THE AVER ADVISORY

SUMMER 2022

presented by Aver Associates *Estate Planners & Trustees*

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TAXPAYER RIGHTS

EU court strikes down Spain's penalty regime for failure to report overseas assets

European Commission v. Kingdom of Spain, Case C-788/19, Court of Justice of the European Union, January 27, 2022

On January 27, 2022, the Court of Justice of the European Union struck down a Spanish regulation that forced thousands of tax residents—owning assets abroad worth more than €50,000—to disclose those foreign assets to the Spanish Tax Agency under penalty of significant fines.

Facts. The Spanish reporting obligation was introduced in October 2012 and requires Spanish tax resident individuals, entities and permanent establishments to use Form 720 to provide information concerning their overseas assets and rights. The assets to be declared include accounts held in foreign institutions, certain securities and rights, life or disability insurance, life annuities and overseas real estate properties or rights on such properties.

Under the regulation, the acquisition, possession or declaration of overseas assets and rights—which were not duly declared in Form 720—were attributed to the oldest tax year which had not yet become statute barred.

The regulation imposed high fines for failing to file Form 720 on time or filing incomplete, incorrect or false information. Taxpayers were also subject to flat-rate fines—for example, a fine of €5,000 per single piece of incomplete data. In addition, the failure to comply was qualified as a serious tax offense, and subject to a penalty of 150% of the amount of tax due.

The European Commission had warned Spain in 2017 of the discriminatory way in which it processed tax declarations of assets held abroad. It demanded immediate changes in the 720-tax model.

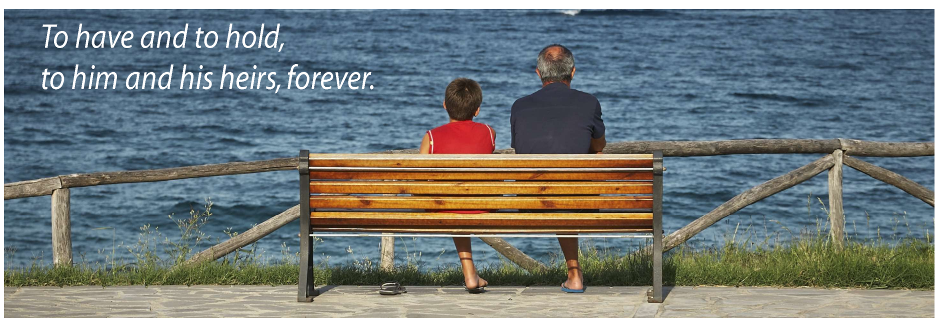
Decision. In regard to the lack of a statutory limitation period, the court found that the practical effect was to allow authorities to make an additional assessment of the tax due without that assessment being subject to any time limit. The court held that the power to invoke a limitation period that had already expired vis-à-vis the taxpayer undermined the fundamental requirement of legal certainty.

The court also found that the penalty regime resulted in disproportionate punishment, because the financial burden could be higher than the value of the undeclared or unduly declared assets and rights.

The penalty regime was also found to be discriminatory, because the financial burden was disproportionate to the penalties imposed for similar infringements in the general tax law.

As a result, the court ruled that the consequences for non-compliance with Form 720 could prevent Spanish taxpayers from investing abroad and, therefore, qualified as a disproportionate restriction on the free movement of capital contrary to EU law.

The Spanish Government has announced that it will change the rules to ensure they are proportional and will guarantee a statutory limitation period. The court's ruling does not invalidate the obligation to provide information concerning assets and rights located abroad. ■



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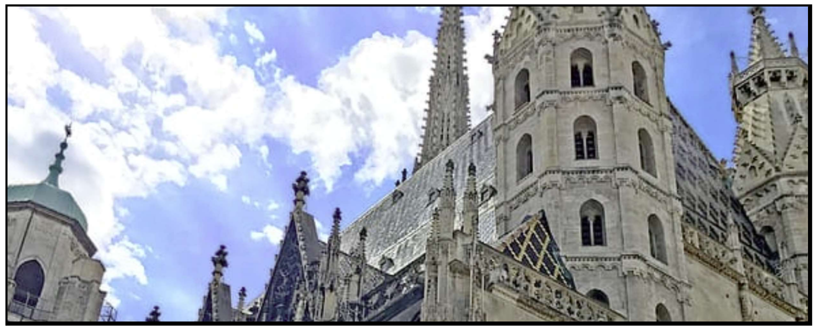

RESIDENCY

Preservation of long-term EU resident status, despite limited presence in EU territory

In re: Landeshauptmann von Wien, Case C-432/20, Court of Justice of the European Union, January 20, 2022

On January 20, 2022, the Court of Justice of the European Union ruled that a third-country national does not lose their long-term resident status even if their presence in the EU is limited to only a few days a year.

Facts. The Austrian Government refused the application of a Kazakh national for the renewal of his long-term residence permit—as an EU resident—on the ground that, during the five years preceding his application, he had only been present in EU territory for a few days each year. Pursuant to an EU *Council Directive*, a long-term resident loses the right to long-term resident status in the event of absence from EU territory for a period of 12 consecutive months.

The Administrative Court of Vienna requested an interpretation from the Court of Justice as to whether the directive meant that any physical stay, no matter how short—during a 12-month period—precludes the loss of long-term resident status.

Decision. The court noted that the meaning of the term "absence" in everyday language is merely "non-presence," and that "any physical presence of the person concerned in that territory is capable of interrupting such an absence."

The court added that where residence—and not merely presence—is required, "the directive expressly states so by using the relevant expressions." A strict interpretation is therefore justified by the objective of the directive; notably, the integration of third-country nationals who have already demonstrated that they are settled, "by bringing their rights closer to those enjoyed by EU citizens," and thereby assuring such persons "an adequate level of legal certainty."

The court ruled that "any physical presence of a long-term resident in the territory of the European Union during a period of 12 consecutive months—even if such a presence does not exceed a total duration of only a few days—is sufficient to prevent the loss of his or her right to long-term resident status." Furthermore, "once that status is acquired, it is not necessary for the person concerned to have his or her habitual residence or centre of interests in the EU." ■

CITIZENSHIP AND RESIDENCY

EU votes on termination of citizenship and residence by investment schemes

On March 9, 2022, the European Parliament overwhelmingly voted—595 of 681 votes—to abolish citizenship-by-investment schemes and to better (more strictly) regulate residence-by-investment schemes in the European Union.

The Parliament stressed that CBI schemes (aka golden passports)—under which high net worth third-country nationals obtain citizenship rights in exchange for a sum of money—undermine the essence of EU citizenship. It described the practice as "free riding" and underscored concerns about the commodification of EU citizenship. The Parliament, in its proposal, requested a phasing out of CBI in the Union by 2025, including in third-countries with a visa-free waiver to the Schengen area.

Both the Commission's president and commissioner hold negative opinions on these programs; their stance may in fact be more aggressive than that of the Parliament. We are speaking of Malta of course, but also of five Caribbean CBI countries. The Commission has already taken legal proceedings against Malta to force the shutdown of its latest CBI program; an outcome which is likely simply a question of time.

Noting the less severe risks posed by RBI schemes (aka golden visas), Parliament called for enhanced rules to help tackle money laundering, corruption, and tax evasion. These rules include more stringent vetting and due diligence systems, reporting obligations for member states, requirements for minimum physical residence of applicants and effectively checking that (biannual in-person reporting appointments and on-site visits to the domicile of the individuals concerned). RBI applicants would be excluded from the current Long-Term Residence Directive.

Since 2014, the European Parliament has expressed its concern regarding CBI and RBI schemes on numerous occasions and called for their termination. It is estimated that—between 2011 and 2019—over 130,000 people have secured residence or citizenship in EU Member States via CBI or RBI schemes. ■

CITIZENSHIP AND VISAS

US to clamp down on citizenship-by-investment schemes

H.R.6911-117th Congress (2021-2022) - No Travel for Traffickers Act of 2022

In March 2022, legislation was introduced in the United States that would, among other objectives, prohibit participation in the US Visa Waiver Program of certain countries that offer citizenship-by-investment programs through which passports are sold in exchange for economic investment in the country.

In addition, the legislation calls for the Executive Branch to try to persuade the United Kingdom and EU countries to eliminate visa-free travel for countries selling passports. In Malta, for example, which operates a citizenship-by-investment program, the legislation would not differentiate between Maltese citizens by birth or by investment; rather, all would have to apply for a visa before entering the United States.

Even in Hungary, which has been among the most prolific issuers of EU citizenship-by-descent—the granting of citizenship to so-called "Hungarians beyond the borders" without the need for these citizens to reside physically in Hungary—there has been a noticeable shift. US-bound Hungarians whose passports list a country other than Hungary as the country of birth have found the online system automatically rejecting their requests for travel authorization. ■

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INTERNATIONAL TAX PLANNING

European Commission proposes directive on misuse of shell entities

Commonly referred to as the “unshell initiative," the European Commission—on December 22 2021—released proposed rules to prevent the misuse of so-called “shell” entities for tax purposes in the EU. The directive targets “the setting up of undertakings within the European Union which are presumably engaged with an economic activity but that, in reality, do not conduct any economic activities”.

The directive establishes a set of measures to identify such shell undertakings along with the tax consequences, including the denial of a tax residence certificate for the shell undertaking. This would in turn prevent the shell entity from benefitting from the relief or reduction of withholding tax based on EU directives or double tax treaties.

If the draft directive is adopted in its current form, member states will need to implement the proposed measures by June 30, 2023 and apply them by January 1, 2024.

Critics, including Luxembourg Finance Minister Yuriko Backes, have commented that the proposed rules “overshoot the mark” and have pointed out that general substance tests are found in various measures already implemented, especially at the EU or international level. It is questionable, therefore, whether an additional layer of anti-abuse provisions is necessary. ■

CELEBRITY ESTATES

Wealth of Bacardi rum empire locked up in trust

Obergericht des Kantons Zürich, December 9, 2021

When Lord Luis Bacardi—the grandson of Facundo Bacardi, creator of the world-famous Bacardi rum—fell seriously ill in 2002, he instructed his lawyers to make arrangements for the financial future of his wife Monika and his only child Maria Luisa, who was born in 2001.

At that time, Luis already had a trust in the jurisdiction of Guernsey. The lawyers established a trust in Liechtenstein called the Bastille Trust and transferred a large portion of Luis’ assets—including his Bacardi Ltd. shares—to the Bastille Trust. When Luis died in 2005, Monika received a distribution from the trust. His daughter’s share was to be accumulated until she reached the age of 18 and then distributed according to Luis' wishes.

Shortly before Maria Luisa’s 18th birthday, the lawyers approached Monika and her daughter Maria Luisa, claiming that a first distribution of the accumulated dividends could not take place when the daughter came of age (as intended in the trust deed) due to alleged tax law concerns. The relationship with their lawyers and trustees quickly spiralled downward from there.

We understand the frustration of Maria Luisa, but we are not questioning the integrity of the advisors. When one reads the legal proceedings before the Zürich cantonal court and does some fact checking online, the impression one gets is that the official tax residency of Monika and Maria Luisa is Monaco, while they spend a lot of time elsewhere—Monika seems to be a globe trotter and to own a property two hours from Monaco, in St. Tropez.

Taking up residence in a jurisdiction like Monaco is tempting for tax and other reasons, but it is not that easy to claim tax residency compared to countries with proper tax treaties (for the avoidance of double taxation) such as Malta and Portugal.

Many tax immigrants in Monaco struggle with the rule that they should spend most of their time in Monaco, are becoming increasingly aware of the fragility of their tax situation and are beginning to take action. The popularity of Luxembourg life insurance solutions for income tax planning seems to be on the rise in Monaco for that reason. For the same reason, we are strong believers that tax immigrants and dual residents in general should consider a trust or foundation for inheritance tax planning. If properly set up, trusts and foundations allow the founders to live wherever they wish. The combination of life insurance and trusts and foundations works well in many countries. Before a distribution is made from the trust, however, the trustee is to take care of the beneficiary and has the legal obligation to ascertain all tax implications for the beneficiary. ■

TRUSTS

No-contest clause applies to a settlor who is the sole life beneficiary of a trust

McMurtrie v. McMurtrie, Supreme Court of Virginia, April 22, 2021, unpublished

The Supreme Court of Virginia recently reversed a trial court ruling, which held that a no contest clause in a trust deed did not apply to the sole beneficiary, when the latter is also the settlor of the trust.

Facts. Alexander McMurtrie created the Alexander McMurtrie Revocable Trust that included a no contest clause, stipulating that any beneficiary of the trust will forfeit their interest in the trust—and that of any of their descendants—if they seek to impair or invalidate any provision of the trust.

The trust provided that the settlor was the sole beneficiary during his lifetime. The settlor requested distribution of the assets of the trust to himself. One of the trustees refused to distribute anything to the settlor on the basis that the trustee had the absolute discretion to distribute the assets of the trust. The settlor argued that the no contest clause did not apply to him because he was defined in the trust as “Trustor”, and not a beneficiary.

Decision. The court held that it was clear that the settlor was the sole beneficiary of the trust during his lifetime, and that the language of the no contest clause required a strict interpretation. As a result, the court held that the no contest clause did indeed apply to the settlor. ■