THE AVER ADVISORY

OCTOBER 2012

presented by Aver Associates *Estate Planners & Trustees* contact@averassociates.com

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TAX AGREEMENTS

New double tax agreement between Switzerland and Malta comes into force

Switzerland's double tax agreement with Malta entered into force on July 6, 2012. The provisions of the agreement will be effective as of January 1, 2013 and will have a positive impact on tax planning involving dividends, interest and royalties.

Dividends and interest. Dividends paid from a Swiss subsidiary to its Maltese parent, and interest payments between related companies, are exempt from withholding tax, provided that:

i) The receiving company owns at least 10% of the capital of the company making payment.

ii) Such participating interest has been held for at least one year.

iii) Both companies are subject to tax in their respective territories; that is, not exempt from income taxes covered by the treaty (for Switzerland, this means no exemption for federal/cantonal/communal income tax).

Otherwise, a 15% withholding tax will be levied on dividend payments, while a 10% withholding tax will apply to interest payments. Dividends paid from a Maltese subsidiary to its Swiss parent are never subject to withholding tax in Malta.

Royalties. The agreement provides for a full withholding tax exemption on royalty income.

Anti-avoidance. The anti-abuse clause, applied to wholly artificial arrangements, shall not affect situations corresponding to an economic reality reflected by a business or management activity. ■

Hong Kong-Malta tax treaty now in force

The Hong Kong-Malta income tax agreement entered into force on July 18, 2012 and will be effective from January 1, 2013 in Malta.

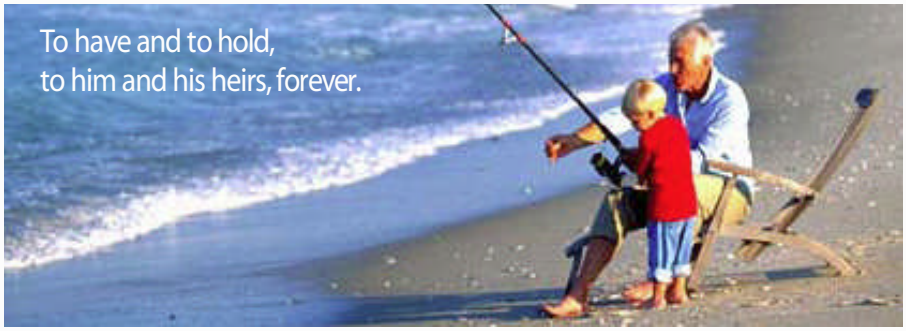
The agreement provides unconditional exemptions from withholding tax for all dividends and interest. ■

New anti-avoidance rule creates uncertainty for India-Mauritius route

India's new general anti-avoidance rule, proposed to be effective from April 1, 2013, spells trouble for Mauritius (read: opportunities for Malta) as an intermediary jurisdiction for investments into India. Almost 40% of investments into India currently come through Mauritius.

The countries plan to discuss the inclusion of a limitation of benefits clause, similar to that of the India-Singapore tax treaty, ensuring benefits to only genuine Mauritius-based firms.

Since 2005, India's tax agreement with Singapore states that only companies spending a minimum of $200,000 p.a. in Singapore can avail the benefits of the treaty. ■



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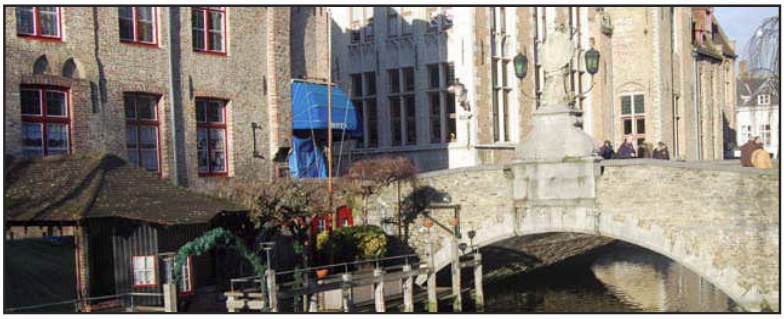

TRUSTS

Excessive powers of advisor strip trust of discretionary character

In re: The X Trust, Belgian Ruling Commission, Advance Ruling 2011.418, December 6, 2011

A recent decision highlights the impact of a settlor's letter of wishes on the tax planning benefits of an irrevocable and discretionary trust. It was held that the settlor retained control of the trust and, as such, any income benefits the settlor would acquire from the trust was held to constitute taxable income.

Facts. The taxpayer is a Belgian citizen who emigrated from Belgium 20 years ago and has since been working around the world for various international firms. He wishes to reside once again in Belgium, where his family resides. The taxpayer has three children living and resident abroad.

Several years ago, as part of a family estate plan, the taxpayer settled an irrevocable and discretionary trust under the laws of Jersey. The taxpayer, his three children, his father, and a charity are named as beneficiaries.

A professional institution was appointed as protector of the trust. In addition, a third party—a private person residing in Belgium—was appointed as an advisor with specific powers and responsibilities, including the power to appoint new trustees, and the power to remove and replace the protector.

According to the terms of the trust deed, the trustee has absolute discretion to change provisions in the trust instrument. However, the terms also state that should such change be necessary during the lifetime of the settlor, the trustee must obtain the written consent of the settlor. And, in fact, the trust deed was recently amended with the written consent of the settlor.

The settlor's letter of wishes states in very general terms that, while the settlor is alive, the trustee is requested to take into account the settlor's wishes on investment, management and distributions. After his death, the trustee is requested to take into account the wishes of the settlor's spouse. The relevant provisions read as follows:

> "Whilst I am aware that the discretions are under your absolute and unfettered control and that this letter has no binding legal effect, you may find it helpful if I express in this letter my considered views for the guidance of the Trustees in the exercise their fiduciary management and administration of the Trust.
>
> During my lifetime, I would like you to have regard for my wishes on distribution, investment and/or management of the capital and income of the trust fund and after my death to be guided by my spouse, if she be so living . . ."

Decision. In ruling that the trust could not be considered a discretionary trust, the commission relied on the facts that:

- The trustee must still obtain the written permission of the settlor in order to make changes to the trust deed.
- The advisor has the power to appoint new and additional trustees, as well as the power to appoint, remove or replace the protector.
- The trustee may only remove or designate additional beneficiaries with the consent of the protector.

The commission held that all benefits—excluding the benefits of the original capital contribution—received by the taxpayer from the trust will be considered taxable income.

Commentary. As has been clear for a couple of years, the Belgian Ruling Commission (consisting of selected tax officials of the Central Administration of Direct Income Taxes), takes a rather limited view towards the notion of "discretionary." While this position is not in line with private international law and the tax code, as the proverb says, "forewarned is forearmed" (un homme averti en vaut deux).

The fact that the Belgian resident settlor would effectively be the sole beneficiary after all, and that the trust in the end is controlled from Belgium, are not helpful facts. One cannot expect the taxman to bless an open door when one pushes it that far. ■

PRIVATE FOUNDATIONS

Founder determined to have relinquished control of assets

Gerechtshof Amsterdam (Amsterdam Court of Appeal), May 31, 2012

An older lady, who was the founder of assets in an Antillean private foundation, was determined to have relinquished control of said assets by the terms of the foundation charter. Consequently, she had no obligation to declare the foundation assets on her tax return.

Facts. The founder transferred the assets of her estate—valued at over 1.3 million euros—into a private foundation. The terms of the foundation charter stated that:

- Upon transfer, the founder no longer retained control of the assets.
- The beneficiary, upon death of the founder, was her only daughter.

The Dutch tax inspector claimed that the founder was obligated to include the foundation assets in her tax return as so-called box 3 capital. The lower court agreed.

Decision. On appeal, the court held that the wishes of the founder were in no way binding on the foundation council and could not be enforced.

The court also took the following circumstances into account:

- Subsequent to establishment of the foundation, the founder was under pressure from a third party to dispose of her assets.
- The founder would likely have disposed of the foundation assets to the benefit of the third party, if she had the power to do so.

Finally, the court noted that the foundation assets were ultimately donated prior to the death of the founder. This further confirmed the finding of the court that no box 3 tax was due. ■

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TAX LITIGATION

Court confirms taxpayer's right to remain silent in tax proceedings

Chambaz v. Switzerland, European Court of Human Rights, April 5, 2012

The Swiss Federal Tax Administration was found to have violated fundamental human rights of a taxpayer; namely, the right not to incriminate oneself and the right to access evidence held by the prosecuting authorities.

Facts. The applicant, Yves Chambaz, is a Swiss national who was born in 1954 and currently lives in Bermuda. He has been the subject of several sets of tax proceedings, also involving a number of companies to which he was connected.

In 1991, the Swiss tax authorities assessed the taxable income of Chambaz and found that the growth of his assets was disproportionate to his stated income. Chambaz challenged the decision.

During the examination of his objection, Chambaz was asked for various items of information, which he refused to provide. The appeal by Chambaz was therefore dismissed and he was fined several hundred thousand euros for refusing to produce the documents requested.

Chambaz then started proceedings at the Administrative Court of the Canton of Vaud. While these were pending (four years after the first tax assessments), the federal tax authorities opened an investigation against Chambaz for tax evasion.

Chambaz asked to consult the tax evasion file in order to be able to defend himself in the proceedings before the Administrative Court. The tax authorities denied his request.

In support of his appeal, Chambaz alleged several violations of his right to a fair trial, arguing that the requirement to produce the information in the assessment proceedings amounted to forcing him to incriminate himself in relation to the tax evasion investigation. He further argued that the simultaneous conduct of the two sets of proceedings was in breach of the presumption of innocence and that the refusal to give him access to the file contravened the principle of equality of arms.

Decision. The court held that by fining Chambaz for refusing to produce all the items requested, the tax authorities had put him under pressure to furnish documents, which would have provided information on his income and assets for tax assessment purposes.

Furthermore, by upholding the fines while an investigation was ongoing into alleged tax evasion concerning matters linked to those in respect of which Chambaz had exercised his right to remain silent, the Swiss courts had obliged him to incriminate himself. The court therefore held that a fundamental human right of Chambaz had been violated.

In regard to the principle of equality of arms, the court reiterated that the only permissible restrictions on access to all evidence in the prosecuting authorities' possession had to be justified by the protection of vital national interests or the preservation of the fundamental rights of others. The court held that no such circumstances were present in this case, and that Chambaz was denied access to certain documents due mainly to his uncooperative attitude.

As a result of these violations, the court ordered Switzerland to pay Chambaz an indemnity equal to all fines issued and all taxes raised. ■

TAX LITIGATION

No requirement for client to verify correctness of professional advice

Hanson v HMRC, Tax Chamber of the First-Tier Tribunal, September 6, 2012

Following an aggressive stance taken by the UK tax authorities (HMRC) to a mistake on a tax return, it was held that an adviser's failure to take reasonable care should not necessarily mean the client should be penalized.

Facts. The taxpayer, Mr. Hanson, submitted a tax return completed by his accountants, who had acted for him for many years. In his return, Hanson sought to claim relief from capital gains tax.

HMRC determined that Hanson did not in fact qualify for the relief claimed, and therefore required him to pay the additional tax liability. In addition, however, HMRC also levied a penalty of £14,000 on the basis that Hanson had not taken reasonable care when submitting his tax return.

Hanson argued that reasonable care could not entail checking that his accountants had given him sound professional advice. HMRC asserted that the error of an advisor was still the responsibility of the taxpayer.

Decision. The tribunal found in Hanson's favor and cancelled the penalty. Hanson demonstrated that he had instructed a reputable firm of accountants, which was in possession of all relevant facts. He had no reason to doubt their competence or their advice that he was entitled to tax relief.

In the circumstances of the case, Hanson was entitled to rely on the professional advice without himself consulting the legislation or any guidance offered by HMRC. ■

CELEBRITY ESTATES

Can't buy me love

Sir Paul McCartney, who was recently remarried to American heiress Nancy Shevell, has used an interesting approach to prenuptial planning.

Despite Sir Paul's acrimonious multimillion-pound divorce from Heather Mills, he reportedly remained steadfast in his refusal to enter into a prenuptial agreement.

However, he and his new wife apparently agreed that she would sign a short legal document, relinquishing her right to make any claim on the trust funds of Sir Paul's children and grandchildren. ■