

How Does Liechtenstein Develop to Ensure its Reputation as a Legitimate IFC?

Article by Roger Frick

Before coming up with a solution/idea, the direction states like the USA, international institutions like the OECD or the European Union might take must be identified. Principally, these organisations and states meet from time to time under the so-called G20 or G8 platform.

It is noteworthy that these countries call themselves industrialised nations that may include the local presence of a highly sophisticated industry with a big local market. This may be in contrast to many small countries considered as being strong in the financial sector and that market as 'offshore countries'. Such countries may offer their services to clients with domicile outside of the country (that is 'offshore'), so participate in a cross-border activity.

There is a clear trend here. These industrialised countries develop measures to assure that their home laws also apply to the other countries as well. Not only do they limit the application of the home law for their nationalities, but also for any person looking for cross-border services (the US Financial Accounts Tax Compliance Act (FATCA) for example). It must also be noted that the FATCA regulation will apply to financial intermediaries outside of the USA, but not to domestic financial intermediaries. There are various reasons for this that would fill an article on their own.

The OECD may plan to introduce a more comprehensive FATCA model on the basis of the tax domicile of a relevant person. The OECD could take, as basis for its own FATCA model, the model 1A (EU5) so that results reached within the USA on FATCA might definitively also have effects on the OECD based automatic information of exchange foreseen by the OECD (OECD FATCA).

On 19 April 2013 the OECD Secretary-General Angel Gurría presented a report to G20 Finance Ministers and Central Bank Governors that highlights measures to ensure that all taxpayers pay their fair share.

The report covers three strategic initiatives:

- Progress reported by the Global Forum on Transparency and Exchange of Information for Tax Purposes including the upcoming ratings of jurisdictions' compliance with the Global Forum's standards on exchange of information on request;

- Efforts by the OECD to strengthen automatic exchange of information;
- Latest developments to address tax base erosion and profit shifting, a practice that can give multinational corporations an unfair tax advantage over domestic companies and citizens.

Commending the Global Forum's achievements, Mr Gurría noted: "Now that the tools exist to investigate cross-border tax evasion, all countries must use them to the full."

Automatic Exchange of Information: The Next Step

Commenting on the latest OECD work to develop a common model for automatic exchange of bank information, Secretary-General Gurría said: "The political support for automatic exchange of information on investment income has never been greater. Luxembourg has changed its position and the US FATCA legislation is triggering rapid acceptance of automatic exchange and propelling European countries to adopt this approach amongst themselves. In response to the G20 mandate to make automatic exchange of information the new standard, the OECD is developing a standardised, secure and effective system of automatic exchange."

The report identifies the Multilateral Convention on Mutual Administrative Assistance in Tax Matters as the ideal legal instrument for multilateralising automatic exchange of information. The Convention provides governments with a variety of means to fight offshore tax evasion and ensure compliance with national tax laws, while respecting the rights of taxpayers. Over 50 countries have either signed or committed to sign. More are expected to sign the Convention at a ceremony to be held at OECD headquarters on 29 May 2014.

What is the Effect of All These Developments in Liechtenstein?

I doubt that the automatic exchange of tax data is in any way related to the exploitation of tax sharing profits of the relevant states and the costs of compliance. Why would larger countries set up the same controlling system just to identify certain non-domiciled clients to collect and report data? The costs are of no relation, and above all, the system originally planned to combat the financing of terrorism and money laundering is used for evidencing tax evasion. I doubt that the states get the funds they need to solve the problems; normally the tendency is that they spend money more ineffectively. Finally, the exact same states probably don't have enough data to share the same amount of data which they request from the 'offshore' countries.

My growing concern is that politicians are elected by the citizens on the basis of certain promises, but they no longer account for their activity and spending. Instead, they attack the taxpayer, most notably those who do not benefit from the extreme redistribution circle as seen in the European Union.

What Type of Services May Liechtenstein Offer in Future?

Whatever the end result, Liechtenstein cannot act on its own and must react and offer solutions to these developments. The political establishment of small states must work together with the financial industry.

One possible solution to consider is that the allocation of profits in cross-border business could be solved according to the essential functions of the activities, risks and costs within a certain state. A small state must therefore prepare itself to implement such a system, unless it is defined in double tax treaties (if the OECD or a single state is ready to adjust the OECD model convention on tax treaties to these needs of small countries, I'm doubtful.) It is one of the essential obligations and rights of small countries to fight for double tax treaties – not just tax information exchange agreements – to underline an equality of benefits in the tax cooperation world. I am concerned and still surprised why the other countries do not sit together to fight against such a new world of mercantilism where ultimately nobody will win.

So the technique may be to identify countries which are ready to share this equality of rights and obligations and to draft tax treaties with protocols which identify the borders of such situations like:

- 1) The nature of foundation/company, where the main purpose of a structure is definitively not to benefit from a treaty. Asset protection or holding activity may be an acceptable reason.
- 2) Ordinary taxation of 12.5 per cent (in the case of Liechtenstein, however dividends and capital gains on shares are fully tax exempt), with an independent local body that takes decisions in the statutory domicile of the structure and is not just executing foreign instructions.
- 3) The recipient (foundation/company) has a full right to use and enjoy the income it receives and the income is its own, because it is not obliged (no contractual, fiduciary or other duty) to pass the payment on to another person, so this recipient is a beneficial owner.
- 4) An irrevocable and discretionary foundation is capable of being the beneficial owner of income and entitled to treaty benefits.
- 5) A foundation which has a holding right in a particular foreign asset where the reason for establishing the foundation was to transfer this asset to it, not to avoid a withholding tax liability, but to assure that the main purpose is to address family asset protection and succession planning with a long-term view, then there should be sufficient purpose to exist and to benefit in cross-border activity.
- 6) In certain cases it might be necessary that the technical knowledge is also based in Liechtenstein. Consider the idea of transferring immaterial rights (patents) into a foundation. In order for a foundation to benefit from a double tax treaty, the person working on the technical side

for the patent development and license should be located – at least partially – in Liechtenstein. Then there might be the substance necessary to apply the double tax treaty benefits. Patent income is taxed in Liechtenstein at only 2.5 per cent.

- 7) Liechtenstein will be a future platform for holding entities and treasury centres, forming part of a large family office activity.

Liechtenstein offers persons, under certain limits and restrictions, the privilege to take residency in Liechtenstein with family members. An asset protection structure with valuable immaterial rights, charitable purpose etc. might be a valid ground to find a way into Liechtenstein.

Other developments are found in the company legislation and mutual fund business where further amendments are expected to address international developments. Another amendment, which I do not favour, but which might come, due to pressure from the G20, is to change the special legislation for directors of companies/foundations where settlers do not live in Liechtenstein. This law was developed to combat money laundering and terrorism financing, but as the G20 countries which do not know this concept mark the professionals with a red flag, whereas they are not doing it for their home market, the only solution may be for Liechtenstein to play the same game as they do. Let us see which way we go. The professionalism in our country, and above all the understanding of privacy needs which is still reflected in the business world and may never be completely understood by politicians, is sufficient basis to stay competitive.

Final remarks

The market participants are working urgently with policymakers to reposition the Liechtenstein financial centre. The goal is to improve the attractiveness and thus the competitiveness of the location. Alongside the unquestionable advantages such as stability, continuity and quality, three key elements are being emphasised: recognition, creativity and openness. Liechtenstein, its market participants and their products and services rely on the greatest possible international recognition. Opportunities in this regard are available especially within the framework of EEA law and a successful policy of international agreements. Liechtenstein needs creativity in the development and marketing of new business areas and openness to cross-border cooperation, new enterprises and new entrepreneurs.

About the Author:

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