



Issues Faced by Families with Cross Border Estates

Overview of International Law

Conflict of Laws

- “ Refers to the resolution of problems resulting from the applicability of diverse laws of two or more countries;
- “ Example probate, divorce, land transfers, etc.;
- “ These conflicts are resolved through international conflict of laws;

International tax

- “ Refers to transactions or events that involve the tax laws of two or more countries;
- “ Also refers to many forms of taxation; capital taxes, estate taxes, income taxes, sales taxes, etc.;
- “ This also involves the access to and flow of information across borders;

Conflict of Laws

- “ Courts faced with a choice of law issue implement a two stage process
 - “ The Court will apply the law of the forum to all procedural matters; including the choice of law rules; and
 - “ The Court will count the factors that connect or link the legal issues to the laws of potentially relevant states, and applies the substantive laws that have the greatest connection;
- “ The factors include nationality of the parties, residence of the parties, the location of land, the location where business is carried on, where the agreement was made, the place where a transaction physically takes place, the place where the occurrence giving rise to the litigation takes place;
- “ The resulting choice (and the principle as well) is known as the “proper law”; that law when, after examining all factors, seems to have the closest and most real connection with the case;
- “ In the result, the general rule is that the proper law is the primary system of the law which governs most aspects of the factual situation giving rise to the dispute;

- “ Confusing in the abstract; example to follow later.

Conflict of Taxing Jurisdictions

2 fundamental principles:

- “ Residence principle: the right of a country to tax residents on worldwide income;
- “ Source principle: the right of a country to tax income earned within its borders.

These principles in practice lead to multiple opportunities for 2 or more countries to tax the same stream of income.

Double Tax Problems in More Detail

Dual residence

- “ A person may be considered a resident of more than one country, resulting in a double tax;

Dual Source

- “ A given stream of income may be considered to be sourced in more than one country, resulting in a double tax;

Residence / Source

- “ One country taxes income on the basis of residence, and the other taxes the same income on the basis of source;

Idiosyncratic Systemic Breakdowns

- “ One country taxes income, and another capital, in respect of the same asset without mechanical credit or deduction matches;

Dual residence and dual source issues are largely (but not always) resolved by the international tax treaty system, failing which a domestic deduction and credit mechanism largely (but not always);

Residence/source issues are handled largely through (but not always) a domestic legislative deduction and credit mechanism.

Double Tax Treaties

Purpose

- “ Agree on the taxing rights between the “source” country and the “residence” country;
- “ Provide for preferential tax rates on certain income; dividends, interest, rent, etc;
- “ Provide for more advantageous tax consequences than domestic law in the source country; eg. permanent establishment;
- “ Generally provide for the exchange of tax information, and treaty double tax relief;
- “ Most are modeled on, and varied off, the standard OECD model.

TIEAs

Purpose

- “ Promote international cooperation in tax matters through the exchange of information;
- “ OECD posits TIEAs are “designed to help detect harmful tax practices as well as the illegal movement of capital”;
- “ Operates through a simple relationship; mutual request and mutual delivery of information protocol.

Doesn't prevent double tax, doesn't provide preferential tax rates, and doesn't agree on taxing rights between “source” and “residence” countries.

CAD

- “ Has approximately 97 Treaties;
- “ Has approximately 22 TIEAs;
- “ Overlaying and interplaying with all of this is a structural change
 - “ Politicians;
 - “ Journalists;
 - “ A fascination with, and mission to discover and crush, the “billions of dollars hidden internationally” thus escaping taxation;
- “ This is likely overstated. Substantially all planning (except criminal) relies on international governmental economic policy decisions; using tax systems to compete for capital to stimulate growth;
- “ But the practical government response is FATCA, CRS, BEPS;
- “ Contributes to rising costs, inertia and uncertainty (think Apple)

Families with Cross Border Estates

- “ Family issues arise from one or more of:
 - “ They may own assets in other jurisdictions;
 - “ They may have heirs in other jurisdictions;
 - “ They may receive bequests from other jurisdictions.

- “ Without careful planning these assets, heirs, or bequests may suffer multiple levels of tax;

- “ With careful planning, these risks will not only be mitigated, but efficiency over base case may be achieved;

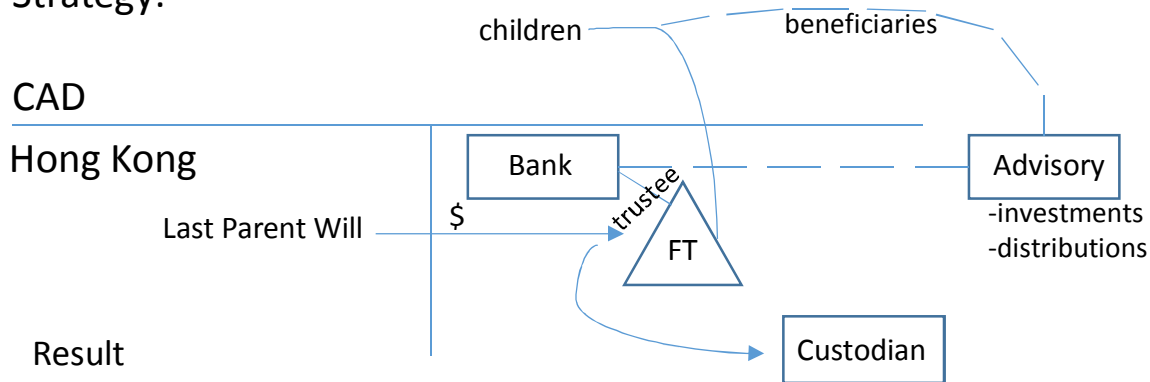
- “ Examples follow.

CAD Inbound Example

Facts: Hong Kong resident parents
 Assets - portfolio assets \$20M
 - H.K. real estate \$15M
 2 children residents of CAD

Purpose: to create a tax free zone for the children

Strategy:



Result

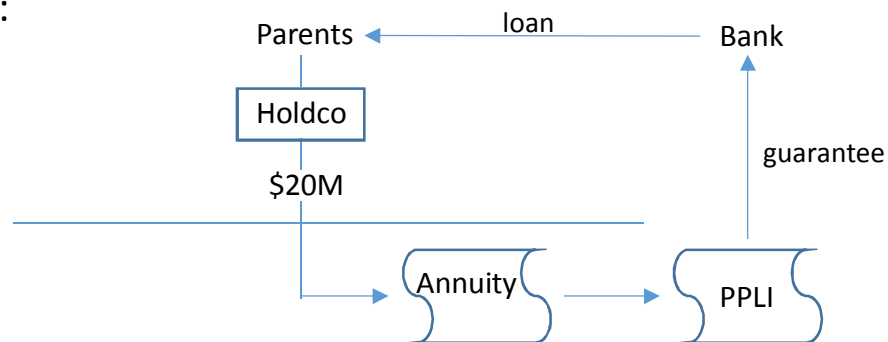
	<u>SQ</u>	<u>Strategy</u>
Income	\$2M	\$2M
Tax	1M	∅
Fees		(75s + 15a)
Arb. @ 10 cap		10M
Payback		2 mos

CAD Outbound Strategy

Facts: CAD family, all reside in CAD
 \$20M financial assets in holdco
 Parents elderly, retired
 Children middle aged

Purpose: Create capital dividend account at death
 Insurance only available internationally

Strategy:



Result

	<u>SQ</u>	<u>Plan</u>
Full cycle tax at Death	(\$11M)	(\$5M)
Costs		(500)
Capitalized arb		\$5.5M

Issues for Families Abroad Investing in CAD

- “ Generally CAD imposes 25% tax on capital gains, interest, dividends, rents, royalties;
- “ Treaty relief; example top 6 trading partners

	Interest	Dividends to Parent	Royalties
US	0%	5%	10%
China	0%	10%	10%
Mexico	0%	5%	10%
UK	0%	5%	10%
Japan	0%	5%	10%
Germany	0%	5%	10%

- “ Thin cap rules deny interest deductibility, pro rata on internal debt > 1.5:1 (only 60% internal debt x total capitalization is incented);
- “ Death of a foreign investor is a non-tax event; no death taxes in CAD applicable to non-residents.

Conflict of Laws Example

Facts: HK resident parents;
Married daughter living in CAD (common law property jurisdiction);
Married son living in US (California; community property jurisdiction);
Daughter and husband have portfolio of \$5M, CAD home \$2M and San Francisco second residence \$3M;
Son and wife have portfolio of \$5M, California home \$2M and CAD second residence \$3M.

Conflicts Issues: What happens if daughter divorces or dies?

Divorce:

- “proper law” determines;
- “in personam” dominates;
- 80/20 daughter, instead of 50/50.

Death:

- unlike matrimonial laws, the portfolio is governed by CAD laws, but the land is governed where it is located;
- Daughter could disinherit estranged husband to 80/20 but California is 50/50 (ex gets better deal).

What happens if son divorces or dies?

Divorce:

- California takes in personam jurisdiction;
- Everything is 50/50;
- CAD Courts won't interfere with this relating to the CAD real estate.

Death:

- Apply for ancillary grant of probate in CAD;
- Since the sole asset is land, Alberta asserts jurisdiction over it;
- Everything 50/50 except for the CAD land;
- CAD would apply a "proper maintenance & support" test;
- With the likely result the ex is successfully disinherited.

Global Philanthropy

Facts: Wealthy Singapore family
Want to set up a family foundation
Father & Mother are Singapore residents & domiciliaries;
Son 1 runs CAD branch of family business in Calgary;
Son 2 runs UK branch of family business in London;
Daughter runs US branch of family business in New York;
Nephew runs portfolio in Geneva.

Purpose: philanthropic & want to maximize effect of giving;
want tax benefits that are available;
want to involve & enrich family member experience.

Family member education / experience:

- trustee responsibility;
- professional trustees
- residence issues;
- educational value;
- constitutional approach / values;
- working together / partnership experience.

Jurisdictional issues

Permitted activities

- “ What is charitable?

Degree of regulation

- “ What hoops must you jump through?

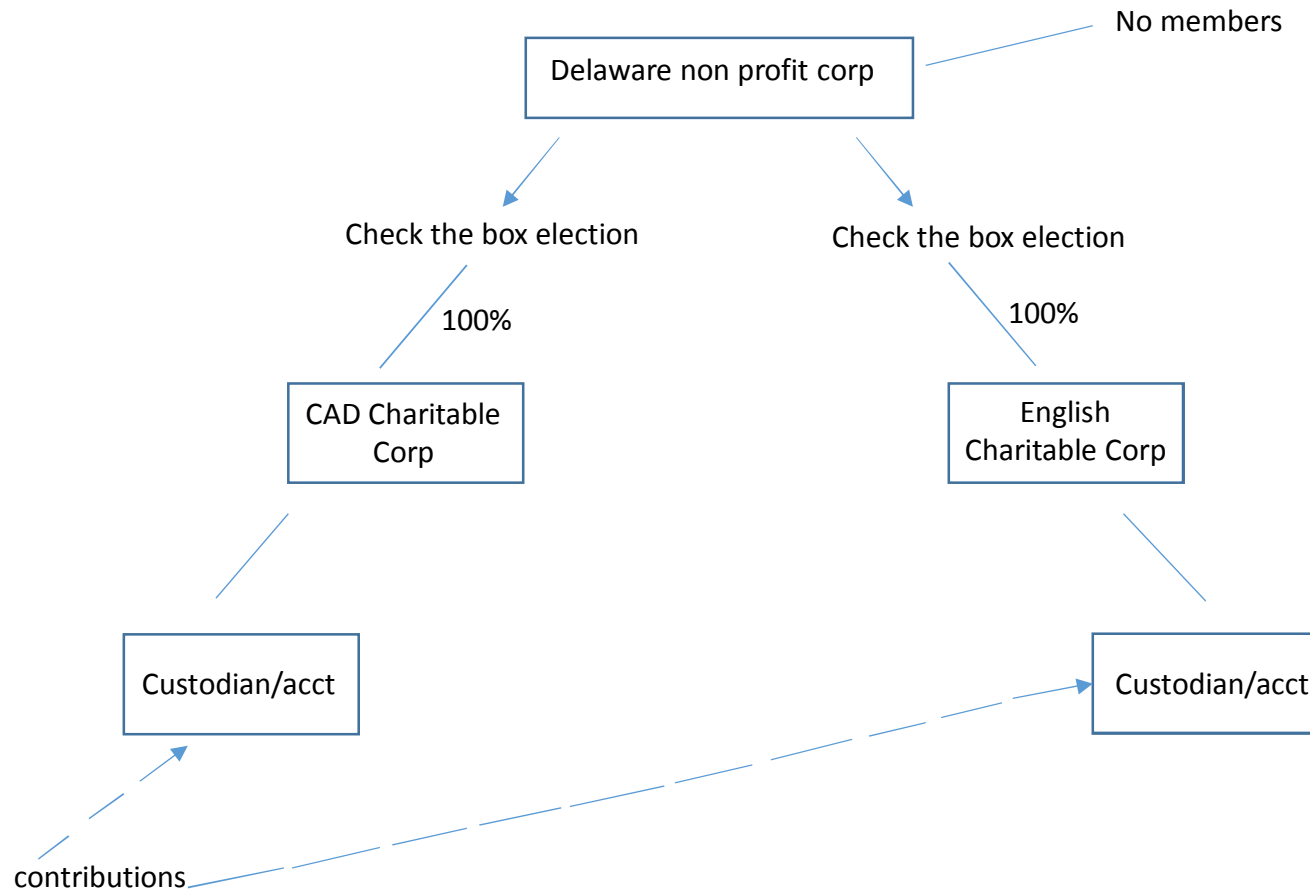
Taxation issues

- “ Are you limited in practice by tax considerations?

The risk & perception of abuse

- “ Taxation smell test;
- “ Money laundering & terrorist financing;
- “ Set up in UK, US, Europe or CAD? Or, Jersey/Guernsey?

Tripartite Qualified Structure



Residence v Citizenship v Domicile

- A. Citizenship
 - US
 - North Korea

- B. Domicile
 - UK
 - States within US – Massachusetts, NY

- C. Residence
 - US
 - UK
 - CAD

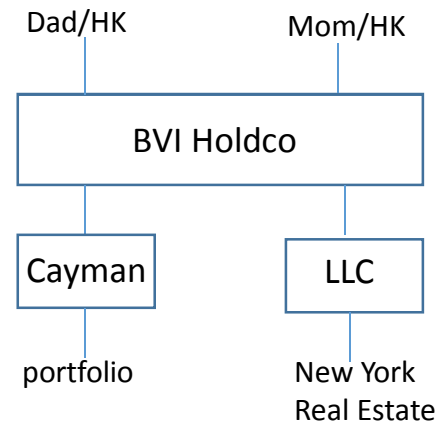
- D. Source based Income Tax system
 - HK
 - Singapore

What is resident?

Vehicle	US	UK	CAD
Trusts	<ul style="list-style-type: none"> - Court Test - Control Test 	<ul style="list-style-type: none"> - Residence settlor & trustees - Domicile of settlor 	<ul style="list-style-type: none"> - Management & control
Corporations	<ul style="list-style-type: none"> - Incorporation - Engaged in US trade or business 	<ul style="list-style-type: none"> - Incorporation - Management & control 	<ul style="list-style-type: none"> - Incorporation - Management & control
Partnerships	<ul style="list-style-type: none"> - Organization (reporting) - Place of business 	<ul style="list-style-type: none"> - Residence - Place of business 	<ul style="list-style-type: none"> - N/A

Global Cross Border Issues

Facts: Wealthy HK Family
Father & Mother own BVI Co 50/50;
BVI Co owns portfolio thru Cayman Co;
BVI Co also owns NY real estate thru LLC;
3 children: Adam, Bob & Charlie;
Adam born in NY, resides in HK;
Bob born in NY resides in HK;
Charlie born in HK, resides China.



Objective – want to give half of Holdco equally to each child (16.7% each)

Issues: Reporting

- FATCA reports;
- CRS reports;
- FIRPTA withholding;
- Dividend withholding;

Tax

- Adam's dominant tax is US (HK source based);
- Bob's dominant tax is UK (US gives credit);
- Charlie's China tax needs consult – may not want China source income;

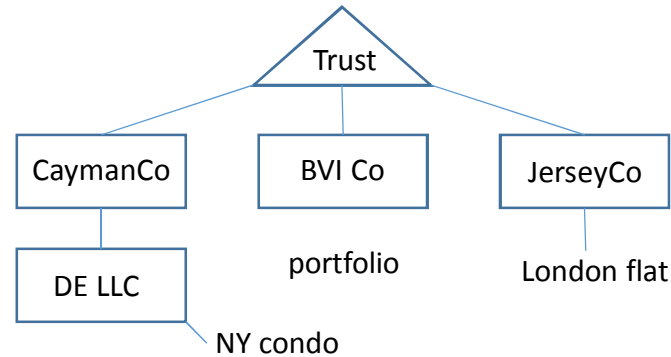
If Adam and Bob own >50% of BVI Holdco, Cayman Co will become a CFC. And if not CFC, then they will be PFICs so interest charges will apply to distributions.

Consider a trust to provide flexibility;

- grantor trust solves PFIC problem;
- grantor trust solves kids tax exposure;
- Trust solves attribution problem to UK;
- Trust solves UK inheritance tax.

Facts: Complicate the example

Diagram



- Issues:
- US Tax
 - PFIC / CFC issues;
 - Foreign non-grantor trust rules – distribution;
 - Is structure right for NY condo?
 - UK Tax
 - Is structure right for London flat?
 - Bob income & gains pattern.

Potential Solutions for Trustees

- Check the box on corporates;
- US domestic PTC structures;
- Drop off trust for NY condo;
- Eliminate Jersey Co.
- CRS reporting;
- FATCA reporting