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NEWSLETTER

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The "silly season" on taxation



Each year at the start of the summer the journalists dust off the "silly season" expression. There is very little real news, so along come the unfounded rumours and "fillers" needed to fill the pages and prepare re-

ports. Somehow taxation never quite falls into this category. Internationally, there is always something new or interesting happening, there are always changes which are not only of interest to the specialists in the profession. Just like New York City, taxation never sleeps.

This is particularly true today. As the international economic recession deepens, so the search for reasons and those responsible develops. The statements issued by the politicians are unambiguous: the benefits offered by the countries with low taxes are sucking the capital and income out of the countries with high taxes, and something must be done about them. Sanctions must be imposed against them. Or rather, to be precise, not against them, as that would be extremely difficult. The British Virgin Islands, for example, where more than a million companies have been incorporated, is an independent country and companies incorporated there

are independent entities. It is impossible to eliminate a country and hundreds of thousands of companies from the international financial system. Instead, sanctions are imposed against those who have connections with such companies. So here is the scapegoat, the real reason behind the recession: the offshore company; the source of all financial problems, and the black sheep that can be paraded before the masses.

But is it really like this? Maybe, but nobody really knows. Just think about the following: when more than 96% of the world's income flows into the pockets of less than 1% of the population, will abolishing offshore companies really redress the balance? Will this really be the case? I'll leave it for you to decide.

Of course, there is always something new. "New York, New York, the city which never sleeps." A couple of years ago there was a song in Russia which was very popular among the young: Moscow never sleeps. I listened to it, and it was a typical summer hit. I would like to wish all the readers of the LAVECO Newsletter a very pleasant summer and a good rest!

Kind regards

László Váradi
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How many offshore companies are there in the world?

I have been trying to answer the question about how many offshore companies there are in the world for four years now. The answer is still quite simple: nobody knows. The same visible and invisible elements have remained in the system, which means that giving an exact figure is impossible. The tables below also show that a number of jurisdictions have not provided details of the number of companies formed in 2008. There are also some jurisdictions which previously issued information on the number of companies formed, but have not made public the figures for last year. It is still not possible to clarify the number of companies

formed in the USA, over recent years primarily as Limited Liability Companies (LLCs), and which are used outside the USA like offshore companies.

There is no great change at the top. The leading threesome is again probably 1. Hong Kong, 2. Panama, 3. British Virgin Islands. Cyprus has shown a significant decrease, with fewer companies being incorporated, presumably as a result of the real estate crisis. Belize and the Seychelles, on the other hand, have shown a healthy increase. The popularity of the latter in particular remains undiminished. In the Seychelles, it is still possible today to issue shares to the bearer.

1. List according to number of companies incorporated

Position	Jurisdiction	Companies formed in 2007	Companies formed in 2008
1	Hong Kong	N/A	98 645
2	Panama	71 178 *	N/A
3	BVI	59 509	52 716
4	Cyprus	29 016	24 453
5	Cayman Isl.	14 238 **	N/A
6	Seychelles	10 295	13 751
7	Belize	10 834	12 297
8	Bahamas	5 310 ***	5 089 ***
9	Samoa	6 073	4 171 **
10	Gibraltar	N/A	N/A
11	Isle of Man	4 682	N/A
12	Jersey	4 050	N/A
13	Anguilla	2 600	N/A
14	Malta	N/A	N/A
15	Mauritius	N/A	3 359
16	Guernsey	N/A	N/A
17	Brunei	N/A	N/A
18	St. Vincent	N/A	N/A
19	Bermuda	N/A	N/A
20	Barbados	477	N/A
21	St. Lucia	N/A	584
22	Labuan	N/A	541
23	Vanuatu	N/A	400 **
24	Madeira	N/A	N/A

2. List of jurisdictions in alphabetical order

Position	Jurisdiction	Companies formed in 2007	Companies formed in 2008
1	Anguilla	2 600	N/A
2	Bahamas	5 310 ***	5 089 ***
3	Barbados	477	N/A
4	Belize	10 834	12 297
5	Bermuda	N/A	N/A
6	BVI	59 509	52 716
7	Brunei	N/A	N/A
8	Cayman Isl.	14 238 **	N/A
9	Cyprus	29 016	24 453
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11	Guernsey	N/A	1 706
12	Hong Kong	N/A	98 645
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14	Jersey	4 050	N/A
15	Labuan	N/A	541
16	Madeira	N/A	N/A
17	Malta	N/A	N/A
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22	Szamoia	6 073	4 171 **
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24	Vanuatu	N/A	400 **

* + 5 359 Private foundations (2007)

** Approximate figure

*** Offshore + local

Tax changes in Hungary

From January 1st 2010, there will be changes in the Hungarian tax system in three elements defining the relationship between foreign and Hungarian companies.

1. The legislation relating to the Hungarian owners, whether companies or individuals, of controlled foreign companies, in which the ownership of more than 10% is held for more than half of a given tax year.

2. Foreign entities receiving interest, royalties or service fees from Hungarian sources will be subject to tax at the rate of 30%.

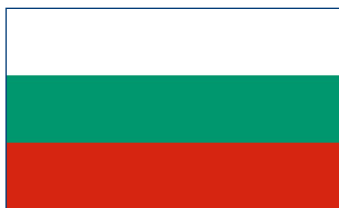
3. A totally new element has been created in Hungarian tax law with the introduction of the term "company with real estate at its disposal". In this way, sale transactions in which it is not the property itself which changes hands, but instead the foreign owner of

a Hungarian company which owns real estate sells their stake in the Hungarian company, will become subject to taxation.



The Bulgarian tax system

Bulgaria joined the European Union along with Romania on January 1st 2007. Based on the rates of corporation tax, it can be said that by EU standards the current tax system in Bulgaria is particularly attractive. Companies resident in Bulgaria are taxed at the rate of 10%, with foreign companies paying an additional 5% if the profit is then taken out



of the Bulgarian company in the form of a dividend. This 5% dividend tax does not have to be paid by the foreign parent company straightaway if:

- there is a valid agreement for the avoidance of double taxation in place, and this does not allow for the taxation of dividends in the country of source.
- the EU directive on subsidiaries (90/435/EEC) can be applied. According to the directive, a company from another member state must have been continuously the holder of a stake of at least 15% for a minimum of 2 years.

Private foundations – one more time



The Trust has been a legal asset protection vehicle under the Anglo-Saxon legal system for more than 800 years. The establishment of the Trust dates back to the times of the Crusades, when wealthy Lords, leaving

to do battle alongside the King, legally transferred their assets, which at the time typically consisted of land and its associated rights, to a Trustee, who, in return for suitable payment, was obliged to look after and maintain the assets to the best of his ability and in the best interest of the Beneficiaries. The Trust is still very popular in countries whose legal system is based on the Anglo-Saxon model.

Continental law, on the other hand, has trouble even defining such a legal form of double ownership, based primarily on a private law agreement. For this reason, the offshore world has seen the very rapid development of a new type of entity, which actually has a long tradition in European law. The private foundation offers numerous advantages:

1. The most important: the private foundation is a legal entity, which is registered in the register of companies, just like a normal company. In contrast, the Trust is merely a private law agreement between the Settlor and the Trustee, with no state register or trace.
2. Unlike companies, private foundations can either not carry out any business activities at all, or can only carry out very restricted ones. The main aim here is the safeguarding of the assets, and the avoidance or minimisation of business risk. It is possible, however, to act as a type of "holding" company for just about any kind of movable and immovable property (cash, shares, real estate, vehicles etc.).
3. The foundation is not a company, that is, it is not possible to obtain shares. A foundation has no shareholders or members; ownership rights, as such, can not be defined here. Beneficiaries are set down in the documentation of offshore asset protection foundations, and the assets of the foundation are administered in their interest.

Naturally, the purposes of a foundation are not restricted to the safeguarding of a family's assets, although this is the most common purpose these days. Foundations for both asset protection and charitable purposes can be established in a number of offshore jurisdictions, of which Liechtenstein, Jersey, St. Kitts and Nevis, the Bahamas and Panama are the most popular.

The agreement between Russia and Cyprus for the avoidance of double taxation

The new agreement for the avoidance of double taxation between Russia and Cyprus is being prepared. Representatives of the Ministries of Finance of the two countries reached agreement and signed the necessary documentation in April of this year. The international convention is expected to be ratified by the legislature of both countries in the course of 2009, and the new tax agreement will come into force on January 1st 2010, though significant changes will only be introduced from 2014. The Russian party promised that Cyprus will be removed from the Russian blacklist, on the basis of which dividends received by a Russian parent company from a subsidiary in Cyprus were not recognised as dividends and were taxed again in Rus-

sia. This "combination", though, was particularly rare, as the typical structure was exactly the opposite, with the Cyprus parent company owning the Russian subsidiary because of the more advantageous taxation of dividends. In this case, there were no restrictions earlier either, and the old agreement could be applied very favourably.



Hong Kong: the springboard to China



It is now more than 10 years since control of Hong Kong was transferred from the British monarch to China, but this change has in no way affected economic life in a negative way. As we have mentioned in earlier editions of our Newsletter, Hong Kong is still one of the most popular jurisdictions for company formation.

The corporate tax system is based on a rather particular element known as the principle of territorial taxation. In the case of Hong Kong, foreign income, that is, income from a source other than Hong Kong, is not subject to taxation, while income from within Hong Kong is. Accordingly, in their annual financial reports, companies must separate income from Hong Kong sources and income from non-Hong Kong sources. While profits from manufacturing, service or commercial activities carried out with other companies

from Hong Kong are subject to 16.5% tax, the tax on similar activities with non-Hong Kong companies is 0%. From this point of view, all other areas of China are considered to be non-Hong Kong sources.

The formation of companies in the People's Republic of China is incredibly difficult and bureaucratic. Administrative regulations can make life for those intending to set up business in China rather irksome, and for this reason numerous enterprises hoping to break into the Chinese market choose Hong Kong, where company formation is both significantly more simple and much less expensive, as the place to form their companies. Once established, a future step may then be to set up another Chinese company. The process will then be less complicated as we are already talking about a local entity. The first company can then even be closed once the "real Chinese company" has been formed. However, more benefits may be available from the application of the agreement for the avoidance of double taxation entered between Hong Kong and China.

The offshore enterprises of the large American companies

A report on the investigation into the largest American companies by the US Government Accountability Office entitled "Large US Corporations and Federal Constructors with Subsidiaries in Jurisdictions Listed as Tax Havens or Financial Privacy Jurisdictions" produced some interesting results. According to the report, of the 100 largest American enterprises 83 had subsidiaries in low-tax countries or jurisdictions. The most popular destinations for the American giga-companies are the Cayman Islands, Bermuda and the British Virgin Islands. It must be said that the report does also recognise that these American companies did not only establish offshore subsidiaries for tax reasons, and that other factors also played a part. At the same time, however, it is

a fact that the list included such American banks as received significant state support to avoid bankruptcy during the worldwide financial recession.



This occurrence is by no means a one-off. A similar British analysis revealed that the major British banks, including LloydsTSB, RBS, HSBC and Barclays had at their disposition more than 1000 offshore subsidiaries. The jurisdictions most favoured by the British financial institutions are the Cayman Islands and Jersey. The HSBC can boast the most offshore subsidiaries, with more than 500 enterprises worldwide.

Nevis: new offshore legislation

St. Kitts and Nevis are a pair of twin islands in the Caribbean, and also a jurisdiction offering the possibility of the formation of companies with beneficial tax conditions. The Nevis Island Assembly, the body responsible for legislation in Nevis, recently passed new company laws. They revised the regulations regarding international insurance companies, which can be formed in Nevis. The requirement on the minimum capital for companies dealing in re-insurance



has been reduced from 200 000 to 75 000 USD.

There have also been changes in the Limited Liability Ordinance, the laws covering Limited Liability Companies (LLC). From now on, if an LLC originally formed outside Nevis wishes to transfer its residence to Nevis, then it must provide a certificate from the original country of incorporation confirming that it has ceased to operate there and has been removed from the register of companies.

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