The Aver Advisory

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presented by Aver Associates Estate Planners & Trustees

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Trusts

Belgian Ruling Commission: Look-through tax applies to income of a trust, not to distributions

Decision 2016.562 of October 3, 2016

In a series of decisions in October and November 2016, the Belgian Ruling Commission clarified the application of the so-called "Cayman" look-through tax, which came into force on January 1, 2015. In the case of trusts, settlors will be liable to tax on the income of the trust, unless they can prove that someone else benefitted from the legal arrangement. When the settlor dies, the income of the trust is taxed in the hands of his heirs, unless they can prove that they enjoy no advantage from the trust.

In decision 2016.562, the Commission had to rule on the application of the look-through tax on a trust which was established under the laws of Jersey. The trust was settled by the father of the applicants prior to January 2015. The now deceased settlor was not resident in Belgium. The applicants are residents of Belgium.

On the basis of the documents submitted, the Commission came to the conclusion that the trust was irrevocable and discretionary. Although the trustee was guided by the ideas of the settlor, it was not bound in any respect and was entirely free to make distributions of assets to the beneficiaries of the trust. Furthermore, the trustee had the right to extend the list of beneficiaries.

The Commission held that the applicants, as heirs (and residents of Belgium), must report the income of the trust in their personal tax returns. It then addressed the question of the taxability of the distributions made by the trust after January 2015 to the beneficiary heirs. The Commission held that distributions remain untaxed. No distinction was made between income realized after January 2015 (in principle subject to the see-through taxation) and income realized before. This means that 'old' income (income that the trust had acquired prior to January 2015), which was not subject to Belgian income tax under the Cayman tax rule, remains tax free, even when distributed.

The Flemish press in Belgium has made some fuss about this "loophole" for discretionary trusts. To be clear, this is not a "loophole" in the application of the Cayman tax. It is the mere application of rules on personal income tax as already confirmed many times by the Ruling Commission. ■

Information Requests

Taxpayer permitted to challenge French exchange of information request

Berlioz Investment Fund SA v Directeur de l'administration des Contributions directes (Case C 682/15), Court of Justice of the European Union, January 10, 2017

Facts. The French tax authority sought information from Luxembourg to determine whether a French taxpayer was entitled to an exemption from withholding tax when it paid dividends to its Luxembourg parent, Berlioz Investment SA. Berlioz complied, in part, but refused to provide certain information which it argued was not foreseeably relevant to the French government's tax inquiry.

Decision. The court held that compliance with the "foreseeable relevance" standard is a condition of the regularity of a tax information request and therefore also of a subsequent information order. It found that Berlioz should be allowed to challenge the legality of the information order issued by the Luxembourg tax authority in support of the French exchange of information request. ■

TAXATION

Italy introduces special tax status for high net worth foreign residents
Finance Act 2017, enacting Article 24 of the Consolidated Income Tax Act

Italy has introduced a new territorial system of taxation designed to attract high net worth individuals. The Italian resident not domiciled (IRND) regime was introduced through the *Finance Act 2017*, approved by the Italian Parliament on December 7, 2016.

Under the new IRND regime Italian-source income and gains are taxable in the usual way, while foreign income and gains can be sheltered from Italian tax, provided the taxpayer pays an annual charge of €100,000. The regime may be extended to family members, at a cost of €25,000 per member.

The regime also applies to succession duties. Property and assets owned and held abroad will be exempt from Italian gift and inheritance tax.

The regime is available to anyone—regardless of nationality or domicile—who has been non-resident in Italy at any time in the nine years before settling in Italy. Individuals are tax resident if they:

- are a registered Italian citizen or
- reside in Italy for more than half the year (183 days).

Individuals must apply to the Italian tax authorities for IRND status and must disclose their tax residency location. Once approved, the taxpayer will be permitted to use the regime for 15 years. The status can be revoked at any time and will terminate immediately if the annual charge is not paid, or is only partially paid, by the due date.

The IRND regime offers more choice for wealthy individuals without a fixed domicile. The regime is similar, for example, to the UK's non-domiciled tax system, which also levies a charge on non-domiciled taxpayers opting to keep their offshore assets beyond UK tax.

The UK's tax benefits for non-domiciled individuals, however, will be significantly reduced as of April 2017, with a new deemed domicile rule that will force long-term residents to become UK-domiciled. ■

TRUSTS

Landmark decision holds no gift tax applicable on transfer of property to trust
Ruling no. 21614 of October 26, 2016, Supreme Court of Italy (5th Department)

Italy's Supreme Court recently considered the issue of whether Italian gift tax applies upon the transfer of property to a trust. The question is whether Article 2 of *Law Decree No. 262* extends the scope of the gift tax from straightforward gifts to any legal arrangement where a person places his assets in a separate instrument for the benefit of another person.

Italian tax authorities maintain that the establishment of a trust creates a taxable event, whereby gift tax applies on the value of the property transferred to the trust. This interpretation has been substantially confirmed by numerous decisions of the Italian Supreme Court.

Facts. An individual resident in Italy settled a trust for the benefit of his descendants. As a self-directed trust, the settlor was also the trustee. The trust property, which included Italian real estate and shareholdings in Italian companies, would be distributed to the beneficiaries upon death of the settlor.

Decision. Rejecting both its previous decisions and the established guidance of the Italian tax authorities, the court held that mere settlement of a trust does not trigger a gift tax obligation. The gift tax applies only at the time of the ultimate and final distribution of the property, from the trust to the beneficiary. In the case of a self-directed trust, no transfer of assets or rights occurs due to the identity of the settlor and trustee.

The court stated that *Law 262* requires the actual transfer of and receipt of the full beneficial ownership and value of the property, with resulting enrichment of the beneficiary.

It noted that in the case of property transferred to a trust, the beneficiary is not immediately enriched, and does not receive the full value of the property until the property is transferred from the trust to the beneficiary, at which time the gift tax would apply.

The court pointed out certain inconsistencies that would arise if the opposite interpretation was adopted, including the need to put the liability for the tax on the trustee, which is in contrast with the provisions of the *Gift Tax Act* placing the liability for the tax upon the recipient of the gift. ■

DUAL RESIDENTS

The Italian Tax Authorities will chase evaders who pretend to be abroad

The Italian Tax Authorities are stepping up their fight against international tax evasion by Italian taxpayers who have become resident abroad since January 1, 2010. Controls will be based on selected lists, which will first target the most irregular situations, following guidelines released on February 3, 2017. Authorities will look for evidence regarding citizens who have remained in Italy despite moving their residence abroad, including:

a. The declared residence in states with a privileged tax regime;
b. Capital movement to and from abroad;
c. Information related to real estate and financial assets held abroad sent by foreign tax authorities under EU directives and automatic data sharing agreements;
d. Residence in Italy of the taxpayer's family members;
e. Data showing the actual presence in Italy of taxpayers;
f. Active electric, water, gas, and phone bills;
g. Ownership of vehicles, motorbikes and boats;
h. Presence of an active VAT account;
i. Relevant corporate positons or holdings.

The Tax Authorities will also check whether the concerned have participated in the Voluntary Disclosure program to declare previously hidden offshore income. ■

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CELEBRITY ESTATES

Billionaire art dealer Wildenstein cleared of tax fraud

In January 2017, a French court cleared art dealer Guy Wildenstein of tax fraud and money laundering, for which prosecutors had requested a €250 million fine and a four-year jail sentence.

Facts. Guy Wildenstein is accused of hiding works of art and large portions of the family estate worth hundreds of millions of euros in a maze of offshore trusts in order to avoid inheritance taxes when family patriarch Daniel Wildenstein died in 2001. At the time, Guy and his brother Alec claimed their father's estate had a value of €40.9 million and paid an inheritance tax of €17.7 million.

Two weeks after Daniel's death, Guy and Alec advised their stepmother Sylvia that it was in her best interests to sign away her rights to the estate in order to avoid being bankrupt by taxes. A few years later, Sylvia sued her stepsons claiming that she was bilked out of her inheritance. Her lawsuit claimed that the family was sitting on trusts and real estate worth billions of dollars.

Suspecting that they had also been cheated, the French tax authorities decided to take a closer look at the value of Daniel's estate. As prosecutors would later learn, simultaneous to the Wildenstein's claim that the estate was worth only €40 million, they were negotiating a loan using €250 million in artwork as collateral.

In 2005, a Paris appeals court voided the inheritance agreement Sylvia had signed and ordered a full inventory of the family's properties including homes in New York and France, a 75,000-acre ranch in Kenya, trust assets, racehorses and artwork.

Amid the upheaval, Alec died in 2008 and Sylvia died in 2010. This leaves 70-year old Guy with the responsibility of ensuring that the family's fifth-generation art-dealing fortune makes it to the sixth.

In 2011, French tax authorities informed the Wildenstein heirs that their audit had found taxable assets worth more than 10 times what the family had declared. In what prosecutors have called "one of the longest and most sophisticated frauds" in postwar France, authorities sought severe penalties against Guy Wildenstein, his nephew and sister-in-law, a notary, two lawyers and two trustees, the Northern Trust Fiduciary Services in Guernsey and the Royal Bank of Canada Trust Company.

Decision. Despite finding that the Wildensteins' financial arrangements—especially the trusts based in the Bahamas, Guernsey and the Cayman Islands—showed a "will to dissimulate," and a "clear attempt to avoid" paying taxes, the court acquitted the defendants based on insufficient evidence and a loophole in the French tax legislation.

The court noted that the law requiring reporting of trust assets only came into force in 2011, 10 years after the Wildenstein patriarch's death. This law does not have retroactive effect and no other French law detailed how the transmission of trust funds were to be taxed until 2011.

"It is not the role of the court to take the place of the legislator," the court said. While the public will no doubt struggle to accept the acquittal, given the wealth of the defendant, the court added that justice must treat everybody equally, "be they rich or destitute." ■

FOUNDATIONS

New Hampshire could be first US state to allow establishment of foundations

The US state of New Hampshire has passed *Senate Bill 225* titled *'Revising the New Hampshire trust code'*. The bill:

- Makes changes to the statutes governing trusts, trust companies and family trust companies.
- Creates a new chapter defining and governing civil law foundations.

If enacted, the bill would allow the formation, registration, and domestication of foundations, from October 1, 2017, making New Hampshire the first US state to allow for the establishment of foundations.

SB225 proposes the *New Hampshire Foundation Act*, which would apply to foundations and foreign foundations. Under the Act, a foundation is a legal entity that holds and manages its assets for the benefit of its beneficiaries or in furtherance of its purposes. Its purposes—which may be charitable or non-charitable—may be set out in either its certificate of formation or bylaws, and must be lawful, not contrary to public policy, and possible to achieve.

The Act uses existing New Hampshire laws for its definitions. For example, it draws on:

- the trust laws to define the rights and duties of the founders, beneficiaries, directors, and protectors, instituting the processes and parameters for modifying or reforming a foundation's governing instruments, and establishing the probate court's jurisdiction over foundations and their internal affairs.
- the company laws for the procedural rules governing the formation, registration, domestication, and dissolution of a foundation.

For New Hampshire tax purposes, a foundation will be taxable in the same manner as a trust and, therefore, generally exempt from tax. The bill amends the state's tax laws so that a foundation will be treated in the same manner as a trust.

A foundation, however, will not be exempt from tax, if it has transferrable interests that are functionally equivalent to company shares or if it directly engages in business activities.

By recognizing foundations, New Hampshire would enable families from countries in which foundations are preferable to trusts as wealth management vehicles to avail themselves of a US-based structure. ■