

A two-way street – Review of tax-planning opportunities under the LI and UK double-taxation treaty

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In 2012, Liechtenstein and the UK agreed a comprehensive, OECD compliant double-taxation treaty (DTT) that provides Liechtenstein and UK taxpayers attractive tax-planning opportunities. The DTT came into force on 1 January 2013 and demonstrates Liechtenstein's commitment to enhanced mutual cooperation in tax matters.

The DTT offers added value for cross-border investments, providing for a full or partial reduction of withholding tax on dividends, interest and royalties, and incorporating the latest OECD provisions on exchange of information and assistance in the collection of taxes.

Eligibility

In order for a Liechtenstein opaque foundation or trust to benefit from reduced or nil withholding taxes, the structure must pass the 'main purpose test', making it evident that the purpose of setting up the structure was neither treaty abuse nor primarily to take advantage of the DTT benefits. HRMC will, however, only apply this 'main purpose test' if there is clear evidence of an abusive purpose. This test has been included in all recent DTTs that the UK has concluded.

A Liechtenstein foundation of an irrevocable and discretionary nature is treated as the beneficial owner of its income and is consequently entitled to the treaty benefits. An irrevocable foundation with named beneficiaries and fixed interests is treated as opaque but transparent for DTT purposes. If the beneficiaries are resident in Liechtenstein, they will be able to claim treaty benefits. The UK will take a 'look-through' approach when there are non-Liechtenstein beneficiaries and may grant access to the DTT between the UK and any third country.

The protocol to the DTT clarifies that the Liechtenstein establishment, a versatile legal entity specific only to Liechtenstein, is also entitled to claim the benefits under the DTT. It further stipulates that a fund for collective investment in transferable securities (UCITS), as well as an alternative investment fund (AIF), should qualify as resident under the DTT. From a UK perspective, the application of the DTT is, however, conditional on the treatment of the Liechtenstein fund as an opaque structure that is ordinarily taxed and regulated under the Liechtenstein UCITS and AIF legislation.

Legal persons in Liechtenstein that are subject only to the minimum corporate income tax, such as private asset structures, charitable foundations and other corporate taxpayers that pursue charitable purposes, are not eligible for the DTT benefits. Even though a trust may not access the DTT under the same rules that are applicable to a foundation, an irrevocable trust with named, fixed beneficiaries or a revocable trust are deemed to be transparent for DTT purposes so that a resident settlor or beneficiary may apply for the treaty benefits (instead of the trust itself).

From a UK perspective, using an irrevocable and fully discretionary foundation (or trust) can provide non-UK-domiciled individuals with tax advantages in terms of sustainable capital gains tax deferrals and long-term shielding of non-UK assets from inheritance tax.

Local substance

It goes without saying that the treaty benefits only apply if the company's effective management and control is in Liechtenstein. This is decisive not only in order to benefit from the treaty benefits, but also to demonstrate that the management and control is outside the UK. This basic rule refers in particular to holding and asset management companies in Liechtenstein, which by nature only have limited 'local substance'. It is insufficient to have board meetings and resolutions of the company that are merely recorded as having taken place outside the UK. Liechtenstein fiduciaries providing the board and administration functions of the Liechtenstein entity must take real decisions; they cannot merely follow instructions.

The application of the new DTT via Liechtenstein structures and the involvement of a Liechtenstein financial intermediary can present a comprehensive and sustainable solution that protects UK, as well as non-UK-based, clients' privacy, provided that the services of the financial intermediaries involved are appropriately aligned and coordinated.

Liechtenstein is also prepared to conclude bilateral agreements on automatic exchange of tax information and to implement the future OECD standard, provided that the counterparties are willing to grant the same level of equivalent, non-discriminating regulations. Liechtenstein and the UK have the same understanding of clarity, predictability of regulation and equal treatment of their taxpayers, as granted in the DTT. Bearing this success story in mind, Liechtenstein strongly supports the OECD's view of international cooperation with the UK and other countries.

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