-residents pay tax on Ukrainian-sourced income only. Non-resident individuals are not eligible for certain deductions and exemptions available to residents for personal taxation purposes.
iii Types of taxable personal income

The Tax Code recognises both monetary and non-monetary personal income.

The Tax Code provides for the following taxable types of personal income (irrespective of residency): employment income, interest and dividends income, gifts, inheritance, investment income, insurance payments, rental income, fringe benefits, amounts of punitive damages paid, and written-off payment obligations to third parties etc.

The Tax Code specifically excludes certain types of income from the taxable basis of both residents and non-residents.

In addition, certain categories of low-income taxpayers are entitled to reduce their respective incomes by the amount of the ‘social tax benefit’.

The Tax Code prescribes that if so provided by the respective international tax treaties, the amount of tax paid by a tax resident outside Ukraine can serve as credit against taxes payable in Ukraine. This applies provided the taxpayer submits a written confirmation from the foreign tax authority acknowledging that such foreign taxes have, in fact, been paid. However, the total amount of any foreign tax credit may not exceed the total amount of personal income tax (PIT) due in Ukraine.

iv Rates

In 2016, a flat rate of 18 per cent PIT was introduced for most types of income for both residents and non-residents.

Interest and royalties are generally taxable at the rate of 18 per cent. Dividends received by individual residents are taxed at different rates, namely: (1) dividends distributed by Ukrainian companies that are subject to corporate income tax are taxed at 5 per cent; (2) dividends distributed by Ukrainian companies that are not subject to corporate income tax (i.e., using simplified taxation system), as well as collective investment arrangements and non-resident entities are taxed at 9 per cent.

Income derived from disposal of real estate is taxable at the rate of either zero per cent or 5 per cent depending on: (1) the type of property; (2) the frequency of disposals; and (3) the duration of the seller’s title to such property. However, disposal of real estate in Ukraine made by a non-resident and disposal of real estate abroad made by Ukrainian resident are taxable at the rate of 18 per cent.

The standard rate for the disposal of moveable property (such as vehicles) is 5 per cent. A single disposal of a car or a motorcycle within a year is non-taxable. An 18 per cent tax rate applies to a non-resident’s income from the disposal of moveable property in Ukraine.

v Gift and succession taxes

Gifts and inheritance are taxable and both are subject to the PIT at the rate of zero per cent, 5 per cent or 18 per cent. The exact rate depends on the residency status of the donator or the testator and on the degree of relation between the donator or the testator and the recipient or the heir (varying from zero per cent for spouses and close relatives (parents and children, grandparents and grandchildren, brothers and sisters), to 18 per cent for inheritance or gifts received from or by non-residents).

Tax residents shall pay PIT on inheritance and gifts irrespective of the location of the acquired assets.
vi Assets tax

Currently the tax code has a consolidated assets tax that consists of land tax, non-land real estate tax and transport tax.

Land tax is payable by individuals holding title to or right of permanent use of land plots in Ukraine irrespective of their tax residency. Particular land tax rates are determined by the municipal authorities and shall not exceed 12 per cent of the cadastral value of a land plot depending on the type of the land plot and the particular rights of its holder (i.e., either title to or the right of permanent use). The Tax Code provides for a number of tax exemptions regarding land tax depending, *inter alia*, on the status of the individual, type of land plot, its area and the purpose of its use.

Residual and non-residual real estate owned by an individual is subject to a non-land real estate tax. The tax rates are set forth by the municipal authorities but shall not exceed 1.5 per cent of the minimum wage per square metre. At the same time, the Tax Code sets forth certain exemptions for the real estate tax (e.g., a minimum real estate area not subject to the real estate tax).

The first 60 square metres (for an apartment), 120 square metres (for a house) or 180 square metres (where the same person owns an apartment and house) are exempt from taxation. This exemption applies only once irrespective of the number of owned properties.

If a taxpayer owns an apartment of more than 300 square metres or a house of more than 500 square metres, the amount of tax due increases by 25,000 hryvnia.

Owners of vehicles registered in Ukraine with an age of less than five years and average market value exceeding 750 times the minimum wage are subject to a transport tax of 25,000 hryvnia per vehicle. The average market value for each vehicle type is determined by the Ministry of Economic Development and Trade of Ukraine.

vii Military duty

To provide the armed forces with funding in view of the ongoing armed conflict in Eastern Ukraine, Parliament has introduced a military duty. Military duty is levied on Ukrainian-sourced income of non-residents and on the worldwide income of Ukrainian tax residents at the rate of 1.5 per cent.

viii Issues relating to cross-border structuring

Ukraine has a wide network of double taxation treaties with approximately 70 countries. In 2017, double taxation treaties with Malta and Luxembourg were finally ratified and are expected to enter into force from 2018. The ratification of amending protocol to the double taxation treaty with Cyprus is pending. The majority of the double taxation treaties entered into by Ukraine are based on the OECD model.

While considering trans-border structuring options, Ukrainian private businesses currently focus on such jurisdictions as the Netherlands, Estonia, Hungary, Slovakia, Latvia and the UAE due to the favourable provisions of the respective double taxation treaties between Ukraine and these countries. Cyprus remains one of the most popular and attractive cross-border structuring options for the majority of Ukrainian businessmen in tax planning and private wealth protection and preservation. However, interest in structuring through the Netherlands, Estonia, Hungary, the UAE and other jurisdictions with favourable tax regimes (e.g., Malta and Luxembourg taking into account recent ratification of the double taxation treaties) for holding, financial and operational companies will continue to grow for the observable future.
Cross-border transactions of Ukrainian companies with non-resident entities are, under certain conditions, subject to transfer pricing rules (TP rules). In general, TP rules apply primarily to transactions with related counterparties. However, they may also apply to transactions between unrelated entities, when, for example, a foreign entity is a tax resident of a ‘low-tax’ jurisdiction or incorporated in a certain legal form allowing such entity not to pay taxes in the jurisdiction of incorporation (this mainly refers to tax transparent entities such as UK partnerships or limited liability partnerships).

Ukrainian TP rules are based on OECD Transfer Pricing Guidelines. These regulations require that prices for goods and services in certain transactions shall be set on the arm’s length principle.

The TP rules apply provided that the following criteria are met: the total taxable income of the respective Ukrainian taxpayer exceeds 150 million hryvnia and the volume of such transactions with any particular counterparty exceeds 10 million hryvnia (exclusive of VAT) in the relevant calendar year (each such transaction is a ‘controlled transaction’). Ukrainian taxpayers are required to report all controlled transactions to the tax authorities on an annual basis.

Based on such reporting as well as on their own monitoring and tax audits, Ukrainian tax authorities have the ability to make transfer pricing adjustments and impose additional tax liabilities in respect of the controlled transaction if the terms and conditions of a particular controlled transaction are not on an arm’s-length basis.

III  SUCCESSION

Rules governing succession are incorporated in the Sixth Book (Chapter) of the Civil Code of Ukraine (the Civil Code). Conflict of law issues arising out of and connected with succession are set forth in the Law on Private International Law. Useful guidelines on the application of the succession legislation are outlined in the Letter of the High Special Court of Ukraine on Civil and Criminal Cases on court practice in succession cases dated 16 May 2013.

Following Roman civil law traditions, succession in Ukraine is regulated either by way of testament or pursuant to the provisions of the Civil Code (succession by law).

A testator’s estate is defined as all the testator’s rights and liabilities remaining in force after his or her death.

The death of the testator triggers probation. Within six months of the commencement of the probation, the heirs may either execute or renounce their rights to succession.

Transfer of title to heirs is effected on the basis of a certificate of inheritance issued by a notary or, in rural settlements, by the authorised officer of municipal government body, upon expiration of a six-month probation period. Issuance of a certificate is mandatory for immoveable property, while for moveable property it is optional (though highly recommended).

i  Intestacy rules

Inheritance by law arises if a testator leaves no valid will and testament. Inheritance by law rules will also apply if the testator has left a will but it was successfully challenged by heirs or if the inheritance was renounced by heirs.

There are several lines of priority of succession. The testator’s estate is distributed among the heirs of each priority line (i.e., the heirs of each priority line exclude the members of the
next lines). This order of succession may be changed upon written and notarised agreement between the heirs when such agreement does not infringe the rights of the heirs that are not parties thereto.

The principle of representation applies (i.e., in case of the death of an heir of the first priority line (e.g., the testator’s son) his or her heirs will have the right to their share of the inheritance).

The Civil Code intestacy rules provide that only individuals may inherit by law. The right to succession may be executed by an heir upon provision of evidence of his or her relations with the testator (e.g., birth or marriage certificate). The heirs of the same priority line inherit the testator’s estate in equal shares; however, they may enter into a separate agreement and decide to distribute the testator’s estate among themselves.

ii Inheritance by will

The Civil Code sets out strict requirements regarding the form of the will. It shall be made by a testator in writing with a statement of the date and place of making a will, with further notarisation and registration. The testator may define as heirs either individuals or legal persons. Only adult persons of full legal capacity may execute a will (they must be 18 years old (or in certain cases 16) or over, and with full mental capacity).

A testator may set out in a will any additional bequests in favour of any designated person (e.g., the right to abide in the inherited real property). The testator may also determine certain preconditions or conditions for his or her heirs to satisfy in order to receive the right to inheritance (e.g., residence in certain place, certain age, etc). However, such preconditions must not contradict the law or principles of public morality.

A document executed in breach of will execution rules set out in the Civil Code or by a person lacking full legal capacity is deemed void ab initio.

A will is deemed void when there is evidence that the testator has executed the purported will, either by coercion or as a result of fraud. Upon a claim by the interested person, such a will may be declared void by court decision.

Spouses may draft a joint will. Apart from a will, a testator may also enter into a succession agreement under which the acquirer obliges to undertake certain actions prescribed by alienator (testator) in return for ownership rights to the testator’s estate.

iii Mandatory inheritance

The testator’s right to choose heirs is limited by provisions of Article 1241 of the Civil Code, which guarantees that underage or disabled children, spouses and parents shall, in any case, inherit at least half of the portion they would have received in the absence of the last will. Under Ukrainian law, the definition of a ‘disabled person’ covers both persons with disabilities and retired persons.

iv Conflict of law issues

As a general rule, succession is governed by the law of the country of the last residence of the testator (i.e., if a citizen of Romania resides and dies in Ukraine the applicable law is that of Ukraine). However, if a testator executes a will, he or she can choose his or her lex patriae (e.g., in the case of a Hungarian testator – the law of Hungary).

There are, however, certain overriding provisions of lex specialis. The form of the act shall correspond to the requirements of the law of the place (country) of the testator’s death. However, the will may not be declared void on the basis of error in form if it corresponds to
the law of the country where the testator’s immovable property is situated, the *lex patriae*,
the law of the country of the last residence, or the law of the country where the will was
executed, whichever is applicable.

Transfer of title to immovable property shall be governed by the law of the state where
such immovable property is situated.

v Matrimonial rules
In recent years, no substantial amendments were made to the Family Code of Ukraine (the
Family Code), the act governing matrimonial relations in Ukraine. Same-sex marriages are
not recognised by the Family Code and their official recognition is unlikely in Ukraine in the
foreseeable future.

The Family Code provides for tenancy-in-common of the spouses’ property with
certain exclusions (e.g., personal belongings, property acquired before the marriage, etc).
This regime can be changed by way of a prenuptial agreement. Prenuptial, maintenance
and alimony agreements must be executed in writing and notarised. However, there is no
developed case law in Ukraine regarding such agreements. Difficulties may arise in the case of
foreign spouses and with conflict of law issues.

IV WEALTH STRUCTURING AND REGULATION
i General overview of private wealth regulation
None of the forms of legal entities provided by Ukrainian corporate legislation may be viewed
as specifically designed for private wealth management purposes. Trusts and foundations are
generally not recognised in Ukraine, though the relevant terminology sometimes appears in
legislation.

The year 2016 brought more significant regulatory developments aimed at establishing
economic and financial transparency. Substantial changes were introduced to the regulation
of the banking sector, which directly affected wealth management and assets protection.

ii Beneficial owners’ disclosure requirements
In mid-2015, requirements governing the disclosure of the UBOs of Ukrainian legal entities
were introduced. Current Ukrainian legislation provides that all legal entities in Ukraine shall
file with the State Registry of Legal Entities and Private Entrepreneurs of Ukraine (the State
Registry) their legal and beneficial ownership information. The filing requirements do not
cover legal entities whose shareholders are exclusively individuals.

Once filed at the State Registry, the UBOs’ personal data (including full name and
place of residence) becomes publicly available from the webpage of the State Registry.

The definition of the UBO included into the AML Law (as defined below) covers both
shareholding and dominant control tests endorsed by the FATF in the 2014’s Guidance
on Transparency and Beneficial Ownership. Moreover, nominee shareholders may not be
registered as the UBOs of Ukrainian legal entities.

Failure to file information on the UBO is sanctioned by a fine (up to 8,500 hryvnia)
imposed on the management of Ukrainian corporate bodies.

Currently, Ukrainian legislation does not provide for any specific rules regarding
controlled foreign companies (CFC). However, in line with the global deoffshorisation drive,
and following Ukraine’s accession to BEPS, the relevant draft CFC law has been prepared,
though it is yet to be considered by the Ukrainian Parliament.
iii New requirements of the National Bank of Ukraine

In 2014, the NBU started to develop a strategy for Ukrainian banking sector reform with the principal goal of securing greater transparency, sustainability and stability. Following the IMF’s recommendations, the NBU has substantially amended legislative requirements for Ukrainian bank owners and ownership structures. At the time of writing, the NBU has already liquidated more than 90 banks, which at the beginning of 2014 represented almost half of the banking system of Ukraine.

The NBU continues to liberalise quite strict currency control regulations. In particular, it is no longer required either for individuals or for legal entities to obtain an individual licence from the NBU for opening a foreign bank account or making an investment abroad, provided the funds transferred to a foreign bank account or the funds for such an investment are held abroad and not transferred from Ukraine.

Since 12 June 2017, legal entities on the basis of an individual licence have an opportunity to invest abroad up to US$2 million (or its equivalent) during one calendar year. Previously the limit for total amount of such transactions was up to US$50,000 per calendar month.

Furthermore, Ukrainian residents (individuals) now have the opportunity to obtain an electronic licence from the NBU for making foreign investment or transfer or deposit to their foreign bank accounts of up to US$50,000 during one calendar year. This procedure is much simpler than the procedure of obtaining a paper licence as envisaged in the past.

iv Anti-money laundering and anti-corruption regime

The Law on Prevention and Counteraction to Legalisation (Money Laundering) of the Proceeds from Crime, Terrorism Financing, as well as Financing of the Proliferation of Weapons of Mass Destruction (the AML Law) together with the Criminal Code of Ukraine (the Criminal Code) is the primary regulatory anti-money laundering act in Ukraine.

In line with the EFF the AML Law aims at compliance with the principal FATF recommendations (including 40 Recommendations) on combating money laundering and terrorist financing.

Ukraine’s anti-money laundering regime includes a two-level strict monitoring system over financial operations performed by residents and non-residents of Ukraine. Initial financial monitoring (identification of a client, details of and grounds for particular financial operation, etc.) of financial operations is conducted by intermediaries, including: banks, insurance (and reinsurance) companies, other financial institutions, stock and commodities exchanges, professional members of the security market (e.g., brokers, dealers), notaries, auditors and individuals rendering accounting services, lawyers and other persons providing legal services, etc., (the initial financial monitoring performers).

The AML Law, inter alia:

a allows outsourcing of client identification or verification to a third party;

b authorises the initial financial monitoring performers to require a client to provide its ownership structure in order to enable them to determine the beneficial owners of the client;

c introduces financial monitoring with respect to national or foreign politically exposed persons and officials of international organisations, establishes a high-level risk for operations involving (or carried out in the interests of) politically exposed persons or officials of international organisations and provides for additional measures of financial monitoring for clients with a high level of risk; and
clarifies the legal basis for the termination of relationships with a client by the initial financial monitoring performers in case the identification or verification of a client is not possible.

The AML Law also provides for the formation of a national analytical database that may be used by the law enforcement agencies of Ukraine and other countries for the purposes of identification, examination and investigation of crimes related to money laundering and other illegal financial transactions.

The major authority with the powers of general supervision of the financial monitoring system is the State Service for Financial Monitoring of Ukraine (the Service). The Service, inter alia, adopts standards and recommendations as to the conduct of financial monitoring and updates the list of persons connected with terrorist activities and subject to international sanctions.

The Criminal Code imposes criminal liability for laundering the proceeds of a crime. The sanction is imprisonment of up to 15 years combined with confiscation of the proceeds of the crime and property of the convicted person as well as deprivation of the right to perform certain activities or hold certain positions for up to three years.

In 2015, Ukraine introduced the Law On Prevention of Corruption, which provides a new electronic system of submission of declarations of politically exposed persons and persons authorised to perform the functions of a state or local government (the Person) and provides for a comprehensive list of information that must be reflected in the declaration.

The following shall be reflected in the Person’s declaration:

- real estate, including real estate under construction, owned by the Person and his or her family members, including joint ownership, lease or other right of possession;
- moveable assets owned by the Person and his or her family members the value of which exceeds 160,000 hryvnia;
- securities, including shares, bonds, cheques, certificates, promissory notes, including those controlled by another person (indicating the share in the company) and other corporate rights, owned by the Person and his or her family members;
- intangible fixed assets owned by the Person and his or her family members, including intellectual property rights that can be monetarised;
- accrued revenues, including revenues from salaries, remunerations, dividends, gifts, etc.;
- cash assets exceeding 80,000 hryvnia, including cash, assets placed in bank accounts, deposits at credit unions and other non-bank financial institutions; and
- all financial liabilities of the Person exceeding 80,000 hryvnia (including loans, liabilities under lease contracts, amount of cash paid in respect of the principal amount of the loan and interest thereto, liabilities under insurance contracts and assets borrowed to other persons, etc.).

V CONCLUSIONS & OUTLOOK

Ukrainian legislation is going through a period of reform with the aim of becoming compliant with international and EU standards. Substantial changes are already visible though the climate for private wealth management and protection in Ukraine is still not friendly enough for the owners of Ukrainian businesses.
There is a growing need to introduce wealth protection structures at the ownership level. Currently, the first generation of Ukrainian businessmen is actively looking into the restructuring of their businesses in order to secure the interests of their families for years to come.

A reliable and effective solution to achieve these goals remains the creation of a cross-border structure with a trust or a foundation at the top. Such structuring provides for a transparent and reliable ownership and control system for the business, and helps to protect the interests of the beneficiaries. Since Ukrainian legislation now emphasises transparency as a major requirement for all such structures, it is important to consider that the UBOs of such structures may be disclosed to Ukrainian authorities and that such information will be publicly available.

In recent years, the Ukrainian tax system has not been stable. Ukraine has joined the BEPS project and developed a list of draft tax laws, but these initiatives have not been adopted yet. Meanwhile, taxpayers can enjoy a wide network of Ukrainian double taxation treaties and the opportunities they create.

Ukrainian law covers the main aspects of succession and matrimonial relations and provides for the possibility to enter into agreements in order to structure such relations and define specific regulation for specific cases. No updates or amendments thereto have been announced by Ukrainian government at this stage.

The AML Law and the Criminal Code serve as the main sources of the Ukrainian anti-money laundering regime. In particular, the AML Law provides for a range of financial monitoring procedures.

Ukraine has taken significant steps towards the creation of a disclosure and transparency regime, in particular, introducing the electronic declaration of assets by PEPs. Finally, Ukraine is developing its first deoffshorisation regulations, which, however, are yet to be adopted.

To sum it up, Ukraine is currently experiencing significant transformations under the banners of transparency and liberalisation. Though there is a long way to go, the course towards the highest European and international standards is clear and positive changes are expected to come in due course.
I INTRODUCTION

The United Kingdom of Great Britain and Northern Ireland constantly strives to maintain a state of harmony between contradictory policy objectives. The United Kingdom maintains a level of government spending of between 40 per cent and 50 per cent of GDP by being a high-tax jurisdiction for its own nationals. This is illustrated by a top rate of income tax of 45 per cent, among the highest in the Organisation for Economic Co-operation and Development countries, and capital gains tax at 20 per cent (other than for residential property).

However, for non-UK-domiciled persons it maintains a status as a relative tax haven, taxing only income and gains arising in or remitted to the United Kingdom, potentially allowing non-working individuals to become resident in the United Kingdom without any direct tax liability at all. In this way, the UK tax system works to attract non-UK persons, in particular those with capital resources or unearned income, while at the same time imposing significantly greater tax burdens on UK nationals. Cecil Rhodes counselled Englishmen to remember that they had won the lottery of life, but clearly did not have the 21st century’s income tax rules in mind.

Historically, the United Kingdom has always had a significant role as a mercantile centre, reflected in the position of the City of London as a major global financial centre, and the cosmopolitan and multicultural make-up of the individuals who live and work there. Building on its commercial strengths, the United Kingdom has sought to maintain a benign tax regime for business, to encourage investment and fund managers, lawyers, accountants and other wealth advisers to establish business in the United Kingdom, with the country being repaid in the tax on the profits of those businesses, rather than tax on the funds or persons advised. It has not sought to attract funds under management into the jurisdiction, but instead to position itself as a centre for the management of such assets. Indeed, with so many of its remaining dependencies and overseas territories being dependent on the revenues they generate from their role as offshore financial centres, the United Kingdom could be seen to have a vested interest in maintaining this distinction.

The outcome of this is that the United Kingdom exists as a relative tax haven and as a home jurisdiction of choice for many wealthy individuals, while at the same time applying some of the highest levels of marginal taxation on its own citizens. It does not seek to attract investment assets but actively courts the managers and advisers of those assets. However,
recent changes and proposals for future changes have started to erode this status and the UK is becoming less favourable to longer-term residents. It remains to be seen whether it will maintain this position.

The current watchword of UK tax policy is ‘fairness’. This does not seem to be applied, however – to paraphrase Marx – in each contributing to the exchequer in accordance with his or her ability to pay, or even progressively, but rather the policy is that every resident or taxpayer should be seen to make a contribution and where unfairness is perceived, steps should be taken to correct it.

II TAX

It has been this desire to achieve a perceived fairness that has characterised the development of the UK tax system in recent years. Efforts have largely been concentrated on ensuring the fair and efficient operation of the existing tax system, closing loopholes, seeking to maximise the collection of existing liabilities and countering the abuses of avoidance and evasion.

i Personal taxation for individuals

Individual taxation

Individual taxation in the United Kingdom is administered on a self-assessment basis. On this basis each taxpayer is required to give Her Majesty's Revenue and Customs (HMRC) sufficient information for HMRC to be able to determine that individual’s liability to tax in any tax year, which by quirk of history runs from 6 April to 5 April in the next year.

Income and capital gains are assessed and taxed separately. Income tax is charged progressively, with individuals earning more than £150,000 per year paying a marginal rate of tax of 45 per cent. Interest income benefits from a £5,000 exemption and dividend income is charged at lower rates.

Capital gains tax also currently has a progressive element, with higher earners paying a higher rate of tax. In recent years, the United Kingdom has moved from a headline capital gains tax rate of 40 per cent (aligned with income tax rates) that reduced to a minimum of 24 per cent (or 10 per cent for certain assets) depending on the length of time that the asset had been owned (known as taper relief) to, in 2008, a lower flat rate (initially 18 per cent, increased to 28 per cent in 2010 and then reduced to 20 per cent in 2016 for higher rate taxpayers) and with no reduction for long-term capital gains. A summary table for the tax year 2016–17 follows:

<table>
<thead>
<tr>
<th>Income tax</th>
<th>Other income</th>
<th>Dividends</th>
</tr>
</thead>
<tbody>
<tr>
<td>Personal allowance</td>
<td>£11,000</td>
<td>Tax-free</td>
</tr>
<tr>
<td>Basic rate</td>
<td>£11,001 to £43,000</td>
<td>20%</td>
</tr>
<tr>
<td>Higher rate</td>
<td>£43,001 to £150,000</td>
<td>40%</td>
</tr>
<tr>
<td>Additional rate</td>
<td>Above £150,000</td>
<td>45%</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Capital gains tax</th>
<th>Other assets</th>
<th>Residential property</th>
</tr>
</thead>
<tbody>
<tr>
<td>Annual allowance</td>
<td>£11,000</td>
<td>Tax-free</td>
</tr>
<tr>
<td>Basic rate</td>
<td>Up to £31,865</td>
<td>10%</td>
</tr>
<tr>
<td>Higher rate</td>
<td>Above £31,866</td>
<td>20%</td>
</tr>
</tbody>
</table>
For the purposes of assessing the thresholds, total income is calculated and assessed first, with the thresholds for capital gains tax being calculated in addition to income.

**The remittance basis**

As discussed above, the defining characteristic of the United Kingdom’s personal tax regime for high net worth individuals moving to the United Kingdom is the remittance basis of taxation. The remittance basis essentially provides that, for those who claim it in any particular tax year, only income and capital gains arising in or remitted to the United Kingdom are subject to taxation. The remittance basis (or versions thereof) has existed within the United Kingdom’s income tax system since it was first introduced in 1799, originally perhaps largely as a result of the administrative problems of assessing foreign income. Only from 1914 was the remittance basis restricted to persons not domiciled in the United Kingdom.

Domicile is a concept of UK law that seeks to identify an individual’s ‘home’. Every person acquires a domicile of origin at their birth, usually the domicile of their father when they were born. A domicile of origin can be replaced by a domicile of choice in another jurisdiction, if the individual moves to that jurisdiction and decides to remain there permanently or indefinitely. In determining whether a domicile of choice has been acquired, the individual’s intention is key and it is possible to remain resident in a jurisdiction for many years without becoming domiciled there.

The continued existence of the remittance basis remained a point of controversy and when a Labour government came to power in 1997, it committed itself to a review of the remittance basis. This review did not produce any significant change until 2008 when the remittance basis charge was introduced. The remittance basis charge is applied to non-domiciled individuals who have been resident in the United Kingdom for seven out of the previous nine tax years. From that point on, in any year in which they wish to claim the remittance basis, they must pay an annual charge of £30,000. From the tax year 2012–13, this was increased to £50,000 for individuals resident in the United Kingdom in 12 of the previous 14 tax years.

**Recent developments**

Since 2010, a number of changes have been introduced to seek to make the United Kingdom’s tax system simpler and fairer. In 2015, it was announced that non-domiciled individuals resident in the UK for more than 15 years would no longer be able to claim the remittance basis. These rules were due to be implemented in April 2017, and it remains the stated intention of the current government that this should be the case. However, the necessary legislation has not yet been introduced.

When passed (as it is assumed will be the case), the rules will provide that once a non-domiciled individual has been resident in the UK in 15 of the previous 20 years, he or she will no longer be able to claim the remittance basis and will be subject to income and capital gains tax on a worldwide basis. As a concession to these ‘long-term non-doms’ the legislation will also provide for an exemption for this charge for assets held in trust after 15 years of residence, providing no further sums are added to such trusts.

That the legislation that will provide for those new rules, that may already be in force, does not yet exist is a particularly unsatisfactory situation for those affected, who if nothing else must be able to expect a degree of certainty from their legislators.
Residency rules

The previous rules on when an individual was considered to be resident in the United Kingdom were defined partly by statute, but largely by the common law. They could be summarised as follows: an individual who was physically present in the United Kingdom in any tax year for a permanent purpose was to be considered resident, whereas an individual who was physically present in the United Kingdom only for a temporary purpose was not. Determining what was a temporary or permanent purpose and for those who wished to give up UK residency when a permanent purpose ceased proved a matter of some contention, in which every factor of an individual’s life had to be considered.

In response to this a new statutory test was introduced from 6 April 2013. This seeks to provide a strict day-count test to determine whether an individual is resident in the United Kingdom. The number of days that will determine whether an individual is resident will depend on five potential ties to the United Kingdom:

a) whether the individual has a partner or minor children in the United Kingdom in the tax year;
b) whether the individual has a home available to them in the United Kingdom in the tax year;
c) whether the individual works in the United Kingdom for more than 40 days in the tax year;
d) whether the individual has spent more than 90 days in the United Kingdom in either of the previous two tax years; and
e) whether the individual has spent more days in any other single jurisdiction than in the United Kingdom in the tax year.

The number of days that an individual can spend in the United Kingdom without being treated as resident will depend on whether they have previously been resident in the United Kingdom and how many ties they have to the United Kingdom in any tax year. Any individual spending less than 15 days in the United Kingdom in any tax year will not be considered resident for that year and any individual present for more than 183 days is conclusively resident.

To decide whether an individual is a ‘leaver’ or ‘arriver’ under the new rules, HMRC has confirmed that the individual may elect to use the old pre-6 April 2013 rules or the new statutory residence test on the basis that the statutory residence test was deemed to be in place for the tax years 2012–13, 2011–12 and 2010–11.

Tax avoidance

It had been thought that an established principle of English law was: ‘Every man is entitled, if he can, to order his affairs so that the tax … is less than it otherwise would be.’ However, in recent years the morality if not the legality of tax avoidance has been questioned by both politicians and the press, culminating in the Chancellor of the Exchequer announcing in March 2012 that he regarded aggressive tax avoidance as ‘morally repugnant’ and would take steps to counteract what might otherwise be regarded as legal tax planning.

For a number of years, the courts have been invoking a doctrine, known as the ‘Ramsay principle’ after a leading case, that allowed transactions to be recharacterised to deny a particular tax result when it was felt that was not the purpose of the legislation that it should deliver that result.

However, this approach by the courts was generally felt to be uncertain and unsatisfactory for taxpayers and government. As a result the government introduced a general anti-abuse rule (GAAR), which applies to tax arrangements entered into on or from 17 July 2013. The purpose of this GAAR is to target ‘artificial and abusive arrangements’ and counteract them to deny any tax advantage sought. It will apply to, *inter alia*, income tax, national insurance contributions, capital gains tax, inheritance tax and the annual tax on enveloped dwellings (ATED).

It is the intention that the GAAR should introduce greater certainty and fairness into the UK tax system, giving taxpayers and tax collectors alike greater clarity as to what is permitted and what is not. Considerable doubt remains as to whether it will achieve this, however. It is notable that there is no clearance procedure for GAAR and a lack of complete independence between the GAAR advisory panel and HMRC. It is still too early to say how exactly the GAAR will apply and indeed how HMRC may choose to apply it. But suffice to say at this stage there is a degree of additional caution surrounding UK tax planning.

At a more general level, the distinction between (illegal) tax evasion and (legitimate) avoidance is becoming increasingly blurred in the political arena. A clear manifestation of this is the moral outrage exhibited when the Panama Papers revealed in April 2016 that the then prime minister’s father had managed a (UK tax-compliant) non-UK resident investment fund. There is increasing social pressure on companies and individuals to conduct their affairs, not just within the letter of the law, but also in a spirit of not reducing their liability to taxation.

**Taxation of high-value residential property**

The rate of transfer tax (stamp duty land tax or SDLT) that applies to residential property has been progressively raised over recent years to increase the level of tax paid by owners of high-value residential property. From 1 April 2016, a surcharge of 3 per cent applies to the rate of SDLT on the purchase of ‘second homes’. This surcharge, which will apply to almost any non-resident purchasing a residential property in the UK, raises the top rate of SDLT paid by individuals to 15 per cent.

The current rates of tax, which apply on increasing portions of the property price above £125,000, are set out in the table below:

<table>
<thead>
<tr>
<th>Purchase price of property</th>
<th>Rate of SDLT</th>
<th>Rate of SDLT on second homes</th>
</tr>
</thead>
<tbody>
<tr>
<td>£0–£125,000</td>
<td>0%</td>
<td>3%</td>
</tr>
<tr>
<td>£125,001–£250,000</td>
<td>2%</td>
<td>5%</td>
</tr>
<tr>
<td>£250,001–£925,000</td>
<td>5%</td>
<td>8%</td>
</tr>
<tr>
<td>£925,001–£1.5 million</td>
<td>10%</td>
<td>13%</td>
</tr>
<tr>
<td>Above £1.5 million</td>
<td>12%</td>
<td>15%</td>
</tr>
</tbody>
</table>

There have been a number of targeted measures designed to counter particular perceptions of tax avoidance, notably with regard to the ownership of high-value residential property. To counter a concern that structures whereby residential properties owned by non-UK companies...
were facilitating the transfer of ownership in those properties without the payment of SDLT, in March 2012, a number of new rules applying to residential properties worth more than £2 million were announced:

a. The rate of SDLT paid by certain non-natural persons purchasing UK residential properties for more than £2 million was raised from 5 per cent to 15 per cent, and the rate for all other purchasers was raised to 7 per cent. The Finance Act 2013 introduced a number of important reliefs that effectively restricted the 15 per cent rate of SDLT to private residential property. The 15 per cent rate was extended by the Finance Act 2014 to properties over £500,000, with effect from 20 March 2014.

b. From 1 April 2013, an annual charge known as the ATED was levied on up to 0.75 per cent of the gross value on certain non-natural persons who own UK residential properties worth more than £2 million. The Finance Act 2013 again introduced reliefs that limited the effect of the ATED to broadly those structures holding private residential property. The Finance Act 2014 introduced two new ATED bandings: an annual charge of £7,000 applying to properties worth over £1 million up to £2 million from 1 April 2015 and, from 1 April 2016, an annual charge of £3,500 for properties valued at over £500,000 up to £1 million.

c. Certain non-resident non-natural persons selling interests in UK properties, subject to the ATED, for more than £2 million will be subject to capital gains tax in the United Kingdom on post-6 April 2013 gains. The value subject to the charge to tax will be extended to disposals of properties over £1 million to £2 million from 6 April 2015 and over £500,000 to £1 million from 6 April 2016.

d. From April 2016, individuals (or married couples) purchasing a second residential property are subject to a 3 per cent surcharge above the standard rates of SDLT, with limited exceptions for de minimis property interests and the replacement of an existing main residence.

These rules are effectively limited to ‘owner-occupied’ residential properties, with ‘genuine businesses’ that own residential property largely being exempt, and while highly targeted, these rules represent two dramatic shifts in UK tax policy. For the first time, the United Kingdom has an annual tax based on the value of assets owned – a wealth tax in all but name. Wealth taxes have been proposed in the United Kingdom previously but never enacted, and while there was considerable discussion in advance of the 2010 general election, the idea seemed to have been discarded. The question will be whether, once introduced, the wealth tax will be extended to cover other assets and taxpayers.

The stated objective of these changes is to encourage property owners to own UK property directly, rather than through non-UK structures, primarily to ensure that the SDLT is not avoided on sale. However, this will also have the consequence of bringing those persons within the scope of UK inheritance tax on death, which can give rise to much more significant tax charges.

Further, UK capital gains tax has previously only been assessed on persons resident in the United Kingdom. The extension of capital gains tax to non-residents again represents a significant departure from the previous norms of UK tax policy. Up to 2012, the United Kingdom had been highly unusual in that it did not seek to tax non-residents on profits derived from the alienation of real (or indeed any other form of) property in the United Kingdom. From 6 April 2015, all non-resident owners of UK residential property are subject to capital gains tax on the sale of such properties at 28 per cent.
Inheritance tax and property

From July 2013, new conditions were placed on the deductibility of loans for inheritance tax planning purposes. It was previously standard planning practice to reduce the liability to UK inheritance tax (IHT) by using loans to finance the acquisition of assets that benefit from advantageous reliefs (business property relief, agricultural property relief and woodlands relief) and excluded status from IHT. The new conditions and restrictions significantly restrict the ability to claim a liability as a deduction for inheritance tax purposes, unless the liability was (originally) used for the original purchase of a residential property.

The impact of these rules are also be more widespread following further changes announced in 2015, which should have come into effect in April 2017. As with the new rules for long-term non-doms, the legislation for these rules is yet to be enacted, although again, it should be presumed that this will occur at some point in 2017. Up to this point, UK residential property owned directly by non-UK domiciliaries or non-UK residents has always been subject to IHT, but shares in a non-UK company that in turn owns UK property have not. In this way, many owners of houses in the UK have fallen outside the scope of IHT.

With effect from April 2017, it is proposed that the IHT rules will be amended so that the value of any interest in a company or other entity that indirectly owns residential real estate in the UK, or did at any time in the preceding two years, is brought within the scope of IHT for non-UK resident individual shareholders or shareholding trusts, on death, where gifts are made in the seven years preceding death, or on the 10-year anniversaries of a trust (as set out below).

These rules will only apply to residential property, or ‘dwellings’; however, there is still some confusion as to what constitutes a dwelling. There is no exemption for principal residences (such as applies to non-resident capital gains tax) or any de minimis values or reliefs for property rental businesses (such as apply to ATED).

These rules will also apply to certain loans advanced (or guarantees given) to individuals or trusts to purchase residential property, so that the lender will be treated as holding an asset within the charge to inheritance tax.

ii Gift and succession taxes

Since 1984, the United Kingdom has applied an estate tax rather than an inheritance tax, but it is called inheritance tax. As an estate tax, IHT is applied to the deceased’s estate on death and (usually) must be paid before the deceased’s property can be distributed among his or her heirs. A single rate of 40 per cent is applied across a UK-domiciled deceased’s worldwide estate, above a tax-free ‘nil rate band’ currently of £325,000.

Unlike jurisdictions that apply a genuine IHT, in the United Kingdom differential rates do not apply to legacies to different persons (e.g., reduced rates for gifts to family members) other than to spouses, who are exempted from the IHT, providing they are UK-domiciled or share the domicile of their spouse. There are further exemptions, including for gifts of property to charity or political parties and reliefs (up to 100 per cent of the tax payable) for closely held businesses and agricultural property.

There is no gift tax in the United Kingdom. However, IHT will apply to some transfers made during a lifetime. Any gift made in the seven years prior to death will be included in the value of the deceased’s estate for the purposes of assessing the total IHT liability, although the rate of tax is reduced on gifts made at least three years before death. Since 2006, most transfers into trusts are immediately subject to IHT at the lifetime rate of 20 per cent, with
additional tax to pay, up to the 40 per cent rate, if the donor dies within seven years of the transfer. The same exemptions for gifts to spouses and charities and reliefs for closely held businesses and agricultural property will be available, as on death.

As is the case in respect of personal taxation, non-UK-domiciled persons (whether resident or non-resident) enjoy a privileged position in that they are only subject to IHT on their UK situs assets, subject to the exception for indirectly held UK residential property set out above. However, unlike with direct taxation, there is a sunset provision, so that non-UK-domiciled persons who have been resident in the United Kingdom in 15 of the preceding 20 tax years are deemed domiciled in the United Kingdom for the purposes of IHT, in any event (again subject to the enactment of the necessary legislation).

This has caused some quirks in the administration of IHT. However, to address one long-standing anomaly a non-domiciled spouse may now elect to be domiciled for UK IHT purposes and the limited spouse exemption for transfers between domiciled and non-domiciled spouses has been extended from £55,000 to £325,000 and linked to the value of the nil rate band.

Since 2006, when the treatment of lifetime transfers into trust was changed so that most transfers became subject to an immediate charge to IHT, which has recently remained largely unaltered. One consequence of the current fiscal austerity has been that the nil rate band of £325,000 that was previously increased each year in line with inflation has been frozen since 2009 and is planned to remain frozen until 2018.

### Cross-border structuring

The United Kingdom has been at the forefront of the international moves to recover unpaid tax liabilities in respect of funds held outside the home jurisdiction. In addition to a number of general and targeted amnesties in the United Kingdom, it has entered into high-profile agreements with Switzerland, Jersey, Guernsey, the Isle of Man and Liechtenstein to enable it to recover unpaid tax liabilities, in respect of funds held offshore.

#### The UK-Swiss agreement

The Swiss agreement provides that there will be a one-off withholding tax applied on funds held in Switzerland that have not been disclosed to HMRC in respect of all past tax liabilities.

From 2013, withholding taxes of 48 per cent on interest income, 40 per cent on dividend income and 27 per cent on capital gains will be applied to all accounts held by UK taxpayers unless the account holder discloses the account to HMRC.

#### The Liechtenstein disclosure facility

The Liechtenstein disclosure facility was the forerunner of the UK-Swiss Agreement and provides an alternative mechanism whereby, for five years from 2009, UK taxpayers can regularise their affairs with HMRC.

The facility allows individuals with assets formed, administered or managed in Liechtenstein to disclose past tax irregularities without fear of criminal prosecution; however, unlike the UK-Swiss Agreement, there is no provision for ongoing withholding taxes or a general withholding levied on all undeclared accounts. This effective amnesty, now closed, provided for the repatriation of significant undeclared funds.
The Jersey, Guernsey and Isle of Man disclosure facilities

The United Kingdom has entered into memorandums of understanding with Jersey, Guernsey and the Isle of Man, setting out further respective disclosure facilities providing UK taxpayers with assets in these jurisdictions the opportunity to bring their UK tax affairs up to date. The disclosure facilities ran from 6 April 2013 until 30 September 2016.

Transparency

The United Kingdom also remains at the forefront of moves to create a new global reporting standard, as well as registers of public ownership of companies and trusts. From 1 April 2016, UK incorporated companies must prepare a publicly available register of ‘persons with significant control’ that can be used to identify beneficial shareholders of those companies. Plans have also been announced for a public register of owners of UK residential property owned by non-resident companies.

iv Entrepreneurs and business owners

It is a stated aim of the current UK government to encourage business and entrepreneurship through the tax system and a number of recent changes have been implemented to achieve this.

When the current government came to power in 2010, it created the Office of Tax Simplification to provide independent advice on reducing the complexities of the UK tax system and the consequential burdens on business. The office has reported this year on a number of issues, but whether it will have any significant effect on the complexity of legislation is not yet clear.

The main rate of corporation tax was reduced from 28 per cent in 2010 to 24 per cent in 2012, 23 per cent in 2013, and now, in 2016, to 21 per cent, with a long-term goal of reducing it to 17 per cent.

From the business owners’ point of view, the amount of capital gains that can qualify for entrepreneurs’ relief, under which the rate of capital gains tax on the sale of businesses or business assets is reduced to 10 per cent, has been kept at the £10 million level that was introduced in 2011; however, a new parallel ‘investors’ relief’ that also reduces the tax rate to 10 per cent on the sale of certain private company shares was introduced in 2015.

Dividends are also subject to more favourable tax rates in the United Kingdom than either interest or earned income, as set out in the table above.

III SUCCESSION

i UK succession rules

A fundamental principle of succession law in the United Kingdom is the freedom of testamentary disposition, so that individuals are generally free to dispose of their estates to whomever they wish and are not subject to forced heirship rules. Only in the absence of a will does the UK mandate how an individual’s estate should be divided.

However, for UK domiciliary residents there are some constraints on this freedom under the Inheritance (Provision for Family and Dependants) Act 1975. This Act provides that a surviving spouse or civil partner will have similar rights to provision from a deceased person’s estate as they would have on divorce. Other family members and dependants also have the right to be provided for from a decedent’s estate, although the level of provision is not prescribed.
Non-UK domiciliary residents are again treated differently from UK domiciliary residents. While the United Kingdom will apply UK law to the devolution of real property situate in the United Kingdom, it will apply the law of the deceased’s domicile to the devolution of their personal property situated in the United Kingdom.

The United Kingdom has not adopted the EU Regulation on Succession and Wills.

ii Matrimonial issues

Division of assets on divorce

In England and Wales, the court has wide powers to make financial provision when a marriage or a civil partnership breaks down, which can include ongoing maintenance payments, provision for children and the adjustment or variation of interests in trusts and other property, as well as the payment of lump sums.

The court has a wide discretion to determine what would be a fair financial outcome for both parties, having regard to all of the circumstances of the case at that time. It will take into account all of the assets of both parties (whether liquid or illiquid and from whatever source and wherever located in the world) including trust interests, assets acquired prior to the marriage and or by way of inheritance, in determining the appropriate financial division and level of provision to be made.

There is no mathematical formula for working out the appropriate division of assets and income. The aim is to achieve a division that is fair, but the court has emphasised that a 50:50 division of assets is frequently the correct result unless there are compelling reasons to the contrary, such as one party having entered a short to moderately long marriage with significantly greater assets than the other. If the court departs from equality, it should give reasons for doing so.

In the joined cases of Miller and McFarlane, the House of Lords drew a distinction between matrimonial property (being property and assets acquired during the marriage through common endeavour) and other property and assets (such as that brought into the marriage or acquired by inheritance or gift during the marriage). Relevant factors used to distinguish these categories of the property would involve assessing its nature and value; the time when and circumstances in which it was acquired; and the way in which it was used during the marriage.

To the extent that the pre-acquired and inherited wealth is kept largely separate and not used as a resource for funding lifestyle during the marriage or civil partnership, it may be possible to protect it and for it to be retained intact in the event of future divorce or dissolution proceedings, subject to any needs-based claim of the other spouse or partner. This is less so if pre-acquired or inherited assets have been used as a family resource during the marriage or civil partnership.

In the exercise of its discretion, the court will always strive to meet the needs of both parties, even if that results in the division of value and potential realisation of pre-acquired or inherited assets.

**Prenuptial agreements**

For many years, prenuptial agreements were not treated as binding or even influential by English courts, but in recent years there have been moves to increase their importance. The leading authority on prenuptial agreements is now the case of *Radmacher v. Granatino*. The essential point of principle arising from the Supreme Court decision in that case is that:

The Court should give effect to a nuptial agreement that is entered into freely by each party with a full appreciation of its implications unless in the circumstances prevailing it would not be fair to hold the parties to their agreement.

The Supreme Court did not set out clear guidelines for judges or lawyers about when and in what circumstances prenuptial agreements would be regarded as fair or unfair. Instead, it said this would depend upon the facts of each particular case, and, if a prenuptial agreement is to be entered into, clear advice should be taken on the procedure.

The Law Commission (the body that advises the government about law reform) published a report in February 2014 considering the role of prenuptial agreements under English law. The report proposed, in particular, that nuptial agreements should be legally binding provided they adhere to procedural safeguards and formation requirements.

**Same-sex marriage**

The Civil Partnership Act 2004 introduced a new legal relationship, distinct from marriage, between same-sex couples. Civil partners have the same legal rights and responsibilities as married couples in many respects, but the institutions are not identical.

A change in the law, which came into effect on 5 December 2011, now enables civil partnerships to be registered on religious premises where religious organisations permit this, and the premises have been approved for the purpose. The new law also states, for the avoidance of doubt, that religious organisations will not be obliged to host civil partnership registrations if they do not wish to do so.

The Marriage (Same Sex) Couples Act 2013 came into force on 13 March 2014, enabling same-sex couples to marry and civil partners to convert their partnerships into marriages.

The government published a formal review on the future of civil partnerships on 26 June 2014, as required by the Act, announcing that it did not intend to make any changes to their operation.

**IV WEALTH STRUCTURING & REGULATION**

i Onshore wealth structuring

Historically, the most commonly used vehicle for wealth structuring onshore in the United Kingdom was the trust, which provided a tax-efficient mechanism through which to separate legal ownership from the beneficial enjoyment of assets; however, following changes to the taxation of trusts in 2006, they have declined in popularity.

The 2006 changes meant that most transfers into trust above the amount of the nil rate band are taxed to IHT at the lifetime transfer rate of 20 per cent and further IHT charges, at a rate of up to 6 per cent are imposed every 10 years. In addition to this, UK-resident trusts are now subject to income and capital gains tax at the highest individual rates: 45 per cent for income and 28 per cent for capital gains.

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4 [2010] UKSC 42.
This has led UK practitioners to look increasingly for alternative structures for wealth structuring. The objective of many structures is now to implement a control structure, while retaining the tax profile of direct ownership. This has led, for example, to the increased use of family limited partnership and family investment company structures.

For individuals seeking to achieve a more beneficial tax profile, the reduction in the rate of corporation tax has increased the attraction of the use of family holding companies. Where profits are accumulated, these can benefit from the lower rates of corporation tax and the exemption from corporation tax of dividends. In addition, by creating different classes of shares with different rights it is possible to achieve a variety of estate planning objectives.

ii Offshore wealth structuring

The United Kingdom’s anti-avoidance rules have largely precluded UK domiciliary residents from structuring wealth offshore, but for non-UK domiciliary residents residing in the United Kingdom, offshore trusts can offer very significant advantages in terms of protecting assets from UK capital gains tax and inheritance tax.

Foundations, which are being adopted in other common law jurisdictions such as the Channel Islands, have no parallel in UK law and are treated for tax purposes either as trusts or companies, depending on the particular structure employed.

V CONCLUSIONS & OUTLOOK

The United Kingdom’s response to the credit crisis and subsequent recession has largely been to increase the burden of indirect taxation (by an increase in VAT) and to reduce corporation tax rates in a bid to encourage enterprise. Although the higher rate of income tax at 50 per cent was introduced in 2010, this was reduced to 45 per cent in 2013 and the United Kingdom has not seen the more draconian proposals put forward by some of its neighbours.

At the macro level in particular it seems to have struck a better balance in its tax system. The introduction of the remittance basis charge allows non-domiciliary residents to demonstrate that they contribute to the UK exchequer and has largely defused the debate as to whether the regime should be abolished in its entirety. At the same time the United Kingdom has sought to increase the perception of its tax system as one that is friendly and stable, not necessarily seeking to be a low-tax jurisdiction but a stable one in which individuals can base themselves for the long term, without undue concern as to the risk of legislative change. This, however, has not been borne out in practice, with successive governments introducing progressive changes, particularly to the taxation of high net worth individuals, that have made long-term planning challenging.

At a micro level, the continued emphasis on countering tax avoidance has made planning for individuals more complicated, as advisers have to take into account not only the relative certainties of the letter of the law, but also in considering the GAAR, the spirit and intent of that legislation in analysing appropriate planning techniques.

In the coming years, it seems that the United Kingdom will seek to consolidate its position as a relatively low-tax jurisdiction among the large developed economies, especially for corporates. While pressure may continue on tax revenues, it seems that any further legislative change will be in the form of targeted measures, such as the new taxes on high-value residential property, rather than a general increase in tax rates.
INTRODUCTION

In the past several years there have been a number of developments in the United States that have had significant implications for wealthy families and their advisers. These include, for example, the enactment of the Foreign Account Tax Compliance Act (FATCA) in 2010, which increased transparency by requiring the cross-border exchange of tax-related information, and the passage of estate and gift tax legislation that ‘permanently’ fixed tax rates and exemptions that had been in flux for a number of years.

Another recent development aimed at increasing transparency is a new Internal Revenue Service (IRS) regulation that treats a US disregarded entity wholly owned, directly or indirectly, by a non-resident alien as a domestic corporation separate from its owner for disclosure purposes under Section 6038A of the Internal Revenue Code of 1986, as amended (the Code). Under the new rule, disregarded entities must now file IRS Form 5472 (which requires an employer identification number) when reportable transactions occur during the tax year and maintain records for reportable transactions involving the entities’ non-resident alien owners or other foreign parties. The new disclosure rules are particularly relevant for non-resident aliens who wish to purchase real estate through a disregarded entity for privacy reasons. As such, non-resident aliens should also be aware of a new US Department of the Treasury Financial Crimes Enforcement Network’s (FinCEN) Geographic Targeting Order (GTO), which requires the disclosure by any title company involved in a real property transaction of identifying information on a FinCEN Form 8300 for qualifying transactions.

Perhaps the most dramatic force of change in the international private client world in recent years, and one in which the United States is not a participant, is the enactment of the Common Reporting Standard (CRS), the reciprocal automatic information exchange agreement developed by the Organisation for Economic Co-operation and Development that was adopted recently in over 100 jurisdictions and is being phased into effect through 2018. Under CRS, entities (including trusts and foundations) must report information on ‘controlling persons’. The broad reporting requirements create significant compliance burdens and challenges for trustees and financial institutions dealing with trusts. For entities, the controlling persons generally are the individuals who exercise control over the entity or who have a direct or indirect controlling ownership interest in the entity. For a trust, the...
controlling persons are defined to include the settlors, the trustees, the protectors (if any), the beneficiaries or class of beneficiaries, and any other natural persons exercising, directly or indirectly, control over the trust.

Although the United States is not a party to CRS, the global reach of CRS will make cooperation of teams of advisers across multiple relevant jurisdictions much more important. For example, US citizens and residents who are ‘controlling persons’ of non-US trusts will be required by trustees and financial institutions to provide ‘self-certification’ information, including their country of tax residence and tax identification numbers. US advisers involved in cross-border structuring will need to be mindful of CRS requirements and the residences of the various individuals involved in trust, foundation and similar structures. Some commentators have suggested that the United States has become an attractive jurisdiction for non-US persons wishing to maintain their privacy.

On the domestic front, President Trump’s proposed tax reform could have significant implications for US estate planning, if enacted. President Trump’s reform would reduce the number of tax brackets from seven to three, and reduce the top tax bracket to 35 per cent. Perhaps most notably, President Trump’s reform also proposes the elimination of the estate tax.

This chapter surveys tax liability, estate planning and wealth management under current US law. Section II of this chapter provides an overview of the US tax system for individuals, including income tax, transfer taxes, and reporting requirements for offshore assets. Section III, infra, summarises the laws of succession in the US, including the estate planning implications of marriage and divorce. Finally, Section IV, infra, discusses the different strategies of wealth management that can minimise US federal and state transfer taxes.

II TAX

i Income tax

US citizens (regardless of where they reside) and residents (collectively, US persons) are subject to US income tax on worldwide income.2 On the other hand, individuals who are neither citizens nor residents of the United States (non-resident aliens) are subject to US income tax only on certain types of US-sourced income, income effectively connected with a US trade or business and gains on the sale of US situs real property.3

A non-citizen of the United States is considered a resident of the United States for income tax purposes if the individual:

- is admitted for permanent residence (i.e., holds a ‘green card’);
- elects to be treated as such; or
- has a ‘substantial presence’ in the United States in a given calendar year.4

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2 IRC Section 61. The top federal individual income tax rate for ordinary income in 2017 is 39.6 per cent, with a lower 20 per cent rate applied to long-term capital gains and qualified dividends. Net investment income may also be subject to an additional 3.8 per cent Medicare surtax. President Trump has proposed tax reform that would reduce the top tax bracket to 35 per cent, include investment interest in income subject to the lower capital gains rate, and eliminate the 3.8 per cent Medicare surtax.
3 IRC Sections 871, 897.
4 IRC Section 7701(b)(1)(A).
An individual satisfies the substantial presence test and is deemed a resident if he or she has been present in the United States for at least 31 days in the current year and for at least 183 days during a three-year period that includes the current year, determined based upon a weighted three-year average.\(^5\)

The use of this ‘weighted average’ can become a trap for individuals who focus only on the total day count and who believe that they can spend up to 182 days each year in the United States without having a ‘substantial presence’ that will cause them to be considered a US resident for income tax purposes. Under the weighted average test, a person may spend, on average, up to 120 days in the United States each year without being treated as a US income tax resident under the substantial presence test. An individual who meets the substantial presence test but spends less than 183 days in the United States in a year can still avoid being treated as a US income tax resident if he or she can establish that the individual maintains his or her tax home in another jurisdiction and maintains a ‘closer connection’ to such foreign tax home by filing a Form 8840 ‘Closer Connection Exception Statement for Aliens’ with the IRS.\(^6\) It is also important to consider whether a non-US citizen may be entitled to protection under a tax treaty between the United States and the jurisdiction the individual considers to be his or her home.

\section*{Gift, estate and GST tax}

There are three types of US federal transfer taxes: estate tax, gift tax and generation-skipping transfer (GST) tax (collectively referred to as transfer taxes). US citizens and US residents are subject to transfer taxes on worldwide assets.\(^7\) The test to determine whether an individual is a US resident for transfer tax purposes is different from the test to determine whether an individual is a US resident for income tax purposes. Whereas the residence test for income tax purposes, as discussed above, is an objective test, residence for the purpose of transfer taxes is determined by a subjective domicile test, turning on the individual's intentions. A person is a US resident for transfer tax purposes if he or she is domiciled in the United States at the time of the transfer.\(^8\) A person can acquire domicile in a place by living there, for even a short period of time, with the intention of remaining there indefinitely.\(^9\)

Subject to provisions of an applicable treaty, a non-US citizen who is not domiciled in the United States is subject to US transfer taxes only on property deemed situated in the United States (US situs assets), including US real estate (which includes condominium apartments) and tangible personal property located in the United States. Shares in US corporations, debt obligations of US persons (subject to important exceptions for certain portfolio debt and bank deposits), and certain intangible property rights issued by or enforceable against US persons are subject to US estate tax but not US gift tax.

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\(^5\) The weighted average test takes into account all of the days of presence in the United States in the current calendar year, one-third of the days in the first preceding calendar year and one-sixth of the days in the second preceding calendar year. Treas. Reg. Sections 301.7701(b)-1(c)(1), (4).

\(^6\) Treas. Reg. Section 301.7701(d)-1.

\(^7\) I.R.C. Sections 2031(a), 2511(a), 2612.


Current income and transfer tax rates

The American Taxpayer Relief Act of 2012 (ATRA) was enacted on 2 January 2013. ATRA allowed the reduced Bush-era income tax rates to sunset after 2012 for individuals with incomes over US$400,000 and married couples filing jointly with incomes over US$450,000. Under ATRA and currently, the top US individual income tax rate is 39.6 per cent for ordinary income and 20 per cent for qualified dividends and long-term capital gains. The lifetime exemption from US gift, estate and GST taxes for US citizens and residents is set at US$5 million (US$10 million for a married couple), indexed for inflation from 2010 for gifts made and for estates of decedents dying after 31 December 2011 (for 2017, the indexed exemption is US$5.49 million for an individual and US$10.98 million for a married couple). The top transfer tax rate is currently 40 per cent.

US citizens and residents for transfer tax purposes may also take advantage of ‘portability’, which permits such persons to use the unused transfer tax exemption amount of the taxpayer’s deceased spouse (if he or she died after 31 December 2010). If a taxpayer is predeceased by more than one spouse, the taxpayer may use the unused transfer tax exemption of the last deceased spouse only. The executor of the deceased spouse’s estate must make an election on the deceased spouse's estate tax return to allow the surviving spouse to use the deceased spouse’s unused transfer tax exemption. The estate of an individual who was a non-resident alien of the United States for transfer tax purposes at the time of such individual’s death is not eligible to make a portability election, and thus such individual’s lifetime exemption from US transfer taxes (which is only US$60,000) cannot be passed on to his or her surviving spouse. More significantly, a non-resident alien surviving spouse may not acquire his or her deceased US spouse's unused lifetime exemption (except to the extent allowed under a US treaty). However, a surviving spouse who becomes a US citizen after the death of the deceased spouse may elect to use the unused transfer exemption of the deceased spouse.

President Trump's tax reform proposal includes repealing the estate tax. It is unclear whether a repeal of the gift and GST taxes also will be proposed. Elimination of the estate tax, but not the gift tax, would make it preferable to hold assets until death, at which point they could be transferred tax-free. Elimination of both the estate and gift taxes (along with the GST tax) would allow individuals to transfer assets without taxation either during life or at death.

Medicare surcharge

The net investment income tax (NIIT) is part of the funding of Obamacare and dictates that citizens and residents of the United States (i.e., any individual other than a non-resident alien) must pay an additional 3.8 per cent Medicare tax on the lesser of the taxpayer’s ‘net investment income’, and the excess of the taxpayer’s modified adjusted gross income (as calculated for income tax purposes) for the taxable year over a certain threshold amount. Likewise, trusts and estates must pay an additional 3.8 per cent tax on the lesser of the trust’s ‘net investment income’, and the excess of adjusted gross income (as calculated by a trust or estate for other income tax purposes) over the dollar amount of the highest tax bracket for a trust or estate for the applicable tax year.
In general, net investment income includes three broad categories of income: (1) gross income from certain interest, dividends, annuities (including annuities received from a charitable remainder trust), royalties and rents; (2) gross income derived from a business in which the taxpayer does not materially participate (income from a trade or business that is a passive activity is subject to the NIIT) or from trading in financial instruments or commodities; and (3) net gains attributable to the disposition of property, other than property held in a trade or business not described in category (1).

iv Reporting requirements and penalties
This section discusses a few of the US disclosure and reporting requirements that are of particular interest to individuals with both US and international interests, but is not an exhaustive list.

**IRS Forms 3520 and 3520-A**

A US person (including a US trust) who: (1) engages in certain transactions with a foreign trust, including creating a foreign trust (whether or not the trust has US beneficiaries) or transferring money or property, directly or indirectly, to a foreign trust; (2) receives a distribution (including a loan) of any amount from a non-US grantor or non-grantor trust; or (3) receives more than US$100,000 in gifts or bequests from a non-US person or a foreign estate or more than a specified amount (in 2016, US$15,671) from foreign corporations or foreign partnerships in any year, must report such amounts on IRS Form 3520 (Annual Return to Report Transactions With Foreign Trusts and Receipt of Certain Foreign Gifts).

Such US person must file a Form 3520 for the year in which any such transfer, distribution, gift or bequest is made by the due date of such person’s federal income tax return for that year, even if the individual is not subject to US income tax on the amount. If an individual fails to file a required Form 3520, a penalty may be imposed in the amount of the greater of US$10,000 or: (1) 35 per cent of the gross value of the property transferred to a foreign trust for failure by a US transferor to report the creation of or transfer to a foreign trust; (2) 35 per cent of the gross value of the distributions received from a foreign trust for failure by a US person to report receipt of the distribution; or (3) 5 per cent of the gross value of the trust. Additional penalties for subsequent filing failures may follow.

In addition, the trustee of a foreign trust with a US owner must file Form 3520-A (Annual Information Return of Foreign Trust a US Owner) in order for the US owner to satisfy its annual information reporting requirements.

**FBAR**

If a US person has a financial interest in or signature or other authority over any bank, securities, or other type of financial account outside of the US, and if the aggregate value of all such accounts exceeds US$10,000 at any time during the calendar year, that person must report such interest for such calendar year. For calendar year 2016, accounts due in 2017 and subsequent years, such report is made on FinCEN Form 114 (referred to as an FBAR form).

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13 If the trust owns an interest in a controlled foreign corporation (CFC) or a passive foreign investment company (PFIC), a US beneficiary may have additional reporting requirements.

14 US law requires a US beneficiary of a non-US trust to obtain from the trustee of a non-US trust a detailed statement of distributions made from the trust to enable the US beneficiary to complete the Form 3520. If such a statement is not filed with the IRS, the distribution could be treated for US income tax purposes as being a distribution of undistributed net income.
on or before 15 April of the succeeding year, with a potential six-month filing extension. For purposes of the FBAR rules, a US person is considered to have a financial interest in an account where title to the account is held by a grantor trust and such US person is the grantor of such trust. A US person is also deemed to have a financial interest in an account owned by a trust in which the US person has a present beneficial interest in more than 50 per cent of the assets or current income. Such beneficiary is, however, not required to report the trust’s foreign financial accounts on an FBAR form if the trust, trustee of the trust, or agent of the trust: (1) is a US person; and (2) files an FBAR disclosing the trust’s foreign financial accounts.

The IRS had initially taken the aggressive position that a beneficiary of a discretionary trust in which the trustee has discretion to distribute more than 50 per cent of the income or principal to the beneficiary (even if the trustee never has made any distributions to such beneficiary) has the requisite present financial interest to require the filing of an FBAR form. However, the preamble to the final regulations released on 24 February 2011, which became effective on 28 March 2011, indicates that a beneficiary of a discretionary trust should not be considered as having a financial interest in such trust requiring an FBAR filing merely because of such person’s status as a discretionary beneficiary.

**FATCA**

FATCA has helped accelerate the global drive towards greater transparency and scrutiny of offshore assets. Under FATCA, enacted in 2010 as part of the HIRE Act (see Section II.v, The HIRE ACT, infra), foreign financial institutions (FFIs) are required to either enter into an agreement with the IRS under which they agree to report to the IRS certain details about their accounts directly or indirectly held by US persons (US accounts) or become ‘deemed compliant’ under the regulations. Non-financial foreign entities (NFFEs) that are publicly traded or engaged in active trading are not required to enter into or comply with an FFI agreement. However, FATCA does require certain ‘passive NFFEs’ (generally NFFEs earning mostly passive income that are not publicly traded) to report to withholding agents and participating FFIs with which the NFFE holds accounts, information on their ‘substantial US owners’ (described in footnote 16), or to certify annually that they have no substantial US owners. FATCA is being implemented in stages as provided in the final regulations released in 2013. Because the United States does not have direct jurisdiction over most FFIs, FATCA compels compliance by imposing a 30 per cent withholding tax on US-sourced income earned after 30 June 2014 and proceeds from the sale of US property after 31 December 2016 on all FFIs that do not agree to provide the IRS with the required information.

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15 US accounts include accounts held by US-owned entities. IRC Section 1471(d)(1). A US-owned entity is an entity with ‘Substantial US Owners’. IRC Section 1471(d)(3). Generally, an entity has Substantial US Owners if a US person owns more than a 10 per cent interest in the entity. IRC Section 1473(2)(A). However, in the case of investment entities, any US ownership will cause it to be a US-owned foreign entity. IRC Section 1473(2)(B). A foreign non-grantor trust would be a US-owned entity if any specified US person holds, directly or indirectly, more than 10 per cent of the beneficial interest in the trust. IRC Section 1473(2)(A)(iii).

16 IRC Section 1473(2)(A); Treas. Reg. Section 1.1471-4(d)(iii)(B)(3). As an alternative, the regulations permit an NFFE to report directly to the IRS certain information about its direct or indirect substantial US owners, rather than to a withholding agent, by electing to become a ‘direct reporting NFFE’.

17 IRC Section 1471 (a)-(b). Withholding on the gross proceeds from the sale or other disposition of property of a type that can produce interest or dividends or dividends that are US source FDAP income will...
The definition of an FFI is broad, including any entity that ‘accepts deposits in the ordinary course of a banking or similar business’, holds financial assets for the account of others ‘as a substantial part of its business’, or is engaged primarily in the business of investing, reinvesting or trading in securities, partnership interests, commodities or any interests therein and would include most investment vehicles unless a specific exception applies. Under this definition, foreign trusts with corporate trustees acting for different customers (including, in most cases, a private trust company that retains outside investment advisers or receives fees for its services) will be FFIs if, in general, 50 per cent or more of the trust’s gross income is attributable to investing in financial assets. A foreign trust that is not an FFI (for instance, a trust managed by an individual trustee) will generally be an NFFE.

Since the implementation of FATCA began, the Treasury Department has entered into many intergovernmental agreements (IGAs) to facilitate the implementation of FATCA. The purpose of IGAs is to remove domestic legal impediments to compliance with FATCA requirements and to reduce burdens on FFIs located in jurisdictions that enter into IGAs (partner jurisdictions). There are two models of IGAs. Under the Model 1 IGAs, covered FFIs report FATCA information to government agencies in their own jurisdiction, which then transmits the information to the IRS. Under the Model 2 IGAs, a partner jurisdiction agrees to facilitate FATCA compliance by its resident FFIs, but those FFIs generally must still register with the IRS and report information about US accounts directly to the IRS.

Despite early opposition to FATCA in many cases, partner jurisdictions are entering into bilateral IGA agreements whereby they will provide information to the United States in exchange for an agreement from the United States to provide such partner jurisdiction with FATCA-like information regarding financial accounts held by the citizens of such partner jurisdiction in the United States. Despite early predictions from some that FATCA would isolate the United States, to a large extent FATCA appears to be evolving into one part of a global system of mutual information sharing, although the impact of FATCA on the willingness of non-US entities to invest in US assets remains to be seen.

Despite growing international acceptance of FATCA, aspects of its implementation remain contentious. For example, the National Taxpayer Advocate has urged the IRS to develop fact-specific guidelines that explain how benign non-filers can obtain a finding of reasonable cause. Critics continue to claim that the reporting requirements are too burdensome and inefficient, especially because some estimates indicate that the cost of enforcing FATCA may be higher than the revenue produced by it. Overall, the impact of FATCA is yet to be understood as the IRS has announced that some provisions will not take effect until as late as 2018. Additionally, some early signs of push-back are emerging, such as certain non-US financial institutions’ reluctance or flat refusal to take on new US clients.

18 IRC Section 1471(d)(4)-(5).
19 Treas. Reg. Section 1.1471-5(e)(4).
21 A 2014 report to the Senate Finance Committee by Democrats Abroad details refusals to take on American clients or closures of US citizen accounts in Belgium, Israel, France, Switzerland and Germany. See Democrats Abroad, October 2014 FATCA Research Project, available at: www.finance.senate.gov/download/art-5-democrats-abroad-2014-fatca-research-stories&download=1. Several media sources have documented foreign banks closing down or refusing accounts held by US citizens (CNN: http://
**Form 8938**

In addition to the reporting and withholding requirements discussed above, FATCA also requires certain individual taxpayers, including US citizens or green card holders permanently residing abroad, with interests in certain foreign financial assets with an aggregate value greater than US$50,000 on the last day of the tax year, or greater than US$75,000 at any time during the tax year, to file Form 8938 (Statement of Specified Foreign Financial Assets), reporting the interest with such individual’s federal income tax return. The obligation to file Form 8938 is in addition to, not in replacement of, any filing obligation such individual may have under the FBAR rules. Whether a US person beneficiary of a discretionary non-US trust will be required to report his or her interest in the trust on a Form 8938 will depend on many factors, including whether such individual received a distribution from the trust in a given tax year and the value of the individual’s interest in other foreign financial assets.

**Forms BE-10 and BE-11**

The BE-10 is a benchmark survey of US investment abroad conducted every five years. The last BE-10 reporting year was 2015 (with those reports including information with respect to 2014). Prior surveys had required only US persons contacted by the Bureau of Economic Analysis (BEA) to file, but a final rule promulgated by the BEA in the Federal Register on 20 November 2014 stated that any US person with a foreign affiliate is required to file a BE-10 report every five years. The final rule marks a significant expansion of US persons obligated to file a BE-10 report. The expansion does not apply to other BEA forms, such as the BE-11 form (Annual Survey of US Direct Investment Abroad), which entities are required to file annually, but only if requested to do so by the BEA. The term ‘US person’ means any natural person or entity resident in the United States or subject to the jurisdiction of the United States, and includes any individual, estate, trust, branch, partnership, associated group, association, private fund, corporation, or other organisation, regardless of whether it is organised under the laws of any state. A foreign affiliate is a foreign business enterprise in which a US person had direct or indirect ownership or control of 10 per cent or more of the voting stock or equivalent interest at any time over the US person’s fiscal year. Generally, a US person’s foreign operation or activity is considered a foreign business enterprise if it is legally separable from the domestic operations or activities of the US person.

**Form 5472**

Generally, except in the case of corporations (or entities that elect to be treated as corporations), a US entity that has a single owner is disregarded as separate from its owner. However, in late 2016, the IRS finalised new regulations that treat a US disregarded entity wholly owned, directly or indirectly, by a non-resident alien as a domestic corporation separate from its owner for Code Section 6038A disclosure purposes. This change means that such entities are required to make additional disclosures when participating in certain transactions.

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Under the new rule, these entities must now file IRS Form 5472 (which requires an employer identification number) when reportable transactions occur during the tax year, and must maintain records of reportable transactions involving the entities’ non-resident alien owners or other foreign parties. The regulation classifies transactions such as any sale, lease, or other transfer of any interest in or a right to use any property as reportable transactions. In order to acquire an employer identification number, the owner may have to obtain an individual taxpayer identification number (as they also would when buying property individually), which many non-resident aliens hope to avoid. Since the new rule became effective for entities’ tax years beginning on or after 1 January 2017, owners without individual taxpayer identification numbers who are required to make these disclosures under Section 6038A should begin the application process as soon as possible in preparation for filing the necessary forms in early 2018. The new disclosure rules are particularly relevant for non-resident aliens who wish to purchase real estate through a disregarded entity for privacy reasons. As such, non-resident aliens should also be aware of a new FinCEN Geographic Targeting Order (GTO) that requires the disclosure by the title company involved in the transaction of identifying information on a FinCEN Form 8300 for qualifying transactions.23

The GTO’s disclosure requirements are applicable to all purchases paid for by cash or cheque of US$3 million or more in Manhattan and US$1.5 million or more in all other boroughs of New York City. The GTO requirements also apply to purchases of US$1 million or more in Miami-Dade, Broward and Palm Beach counties in Florida, as well as purchases of US$2 million or more in San Diego, Los Angeles, San Francisco, San Mateo and Santa Clara counties in California.

A Form 8300 must include information about the identity of the purchaser, the purchaser’s representative, and the beneficial owners, as well as information about the transaction itself, including the closing date, payment amount, purchase price and address of the real property involved in the transaction. In addition, the form requires disclosures about the entity used to purchase the property, including the names, addresses and taxpayer identification numbers for all members, and the reporter must obtain copies of driver’s licences, passports or similar documents from the purchaser, the purchaser’s representative and the beneficial owners.

The purpose of the GTO is to provide law enforcement with data to improve efforts to address money laundering in the real estate sector. The GTO went into effect on 24 February 2017, is effective for 180 days, and likely will be extended.

v  Scrutiny of non-US trusts by the US government

The environment in the United States continues to be hostile towards non-US trusts, as the US government perceives such trusts as potential tax avoidance vehicles.

The HIRE Act

The Hiring Incentives to Restore Employment Act (HIRE), in effect since 2010, broadened the range of non-US trusts considered to have US beneficiaries, resulting in tax liability under the grantor trust rules where the trust had been created by a US grantor. Under the Code,

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a non-US trust with US beneficiaries that is created by a US grantor is treated as a grantor
trust for US income tax purposes, meaning that the US grantor must include the income
of the trust in his or her personal income tax return. HIRE provides that a non-US trust is
considered to have a US beneficiary even if a US person holds only a contingent interest and
even if no US person is expected to receive any distribution, but a distribution (including
by exercise of limited power of appointment) to a US person is permissible under the trust
instrument. HIRE also establishes a presumption that a non-US trust to which a US person
has transferred property has a US beneficiary unless the transferor furnishes information to
the Treasury Department sufficient to rebut this presumption.

Importantly, HIRE treats the use of a non-US trust’s property by a US person as a
distribution to such person equal to the fair market value of the use of such property, to the
extent the US person does not pay fair market value rent for the use of such property.

vi Consequences of non-compliance with US tax and reporting requirements
There has been much publicity about the US government’s attempts to uncover tax
non-compliance with respect to offshore assets, especially in light of the need for increased
revenues.

Offshore voluntary disclosure programme
The IRS began an open-ended offshore voluntary disclosure programme (OVDP) in 2012 to
courage taxpayers to come forward to report previously undisclosed foreign accounts,
assets and income for the most recent eight tax years for which the due date has already
passed. OVDP is open to all taxpayers.

Participants in the OVDP, in addition to paying any taxes and interest due, along with
applicable accuracy related and delinquency penalties, must generally pay an offshore penalty
equal to 27.5 or 50 per cent of the highest aggregate balance in foreign bank accounts or
entities, or value of foreign assets during the period covered by the voluntary disclosure.24
This value encompasses ‘all of the taxpayer’s offshore holdings that are related in any way to
tax non-compliance, regardless of the form of the taxpayer’s ownership or the character of
the asset’.25 It is important to note that certain taxpayers may qualify for reduced offshore
penalties. The OVDP penalty structure applies in lieu of other applicable civil penalties,

24 The increased 50 per cent penalty applies to taxpayers who submitted OVDP pre-clearance letters to the
IRS after 4 August 2014 and where there has been a public disclosure prior to the pre-clearance letter that
either (a) the foreign financial institution where the account is held, or another facilitator who assisted in
establishing or maintaining the taxpayer’s offshore arrangement, is or has been under investigation by the
IRS or the Department of Justice in connection with accounts that are beneficially owned by a US person;
(b) the foreign financial institution or other facilitator is cooperating with the IRS or the Department
of Justice in connection with accounts that are beneficially owned by a US person; or (c) the foreign
financial institution or other facilitator has been identified in a court-approved issuance of a summons
seeking information about US taxpayers who may hold financial accounts (a ‘John Doe summons’) at
the foreign financial institution or have accounts established or maintained by the facilitator.’ Taxpayers
who disclosed to OVDP before 4 August 2014 or did not use a financial institution or facilitator that
featured in one of the above public disclosures will be penalised at 27.5 per cent. See Offshore Voluntary
Disclosure Program Frequently Asked Questions and Answers, IRS (8 February 2016), available at:
www.irs.gov/individuals/international-taxpayers/offshore-voluntary-disclosure-program-frequently-asked-
questions-and-answers-2012-revised.

25 Id.
including penalties for failure to file an FBAR, failure to file information returns, fraud, failure to file a tax return, failure to pay the amount of tax shown on the return, and accuracy-related penalties on underpayments. Additionally, taxpayers who voluntarily enter the OVDP before the IRS has identified the taxpayer as delinquent may avoid criminal prosecution.

**Streamlined filing compliance procedures**

Since 2014, streamlined filing compliance procedures have expanded from applying only to non-resident US taxpayers to include US persons living inside the United States. Now, all individual taxpayers residing in the United States can participate in the streamlined filing compliance procedures. The individual must execute a ‘certification’ stating that his or her failure to file US tax returns, pay US tax or report reportable assets was non-wilful.

Taxpayers outside the United States who qualify for this procedure will not be liable for any penalty, while those inside the United States will be subject to a 5 per cent ‘miscellaneous offshore penalty’ on the foreign assets that gave rise to the non-compliance. The 5 per cent penalty is in lieu of the standard 50 per cent OVDP penalty. The negative aspect of the streamlined procedure is that, unlike OVDP, it does not protect against criminal prosecution, and once a taxpayer makes a submission under this procedure, OVDP is no longer available.

**Delinquent filings**

If a taxpayer has not been previously contacted by the IRS regarding an income tax examination or a request for delinquent returns, the IRS will not impose a penalty for failure to file delinquent FBARs if the taxpayer: (1) files the delinquent FBAR reports; (2) attaches a statement explaining why the reports are filed late; and (3) has no underreported tax liabilities. FBARs for tax years going forward must still be filed by their due date of 15 April (with the possibility of a six-month extension) of the succeeding year.

A taxpayer who failed to file Form 3520 or Form 5471 (information return of US persons with respect to certain foreign corporations) will not have a penalty imposed on him or her if the taxpayer: (1) has reported and paid tax on all taxable income with respect to all transactions related to the controlled foreign corporations or foreign trusts; (2) files delinquent information returns with the appropriate service centre; and (3) files a statement explaining why the information returns are filed late. The top of the first page of each information return should be marked ‘OVD – FAQ #18’ to ensure proper processing.

**III  SUCCESSION**

i  **Overview**

**State jurisdiction**

In the United States, state law determines how and to whom property will be distributed upon death. Succession law thus varies from state to state, but the fundamental principle underlying American succession law is testamentary freedom, with some exceptions discussed below. The testator’s freedom to determine the disposition of property at death generally is manifested through a will and will substitutes (such as revocable *inter vivos* trusts, contracts, life insurance policies, pension plans and joint accounts). Intestacy statutes provide a default framework for assets not otherwise disposed of by the decedent.
Estate administration

Following an individual’s death, his or her will, if any, is submitted to a state probate court, which validates the will, confirms fiduciary appointments and generally supervises the administration of the estate. As part of the probate process, the will and ancillary documents, which may include a detailed inventory of probate assets, generally become a matter of public record, but this may vary among states. Assets that pass to the surviving joint tenants or by contractual beneficiary designation are considered non-probate assets and therefore are not subject to the probate court process, although such assets generally are still subject to estate tax.26

Because of the potential delay, cost and lack of privacy often associated with the probate process, Americans are increasingly relying on will substitutes, such as revocable inter vivos trusts, which function similarly to a will in that beneficiaries generally receive assets at the donor’s death but differ in that such assets pass pursuant to the existing trust deed, thereby avoiding the need for probate.

If an individual dies without a will and thus dies ‘intestate’, or dies with a will that fails to dispose of all probate assets, the relevant state court appoints an individual, typically the surviving spouse or children, to administer and distribute the intestate property pursuant to the state’s intestacy statute.

ii Property division at death

Elective share right of surviving spouse

While testamentary freedom is the linchpin of US succession law, that freedom is not unfettered. In fact, states have enacted increasingly generous provisions for surviving spouses, often at the expense of surviving children and notwithstanding the testator’s express declarations to the contrary. Virtually all US jurisdictions protect against spousal disinheriting either through community property concepts or elective share laws that entitle spouses to a ‘forced’ share of the decedent spouse’s estate.27 Although state law varies widely in the amount of the elective share and the variables (length of marriage, presence of minor children, surviving spouse’s net worth, etc.) used to determine such amount, most states set the amount between one-third and one-half of the decedent’s estate.28 Spouses in New York, for example, may choose to take the greater of US$50,000 (or, if the net estate is valued at less than US$50,000, the entire net

26 Examples of non-probate assets include the following: property owned and held in joint tenancy, tenancy by the entirety or, in certain states, community property with the right of survivorship; property transferred into an inter vivos trust prior to the settlor’s death; real property subject to transfer under a transfer-on-death deed; assets held in a pay-on-death account or ‘Totten trust’ bank account; proceeds of a life insurance policy; and individual retirement accounts with a named beneficiary.

27 Arizona, California, Idaho, Louisiana, Nevada, New Mexico, Texas, Washington and Wisconsin have community property laws, while the remaining states have elective share laws (Alaska is an opt-in community property state that gives both parties the option to make their property community property). Georgia currently is the only state that does not recognise dower or curtesy, community property or elective share concepts. See Community Property, I.R.S. Pub. No. 555 (2016), available at: www.irs.gov/pub/irs-pdf/p555.pdf; Terry L Turnipseed, ‘Community Property v. The Elective Share’, 72 La. L. Rev. 161, 162 (2011).

28 Note that in the event of intestacy, each state’s intestacy statute will determine the amount to which the surviving spouse is entitled. Elective share laws are thus generally relevant only when a surviving spouse receives less under the decedent spouse’s will than what he or she is entitled to receive as the elective share.
estate) or one-third of the decedent spouse’s net estate in lieu of taking benefits under a will. The amount that passes as the elective share generally qualifies for the marital deduction for federal and state estate tax purposes.

**No forced heirship right of children**

Unlike many civil law systems, no US jurisdiction (with the sole exception of Louisiana, whose laws are predominantly derived from the French Napoleonic Code) recognises forced heirship rights of children. Thus, although testators cannot disinherit spouses, they can freely disinherit children. Even citizens or domiciled individuals of countries that recognise forced heirship rights (such as Switzerland and France) may be able to defeat forced heirship claims with respect to US situs assets by moving such assets to states such as New York, New Jersey or Connecticut (to name a few) that permit non-domiciled individuals to elect to have local law govern the disposition of property located within that state. The decision In the matter of *Renard*, the seminal case involving forced heirship, illustrates this principle. In that case, New York’s highest court upheld a French-domiciled individual’s choice of law direction to have New York law govern the disposition of her assets situated in New York (where she resided for several decades before returning to her native France, leaving behind several financial accounts), thereby defeating her son’s claims to a forced share in such assets under French forced heirship law.

**Succession on intestacy**

When the wishes of a decedent are not expressly known (that is, when the decedent dies without a will or has a will that fails to dispose of all probate property), state intestacy statutes mandate how the decedent’s estate will be divided. These statutes are intended to approximate the ‘presumed will’ of the decedent by enforcing a distributive scheme that the decedent likely would have chosen. Typically, surviving spouses receive a preferential disposition (in some cases, the entirety of the estate) and the balance thereafter, if any, passes to children or, if there are none, to more remote descendants or other family members.

### iii Applicable developments affecting succession

#### Definition of marriage

The Supreme Court in its 2015 decision in *Obergefell v. Hodges* held that states must license marriages between same-sex couples and recognise same-sex marriages performed in other states. (Two years earlier, in *United States v. Windsor*, the Supreme Court invalidated Section 3 of the Defence of Marriage Act (DOMA), which limited the definition of marriage for the purposes of federal law to opposite-sex couples.) Consequently, the tax benefits provided to married couples under state and federal laws are now available to same-sex couples.

29 NY Estates, Powers and Trusts Law (EPTL) Section 5-1.1-A(a)(2).
31 Article 1493 of the Louisiana Civil Code.
Under federal law, these benefits include the ability to utilise the unlimited marital estate tax deduction, split gifts and elect portability. Under state law, same-sex couples should now have succession rights, such as spousal elective share rights, intestate inheritance rights and fiduciary appointments over intestate estates. It should be noted that while this decision has nationwide impact, it must be implemented at the state level. In light of these changes, same-sex couples may wish to re-examine estate and tax planning done before the repeal of DOMA and the elimination of same-sex-marriage bans. For example, same-sex couples may be able to amend past income tax returns for open tax years to elect married filing jointly status, which may result in a lower effective rate of tax. In addition, it is important to note that neither Obergefell nor Windsor altered the legal status of domestic partnerships or civil unions. Thus although civil unions and domestic partnerships confer spousal-like benefits in some states, same-sex couples must marry if they wish to guarantee that their partnerships are on an equal footing with opposite-sex marriages.

Property division on divorce

Under the laws of most states, property acquired or earned by either spouse during marriage generally is considered marital property (or community property), whereas property acquired prior to marriage, acquired by gift or inherited (whether outright or in trust) is considered separate property. As a general rule, an individual’s separate property is not subject to equitable distribution in a divorce proceeding. But conceptions of what types of property should be taken into account in determining equitable distribution of marital property in the event of divorce have changed over time, with some courts taking into account the value of an individual’s separate property in determining what constitutes an equitable distribution of marital property and in setting the amount of spousal maintenance payments.

Moreover, in some states, ‘interests’ in trusts may be considered part of the marital estate in determining the equitable distribution award if the receiving party has a ‘sufficiently concrete, reasonable and justifiable expectation’ of a benefit attached to such interests. This is an evolving area of the law, and it is important to bear in mind that the protection of assets held in trust may be eroding in some states in the divorce context.

Notably, New York courts have in the past taken into account intangible assets, such as business goodwill, professional licences and educational degrees, for the purposes of measuring a spouse’s ‘increased earning capacity’ to value marital property and determine maintenance awards. In 2016, the New York legislature enacted a law that overturned case law that counted enhanced earning capacity as marital property, but the new law does permit courts to take contributions to a spouse’s enhanced earning capacity into account when deciding on the equitable distribution of marital property.

34 Bender v. Bender, 258 Conn. 733, 747-49 (2001) (where court stated that ‘sources of deferred income, such as pension benefits and trust interests, whether vested or not, constitute property subject to distribution, provided that the contingent nature of the interest does not render the interest a mere expectancy’); see also SL v. RL, 55 Mass. App. Ct. 880, 884, 774 N.E.2d 1179, 1182 (2002) (where court held that the wife’s future interest in certain non-marital trusts ‘[was] subject only to her surviving her [then living] mother, a condition [that Massachusetts precedent] considered not to bar inclusion within the marital estate’); In re Marriage of Rhinehart, 704 N.W.2d 677 (Iowa 2005) (where court held that undistributed income from an irrevocable trust was not a marital asset that was subject to division, but that the wife’s future interest in such trust could be considered when determining equitable division of property).


IV WEALTH STRUCTURING & REGULATION

This section focuses on domestic planning strategies for US persons. It provides a short discussion of ‘pre-immigration’ planning for non-resident aliens of the United States who wish to become US residents or citizens. Pre-immigration planning is a separate and complex area and an in-depth discussion is beyond the scope of this chapter.

There are several planning strategies that can be utilised to minimise the effect of US federal and state estate taxes. Lifetime irrevocable trusts are the most popular tool because of the many advantages to making gifts during life, including, for example:

- the avoidance of state transfer tax in jurisdictions with an estate tax, but no gift tax;
- the federal gift tax is tax-exclusive, which means that an individual does not pay tax on the gift tax, whereas the federal estate tax is tax-inclusive, which means a decedent’s estate pays tax on the portion of the estate used to pay estate tax; and
- all the appreciation on assets after the gift is made is outside of the taxable estate at death.

The uncertain future of the US$5 million exemption from US gift, estate and GST taxes caused many individuals to make lifetime exemption gifts before year-end 2012. While ATRA made the exemption amount ‘permanent’ (indexed for inflation), the experience of the past decade shows that Congress could always change course.

i Grantor trusts

Many high net worth individuals choose to set up trusts for their children and further descendants and fund them with some or all of the lifetime gift and GST tax exemption. The benefits of such trusts can be leveraged if they are structured as grantor trusts, which are trusts over which the individual funding the trust (the grantor) retains certain powers (e.g., the power to substitute assets of equal value for the trust assets) that cause the grantor to be treated as the owner of the trust assets for income tax purposes (but not for estate and gift tax purposes).37 Because the grantor of such a trust is legally responsible for payment of the income taxes on the trust’s income, the payment of such taxes would not be deemed a further gift to the trust, thereby enabling the trust to grow on an income tax-free basis.38 If properly drafted, the grantor trust status may be cancelled at any time if the tax burden becomes too great.

Making a loan to a grantor trust at a low rate of interest is another means to leverage the benefits of such a trust. If the trust’s investments perform better than the applicable interest rate set by the IRS, the excess appreciation remains in the trust with no gift tax consequences. In addition, the grantor may sell to the trust assets that are expected to appreciate in exchange for consideration of equal value (including the trust’s promissory note). A transfer by sale would remove the assets sold to the trust and any appreciation thereon from the grantor’s estate, although the sale proceeds paid to the grantor would remain part of his or her estate. If the assets sold to the trust appreciate at a greater rate than the sale proceeds, the appreciation would have been passed to the grantor trust without the imposition of estate or gift tax.

37 See IRC Sections 671–79.
38 IRC Section 671.
Because a grantor trust is considered to be owned by the grantor for income tax purposes, there would be no income tax consequences on the sale to the trust, or on the payment of interest under a loan during the grantor’s lifetime.  

The IRS has made attempts to challenge the use of sales to grantor trusts. To date, those attempts have generally been unsuccessful, but the IRS seems to have renewed its efforts in two companion cases before the Tax Court, *Estate of Donald Woelbin v. Commissioner* and *Estate of Marion Woelbing v. Commissioner*. Accordingly, practitioners should be aware of the dialogue on this subject.

### ii Grantor-retained annuity trusts

A grantor-retained annuity trust (GRAT) is a statutorily authorised trust that allows a grantor to transfer the appreciation in the value of property above a fixed interest rate during a specified period at a nominal gift tax cost. The grantor retains the right to receive an annuity for a specified period of years (for example, two years) equal to the value of the assets transferred to the GRAT at the time of funding, plus a fixed interest rate set by the IRS. The annuity can be paid in cash or in kind. At the end of the term of years, the remaining assets of the trust (i.e., the appreciation in the value of the GRAT assets during the GRAT term over the fixed interest rate), pass to the designated remainder beneficiaries (usually one or more trusts for the grantor’s children). If the assets appreciate at a higher rate than the statutory rate of return, that appreciation is transferred at the end of the GRAT term to the designated remainder beneficiaries with no estate or gift tax. If the GRAT is unsuccessful, the grantor (or the grantor’s estate) receives back the remaining GRAT assets and the remainder beneficiaries have no obligation to repay any shortfall. GRATs are powerful tools because they may pass assets with very little added risk. However, the need to pay annuity amounts requires a valuation of the asset used to fund the GRAT at formation and on each annuity date. For this reason, GRATs are often (though not always) funded with marketable securities, the value of which is easy to determine and not likely to be challenged by the IRS.

### iii Partnerships

Interests in partnerships may be either given or sold to family trusts to facilitate the transfer, ownership and management of certain assets. Such partnerships are often referred to as ‘family limited partnerships’ (FLPs) because they permit several family members and entities to pool their assets and make investments that might not be available to some family members or entities (e.g., due to securities laws that require investors in certain products to have a certain minimum net worth). In the case of a sale or gift of an FLP interest, the value of the transferred interest should be determined by a professional appraiser. It can be expected that the FLP interest given or sold would be valued by an appraiser at a lower value than

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41 See IRC Section 2702.
42 IRC Section 2702(b); Treas. Reg. Section 25.2702-3.
the sum of the underlying assets to reflect that the interest being transferred is a minority, unmarketable interest, and also to reflect illiquidity caused by any restrictions placed on the transfer of such interests by the FLP’s operating agreement.

FLPs generally are not appropriate vehicles for residences or other personal assets that will be used by family members. They continue to be scrutinised by the IRS and may cause adverse tax consequences if they are found to have no apparent business or other non-tax purpose, or where the individual funding the FLP exercises control over the underlying assets without respecting the entity formalities.44 However, when an FLP is properly structured and administered, taxpayers have been successful in defeating these challenges.45 Moreover, the IRS may assert that the discount applied to the FLP assets is overstated.46 In September 2016, the IRS released proposed regulations addressing discounts in the valuation of certain interests in family-owned entities under Code Section 2704. If adopted, these regulations would eliminate some currently available valuation discounts in certain transactions.47

iv Pre-Immigration Planning

Non-US citizens who plan to become US citizens in the future should undertake pre-immigration planning to protect their assets from the potential application of US tax laws. Pre-immigration planning is a complex area that often involves both US and non-US trusts, careful planning to obtain a step up in capital gains basis of assets, and other sophisticated planning tools. Pre-immigration planning should begin as soon as possible for individuals planning to become US citizens. If a non-US grantor of a non-US trust, with one or more US beneficiaries, becomes a US resident within five years of funding the trust, the grantor becomes subject to US income tax on all of the trust’s income and on capital gains for any year in which the trust had a US beneficiary. The trust also becomes subject to increased reporting obligations.

V CONCLUSIONS & OUTLOOK

The urgent need for tax revenue, coupled with the US government’s distrust of the offshore world, shows no sign of abating. As many governments worldwide share those driving forces, all indicators point to an increasingly global system of information sharing and enforcement.

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44 See, e.g., Estate of Turner II, 138 TC 306 (2012) (consolidated asset management generally is not a significant non-tax purpose for a taxpayer’s formation of an FLP).
45 See, e.g., Estate of Stone, TC Memo 2012-48 (holding that the decedent had two non-tax motives for the establishment of an FLP owning woodland parcels: (1) to create a family asset that would later be developed and sold by the family; and (1) to protect the land from partition actions).
46 Estate of Koons v. Comm’r, TC Memo 2013-94 (rejecting estate expert’s regression analysis as overstating the marketability discount as 31.7 per cent and adopting IRS’s expert discount of 7.5 per cent instead); Holman v. Comm’r, 130 T.C. 170 (2008) (IRS successfully argued that the appropriate discount for lack of control and lack of marketability should be roughly half the discount claimed by the taxpayers).
ABOUT THE AUTHORS

PABLO ALARCÓN

Alarcón Espinosa Abogados

Pablo Alarcón gained his law degree in 1986 from Universidad Pontificia de Comillas, and his area of expertise is tax law.

Mr Alarcón was a partner in the legal and taxation department of Ernst & Young in Madrid until 1998, and from 1998 to 2000 he held the posts of secretary of the board of directors and asset planning manager of UBS España, SA. He joined Gómez-Acebo & Pombo in September 2000 and was a partner at the firm from 2002 to 2010. He is the founder of his own law firm. He has made various contributions to specialised publications and journals.

He has been a member of the Madrid Bar Association since 1986, and is also a member of the International Bar Association, American Bar Association, AEDAF (Association of Tax Professionals) and ITSG (International Tax Specialists Group).

Mr Alarcón has been teaching international taxation for many years at the IE University and Law School where he is Academic Director of the Global Tax Law Master programme.

MAXIM ALEKSEYEV

ALRUD Law Firm

Maxim Alekseyev is a co-founder and senior partner of ALRUD Law Firm and head of ALRUD Law Firm private client and tax practices. He is an expert in foreign economic and business activity, investments, corporate and commercial issues.

He graduated from the Moscow State Institute of International Relations of the Ministry of Foreign Affairs of the Russian Federation.

Maxim Alekseyev leads projects dealing with both Russian and foreign partners within the territory of Russia and abroad. In his private client practice, Maxim has extensive experience in advising HNWIs on various types of issues to help them manage and secure their assets, business and family relations. He advises clients on different aspects of estate planning and administration, personal wealth management, as well as family business governance, and risk management in respect of assets protection. Maxim is acknowledged as a leading Russian expert focusing on private wealth planning, succession, onshore and offshore structures, private banking and individual taxation.

Maxim Alekseyev is a member of the International Bar Association (IBA), the American Bar Association (ABA), the Inter-Pacific Bar Association (IPBA) and the Society of Trust and Estate Practitioners (STEP), a professional body joining the world’s most prominent experts specialised in the management of personal finance.
ALEC R ANDERSON
Conyers Dill & Pearman

Alec R. Anderson is global head of the trust and private client group and a director in the Bermudian office of Conyers Dill & Pearman. He joined Conyers in 1985 and became a partner in 1991. He is also a director and president of Codan Trust Company Limited, a licensed trust company and a controlled affiliate of Conyers Dill & Pearman.

Mr. Anderson’s practice includes trust and estate planning for international private clients and advising on various cross-border transactions involving trusts, especially the restructuring, modification and variation of trusts. He also has expertise in trust dispute resolution and assisting mediated resolution of contentious trust matters. Additionally, his practice includes involvement in the protection of family wealth from divorce and other litigation.

Mr. Anderson is a regular speaker at conferences and contributor to many trade and legal publications. He has published several chapters in books on trust and private client practice in Bermuda. He is the Bermudian editor of the journal Trusts & Trustees. He is also the chairman of the Bermuda Trust Law Reform Committee. Mr. Anderson has been recognised as a leading private client lawyer by Chambers Global, which ranks Mr. Anderson in band 1 for international private client work and notes that he is described by sources as ‘top of the top-tier lawyers’.

PHILIPPOS ARISTOTELOUS
Elias Neocleous & Co LLC

Philippos Aristotelous is a partner in the corporate and commercial department of Elias Neocleous & Co LLC. He graduated in law from the University of Kent in 2003. He is a barrister of the Inner Temple and was admitted to the Cyprus Bar in 2005. Mr Aristotelous specialises in international taxation and trusts. He was the national reporter for the Tax Committee of the International Bar Association from 2009 to 2011 and he is a member of the Society of Trust and Estate Practitioners and the International Tax Planning Association.

FERENC BALLEGEER
FB-Private Wealth Law

Ferenc Ballegeer has been a lawyer since 2001 and is a member of the Brussels Bar. Ferenc founded FB-Private Wealth Law in 2012. FB-Private Wealth Law assists international and Belgian private clients, expats and their families with regard to tax law and estate planning. Ferenc is an active member of the International Association of Young Lawyers (AIJA) and chairs the Regional Taxes Task Force of the American Chamber of Commerce in Belgium (AmCham Belgium). He is invited regularly as a speaker on estate planning and tax topics. Ferenc is also a board member of çavaria, the Flemish LGBTI organisation.

MARK BARMES
Lenz & Staehelin

Mark Barmes is a member of the private client practice group of Lenz & Staehelin and former head of the group in the Geneva office. He advises individuals and trustees on all aspects of wealth planning in both international and domestic contexts. He particularly assists foreign
private clients and trustees to establish themselves in Switzerland and to resolve disagreements. He is on the board of Swiss trustee companies and contributes actively in the field of wealth planning in Switzerland through membership and lecturing for the Society of Trust and Estate Practitioners and as a committee member of the Swiss Association of Trust Companies.

**SARA BEHESHTI**  
*O’Sullivan Estate Lawyers LLP*

Sara’s practice involves estate planning, estate administration, estate dispute resolution and real estate matters arising in the trust and estate context. Sara’s estate planning practice includes will and trust planning, incapacity planning and estate administration. Sara also advises executors, beneficiaries and trustees on estate and trust administration. Sara is frequently retained by lawyers, financial institutions, executors and individuals to act on real estate issues arising in estate planning, estate administration and estate litigation matters. Sara also has broad experience in real estate transactions and estate conveyancing matters. She also provides title opinions and advice on claims affecting title, fraud prevention and the registration of title transfers, cautions, court orders and certificates of pending litigation.

**MARK BIDDLECOMBE**  
*Nerine Trust Company Limited*

Mark Biddlecombe LLB, ACIB, BSc, TEP, has been involved in the fiduciary services industry since 1991. Qualified as a barrister and as a solicitor, and a full member of the Society of Trust & Estate Practitioners (STEP), Mark has devoted his career to looking after the interests of high net worth individuals and families.

Mark has a broad international experience, and has worked in Jersey, Singapore and London, working for trust companies, law firms and accountants, giving him a broad perspective on the needs of the international private client.

Mark is group in-house legal counsel for Nerine, and a director of Nerine’s holding company. He also holds board positions on a select number of external boards.

**KARL BINDER**  
*Wolf Theiss*

Dr Karl Binder is a partner at Wolf Theiss and specialises in real estate and private client matters. He is frequently seen as adviser on Austria’s most prominent real estate transactions, including both large-scale portfolio deals and the acquisition of trophy real properties. Besides being an expert in all kinds of real estate matters, Mr Binder is known for his expertise in estate and succession planning and inheritance law, resulting from some 300 probate proceedings he has handled thus far. He regularly advises international private clients, including prominent public figures, wealthy individuals and family offices. Mr Binder holds an LLM degree in European business law and has more than 12 years of professional experience. He is co-author of the standard commentary on Austrian land register law.
JEAN-PHILIPPE CHETCUTI

Chetcuti Cauchi Advocates

Jean-Philippe is co-founder and senior partner of Chetcuti Cauchi Advocates. He has significant experience in advising local and foreign corporations and investors in Europe, and acts as legal counsel and tax consultant to individuals, business families and companies seeking a tax-efficient commercial or residential base in Malta or Cyprus. His main specialisation is supporting UHNWI and private clients in relation to their immigration and estate planning requirements.

Jean-Philippe is recognised for his in-depth experience in trust and estate administration and corporate and asset protection structures, and for his handling of sophisticated domestic and international transactions. He is a key adviser in European citizenship by investment programmes and acts for family offices around the globe.

His leadership is especially recognised in the area of Maltese immigration law and he has represented a number of professional associations on policy reform issues concerning Malta’s attractiveness for foreign retirees and expatriates.

HENRY CHRISTENSEN III

McDermott Will & Emery LLP

Henry Christensen III is a member of the international law firm of McDermott Will & Emery LLP, where he is the co-managing partner of its private clients practice group in New York, and managing partner of its international private clients practice. He conducts an active practice advising clients in connection with their tax and estate planning and in tax and probate dispute work, and has an extensive international practice advising multinational families, family offices, and trustees. He is the former chair of the International Committee and a former Regent of the American College of Trust and Estate Counsel (ACTEC) and is the Chancellor and a past President of the International Academy of Estate and Trust Law (IAETL). He often meets with the US Treasury on behalf of ACTEC and other professional organisations regarding tax policy. He is an honours graduate of Yale College and Harvard Law School.

Mr Christensen has taught courses in international estate planning in the graduate estate planning programme at the University of Miami Law School and in the graduate tax programme at New York University Law School. He has written and lectured widely on various tax and estate planning subjects, including at the Heckerling Institute, ALI-ABA, ACTEC, the IAETL and PLI. He is the author of the treatise, *International Estate Planning* (Matthew Bender & Co., 2nd edition, September 1999), updated annually. He is a member of the Board of Editors of *Trusts and Trustees*, published by Oxford University Press.

CHUA YEE HOONG

KhattarWong LLP, a member of Withers KhattarWong

Yee Hoong is a partner of law firm KhattarWong LLP, a member of the Formal Law Alliance Withers KhattarWong. She advises companies, businesses and individuals on Singapore tax, the application of tax treaties and Singapore tax residence requirements. She also acts for clients in applying for grant of representation in the Singapore courts, the administration of estates and estate planning.
GEOFFREY CONE

Cone Marshall Limited

Geoffrey Cone graduated from University of Otago, New Zealand with LLB honours and a postgraduate diploma in tax and trust law. He commenced practice in 1980 in Auckland, New Zealand then moved to Christchurch, where he was a partner and the chairman of partners in a leading law firm. There he practised in commercial litigation as well as tax and trust advisory work and appeared in the courts at all levels as leading counsel, including the Privy Council. After working in the British West Indies as a litigator for two years he returned to practise in 1997 in Auckland, following which he established his own practice in 1999. His firm, Cone Marshall Limited, is the only New Zealand law firm to specialise exclusively in international trust and tax planning, and it provides trustee and trust management services through its affiliated companies. He is a member of STEP.

KEITH CORBIN

Nerine Trust Company Limited

Keith Corbin ACIB, TEP, has been involved in the international fiduciary services industry for 40 years, during which time he has managed operations in a number of major international finance centres.

He is the executive chairman of the Nerine Group of Fiduciaries, which has offices in the BVI, Guernsey, Switzerland, Hong Kong and India, where Nerine became the first independent trust company to establish a presence.

Keith also serves as independent director of public and private companies outside of the Nerine Group and these appointments include the chairmanship of board committees. He has also served as chairman or committee member of various industry bodies.

RUTH CORNETT

Christie’s

Prior to joining Christie’s, Ruth Cornett worked as a tax adviser in a number of professional firms in the City and the West End of London. After training as an art historian and working as a curator in the V&A, Ruth changed careers in 1992, studying law and qualifying as a chartered tax adviser in 1998 and as a trust and estate practitioner in 2008.

Ruth advises a broad spectrum of clients on a range of tax matters with a particular emphasis on the taxation of chattels, capital gains tax and inheritance tax. Ruth also serves as an observer on the Historic Houses Association tax and political committee and has lectured for the Society of Trust and Estate Practitioners and Christie’s Education.

EMILY DEANE

STEP

Emily Deane TEP is technical counsel at STEP. She graduated from Keele University with a BA (Hons) in English and subsequently from Westminster University with a Graduate Diploma in Law. She was admitted to the Roll of Solicitors in England and Wales in 2005 and she has practised as a private client and trust solicitor since qualifying. In recent years she has been based in Bermuda and the Cayman Islands specialising in all aspects of the private client
industry including wills, property, tax planning, estate administration, onshore and offshore trusts and litigation.

KATHERINE DEMAMIEL

Sullivan & Cromwell LLP

Katherine DeMamiel is an associate in the New York and London offices of Sullivan & Cromwell's estates and personal group. Ms DeMamiel received her JD from the University of Virginia School of Law in 2010 and her BA from Baylor University in 2007. She has participated in the representation of international families and fiduciaries with respect to a broad range of tax and planning issues, including extensive advice with respect to trust and family business planning. Ms DeMamiel is a co-author of the article entitled ‘Planning for the Non-Citizen Spouse’ published in the June 2016 edition of the Journal of Taxation, and was named as a ‘One to Watch’ in the Private Client Global Elite 2017 by Legal Week.

IAN DEVEREUX

Stephenson Harwood

Ian has been a partner at Stephenson Harwood since 1988. He is also head of the private wealth group in Greater China. Ian has a wide range of experience of advising individuals and families in Hong Kong on a variety of issues ranging from preparing wills, advising families on complex trust structures, philanthropic, succession and estate planning objectives.

He also has experience in all property-related transactions, including advising on acquisitions and dispositions of property (residential, commercial and industrial) in Hong Kong and the People’s Republic of China, acting for both listed and private companies in joint developments, acquisitions, sales by way of tender, public auction and private treaty, financing arrangements and leases.

He has been recognised as a ‘Leading Individual of Real Estate China (International & Hong Kong Firms)’ by Chambers Asia-Pacific from 2009 to 2017. Ian has been mentioned in The Legal 500 in the last few years for Real Estate, as well as for Private Client/Wealth Management in The Legal 500 Asia Pacific in 2013 and 2014, and Tax Directors Handbook in 2014. He speaks English and Cantonese. He is a full member of STEP (Society of Trust and Estate Practitioners) and a FFI (Family Firm Institute) Certificate Holder in Family Business Advising and Family Wealth Advising.

KIRA EGOROVA

ALRUD Law Firm

Kira Egorova is of counsel and head of the international accounting and corporate support department at ALRUD Law Firm. Her principal area of practice is private client law.

She graduated from the Moscow State University department of economics with a degree in economic cybernetics.

Kira Egorova advises private clients, families with dynastic wealth and family offices, as well as their counsels. Her clients also include corporate executives, business owners (and former business owners who have experienced a liquidity event), professionals, fund managers, private foundations and others. She counsels clients in connection with the significant number of projects involving purchase of luxury items and other property. Kira has extensive experience
in advising the Russian HNWIs on development of ownership and succession structure for diversified private and business assets, located in different jurisdictions. Kira leads projects of negotiations and conclusion of shareholder agreements and associated matters.

Kira is a regular contributor of articles to publications and a frequent lecturer at conferences and seminars on current legal issues within her areas of practice.

Kira Egorova is a member of Society of Trust and Estate Practitioners (STEP) and the International Bar Association (IBA).

**RICHARD FRIMSTON**
*Russell-Cooke LLP*

Richard graduated in physics from Imperial College London. He is a solicitor and notary public of England and Wales. Richard has been a partner with Russell-Cooke LLP since 1982 and head of the private client group since 1993.

He has particular expertise in dealing with multi-jurisdictional estates, especially France. Richard is chairman of the STEP EU Committee and co-chair of STEP Public Policy Committee and sits on the EU Committee of the Law Society of England and Wales.

Richard contributes to Sweet & Maxwell Private Client Business and European Cross-Border Estate Planning and the international chapters to Heywood & Massey and Jordans Court of Protection Practice, Oxford University Press International Protection of Adults and Sellier and Dalloz EU Succession Regulation.

He was a member of the EU Commission groups of experts PRM-III/IV and PRM-III and has given evidence to the EU Parliament Legal Affairs Committee and the House of Lords EU Sub-Committee E.

**MASAYUKI FUKUDA**
*Nagashima Ohno & Tsunematsu*

Masayuki Fukuda is a finance law partner with Nagashima Ohno & Tsunematsu. As a specialist in trust law and finance laws, he has extensive experience and skills in structured-finance and securitisation, real-estate finance and other finance and corporate transactions, including various complicated cross-border, domestic corporate and asset finance transactions. Using his extensive knowledge and experience of trust law, security laws, investment regulations and family and inheritance laws, he currently focuses on planning and advising on optimal private wealth management structures for foreign clients as well as Japanese clients in collaboration with private bankers and other financial advisers. He has an LLM from the University of Pennsylvania (1999) and is qualified to practise in Japan and New York.

**LINE-ALEXA GLOTIN**
*UGGC Avocats*

Line-Alexa Glotin is a partner and head of the private client and tax department at UGGC Avocats in Paris. She advises private clients and institutions in a domestic and international context. She has extensive experience in assisting individuals, family businesses, family offices, charities, trustees and foundations (including art foundations), notably in regard to the transfer and restructuring of private assets, tax planning and estate planning. Ms Glotin also advises on voluntary disclosures and assists clients in tax litigation. She studied law at the Panthéon-Assas University, where she received an advanced studies degree in business law and
tax. She is notably a member of the International Academy of Estate and Trust Law (IAETL), STEP and the International Bar Association. She publishes regularly and is a lecturer in her field of experience abroad in private client forums.

ANNA KATHARINA GOLLAN
P+P Pöllath + Partners

Dr Anna Katharina Gollan LLM is admitted as attorney-at-law and specialist tax lawyer. Her thesis was awarded the W Rainer Walz prize of Bucerius Law School. As a counsel at P+P Pöllath + Partners, she focuses on legal and tax advice with regard to inheritance law, succession planning, foundation law and non-profit law. Dr Gollan is an adjunct lecturer for non-profit and foundation law as part of the postgraduate programme ‘Inheritance Law & Business Succession’ at the University of Münster. She is a member of the Inheritance Law Committee of the German Bar Association (Deutscher Anwaltverein). She has authored numerous publications in her practice areas.

CHRISTOPHER GROVES
Withers LLP

Christopher Groves started work at Withers in 1999 as a trainee solicitor, qualifying into the private client department in 2001, and was made a partner in 2007.

He works in the funds, investment trust and tax team of the wealth planning department and specialises in advising both UK-domiciled and non-UK-domiciled high net worth individuals in relation to their personal and business affairs.

Mr Groves's practice includes advising individuals and trustees on UK tax issues, investment structuring for private investors and asset managers, and UK and international trust and estate planning.

EMMA HAMILTON
O'Sullivan Estate Lawyers LLP

Emma's practice includes estate planning, estate administration and estate dispute resolution. Prior to joining O'Sullivan Estate Lawyers, Emma practiced trusts and estates at a full service firm in Calgary. She has experience in will, trust and succession planning, wealth transfer and incapacity planning, probate, estate and trust administration, special trust and estate court applications and family law matters, including domestic contracts. Emma is currently completing the Diploma Programme of the Society of Trust and Estate Practitioners (STEP).

YUSHI HEGAWA
Nagashima Ohno & Tsunematsu

Yushi Hegawa is a tax partner with Nagashima Ohno & Tsunematsu. As a specialist in tax law, Mr Hegawa is fluent on all matters regarding Japanese taxation, such as tax-free reorganisations, tax-efficient mergers and acquisitions, financing and capital markets transactions, taxation of wealthy individuals, international taxation on inbound investment by foreign-owned businesses and outbound investment by Japanese businesses, and transfer pricing. He has also represented many foreign-owned taxpayers before Japanese courts and tax tribunals in controversial tax cases and has secured successful results. Mr Hegawa receives high praise from media such as
Chambers Asia, Best Lawyers and The Nikkei. Mr Hegawa received his LLB from the University of Tokyo and his LLM from Harvard Law School, and is admitted to practise in Japan and New York.

GEORGE HODGSON

STEP

George Hodgson is chief executive at STEP, the worldwide professional body for those specialising in advising families across generations. Prior to joining STEP he held a senior policy position at the Association of British Insurers, the main insurance industry trade body in the United Kingdom and has also served on the staff of the Treasury Committee of the UK House of Commons. Prior to moving to public policy work, Mr Hodgson had a career in investment banking that spanned over 20 years as a top-rated economist and investment strategist. He holds economics degrees from the University of Durham and the University of Stirling, and is the author of many articles and research reports on trusts, taxation and investment issues.

HASAN INETAS

Marxer & Partner Rechtsanwälte

Hasan Inetas is a partner at Marxer & Partner Rechtsanwälte. He attended the University of Innsbruck, the University of Cologne and Harvard Business School. His main areas of practice include family businesses, corporate law, trust and foundation law.

HENG JIA

Lee Hishammuddin Allen & Gledhill

Heng Jia is an associate in the firm’s tax, GST and customs practice where her primary areas of practice include tax litigation, tax advisory and planning, transfer pricing and private clients. She read law at the University of Exeter and is trained as a barrister.

VALERIA KEMERER

Estudio Beccar Varela

Valeria Kemerer is a senior lawyer. She started her career at EBV in 2015. Her practice areas include company law and general business law. Valeria received her law degree from the University of Buenos Aires (1998). She represented the University of Buenos Aires in the following programmes: ‘International Business Transactions’, the Southwestern University, California and ‘International commercial arbitration moot (Vienna, Austria)’. Valeria teaches ‘Commercial and Custom Law’ at the Argentine and German Chamber of Commerce and Industry. She is a member of the Buenos Aires Bar Association, the International Bar Association and the Family Firm Institute.

MARIA KILATOU

PotamitisVekris

Maria is a tax lawyer, advising companies and individuals on tax planning and structuring, direct and indirect taxes, filing requirements and regulatory compliance. She advises on income tax, VAT and stamp duty liability for companies and individuals, as well as the taxes
arising from the purchase, sale, transfer and ownership of real estate and moveable assets. Maria has experience in the area of transfer pricing, as well as the application of European and international tax legislation to Greek nationals and residents. She also represents high net worth individuals on tax-related disputes and in cases of audits by the tax authorities.

TONI ANN KRUSE

McDermott Will & Emery LLP

Toni Ann Kruse is a partner in the law firm of McDermott Will & Emery LLP and is based in the firm's New York office. As a member of McDermott's highly regarded private clients practice group, Toni Ann focuses her practice on all aspects of estate and wealth transfer planning. She advises clients on estate, gift and generation-skipping transfer tax issues, trust and estate administration, and charitable planning, as well as contested trust and estate matters. Her experience includes significant work with family companies, drafting and administering complex estate plans for domestic and multinational high net worth individuals and families, implementing leveraged wealth transfer techniques and counseling fiduciaries in estate administration. Toni Ann has been appointed a 2016–17 ACTEC Foundation Young Leader. She also serves as chair of the New York office’s Pro Bono and Community Service Committee. Toni Ann received both her BA and JD from Boston College. While in law school she was the note editor for the Boston College Journal of Law and Social Justice.

ELIZABETH KUBANIK

Sullivan & Cromwell LLP

Elizabeth Kubanik is an associate in the New York office of Sullivan & Cromwell's estates and personal group. Ms Kubanik received her JD from Vanderbilt University School of Law in 2011 and her BA from the University of Virginia in 2005.

ASHLEY LEE SI HAN

Lee Hishammuddin Allen & Gledhill

Ashley is a senior associate in the firm's corporate practice group and her key focus is corporate and commercial transactions, for which she drafts the transactional papers from a tax and GST angle. She also works closely with colleagues from the firm’s tax, GST & customs practice when called on to advise corporate clients on matters pertaining to capital allowance, stamp duty and withholding tax. Ashley co-authored the CCH Tax Cases Digest, a publication that summarises and discusses various GST cases from the Commonwealth.

LAURI LEHMUSOJA

Hannes Snellman Attorneys Ltd

Lauri Lehmosoja is a counsel in the Hannes Snellman tax group. He advises clients especially in matters related to international taxation, tax litigation, tax aspects of financial instruments and incentive schemes. He is a frequent lecturer at various conferences and seminars. He is an officer in the Taxes Committee of the International Bar Association, and in 2012–13 he was also the national reporter for Finland on the International Bar Association.
Prior to joining Hannes Snellman in 2011, Mr Lehmusuoja was a senior tax adviser at Deloitte, and prior to that a tax specialist in the international department of the Finnish Tax Administration.

**ENRIQUE LÓPEZ RIVAROLA**  
*Estudio Beccar Varela*

Enrique López Rivarola has been a lawyer at the firm since 2010. He started his career at EBV in 2008. His practice area includes tax law. Enrique received his law degree from the Universidad de Buenos Aires (2010) and obtained a Specialisation in Tax Law from the Universidad Austral (2014). He is a member of the Buenos Aires Bar Association and the International Bar Association.

**SŁAWOMIR ŁUCZAK**  
*Sołtysiński Kawecki & Szlęzak*

Sławomir Łuczak graduated with a law degree from University of Poznan. He joined SK&S in 1998 and became a partner in 2007. He previously gained experience in a recognised French audit firm. He has broad experience in international tax law and in representing clients in tax and customs matters before the tax and customs authorities and administrative courts. He also advises on tax issues in relation to restructuring projects and consolidation. He is a member of the International Fiscal Association (IFA), Association Européenne d’Études Juridiques et Fiscales (AEEJF) and Regional Council of Attorneys in Warsaw.

**ASPASIA MALLIOU**  
*PotamitisVekris*

Aspasia has over 25 years of specialisation in advising on tax law and representing clients before the Administrative Courts and the Council of State. She has vast experience in advising on income, inheritance, donation and capital gains tax imposed on individuals and companies, the tax arising from a broad range of transactions and indirect taxation. Her studies in economics have afforded her a business-minded approach to the practice of law.

Aspasia has taken part in committees set up to examine tax legislation in the context of public consultations at the Ministry of the Economy and working groups at the Hellenic Federation of Enterprises for the improvement of taxation system. She is secretary of the Greek Association of Tax Law and Fiscal Studies, in which capacity she has organised and participated in numerous seminars, lectures, conferences and working groups on the interpretation of tax legislation in Greece and abroad. Aspasia has taught courses on tax law at ALBA Graduate Business School and seminars at the Athens Law Society and the Ministry of Finance on developments in the tax code. She has been widely published in newspapers and periodicals and conducts research for tax law publications. Since 2011, Aspasia has acted as editor of the *Tax Law Bulletin*, a leading Greek publication she has contributed to as a director for the last 25 years.
TODD D MAYO

*Perspecta Trust LLC*

Todd D Mayo is a principal and general counsel of Perspecta Trust. In those roles, he works with clients in designing and implementing trust and wealth strategies, and he oversees legal matters within the company. Todd also is an attorney in Vanderwal Martens, where he focuses on private client matters.

Todd is the principal author of several portions of New Hampshire's trust laws. In addition, as a member of a public-private working group that revised the state's banking laws, he was a principal author of the New Hampshire Trust Company Act and the New Hampshire Family Trust Company Act. He is also the principal author of the New Hampshire Foundation Act, by which New Hampshire became the first US state to allow the formation and domestication of civil-law foundations.

Todd is a member of the Society of Trusts and Estates Practitioners, a former president of the New Hampshire Trust Council, and a former chair of the New Hampshire Bankers Association's Trust Committee.

Todd is the author of *New Hampshire Trust Laws: Statutes and Commentary*, an annotated reference on the state's trust laws.

PRISCILLA MIFSUD PARKER

*Chetcuti Cauchi Advocates*

Priscilla is one of the partners of Chetcuti Cauchi Advocates and she heads the corporate services department with the firm's corporate administration arm. She mainly specialises in the use of European trusts and estate planning strategies for wealth preservation and succession planning.

Priscilla's practice revolves around assisting clients in the business start-up stage or with acquisitions, corporate restructurings and shareholder matters, and providing day-to-day company law and tax advice to companies under the firm's administration.

Priscilla has experience in advising UHNWI with their wealth structuring and wealth preservation strategies. Working closely with the firm's significant international client base, she provides tailor-made, tax-efficient solutions through trusts and corporate structures set up in Malta and Cyprus. She is also heavily involved in executive relocation planning, and related legal and tax matters.

ALAN MILGATE

*Rawlinson & Hunter*

Alan is a partner with Rawlinson & Hunter in the Cayman Islands and specialises in private client services, including international trust structures, private trust companies and purpose trusts, estate planning and wealth management.

He advises on the establishment and ongoing administration of Cayman Islands trusts and companies, including acting as a director of a number of private trust companies, other regulated entities and other client companies. Alan is a director of The R&H Trust Co Ltd and The Harbour Trust Co Ltd, duly licensed Cayman Islands trust companies owned and operated by Rawlinson & Hunter in the Cayman Islands.

Alan has over 20 years of international experience in the financial services industry and joined the Cayman practice in December 1997. Prior to moving to Cayman, his career included experience with the taxation practice of Deloitte in Canada and audit and assurance
services in Canada, New Zealand and the Cayman Islands. He is a qualified chartered accountant (Canada), trust and estate practitioner (TEP) and a chartered financial analyst (CFA) charter holder.

He is the chairman of the Cayman Branch of STEP, is a member of STEP Global Council, an immediate past chairman of the Cayman chapter of AIMA and member of the Cayman Islands Institute of Professional Accountants.

PETER MONTEGRIFFO QC
Hassans International Law Firm

Peter’s area of expertise is in commercial and private client matters. He has also advised on numerous financial services, regulatory and trust related matters. Peter was closely involved in the IPOs of various gaming companies established in Gibraltar, which have been listed on the London Stock Exchange.

Peter has been closely involved in drafting numerous changes to Gibraltar’s legislation in trusts, financial services and gaming areas. His knowledge of these fields has led him to contribute to a large number of articles and books on Gibraltar’s legal system and financial services sector.

Peter regularly speaks at international conferences relating to these areas of practice. His work frequently requires him to deal with multiple jurisdictions as a result of which the firm has built a considerable bank of international knowledge in tax and private client arrangements.

Peter was also Gibraltar’s Minister for Trade and Industry, with responsibility for economic development and financial services, between 1996 and 2000. Having graduated from Leeds University, Peter attended the Inns of Court School of Law as a member of Lincoln’s Inn. He qualified as a barrister in 1982, becoming a partner of Hassans in 1988. Peter was appointed as Queen’s Counsel in Gibraltar in June 2014.

DP NABAN
Lee Hishammuddin Allen & Gledhill

DP Naban heads the tax, GST and customs practice at Lee Hishammuddin Allen & Gledhill together with S Saravana Kumar, a partner in the same practice group. They pioneered private client practice in Malaysia in addition to spearheading tax and customs litigation and advisory work. They have a strong track record of successfully representing taxpayers for major landmark tax appeals. A senior partner of the firm, Naban is a highly acclaimed Band 1 tax lawyer (Chambers Asia). He has appeared in some of Malaysia’s most significant recent tax disputes, where clients describe him as ‘outstanding’ and recommend him for his ‘superb’ advocacy skills.

ELIAS NEOCLEOUS
Elias Neocleous & Co LLC

Elias Neocleous is managing partner of Elias Neocleous & Co LLC. He is a graduate of Oxford University and a barrister of the Inner Temple, and was admitted to the Cyprus Bar in 1993. He is a founder member of the Franchise Association of Greece, a member of the International Bar Association and the International Tax Planning Association, an honorary member of the Association of Fellows and Legal Scholars of the Center for International Legal Studies, honorary secretary of the Limassol Chamber of Commerce and Industry and serves on
the committee of STEP Cyprus. His main areas of practice are banking and finance, company matters, intellectual property law, international trade, tax and trusts and estate planning, and he has many publications to his credit in the fields of corporate, taxation and trust law.

FRÉDÉRIC NEUKOMM
Lenz & Staehelin

Frédéric Neukomm is a partner and a certified tax expert in the Geneva office and a member of the private client practice group. His main areas of work are company tax law and tax law for high net worth individuals. He also works in the fields of banking and finance.

ELENA NOVIKOVA
ALRUD Law Firm

Elena Novikova is of counsel at ALRUD Law Firm. Her principal areas of practice are general tax planning, tax advice for corporate restructuring, accounting consulting, taxation of individuals, tax expertise of business transactions and incentive plans.

She graduated from the Moscow State Academy of Business Administration, specialising in financial management and accounting. In 2005 she successfully secured a qualification in international standards of financial statements – ACCA DipIFR. She has been an ACCA member since 2012.

Elena possesses profound experience in accounting, corporate taxation and international taxation, management accounting and communication with the Russian tax authorities. She provides ALRUD clients with advice on a diverse range of complicated tax issues, supports them during tax audits, represents clients’ interests in negotiations with state authorities, participates in performing tax due diligences and tax audits.

Elena, together with the ALRUD tax team, provides ongoing tax support for JVC, Tupperware and Moody’s Investors Service with regard to their operating in Russia and the CIS. She performs tax expertise of the incentive plans, secondment and other employment issues for ALRUD clients.

SILVIA ON
Stephenson Harwood

Silvia On is a consultant in the private wealth group of Stephenson Harwood based in Hong Kong. She advises individuals and families on their succession and estate planning needs. Her experience ranges from drafting wills for individuals to setting up complex structures for families. In particular, she has helped a number of wealthy families set up trust structures to hold the family’s wealth and to achieve the family’s succession needs. She also has worked and assisted family offices on a variety of matters, including helping one family set up a number of different trust structures to hold the family’s diversified assets and achieve the family’s philanthropic objectives. She also advises Hong Kong charities and advises on the setting up of Hong Kong charities.

She has been identified as an Associate to Watch by Chambers Asia-Pacific (now Chambers Global High Net Worth Guide) for Private Client/Wealth Management (International Firms) from 2013 to 2017. Also, from 2013 to 2017, she was listed in the Citywealth Leaders List. Silvia was also featured in ‘The IFC Power Women Top 200’ by Citywealth from 2014 to 2017. Silvia was named as a Rising Star in the Spears Asia Index and Forty under Forty 2016 by Asia
Legal Business. Silvia is also listed in *Who’s Who Legal: Private Client* in 2016 and 2017. Silvia contributed the article ‘Considering a Trust in Pre-IPO Planning’ in the *IPO Handbook for Hong Kong 2015* and contributed the article ‘Trusts are not bullet proof armour’ in *The Journal of International Tax, Trust and Corporate Planning*. Silvia was also invited to teach at the CEIBS Family Office Diploma Programme 2016. She is also a fellow of ACCA (Association of Certified Chartered Accountants) and a member of STEP (Society of Trust and Estate Practitioners).

**ROBERTO PADILLA ORDAZ**  
*Chevez Ruiz Zamarripa y Cia, SC*

Roberto Padilla Ordaz is a partner and specialises in federal taxation matters in Mexico, with an emphasis on M&A, financial institutions and investment structures. Roberto is a public accountant from the Instituto Tecnológico Autónomo de Mexico (ITAM) in Mexico City, where he took a postgraduate course in corporate advisory. Roberto holds a master’s degree in tax law from Universidad Panamericana in Mexico City. He has contributed to several publications on taxation topics. Roberto is a current member of Young IFA Network in Mexico City.

**MARGARET R O’SULLIVAN**  
*O’Sullivan Estate Lawyers LLP*

Margaret O’Sullivan exclusively practises estate planning; estate litigation; advising executors, trustees and beneficiaries; and administration of trusts and estates. Prior to establishing an independent trusts and estates boutique firm, she was a partner at Stikeman Elliott, where she directed its trusts and estates practice. She is a past deputy chair and member of the board of directors and council for the Society of Trust and Estate Practitioners (STEP) Worldwide; past chair of the professional standards committee of STEP Worldwide; past member of the management and finance committee; past deputy chair of STEP (Canada); past chair of the editorial board for STEP Inside; past chair of the Trusts and Estates Law section, Ontario Bar Association; elected fellow, ACTEC, 1995; and academician of The International Academy of Estate and Trust Law. She received the 2014 STEP Founder’s Award for Outstanding Achievement and the Ontario Bar Association’s 2013 Award of Excellence in Trusts and Estates Law. She has written two textbooks for the Trust Institute of the Institute of Canadian Bankers: *Engineering of a Trust* and *Trust and Estate Management*. She is also author of the Canada chapter of *International Succession Laws* (Tottel 2009) and contributing author to *Widdifield on Executors and Trustees* (Carswell 2002), *Key Developments in Estates and Trusts Law in Ontario* (Canada Law Book 2008) and to *The International Comparative Legal Guide to: Private Client 2016* (Global Legal Group 2015). She was called to the Ontario Bar in 1983.

**JANOS PASZTOR**  
*Wolf Theiss*

Janos Pasztor is a senior associate heading the tax practice group at Wolf Theiss Budapest. He completed his studies at the Faculty of Law of Eötvös Loránd University and has an LLM degree in international taxation (WU Vienna). He is also a qualified and chartered tax adviser in Hungary. Prior to joining Faludi Wolf Theiss in 2014, Janos worked at Ernst & Young Hungary as a tax manager and attorney-at-law. Janos specialises in domestic and international tax planning, tax restructuring and also provides comprehensive tax and legal
advisory for high net worth individuals. He regularly represents clients in tax litigation proceedings relating to all major types of taxes. Janos also frequently presents at domestic and international events on cross-border taxation, tax litigation and tax restructuring, as well as providing lectures on tax matters. Janos speaks fluent English and German.

**JOSÉ PEDROSO DE MELO**

*SRS Advogados*

José Pedroso de Melo is a specialised tax lawyer with solid experience in this area, advising in domestic and international tax law, banking and insurance, corporate and high net worth individuals’ assets restructuring, mergers and acquisitions operations, compliance procedures and tax litigation.

He began his career in the international audit firm Mazars Portugal, as tax manager, and later joined the tax departments of Garrigues and PLMJ, two of the major law firms in Portugal. He is currently managing associate of the tax department at SRS Advogados.

Recognised as a tax expert by the Portuguese Bar Association, where he is inscribed since 1998, he is a member of the AFP (Portuguese Fiscal Association). He is recommended as a tax lawyer by the international legal directories *The Legal 500* and *Chambers and Partners*. He is also a tax arbitrator at the Centre of Administrative Arbitration (CAAD).

A speaker at several conferences on tax law, he is frequently invited to publish opinion articles regarding tax issues in economic newspapers and is a regular commentator on a specialised TV channel.

**ALINA PLYUSHCH**

*Sayenko Kharenko*

Alina Plyushch is a counsel with Sayenko Kharenko specialising in corporate law, M&A, corporate finance, capital markets and private wealth management.

Alina has 18 years of professional experience in advising clients on corporate restructurings, share and asset sales, joint ventures, private placement and capital markets transactions.

Ms Plyushch is one of the leading specialists in Ukraine in the private wealth management area and has extensive experience in advising on protection of beneficial owners’ interests both in Ukraine and abroad, including corporate restructuring, creation of trusts, and incorporation of foundations and segregated portfolio companies.

Ms Plyushch is recommended in M&A law by the leading international directory *Best Lawyers International 2018*; recognised among other notable practitioners in *Corporate/ M&A by Ukrainian Law Firms 2017*; and is listed among the world’s best private client lawyers by the independent review *Who’s Who Legal: Private Client 2016*.

Alina earned her graduate diploma in law and postgraduate diploma in legal practice from BPP University Law School (London) and law degree *summa cum laude* from the Academy of Advocacy of Ukraine.
SIMONE RETTER

*Retter SÀRL*

Simone Retter has been a member of the Luxembourg Bar since 1985.

For more than three decades, Simone Retter has been advising high net worth families and entrepreneurs on the legal structuring of their wealth and investments. Her areas of expertise reach from corporate and civil law to estate planning matters.

In 2009, she founded Retter Attorneys, a boutique law firm exclusively dedicated to private clients. Simone Retter concentrates her activity on a short list of ultra-high net worth families for which she provides legal and family office services and assists them in their global wealth structuring and estate planning. Simone Retter holds a master’s degree in law from the University of Paris (Panthéon-Sorbonne) and is a graduate from the Paris Institute of Political Studies (Sciences-Po) – Economic and Finance Section. She attended successfully the Executive Program for Overseas Bankers at Wharton Business School, University of Pennsylvania (USA). She lectured in commercial law from 1998 to 2000 and currently on the master’s in wealth management at the University of Luxembourg.

Simone Retter has been a member of the board of directors of the Luxembourg Central Bank since December 2014. Simone Retter has been extensively involved in the drafting of a new private wealth foundation legislation for Luxembourg deposited in June 2013 by the Luxembourg government with the Luxembourg parliament. Previously, she drafted the law on family office activities in Luxembourg, enacted by the Luxembourg parliament on 21 December 2012. Simone Retter is a member of the Private Banking Group of the Haut Comité de la Place Financière of Luxembourg.

She is a member of the Society of Trust and Estate Practitioners (STEP).

Simone Retter is listed in the *Citywealth Leading Lawyers* list, in the Legal Media Group’s *Expert Guides* to the world’s leading lawyers, in the *Guide to the World’s Leading Women in Business Law* and in the *PLC Which Lawyer Year Book* as a recommended private client lawyer.

DMYTRO RIABIKIN

*Sayenko Kharenko*

Dmytro Riabikin is an associate at Sayenko Kharenko specialising in private wealth management, M&A, corporate law and securities market.

Dmytro has seven years’ experience of advising clients on various private wealth management issues, including protection of the interests of beneficial owners of Ukrainian and foreign businesses by means of corporate restructuring and setting up trusts.

Dmytro earned his master’s degree *summa cum laude* in private international law from the Institute of International Relations of Taras Shevchenko National University of Kiev. In 2016, Dmytro received a PhD in Private International Law.

JOHN RICHES

*RMW Law LLP*

John works with family offices on a cross-border basis and deals with structuring for UK residents and resident non-domiciled families. He creates structures for active entrepreneurs to hold business interests. He is recognised as a leading authority in the area of family governance and has written and spoken extensively on this topic.
John founded RMW Law LLP in July 2011 with Samantha Morgan. RMW Law LLP is a niche legal practice dedicated to working for a limited range of international families and family offices. John remains a consultant at international law firm Withers LLP, where he was a partner from 1996 to 2011.

John has had a variety of senior posts within the Society of Trust and Estate Practitioners over many years. As co-chair of the public policy committee, John has been responsible for liaising with national and supranational bodies on matters of tax policy affecting wealthy families, and has been consulted by the Organisation for Economic Co-operation and Development in respect of its initiative for high net worth individuals; he has also attended a number of sessions of the Financial Action Task Force (FATF) Private Sector Consultative Forum, where FATF seeks views from the private sector on its proposals and guidance to member states. He has been working extensively over the last 12 months with OECD in representing the views of the private wealth sector on the introduction of the Common Reporting Standard.

ANDREAS RICHTER

P+P Pöllath + Partners

Dr Andreas Richter, LLM, is a partner and a member of the management board at P+P Pöllath + Partners. He has outstanding experience in business and wealth succession, estate planning, legal and tax structuring of private wealth and family offices, corporate governance for family-owned businesses, expatriation taxation and charities, as well as in trust and foundation law. Some of Germany’s leading family offices, family businesses and foundations, as well as their peers abroad, form the client base for Andreas’s work as a legal and tax adviser. Clients in common law jurisdictions often engage Andreas due to his background in English law (BA Hons, Trinity College, Cambridge) and US law (LLM, Yale Law School). He is listed in domestic and international rankings as one of the leading lawyers in his practice areas. Among others, Who’s Who Legal: Private Client 2016 lists Andreas Richter as the only German lawyer among the 15 ‘Most Highly Regarded Individuals’ worldwide.

Andreas is the managing director of the Berlin Tax Policy Forum, chairman of the executive board of the postgraduate programme ‘Inheritance Law & Business Succession’ at the University of Muenster/Westphalia and Academician of the International Academy of Estate and Trust Law. He serves as a member on boards of family offices, foundations and family businesses and acts as executor.

Andreas is the editor of the leading German compendium on foundations and trusts and related tax issues. He also is the author and editor of numerous other publications, commentaries and compendiums, in particular on family offices, foundation law, business succession and all tax-related matters.

HEINI RÜDISÜHLI

Lenz & Staehelin

Heini Rüdisühli is a partner in the Zurich office, where he leads the private client practice group. His main field of activity is national and international tax planning for private individuals as well as taxation of corporate reorganisations and acquisitions. In addition, Heini Rüdisühli specialises in inheritance law and succession planning as well as executorship of estates. He has a broad knowledge of trusts.
NICOLA SACCARDO

Maisto e Associati

Nicola obtained a degree in business administration from the Bocconi University in Milan and a degree in law from the State University, as well as a master of laws (LLM) in international taxation from the University of Leiden (The Netherlands). He is admitted to the Italian Bar and the Italian Association of Chartered Accountants. He is a member of the Executive Council of the International Academy of Estate and Trust Law and chair of its Tax Committee. He is a member of STEP Italy and of the International Client London UK Satellite SIG Committee of STEP. He is ranked as leading expert in several legal directories, including Chambers High Net Worth 2017, Legal Week Private Clients Global Elite and Citywealth Leaders list. He is author of many publications on Italian tax matters and is frequent speaker at conferences. His areas of expertise include international and EU tax law and taxation of trusts, estates and HNWIs.

NIKLAS JRM SCHMIDT

Wolf Theiss

Dr Niklas JRM Schmidt, TEP, is a partner at Wolf Theiss, the largest Austrian law firm. He has been admitted as a lawyer and as a tax adviser. His areas of specialisation include tax law and private clients. Mr Schmidt is frequently engaged as a speaker at tax conferences and has been a visiting lecturer at various universities. Currently, he is a member of the examination commission for the ‘Certified Financial Planner’ exam in Austria, and he sits on the editorial board of the SteuerExpress magazine. Furthermore, Mr Schmidt is a member of the International Fiscal Association (IFA), the International Bar Association (IBA), the International Tax Planning Association (ITPA) and the Society of Trust and Estate Practitioners (STEP). He has been named one of Austria’s top 10 tax lawyers in the Austrian magazine TREND and is ranked in band one by most international legal directories.

CLAUDIA SHAN

Cone Marshall Limited

Claudia Shan graduated from the University of Auckland, New Zealand with a BCom/LLB conjoint degree. She has been in legal practice since 2004. She has also worked for two leading offshore law firms in the Channel Islands and was at the time enrolled and admitted to practise as a solicitor of the Supreme Court of England and Wales. Prior to entering practice in a leading New Zealand law firm, she worked in the Auckland office of a global chartered accountancy firm focusing on tax. Claudia specialises in all aspects of trust, private client and international wealth planning. Claudia has advised a wide range of clients, both residents and non-residents, on local and foreign trusts, offshore fund repatriation, tax residency, asset protection, FATCA, international compliance, tax and trust law issues. She is a member of STEP.

SM SHANMUGAM

Lee Hishammuddin Allen & Gledhill

SM Shanmugam is a partner in the dispute resolution department (corporate litigation). As a litigator, Shan has notable experience in advising and acting as counsel in cases involving breach of directors’ duties, securities litigation involving market misconduct and insider
trading, shareholders’ dispute and negligence lawsuits. He also has experience in commercial arbitration. Shan has acted and defended regulators, private companies, public listed companies and government agencies and appears frequently before the High Court and appellate courts. He is also experienced in representing private clients for contentious and non-contentious probate and administration matters.

MIGUEL MARÍA SILVEYRA
Estudio Beccar Varela
Miguel María Silveyra started his career at EBV in 1998 and has been a partner of the firm since 2009. He specialises in family business governance and family estate planning. He has advised several families in the process of negotiation, planning and designing of their corporate governance rules, in drafting their family protocols and shareholders’ agreements, and in planning their estate and business succession. Miguel received his law degree from the Universidad Católica Argentina (1993) and obtained his LLM from the Universidad Austral (Buenos Aires, Argentina, 1995) and his Diploma in Advanced Studies from the Universidad Autónoma de Madrid (Madrid, Spain, 2004). He worked as a foreign associate at Gomez Acebo & Pombo (Madrid, Spain, 2004). He is a member of the Buenos Aires Bar Association, the International Bar Association and the Family Firm Institute.

SUSAN SONG
Sullivan & Cromwell LLP
Susan Song is an associate in the New York office of Sullivan & Cromwell’s estates and personal group. Ms Song received her JD from Columbia Law School in 2011 and her AB from Princeton University in 2005.

STEFAN STELLATO
Hannes Snellman Attorneys Ltd
Stefan Stellato is an associate in the Hannes Snellman tax group. Prior to graduation from the University of Helsinki, he spent a semester studying at a university in New York. Besides his master of laws degree, he holds a master of science (economics and business administration) degree from Hanken School of Economics in Helsinki.

MARKUS SUMMER
Marxer & Partner Rechtsanwälte
Markus Summer is a partner at Marxer & Partner Rechtsanwälte, Liechtenstein’s oldest and largest law firm. He has obtained legal degrees from the University of Innsbruck, King’s College London and the University of Texas at Austin, and an MBA from Edinburgh Business School. His areas of special interest include tax law, trust and foundations, corporate law, finance law and investments. He is a member of the Society of Trust and Estate Practitioners and of the International Fiscal Association.
SILVANIA TOGNETTI
*Tognetti Advocacia*

Tognetti Law’s main partner, Silvania Tognetti, is both a national and international expert in tax law, and is regarded for her versatility, deep understanding within various legal areas, and creativity. These features can be seen by the diversity of clients and the successful projects carried out throughout her career, which includes the public sector (the State Attorney of Rio de Janeiro, Representative of the Federal Revenue before the Board of Contributors of Rio de Janeiro, Secretary of Finance of Rio de Janeiro), enterprises (investment banks, international tax consultancy), and law firms (attorney in corporate reorganisation, mergers and acquisitions, administrative and judicial tax litigation, and succession planning). Since 2006, Mrs Tognetti has been recommended as a tax lawyer by *Chambers Global*. She attended the Federal University of Rio de Janeiro (JD, 1993), and she attended the graduate programme (1994) and holds a master’s degree (2001) from Universidade Cândido Mendes in Rio de Janeiro. She also has a PhD from the University of São Paulo (2009). Her professional memberships include ABDF, IFA, IBA, ABA and IBDT.

ALFREDO SÁNCHEZ TORRADO
*Chevez Ruiz Zamarripa y Cia, SC*

Alfredo Sánchez Torrado is a partner and specialises in federal taxation matters in Mexico, with an emphasis on international transactions, M&A, financial products, investment structures and estate planning. Alfredo is a CPA from the Instituto Tecnológico Autónomo de Mexico (ITAM) in Mexico City, where he has taken postgraduate programmes in international taxation. He obtained the tax specialist certification from the Mexican Institute of Public Accountants. He is the author of numerous publications on taxation matters and is an active member of the Tax Committee of the Mexican Institute of Financial Executives (IMEF) and of the Mexican chapter of the Society of Trust and Estate Practitioners (STEP). Alfredo is a board member of several corporations and he is a member of their audit and compensation committees.

EKATERINA VASINA
*ALRUD Law Firm*

Ekaterina Vasina is an associate at ALRUD Law Firm. Her principal areas of practice are private clients, mergers and acquisitions and corporate law.

She graduated with an honours degree from the law department of the Lipetsk State Technical University, with a specialisation in civil law.

During her studies at university, Ekaterina worked as an attorney for a Russian consulting company. She joined ALRUD Law Firm in 2008.

During her work, Ekaterina has been involved in projects related to the structuring of assets (both Russian and foreign) owned by wealthy families for the purpose of protecting assets against claims of third parties, estate planning and other purposes; participated in the preparation of opinions and comments on various issues of family and inheritance law, including when relations include the foreign element; has been involved in projects related to trusts and foundations establishment for Russian HNWIs; and has drafted wills and marriage contracts.
Ekaterina also advises clients on corporate law, accompanies M&A projects and projects related to corporate restructuring and reorganisation.

Ekaterina is a member of the International Bar Association (IBA).

JOHN F WILSON

McKinney Bancroft & Hughes

John Fitzgerald Wilson is a commercial litigation attorney whose areas of expertise include Admiralty litigation, trust litigation, and fraud recovery involving the tracing and recovery of stolen assets. In addition to his litigation work, Mr Wilson advises several of the larger Bahamian trust companies and is actively engaged in the firm’s work in the private client area, advising high net worth individuals on the use of various offshore products.

Following his education at the University of Buckingham in England, he was admitted to the Bar of England and Wales and the Bahamas Bar in 1994. He was also admitted to the Honourable Society of Lincoln’s Inn of the United Kingdom. Mr Wilson was admitted to partnership in the firm in 2001. He was the first Bahamian to appear as lead counsel during the Privy Council’s historic first sitting in the Bahamas, and he was commended by the Law Lords for the skill with which he presented his client’s case. In February 2016, Mr Wilson was the sole winner of the Client Choice Award in the Bahamas in the area of litigation.

Mr Wilson is the contributing editor for the Bahamas chapter of the English version of the International Real Estate Handbook published by John Wiley & Sons, a publication directed to high net worth Europeans and their professional advisers, a contributing editor to Carter-Ruck on Libel and Privacy and a contributing editor to ADR and Trusts. Mr Wilson regularly writes articles and delivers speeches in his field.

BASIL ZIRINIS

Sullivan & Cromwell LLP

Basil Zirinis has been a partner in Sullivan & Cromwell’s estates and personal group since 1994 and leads its international private client practice from London and New York. He represents individuals, fiduciaries and family-controlled businesses throughout the world in a broad range of matters, including estate and trust planning, family business governance and transition, estate and trust administration and litigation. Mr Zirinis has extensive experience in trust and estate litigation and has been involved in many of the leading litigations in this area in the past 25 years in the United States and abroad. He speaks regularly at international conferences regarding US and international tax and estate planning, including most recently in Shanghai, London, Lake Como, Bermuda, New York and Istanbul.
CONTRIBUTING LAW FIRMS’ CONTACT DETAILS

ALARCÓN ESPINOSA ABOGADOS
Paseo de la Castellana 74, 2A
28046 Madrid
Spain
Tel: +34 91 411 49 76
palarcon@alarcon-espinosa.com
www.alarcon-espinosa.com

ALRUD LAW FIRM
17 Skakovaya Street
Building 2, 6th Floor
125040 Moscow
Russia
Tel: +7 495 234 9692
Fax: +7 495 956 3718
kegorova@alrud.com
evasina@alrud.com
malekseyev@alrud.com
enovikova@alrud.com
info@alrud.com
www.alrud.com

CHEVEZ RUIZ ZAMARRIPA Y CIA, SC
Vasco de Quiroga 2121
4th floor, Santa Fe
01210 Mexico City
Mexico
Tel: +52 55 5257 7000
Fax: +52 55 5257 7001/02
sanchezt@chevez.com.mx
rpadilla@chevez.com.mx
www.chevez.com

CHRISTIE’S
8 King Street, St James’s
London
SW1Y 6QT
United Kingdom
Tel: +44 20 7839 9060
Fax: +44 20 7389 2300
rcornett@christies.com
www.christies.com/services/heritage-taxation/overview/

CHETCUTI CAUCHI ADVOCATES
120 St Ursula Street
Valletta VLT 1236
Malta
Tel: +356 2205 6105/6121
Fax: +356 2205 6201
jpc@cclex.com
pmp@cclex.com
www.cclex.com
CON Contributions Law Firms’ Contact Details

**CONE MARSHALL LIMITED**
Level 3
18 Stanley Street
Auckland 1010
New Zealand

PO Box 137069
Parnell
Auckland 1151
New Zealand

Tel: +64 9 307 3950
Fax: +64 9 366 1482
gcone@conemarshall.com
cshan@conemarshall.com

www.conemarshall.com

**ESTUDIO BECCAR VARELA**
Tucumán 1, Third Floor
Buenos Aires
Argentina
Tel: +54 11 4379 6800
Fax: +54 11 4379 6869
msilveyra@ebv.com.ar
vkemerer@ebv.com.ar
elopez@ebv.com.ar

www.ebv.com.ar

**CONYERS DILL & PEARMAN**
Clarendon House
2 Church Street
PO Box HM 666
Hamilton HM CX
Bermuda
Tel: +1 441 295 1422
Fax: +1 441 292 4720
alec.anderson@conyersdill.com
www.conyersdill.com

**FB-PRIVATE WEALTH LAW**
Avenue de l’Opale 115/b6
1030 Brussels
Belgium
Tel: +32 2 309 73 66
Fax: +32 2 309 73 99
ferenc@advocaatballegeer.be
www.fbprivatewealthlaw.com

**ELIAS NEOCLEOUS & CO LLC**
Neocleous House
195 Makarios III Avenue
PO Box 50613
3608 Limassol
Cyprus
Tel: +357 25 110 110
Fax: +357 25 110 001
info@neo.law
www.neo.law

**HANNES SNEILLMAN ATTORNEYS LTD**
Eteläesplanadi 20
00130 Helsinki
Finland
Tel: +358 9 228 841
Fax: +358 9 177 393
lauri.lehmusoja@hannessnellman.com
stefan.stellato@hannessnellman.com
www.hannessnellman.com

**HASSANS INTERNATIONAL LAW FIRM**
57/63 Line Wall Road
Gibraltar GX11 1AA
Tel: +350 200 79000
Fax: +350 200 71966
peter.montegriffo@hassans.gi
www.gibraltarlaw.com

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KHATTARWONG LLP, A MEMBER OF WITHERS KHATTARWONG
80 Raffles Place
UOB Plaza 1 #25-01
Singapore 048624
Tel: +65 6238 3016/6535 6844
Fax: +65 6534 1090/6534 4892
chuayehoong@witherskhattarwong.com
www.witherskhattarwong.com

LEE HISHAMMUDDIN ALLEN & GLEDHILL
Level 6, Menara 1 Dutamas
Solaris Dutamas
No. 1 Jalan Dutamas 1
50480 Kuala Lumpur
Malaysia
Tel: +603 6208 5888
Fax: +603 6201 0122
tax@lh-ag.com
www.lh-ag.com

LENZ & STAHELIN
30 route de Chêne
PO Box 6165
1211 Geneva 6
Switzerland
Tel: +41 58 450 70 00
Fax: +41 58 450 70 01
mark.barmes@lenzstaehelin.com
frederic.neukomm@lenzstaehelin.com
heini.ruedisuehli@lenzstaehelin.com
24 Brandschenkestrasse
8027 Zurich
Switzerland
Tel: +41 58 450 80 00
Fax: +41 58 450 80 01

MAISTO E ASSOCIATI
Piazza Filippo Meda 5
20121 Milan
Italy
Tel: +39 02 776931
Fax: +39 02 776933 00

Piazza D’Aracoeli 1
00186 Rome
Italy
Tel: +39 06 4544 1410
Fax: +39 06 4544 1411

2 Throgmorton Avenue
London
EC2N 2DG
United Kingdom
Tel: +44 20 7374 0299
Fax: +44 20 7374 0129
n.saccardo@maisto.it
www.maisto.it

MARXER & PARTNER RECHTSANWÄLTE
Heiligkreuz 6
PO Box 484
9490 Vaduz
Liechtenstein
Tel: +423 235 81 81
Fax: +423 235 82 82
markus.summer@marxerpartner.com
hasan.inetas@marxerpartner.com
www.marxerpartner.com
MCDERMOTT WILL & EMERY LLP
340 Madison Avenue
New York
10173-1922 New York
United States
Tel: +1 212 547 5658
Fax: +1 212 547 5444
hchristensen@mwe.com
www.mwe.com

MCKINNEY BANCROFT & HUGHES
Mareva House
4 George Street
Nassau
The Bahamas
Tel: +242 322 4195
Fax: +242 328 2520
jfwilson@mckinney.com.bs
www.mckinney.com.bs

NAGASHIMA OHNO & TSUNEMATSU
JP Tower, 2-7-2 Marunouchi
Chiyoda-ku
Tokyo 100-7036
Japan
Tel: +81 3 6889 7000
Fax: +81 3 6889 8000
yushi_hegawa@noandt.com
masayuki_fukuda@noandt.com

NERINE TRUST COMPANY LIMITED
Nerine House, St George’s Place
St Peter Port GY1 3ZG
Guernsey
Tel: +44 1481 701 300
Fax: +44 1481 711 224
keith.corbin@nerine.com
mark.biddlecombe@nerine.com
www.nerine.com

O’SULLIVAN ESTATE LAWYERS LLP
Toronto-Dominion Centre
TD Bank Tower
66 Wellington Street West, Suite 3430
PO Box 68
Toronto
Ontario M5K 1E7
Canada
Tel: +1 416 363 3700
Fax: +1 416 363 9570
mosullivan@osullivanlaw.com
sbheshti@osullivanlaw.com
ehamilton@osullivanlaw.com
www.osullivanlaw.com

PERSPECTA TRUST LLC
One Liberty Lane East
Hampton, NH 03842
United States
Tel: +1 603 929 2671
tmayo@perspectatrust.com
www.perspectatrust.com

POTAMITISVEKREIS
9 Neofytou Vamva str.
10674 Athens
Greece
Tel: +30 210 338 0000
Fax: +30 210 338 0020
aspasia.malliou@potamitisvekris.com
maria.kilatou@potamitisvekris.com
www.potamitisvekris.com

P+P PÖLLATH + PARTNERS
Potsdamer Platz 5
10785 Berlin
Germany
Tel: +49 30 25353 132
Fax: +49 30 25353 999
andreas.richter@pplaw.com
katharina.gollan@pplaw.com
www.pplaw.com
RAWLINSON & HUNTER
2nd floor, Windward 1
Regatta Office Park
Grand Cayman KY1-1103
Cayman Islands
Tel: +1 345 949 7576
Fax: +1 345 949 8295
alan.milgate@rawlinson-hunter.com.ky
www.rawlinson-hunter.com

RETTER SÀRL
14 avenue du X Septembre
L-2550 Luxembourg
Tel: +352 27 99 01 03
Fax: +352 27 99 01 039
simone.retter@retter.lu
www.retter.lu

RMW LAW LLP
16 Old Bailey
London
EC4M 7EG
United Kingdom
Tel: +44 20 7597 6109
Fax: +44 20 7100 5129
john@rmwlaw.co.uk
www.rmwlaw.co.uk

RUSSELL-COOKE LLP
2 Putney Hill
London
SW15 6AB
United Kingdom
Tel: +44 20 8789 9111/8394 6217
Fax: +44 20 8788 6552
helpdesk@russell-cooke.co.uk
richard.frimston@russell-cooke.co.uk
www.russell-cooke.co.uk

SAYENKO KHARENKO
10 Muzeyny Provulok
Kiev 01001
Ukraine
Tel: +380 44 499 6000
Fax: +380 44 499 6250
aplyushch@sk.ua
driabikin@sk.ua
www.sk.ua

SOŁTYSIŃSKI KAWECKI & SZLĘZAK
26 Jasna Street
00-054 Warsaw
Poland
Tel: +48 22 608 70 56/71 68
Fax: +48 22 608 70 70/70 70
slawomi.luczak@skslegal.pl
www.skslegal.pl

SRS ADVOGADOS
Rua D Francisco Manuel de Melo, 21
1070-085 Lisbon
Portugal
Tel: +351 21 313 20 00
Fax: +351 21 313 20 01
jose.melo@srslegal.pt
www.srslegal.pt

STEP
Artillery House (South)
11–19 Artillery Row
London
SW1P 1RT
United Kingdom
Tel: +44 20 3752 3763
Fax: +44 20 7340 0501
george.hodgson@step.org
emily.deane@step.org
www.step.org

STEPHENSON HARWOOD
18th floor, United Centre
95 Queensway
Hong Kong
Tel: +852 2868 0789
Fax: +852 2868 1504

© 2017 Law Business Research Ltd
ian.devereux@shlegal.com
silvia.on@shlegal.com
www.shlegal.com

SULLIVAN & CROMWELL LLP
125 Broad Street
New York NY 10004
United States
Tel: +1 212 558 4000
Fax: +1 212 558 3588
zirinisb@sullcrom.com
demamielk@sullcrom.com
kubanike@sullcrom.com
songs@sullcrom.com
www.sullcrom.com

TOGNETTI ADVOCACIA
Rua do Rocio, 288
cj 44 Vila Olímpia
04552-000 São Paulo
Brazil
Tel: +55 11 3045 3131
silvania.tognetti@tognetti.com.br
www.tognetti.com.br

UGGC AVOCATS
47 rue de Monceau
75008 Paris
France
Tel: +33 1 56 69 70 00
Fax: +33 1 56 69 70 71
la.glotin@uggc.com
www.uggc.com

WITHERS LLP
16 Old Bailey
London
EC4M 7EG
United Kingdom
Tel: +44 20 7597 6000
Fax: +44 20 7597 6543
christopher.groves@withersworldwide.com

WOLF THEISS
Schubertring 6
1010 Vienna
Austria
Tel: +43 1 515 10
Fax: +43 1 51510 25
niklas.schmidt@wolftheiss.com
karl.binder@wolftheiss.com
Kálvin tér 12–13
Kálvin Square 4th floor
1085 Budapest
Hungary
Tel: +36 1 4848 800
Fax: +36 1 4848 825
pasztor.janos@wolftheiss.com
www.wolftheiss.com