# The Aver Advisory

SPRING 2020

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# Privacy

## Random searches of digital devices at US borders ruled unconstitutional

*Alasaad et al. v. McAleenan et al., US District Court (Boston, MA), November 12, 2019*

A US federal court has ruled that random searches of travelers' electronic devices by federal agents at airports and other US ports of entry are unconstitutional.

**Background.** Agents of US Customs and Border Protection and US Immigration and Customs Enforcement have increasingly granted themselves broader discretion to undertake manual inspections of travelers' electronic devices including cell phones, laptops or tablets and to scan through their contents. Based only on intuition rather than facts, agents have demanded that travelers turn over their devices if they have doubts about a traveler's true intent in entering the US. On these occasions, agents often detain the individual while they examine their emails, text messages and social media accounts.

The number of electronic device searches at the border has ballooned from about 8,500 in 2015 to more than 30,000 in 2018, notes the American Civil Liberties Union.

**Decision.** The court noted that while US Customs and Immigration agents have a paramount interest in protecting the border, the privacy interests of all travelers to the US, whose troves of personal information could otherwise be searched without cause, had to be balanced against their privacy rights. The court held that to the extent that US Customs and Immigration policies allowed for such searches without cause, they violated the US Constitution's Fourth Amendment protections against unreasonable search and seizure.

The court stated that in order to search a device, border agents must articulate specific facts that would allow them to draw an inference that a traveler's device contains digital contraband—for example, child pornography or counterfeit media. Requiring agents to detail "reasonable suspicion"—as opposed to impermissible or unlawful travel motives, for example—should greatly reduce the number of random searches by border agents. ■

## Court confirms beneficiaries' rights to information

*Dawson-Damer v. Taylor Wessing, 2020 EWCA Civ 352, March 11, 2020*

The England and Wales Court of Appeal recently clarified that beneficiaries have access to advice obtained by the trustees for the benefit of the trust.

**Background.** Ashley Dawson-Damer and her two children are beneficiaries of certain Bahamian trusts, which held in excess of $400 million. These family trusts were restructured between 1988 and 1992 and the claimants discovered that substantial funds had been paid out of one of the trusts for the benefit of other beneficiaries, potentially in breach of trust.

The claimants served a formal request—under the UK *Data Protection Act*, seeking all data for which they were subjects—on London solicitors, Taylor Wessing, who acted for the trustee.

**Decision.** The UK Court of Appeal confirmed the well-established principle that under English law a beneficiary is in a position of so-called "joint privilege" with a trustee and that, as a result, personal data sought by a trust beneficiary cannot be withheld on the grounds of legal advice privilege belonging to the trustee. ■

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# Tax Treaties

**Court confirms that treaty shopping is not abusive**

*Canada v. Alta Energy Luxembourg S.A.R.L., 2020 FCA 43, February 12, 2020*

Canada's Federal Court of Appeal recently confirmed that a Luxembourg corporation could rely on the *Canada-Luxembourg Tax Treaty* to claim an exemption from Canadian tax on a $380 million capital gain realized on the sale of shares of a Canadian company engaged in oil and gas exploration.

**Facts.** The original holder of the corporate shares was a Delaware LLC, which did not have access to any tax treaty exemption. As part of an international restructuring, Alta Energy was incorporated in Luxembourg and the subject shares were transferred to it at a time when there had been no gain in value of the shares.

Alta Energy later sold the shares at a substantial gain and then claimed the tax treaty exemption. The issue on appeal was whether the restructuring transactions resulted in an abuse of tax laws, and whether the tax authority could then apply Canada's general anti-avoidance rule (GAAR) to deny the taxpayer from claiming the treaty exemption.

The tax authority argued that, in order to obtain the benefits of the treaty, Alta Energy itself needed to make an investment in the Canadian company and the underlying assets of the business.

**Decision.** The court noted that the words of the treaty require that its benefits apply to Luxembourg residents, not investors. There is no distinction in the treaty between residents with strong economic or commercial ties and those with weak or no economic or commercial ties. If a person satisfied the definition of resident, then that person is a resident for purposes of the treaty.

The court clarified that GAAR cannot be used to justify adding a requirement for investment that is not present in the treaty.

On the issue of abusive tax planning, the court held that treaty shopping, in and of itself, is not abusive. It noted that a person will qualify for the exemption under the Luxembourg treaty if:

- that person is a resident of Luxembourg for the purposes of the treaty, and
- the value of the shares is principally derived from immovable property (other than rental property) situated in Canada in which the business of that corporation is carried on.

Finding that the taxpayer satisfied these requirements, and that nothing beyond being a "resident" is required to access the treaty, the Court held that the taxpayer was entitled to the exemption from Canadian tax provided in the treaty.

**Comments.** While the taxpayer in the Alta Energy decision was successful, the ability to rely on this case is limited. Historically, Canada's main tool to combat treaty abuse, including treaty shopping, has been the GAAR. However, the *Multilateral Convention to Implement Tax Treaty Related Measures to Prevent Base Erosion and Profit Shifting* (MLI) introduces countermeasures to prevent treaty abuse, such as the principal purpose test (PPT).

The MLI is an international tax treaty that modifies the majority of bi-lateral tax treaties to incorporate these countermeasures, with coming-into-effect dates that vary from treaty to treaty. The MLI imports the PPT into most of Canada's tax treaties in respect of treaty exemptions for tax on capital gains realized in taxable periods beginning as early as June 1, 2020, even if the gains accrued in prior periods.

The Alta Energy decision may encourage taxpayers wishing to crystalize accrued gains prior to the coming-into-effect of the PPT. ■

# International Tax Planning

**Court rules right to freedom of establishment does not include right to import foreign tax losses**

*AURES Holdings a.s. v. Czech Appellate Financial Directorate, Court of Justice of the European Union, Case C-405/18, February 27, 2020*

The Court of Justice of the European Union recently held that freedom of establishment, as defined by the *Treaty on the Functioning of the European Union*, does not require a host state to allow relief for losses sustained by a company in another member state against profits subsequently arising in the host state.

**Facts.** Aures was founded in 1992 as the successor company of AAA Auto Group N.V, which was incorporated in the Netherlands. Aures had its place of effective management in the Netherlands and was deemed to be Dutch tax resident.

In 2007, Aures incurred tax losses in the Netherlands. In 2009, the company transferred its place of effective management to the Czech Republic and thereby became Czech tax resident.

Aures submitted a claim to deduct the losses generated in 2007 in the Netherlands against its taxable profits generated in the Czech Republic for the 2012 tax period. The Czech tax authorities rejected the claim taking the position that a tax loss carry-forward can only be utilised if the losses were incurred in the Czech Republic and not in another Member State. Aures appealed arguing that the company was exercising its right to freedom of establishment when it transferred its place of effective management to the Czech Republic and that being prohibited from using tax loss carry-forward, in the Czech Republic for tax losses incurred in the Netherlands amounted to a violation of that freedom.

**Decision.** The court ruled against Aures. It held that freedom of establishment does not prevent a member state from limiting the use of tax losses in its jurisdiction where those losses were incurred in another member state prior to the transfer of a company's place of effective management. ■

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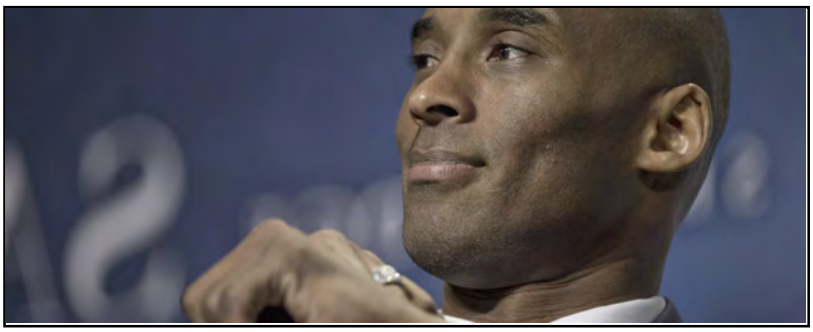

# Estate Planning

**Court declares napkin will to be valid**
*Gust v Langan, Court of Queen's Bench for Saskatchewan, 2020 SKQB 42*

A will written by hand on a McDonald's napkin has been declared legally valid by a Canadian court. While holograph wills are recognized as valid in the Canadian Province of Saskatchewan, the court noted that they are often drawn so informally that the court is uncertain whether the author of the document intended to create a will.

Philip Langan, who died in 2015 at age 80, left only a napkin with his name and instructions to split his property evenly between his seven children. The court found that the deceased wrote the will while sitting in a McDonald's restaurant because he thought he was having a heart attack.

Relying on sworn affidavits from three of Langan's children, testimony that he had referred to the napkin as his will, and the fact that at the time of writing it, Langan thought he was having a heart attack, the court found "sufficient evidence to establish circumstances that support a finding that Langan had the requisite testamentary intention to create a will." ■

**Beneficiary List doesn't exist**
*Will of Katz, 2019 WL 1750684 (New York Surrogate's Court, April 16, 2019)*

*In re Will of Katz*, the decedent's will instructed the executor to distribute an estate worth over $10 million to "people and charities on a list to be provided to him by the testator." The problem was that the list was never created.

New York's Surrogate's Court held that despite the lack of existence of the list, the will is a valid testamentary instrument. The court granted the executor's motion for examinations likely to find evidence as to the testator's intention regarding the list that was never presumably created.

The first and most obvious lesson from the case is that if a provision in a will refers to a list, it is best to prepare that list contemporaneously with the will. ■

# Celebrity Estates

**NBA superstar Kobe Bryant's death reminds us to expect the unexpected**

Kobe Bryant took life by the horns. He earned an estimated $680 million during his 20-year career between endorsements and his actual Los Angeles Lakers' salary. He also co-founded the successful venture capital firm Bryant Stibel, which was expected to fill the role that charity normally plays with ultra-high-net-worth retirees.

At 41 years of age and with an exciting new investment career ahead of him, estate planning was not likely a priority for Kobe Bryant. Nonetheless, Bryant did establish a trust in 2003 to support his wife and his first daughter Natalia, now 16 years old.

Bryant's trust was modified several times and was last updated in 2017 to include his third daughter Bianka (2 years old), and his second daughter Gianna (13 years old), who passed away with her father in a helicopter crash.

Unfortunately, the trust was not updated following the newest addition to Kobe's family in 2019. Kobe's wife, Vanessa Bryant, recently applied to the court to add his infant daughter Capri (7 months) to the trust.

It is obvious that Kobe was aware of the need to update his trust after the birth of Capri—as he had already amended the trust several times before. A standard revocable trust can always be updated during the lifetime of the settlor. Upon the death of the settlor, however, the trust becomes irrevocable. Any changes must then be approved by the court.

It is also clear that Vanessa is aware of the implications of this omission; that Capri and her descendants stood to be deprived of a one-third share of the trust assets, representing at least $200 million.

In addition, following Kobe's death, there were no court proceedings—implying that Kobe did not die without a will, that there was no will to probate, and that he had likely established a trust, which afforded his family a degree of privacy. Some privacy has now been lost.

This situation highlights the importance of carrying out an annual review of a client's estate plan to ensure that it accurately reflects changing laws, changing family situations and the settlor's current wishes. ■

# Information Exchange

**Complaint over 'insecure' CRS data exchange**

British law firm Mishcon de Reya has lodged a complaint with the French data protection watchdog CNIL *(Commission Nationale de l'Informatique et des Libertés)*, alleging that the automatic exchange of client account data pursuant to the OECD's Common Reporting Standard (CRS) is insecure and thereby unlawful under the *EU General Data Protection Regulation*.

The CRS system connects the tax authorities of 86 countries. In 2018 alone, the system transmitted 4,400 bilateral messages concerning 41 million accounts. Information exchanged under the CRS includes sensitive personal data—including the name, date and place of birth, and tax identification number of the account holder—as well as financial data about the financial account itself such as the account number and balance. This exposes account holders to risks of hacking and could lead to blackmailing, kidnapping and identity theft.

Mishcon de Reya published a list of hacking and data breach incidents in the context of international exchange of information. The number of incidents and their scale are shocking. Feel free to let us know if you would like to receive a copy of the list. ■