

NEWSLETTER

Is offshore asset protection necessary?

Somewhere back at the beginning of the 1990s, when, as a young man, I delved deep into the mysteries of the offshore world, I didn't even understand the question. I remember seeing an advertisement on this topic in a Russian magazine. A hunter, with a rifle on his back, was warming his hands by a blazing fire in the woods, and above the picture were the words: "Have you protected what you have earned?"

But if it's mine, exactly who do I have to protect my fortune from? Who would want to take away from me what is legally mine. Why is all this necessary at all, and who on earth could even consider the twisted notion of taking anything away from me? These were my reactions at the time. Looking back today, I can still say that this was probably completely normal. All the while a person has no particular wealth to speak of, just promises and dreams, and "one day that'll be me...", they can not even begin to imagine the problems that come with having, managing and protecting wealth.

I now view the whole situation completely differently. I have been through and experienced an awful lot over the last 15 years or so, and have myself owned various movable property and real estate. Putting aside my earlier naivety, I can state quite categorically that yes, wealth does need to be protected, or rather, failure to manage wealth in the most suitable legal form of ownership can lead to serious losses.

So just who are these "intruders" who want a slice of the cake? I am sorry for the pejorative turn of phrase, but I am just trying to imitate the logic and terminology which a wealthy asset holder employs, or may employ. And from his point of view this is totally rational, as who in their right mind would want to embrace those who are trying to get hold of the assets which, legally or illegally, they have acquired. The desire for ownership is probably as old as ownership – or private ownership – itself, and this desire is very strong and never-ending.

The dangers can typically be divided into two groups. On the one hand, there are the attempts of the ever-present and resolute state or states to take a share, via legal chan-

nels (tax, customs, duties), of the income acquired on, or by those living on, their territory. On the other hand, in the private sphere, be it the private business sphere or inter-personal relationships, there are those who will lay claim, with or without good reason, to the fortune of others.

In the case of state deductions, we are particularly sensitive to secondary or multiple taxation, which is still present today in many forms, some open and others more concealed. Just think about the products we buy with our wages, which have already had income tax deducted; the shop has to charge VAT, and it is us, as private individuals, who are the end users, and who feel the burden. And the situation is even worse for smokers and drinkers, who, in certain countries, are also subjected to a luxury tax or duty on top of VAT.

At the same time, the State also has a predilection for imposing inheritance taxes when the inheritance is received, claiming that the inheritor has made a material gain "for nothing". The State is not in the least bit interested in the fact that the person leaving the assets was an honest and model tax-payer, who never cheated the tax-man out of a single penny.

Intruders from the private sphere may be less conspicuous, as their claims to the fortune may come about by chance. This, however, can be just as inconvenient, particularly in the case of an aggressive or malicious attack. Just think, for example, about the claim for damages which may be instigated against a wealthy man following a simple traffic accident, or a divorce settlement, whether justified or not, arising from a failed second marriage.

I could go on and on listing the examples, and the list would still be incomplete. The conclusion is that yes, wealth should be properly managed and protected. But how can an offshore vehicle contribute to all of this? What type of offshore legal entities are there, and what are the benefits?

The essence of offshore asset protection is that the owner of the assets should be an offshore legal entity incorporated in a country where there will be no tax on the capital itself, or on any returns on the capital. There should be no restrictions in place, and in the case of inheritance, the country in question should not impose any tax or duties, or



if it does, then these should either be very low or, if possible, a fixed amount.

I would like to highlight three such offshore vehicles: the offshore company, the offshore trust and the offshore asset protection foundation. In the case of an offshore company, the owner of the assets will be an offshore company to which the assets are transferred, either for remuneration or not. Such a transfer of assets already offers greater protection against loss, as the assets now represent the property of a legal entity. The company, however, has an owner, and in legal proceedings the assets could be included. Although it is more difficult to obtain the shares of an offshore company from the owner through litigation, it is not particularly difficult to seize the assets, particularly if large sums are involved.

This is one of the reasons for the popularity in Anglo-Saxon practice of the “Trust”, in which the assets are transferred to a “trustee”, which is normally registered or resident in a tax-free jurisdiction, and which is not subject to tax on the assets or their returns in the given jurisdiction. The person forming the trust, the “Settlor”, is no longer the legal owner of the assets, as these have now been transferred to the trustee. The biggest disadvantage of the Trust is that it is not in itself a legal entity, and although it has a tradition dating back 800 years in Anglo-Saxon countries, it is something of an intangible solution in countries with the continental legal system, where it has not been accepted too warmly.

The foundation for the protection of assets is a combina-

tion of the other two, as it is in itself a legal entity, but, like the trust, has no owners, just beneficiaries. This is a non-profit organisation, which can carry out no business activity other than the management of the assets. The assets themselves can consist of any movable or immovable property, money held in bank accounts, stocks and shares, etc. Perhaps the best known of these are the Liechtenstein foundations, which today are a privilege reserved for the world’s super-rich. However, foundations formed in, say, Panama or the Bahamas, offer the same security, while the costs of formation are only a fraction of those in Liechtenstein. In today’s practice, asset protection foundations mean that a family can manage its fortune or portfolio through one or more foundations, with the beneficiaries remaining outside this circle. The inclusion and support of third persons is not typical, and the sponsoring of public projects is not advisable, as any of these may harm the “reputation” of the foundation.



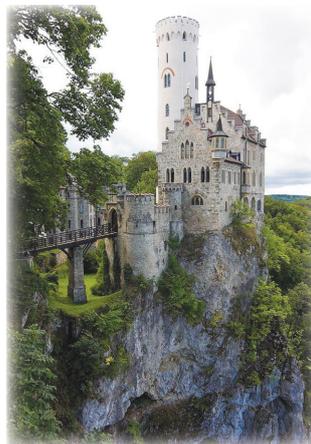
I can picture now many of my clients sighing deeply, with many raising their eyebrows more than just a little. What problems!?! Yes, assets bring problems. But as I sometimes say somewhat sarcastically to my male friends: this is like hair – you have to enjoy it while it’s there! When you lose your hair, there’s no point in wanting to brush it. So isn’t it better to care for it,

and regularly visit the hairdresser? LAVECO Ltd. can actively help its clients in the “caring department”, drawing on 16 years of experience gathered through dealing with many different cases over the years. Don’t be afraid to approach us – we can help you protect the fruits of your labours.

László Váradi
Managing Director
LAVECO Ltd.

Liechtenstein: princely banks

The principality of Liechtenstein is one of the most interesting mini-states in Europe. The country, with a population of barely 30 000, consists of several villages, sandwiched between Switzerland and Austria. It is one of those very rare countries where it is all but impossible to acquire citizenship, even if you’ve been living there for 35 years. Foreigners can benefit from the advantageous company formation laws and extremely reliable banking system. The costs of forming a company are rather high in



comparison with other jurisdictions offering similar taxation benefits, and the generally assumed prestige can also be questioned, as a number of countries have blacklisted Liechtenstein companies, with bank transfers going there drawing special attention from the tax authorities. As a result, this type of company is not particularly suitable for business transactions and money transfers.

There is no denying, however, the benefits of the high levels of service of the banks in Liechtenstein, with their wide-ranging investment products and the decades of

experience and professionalism of the bankers themselves. The banks specialise in offering so-called private banking services. They are only prepared to open accounts for clients willing to invest a minimum of several hundred thousand Swiss francs, which have to be kept in a deposit account. The sum deposited in the account can be used for investment purposes, and obviously any amounts above the required deposit can be transferred elsewhere. Transfers and the spending of money are naturally allowed, though generally this can not be done on a daily basis, or even too often. The majority of the banks simply do not have the infrastructure to deal with more than 1 or 2 transactions a month, let alone the turnover typically generated on a current account. This is the typical banking practice, which just about every bank in Liechtenstein offers.

During the summer, however, LAVECO Ltd. entered an agreement with a bank in Liechtenstein whose practice differs somewhat from the above. The differences are basi-

cally two-fold. The first is that it is not necessary to deposit several hundred thousand in the account, and keep that amount there at all times. The second is that the bank places no limit on the number of transactions, so the account which was opened as a deposit account can effectively be used like a current account. It is also possible to track transactions through the Internet, and although it is not yet possible to instigate transfers or other banking operations electronically, this is expected to change in the future, obviously to the benefit of the client.

The reliability of banks in Liechtenstein is exceptional, even by world standards. In addition to offering a wide range of services to their clients, the banks are also outstanding in the area of secrecy. It would be very difficult to give even one example of a bank in Liechtenstein revealing information about the movement on an account to foreign authorities, even if backed by court or legal orders.

Bahamas: the forgotten offshore jurisdiction

In the first half of the 1990s, the Bahamas was an extremely popular jurisdiction for the formation of offshore companies, on a par almost with the British Virgin Islands. This popularity was due to the well-defined company law, which followed the standard model in this field, the so-called IBC (International Business Company) format. The minimum requirement for incorporation was one director and one shareholder, but the details of the directors and shareholders were not publicly available as this information was not included in the public company records. Companies generally paid a fixed annual tax, or re-registration duty of 100 USD, irrespective of turnover. Companies registered in the Bahamas were not required to file accounts, so there were no accountancy fees either.

The Bahamas IBC was ideal, both from the point of view of simple administration and from that of the low and fixed annual costs. Complete anonymity was also guaranteed as the details of the directors did not appear in the official state records.

The situation changed radically from 2000, when the laws regulating the formation and operation of offshore companies were changed as a result of pressure from international organisations. Only registered shares could be issued, as opposed to the bearer shares freely available previously. Following the changes in the law, the details of the directors became available at the Registrar of Companies; and these details were not only available at the time of formation, but any subsequent changes were only valid if they were registered by the local authority. The low annual tax of 100 USD was raised to 350 USD, which also meant that the Bahamas were no longer competitive pricewise. The number of companies being formed fell by 50-60 %. The main reason for this was that the Bahamas' main competitors – the British Virgin Islands, Belize, Niue, the Seychelles – did not introduce such strict legislation at the time. In the midst of all this competition, the more “liberal” jurisdictions easily took

business away from the Bahamas. At the same time, none of the jurisdictions can be certain that they won't themselves become subject to the same sort of international pressure which forced the Bahamas to change their legislation.



If that is the case, then the Bahamas will be at an advantage, as they have already made the necessary changes, and new ones can not be expected. They also have 7 years of experience of how to work under the new conditions. In the opinion of the experts at LAVECO Ltd., although the Bahamas is currently an unfairly neglected offshore destination, from the point of view of stability it is still very positive,

and no further changes in the law are expected. In international comparison, the incorporation and maintenance costs are similar to those of a British Virgin Islands company, so we particularly recommend the Bahamas company to those who maybe already have a BVI company, and are looking for a slightly different jurisdiction, which still offers similar parameters.

Is it worth buying real estate through an offshore company?

The question is very complex, and there is no hard and fast answer. The following description should not be construed as tax advice in a concrete case, as every case should be individually analysed with a tax advisor specialising in this area. At the same time, our clients often ask us this, so this really is a Frequently Asked Question.

We should approach the answer from the point of view that real estate development is a specialised activity. The legislation of many countries, as well as the agreements for the avoidance of double taxation clearly state that any profits arising from the development of real estate should be taxed in the country where the real estate is situated. In this light, then, it makes no difference whether the property is owned by an offshore or local company. In both cases, the place of taxation is the country where the real estate is situated. What constitutes income, however, is another question. There are typically two types of income here; the first is rental income, which is

almost unequivocally subject to tax where the real estate is situated. There are some exceptions, but generally the profit made from the sale of real estate also falls into this category – most countries are happy to tax income accruing from property speculation.

So it is difficult to reduce tax by owning property through an offshore company, and renting it out or selling it. The situation can be different, however, if the offshore company does

not own the property itself, but the development project company which is registered in the country where the real estate is situated. In the case of a sale, then, it is not the property which changes hands, but its direct owner, the local company. This, though, may not be too beneficial from the tax point of view, and so it is possible that the shares of the offshore company will

be sold, and so the new owner will acquire both the offshore company and the local company, while making payment for the transaction to a second offshore company. In this case, it is not the property which changes hands, but the companies, thus avoiding the requirement to pay registration fees, stamp duties, and lawyers' fees. In many cases, this structure makes it possible to avoid very high levels of taxation.



THE LAVECO GROUP

UNITED KINGDOM LAVECO LTD.

Third Floor, Blackwell House,
Guildhall Yard, London
EC2V 5AE United Kingdom
Tel.: +44-207-556-0900
Fax: +44-207-556-0910
E-mail: london@laveco.com

HUNGARY LAVECO KFT.

33/a Raday Str.,
Budapest
Hungary 1092
Tel.: +36-1-217-96-81
Fax: +36-1-217-44-14
E-mail: hungary@laveco.com

CYPRUS LAVECO LIMITED

Despina Sofia Complex
Apartment 202, United Nations 8
Drosia 6042, Larnaca, Cyprus
Tel.: +357-24-636-919
Fax: +357-24-636-920
E-mail: cyprus@laveco.com

BULGARIA LAVECO OOD

"Porto Lagos" No.1, Ent.2, Floor 5,
Ap.42, 1463 Sofia, Bulgaria
Tel.: +359-2-953-2989
Mob.: +359-888-126-013
Fax: +359-2-953-3502
E-mail: bulgaria@laveco.com

ROMANIA OPTITAX CONSULT S.R.L.

59 Buzesti Str., A5 Block
1st Scale, 1st Floor, 62nd Flat
1st District, Bucharest, Romania
T: +40-21-311-61-76, Mob: +40-747-595-132
Fax: +40-21-311-61-82
E-mail: office@optitax.ro

WEB SITE: www.laveco.com