The Aver Advisory

AUTUMN 2018

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Privacy

Information exchange under Common Reporting Standard challenged

In re: UK Information Commissioner's Office, Complaint filed July 24, 2018

In July 2018, a formal complaint challenging the legality of the CRS and beneficial ownership registers was filed by the law firm Mishcon de Reya, on behalf of an unidentified EU citizen. The complainant has international ties and now lives in Italy. She lived in the UK for several years and still has a UK bank account with a modest balance.

The complaint argues that the public disclosure and exchange of sensitive data about the internal governance and ownership of private companies is over-reaching and unnecessary to achieve the stated objectives of the CRS—to fight tax evasion, money laundering and other financial crimes.

The CRS affects all account holders regardless of account size. Potentially exposed information includes personal data, such as the name, date and place of birth, and tax identification number of the account holder; as well as financial data, such as the account number and account balance.

It is argued that the public disclosure of this data exposes compliant account holders to risks of hacking and data loss, and could lead to large scale identity theft.

More than 100 countries have joined the CRS, many of which have lesser standards of data protection and information security than exist in the UK.

The complaint contends that the exchange of information under the CRS infringes on an individual's fundamental rights to privacy and data protection. Such rights are the foundation of the *General Data Protection Regulation*—entered into force on May 25, 2018—and emanate directly from *European Convention on Human Rights* and the EU's *Charter of Fundamental Rights*. To be justified, an infringement of these rights must have a clear legal basis, pursue a legitimate public interest, and be proportionate.

The complainant's lawyer's note that there is a wealth of evidence supporting their complaint, including comparisons between the CRS and the *Data Retention Directive*, the latter of which was effectively declared illegal by the European Court of Justice in 2016. ■

Beneficiaries of foreign trusts to be excluded from UK public registry

UK Department for Business, Energy & Industrial Strategy, "A Register of Beneficial Owners of Overseas Companies and Other Legal Entities", Consultation Response, March 2018

In a recently published consultation paper, the UK Government addressed the scope of application of a new public register of beneficial ownership of foreign companies and entities. The draft *Registration of Overseas Entities Bill* requires foreign entities, who own or wish to own land in the UK, to take steps to identify and register their beneficial owners. Most importantly, the register will exclude the beneficiaries of trusts.

The paper notes that "unlike companies, trusts are typically used by private individuals for managing family owned assets including for minors and vulnerable family members. Publishing these persons' details would not be proportionate and effective especially as disclosure would undermine family confidentiality." The draft bill will be introduced to the UK Parliament in the summer of 2019 and the register will be operational in 2021. ■

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Taxation

Dutch company found to be resident in Canada based on effective management and control test

Landbouwbedrijf Backx B.V. v. The Queen, Tax Court of Canada, 2018 TCC 142

A Canadian court recently found that a Dutch-incorporated company (BV), with its sole director resident in The Netherlands, was resident in Canada due to the location of its central mind and management.

Facts. The case involved two individual shareholders/directors—the Backxes—who previously owned and operated a dairy farm in The Netherlands. In 1998, the Backxes sold their Netherlands farm and immigrated to Canada. Prior to immigrating, the Backxes resigned as directors of BV, but remained as shareholders. The new director lived in The Netherlands and was the sister of the wife.

In 1998, after immigrating, the Backxes purchased a Dairy farm in Canada, which was 51% owned by the Backxes and 49% owned by BV. In 2009, the Dutch company sold its interest in the farm for $4.5 million, resulting in a capital gain of $1.7 million.

The Backxes claimed that the transaction was protected under the *Canada-Netherlands Tax Treaty* and that the gain was not subject to tax.

Decision. The court found no evidence that the director in The Netherlands exercised effective management and control over the company. For example:

- The sister had no experience in farming and no prior business experience.
- The sister became director to assist the Backxes with their tax planning.
- The sister had no responsibilities beyond administrative tasks.
- It was the Backxes, not the sister, who made all decisions regarding both the purchase and sale of the farm in Canada.
- The sister only got involved after decisions had been made in order to provide corporate authorizations.

The court found that it was the Backxes, as *de facto* directors, who managed and controlled the Dutch company. ■

Taxation

Denial of EU freedom of establishment under 1999 EU-Switzerland Agreement

Christian Picart v Ministre des Finances et des Comptes publics, Court of Justice of the European Union (C-355/16), March 15, 2018

In March 2018, the European Court of Justice held that a natural person who transfers his place of residence to Switzerland and then manages shareholdings in companies located in EU member states from Switzerland, may not rely on the provisions concerning the freedom of establishment set out in the *1999 EU-Switzerland Agreement on the Free Movement of Persons* (AFMP), for capital gains tax purposes.

Facts. Christian Picart, founder of the restaurant chain Buffalo Grill—with over 350 steakhouse restaurants throughout France, Spain, Switzerland and Luxembourg—is a French national. In 2002, he transferred his residence from France to Switzerland. At the time of this transfer, he held significant shareholdings in a number of French companies.

Picart declared an unrealised capital gain on the shares, appointed a tax representative in France and provided a bank guarantee, in order to benefit from a suspension of payment of the tax payable on that capital under French law.

In 2005, Picart transferred his shares and the suspension ended as a consequence. The French tax authorities reassessed the capital gain declared and found Picart liable for income tax and social security contributions retroactive to 2002, along with penalties.

Decision. The court found that Picart's situation did not fall within the notion of "self-employed persons" within the meaning of the AFMP and therefore he could not rely on that agreement.

"When a natural person transfers his residence from one state to another state party to that agreement, while maintaining his economic activity in the first of those two states, without undertaking every day, or at least once a week, a journey from the place of his economic activity to that of his residence," the court said, then this situation "provides for the immediate taxation of the unrealised capital gains on significant shareholdings held by that person in companies governed by the laws of the first state at the time of the transfer of residence." ■

Privacy

Switzerland hesitates on plans to abolish bearer shares

Swiss Federal Council, Consultation Paper, April 24, 2018

Switzerland's plan to abolish bearer shares has stalled. The draft bill, published in January 2018, proposes the automatic conversion of bearer shares into registered shares upon the bill's entry into force. The holders of bearer shares who do not comply within the stated timeframe would automatically lose all rights to such bearer shares—akin to expropriation.

Three out of Switzerland's four most powerful political parties have opposed the bill on grounds that it goes beyond what the FATF or the OECD demanded. The bill is therefore unlikely to find support in Parliament. ■

No collection of beneficial ownership data at time of US company formation

Counter Terrorism and Illicit Finance Act (HR 6068), Cmte on Financial Services, June 11, 2018

A June 2018 revision of the draft US *Counter Terrorism and Illicit Finance Act* has been stripped of provisions that would require collection of beneficial ownership data at the time of company formation.

The federal bill was introduced to Congress last November and included the creation of a national directory of beneficial owners of legal entities. These clauses were eliminated just before the bill passed to the House Financial Services Committee for 'mark-up' (the process by which bills passing through Congress's two houses are edited to be compatible with one another). ■

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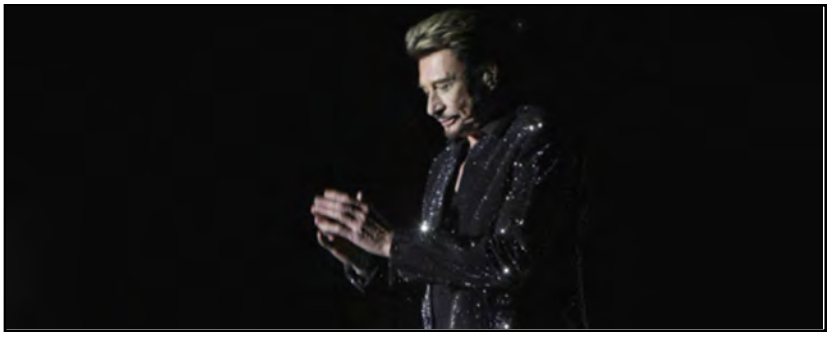

Trusts

Court stops beneficiaries from terminating trust

Horgan v. Cosden, 2018 WL 2374443 (Florida 2nd DCA 2018)

The Florida appellate court recently held that a trust could not be terminated because doing so would go against the settlor's intent. The decision is a reminder that just because all beneficiaries agree that a trust should be terminated, a court will not always automatically grant such termination.

Facts. A revocable trust became irrevocable upon the settlor's death. The trust provided for the income generated by the trust to be distributed to the settlor's son at least quarterly, for his lifetime, with the remainder to pass to three educational institutions at her son's death.

The beneficiaries entered into an agreement to terminate the trust and divide the $3 million of trust assets between them based on their interests. They argued that doing so would be in the best interests of themselves, as beneficiaries, and would eliminate unnecessary expenses and trustee fees.

The trustee of the trust did not sign the agreement and argued that termination of the trust was not in accordance with the settlor's intent.

Decision. The court explained that a settlor's intent is at the heart of trust interpretation. In this case, the settlor wanted to provide for her son financially through incremental distributions of income during his lifetime and then give the entire remaining principal to the educational institutions named in the trust.

The court also pointed out that the settlor amended her trust at an earlier date and could have made an outright distribution to her son at that time but chose not to. As such, the court found that terminating the trust before the settlor's son's death would frustrate the purposes of the trust. Consequently, the court prohibited the termination of the trust. ■

Celebrity Estates

Legal battle intensifies over estate assets of French rock legend Johnny Hallyday

Hugely popular in France and credited for having brought rock and roll to the French Republic, Johnny Hallyday was usually referred to as simply "Johnny". While considered a national monument and part of the French cultural legacy, Johnny was outspoken about his frustration with the French tax system.

To avoid the high tax rate imposed by the French government, Hallyday owned a chalet in Gstaad, Switzerland, from 2006 to 2015. He said he would move his residency back to France, if it changed its tax laws.

Following an investigation by a Swiss journalist in January 2014, which showed that Hallyday did not spend enough time in Gstaad to qualify as a Swiss resident, Johnny stated that his primary residence was in the US. At the time of his death in December 2017, Hallyday was living in Los Angeles, California.

In 2014, Hallyday prepared a will under California law by which he disinherited his two oldest children and left the entirety of his estate—worth an estimated €100 million—to his fourth wife and their two adopted school-aged children.

His older children have contested the will, arguing that under France's forced heirship rules, they cannot be disinherited. In April 2018, a French court issued a temporary freeze of several of Hallyday's estates in France. Whether Johnny's last wishes are respected, will now depend on a judicial determination of his primary residence. ■

Life Insurance

New York raises standards for brokers of life insurance

Revised Text of Proposed Reg. 187 "Best Interest" Amendments, NYDFS, May 2018

New York has revised its proposed regulation for a best-interest standard to spell out the duties of sellers of life insurance and annuity products in the state.

The changes include a requirement for insurers to establish protocols to ensure that any advice given to consumers is in their best interest.

A recommendation is in the best interest of a consumer if it furthers the consumer's needs and objectives, and is made "without regard to the financial or other interests of the producer, insurer or any other party."

The new rules would:

- Require disclosure of all suitability considerations and product information that form the basis of any recommendation.
- Permit agents or brokers to make a recommendation only if they have a "reasonable basis to believe that the consumer can meet the financial obligations under the policy."
- Prohibit an agent or broker from telling a consumer that a recommendation is part of financial planning, investment advice or related services (unless the agent or broker is a certified professional in that area).

New York's best-interest regulation is considered one of the toughest in the United States.

The new rules come into effect August 1, 2019, for annuity contracts, and six months afterward for life insurance contracts. ■