



The New Liechtenstein Tax Act Transition Period for Holding and Domiciliary Companies expires at the end of 2013

Background

The New Liechtenstein Tax Act came into effect on 1 January 2011. The aim of the change of the Tax Act was to be internationally compatible and EEA-compliant. In order to avoid any risk of violating the EEA Agreement regarding the prohibition of state aid, the special company tax for holding and domiciliary companies had to be abolished after a transition period of 3 years. This transition period expires on 31 December 2013.

Companies affected by this change have to comply with the new Liechtenstein Tax Act de jure from 1 January 2014. Companies with a business year different to the calendar year are required to take urgent action. For these companies, the New Liechtenstein Tax Act applies for the first time for the business year which ends in the year 2014.

Taxation principles under the New Liechtenstein Tax Act

Legal entities that are taxable in Liechtenstein because of their domicile or place of actual management are, under ordinary taxation rules, subject to the ordinary corporate income tax on all taxable earnings at a standard rate of 12.5 percent, whereby the minimum corporate income tax is CHF 1'200 per annum. There is no capital tax.

As an alternative to the special company tax, the legislator has provided for a new tax privilege for legal entities which are only engaged in asset management and do not perform any commercial activity. Such Private Asset Structures (PAS) are subject only to the minimum corporate income tax of CHF 1'200 per annum.

Taxation of Trusts

Trusts (specific asset endowments without personality) whose domicile or actual management is located in Liechtenstein are subject to, the minimum corporate income tax of CHF 1'200. A tax assessment does not occur. A Trust reg. is considered as an entity with personality and therefore ordinary taxation or taxation as a PAS is applicable.

Taxation of Charitable Organisations

Upon application, the tax authorities exempt legal persons and special asset dedications without legal personality from tax liability, if such entities exclusively and irrevocably pursue common-benefit purposes as defined in the Law on Persons and Companies (PGR) without the intention of making a profit.

Ordinary taxation

For the ordinary taxation, the net corporate income is generally based on the accounting principles

of the PGR. However, the New Liechtenstein Tax Act unilaterally excludes inter alia the following from the taxable net corporate income:

- Capital brought in by members or endowments to foundations by founder
- Capital growth due to inheritance, bequest or gift
- Foreign permanent establishment results
- Rental and lease income as well as capital gains from real estate situated abroad
- Dividends and capital gains arising from the sale or liquidation of participations in domestic or foreign legal persons

Furthermore, the New Liechtenstein Tax Act allows the so-called notional interest deduction of currently 4 percent of the modified equity to reduce the tax base. The rate of 4 percent can be changed by the Liechtenstein Government every year. In simple terms, the modified equity reflects the net assets, which could generate taxable income. This results in the fact that a tax liability of the taxable assets, which are financed with equity, only arises on income of more than 4 percent.

If a company is subject to ordinary taxation, it must prepare financial statements and file a tax return every year. To benefit from all the mentioned tax reliefs under the New Liechtenstein Tax Act, the accounting requirements are increasing. Particularly in cases where there are more asset classes or more than one bank involved, the short form accounting does not give the required information for filing the tax return. The submission deadline for the tax return is determined by the tax authorities each year but generally the tax return must be submitted within 6 months after the end of the business year.

Private asset structures (“PAS”)

Under the new Liechtenstein Tax Act, an entity taxed as a PAS can benefit from a privileged taxation. Every legal person can qualify as a PAS. Such PAS are subject only to the minimum corporate income tax of CHF 1'200 per annum. A legal entity qualifies as a PAS if it meets the following requirements:

- No commercial activity
- No public issuance of its own stocks or shares and no trading on a stock exchange
- No advertising to shareholders / investors
- No receipt of compensations or reimbursements by shareholders / investors or third parties (no asset management fees)
- Articles of the company contain the restrictions as a PAS (This criterion is deemed fulfilled if the articles exclude commercial activities)
- Ownership of shares in the PAS is restricted to natural persons (intermediate legal entities forming a so-called PAS chain are allowed)

The main criterion to qualify as a PAS is the lack of commercial activity. The New Liechtenstein Tax Act exemplifies, by reference to the Asset Management Act (safe harbour), what is not considered as a commercial activity. This includes the acquisition, possession, management and sale of transferable

securities such as bonds and stocks; money market instruments; shares in investment undertakings; options; futures and derivatives that can actually be delivered or settled in cash. Buying, holding and selling of precious metals, artwork and similar material assets is generally possible, as long as no commercial trading takes place. As the mere exercise of ownership by the owner as such is not considered a commercial activity, the legislator does not qualify the holding of a real estate as a commercial activity as long as the real estate is used by the owner and not rented. Rental of a real estate qualifies as commercial activity. If holding shares, it is important to ensure that neither the PAS, nor its shareholders or beneficiaries exercise any control through direct or indirect influence on the management of the company, otherwise commercial activity is assumed. To grant an interest-bearing credit in general or to grant none interest-bearing credit to third parties, qualifies as commercial activity. Only granting none interest-bearing credit to the owner is compatible with the PAS status. We have to say that even a single activity not allowed may lead to the loss of the PAS status and result in the ordinary taxation of the entire net income.

If a company wants to apply for the PAS status, the application form needs to be submitted to the tax authorities before the start of the business year in which the New Liechtenstein Tax Act is applicable. That means, for companies where the business year is equal to the calendar year, the submission of the application form has to be done by 31st December 2013.

To evaluate whether a company qualifies as a PAS, the Liechtenstein tax authorities request certain information and documents.

Companies with the PAS status do not have to file a tax return. However, the company must declare any changes to the tax authorities which might have an impact on maintaining the PAS status.

Advantages and disadvantages of ordinary taxation and the PAS status

There are various advantages and disadvantages between ordinary taxation and the PAS status. We have listed these in a table on the last page of this newsletter.

One of the main disadvantages of the PAS status is the fact that a company with the PAS status is unlikely to benefit from double taxation treaties. The main disadvantage of the ordinary taxation in comparison to the old tax regime for a holding or domiciliary company is that the companies have to pay taxes depending on the annual taxable net corporate income. By taking the right measures, the disadvantages can be mitigated.

Underlying (offshore) company

The tax burden in Liechtenstein might be optimised by spinning off the assets which result in taxable income in Liechtenstein (interest-bearing loans, bonds, gold, etc) into an underlying (offshore) company. The profits in the underlying (offshore) company are not taxed and the distribution of these profits to the Liechtenstein parent company is tax exempt in Liechtenstein.

Where there is no other taxable corporate income in the Liechtenstein company, the Liechtenstein company only has to pay the minimum corporate income tax in the amount of CHF 1'200 per annum.

Explicit revocable right

In the case whereby the articles of a foundation, a foundation-like establishment or a trust with legal personality (Trust reg.) contain an explicit right to revoke the entity, the income and the assets of the entity are from a Liechtenstein tax perspective attributed to the founder/settlor. The company itself only has to pay the minimum corporate income tax of CHF 1'200 per annum. We must add that the explicit revocable right might have unfavourable tax consequences abroad.

Conclusion

Based on the introduction of the New Liechtenstein Tax Act as per 1st January 2011 and with the end of the transition period being 31st December 2013, we recommend to analyse the tax consequences of this change for all companies which qualified as holding or domiciliary company under the Old Liechtenstein Tax Act. With selective measures the taxation in Liechtenstein can be kept at a low level.

If the company only holds a portfolio at a bank, the PAS status might be a way going forward. However, if there is extensive trading in the portfolio and in most other cases going beyond the holding of a financial portfolio, the PAS is probably not the best solution. In such cases, we recommend to consider restructuring of the assets well ahead of the end of the transition period to reduce the corporate income taxable in Liechtenstein.

Disclaimer

This document was only prepared for information purposes and does not constitute legal or tax advice. We assume no liability or responsibility for any ambiguity, incorrectness or inaccuracy of this document and recommend to analyse each case with your tax adviser under consideration of all circumstances.

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| | Types of taxation | | |
|-----------------------------------|--|-------------------------|--|
| | Ordinary taxation | Private asset structure | Explicit revocable right |
| Application | By law | By request | By request |
| Taxation basis | 12.5% on the taxable net corporate income | CHF 1'200 per annum | CHF 1'200 per annum / possibly restricted tax liability of the founder/settlor |
| Tax free incomes / tax deductions | <ul style="list-style-type: none"> Foreign permanent establishment results Rental and lease income as well as capital gains from real estate situated abroad Dividends arising from and capital gains from the sale or liquidation of participations in domestic or foreign legal persons Notional interest deduction of 4% on the modified equity | Not applicable | <p>Not applicable for the company</p> <p>In case of a restricted tax liability of the founder/settlor through a permanent establishment, the same rules as at the ordinary taxation are applicable</p> |
| Financial statements | To be done | Not necessary | Not necessary |
| Tax return | To be done | Not necessary | Not necessary |

| Ordinary taxation | | Private asset structure | |
|--|--|---|---|
| Advantages | Disadvantages | Advantages | Disadvantages |
| <ul style="list-style-type: none"> Various incomes are tax free, on the other incomes the notional interest deduction of 4% can be used Double taxation treaty might be applied By taking advantages of the various exemptions of the tax base, a low taxation can be achieved in Liechtenstein | <ul style="list-style-type: none"> Taxation of the effective income (this is only a disadvantages in comparison with the taxation under the Old Liechtenstein Tax Act as holding or domiciliary company) A financial statement has to be prepared and a tax return has to be submitted | <ul style="list-style-type: none"> Minimum corporate income tax of CHF 1'200 per annum No financial statements to be prepared and no tax return has to be submitted | <ul style="list-style-type: none"> Application to PAS requests certain information and documents Constant controlling of PAS status because of the reporting obligation to the tax authorities One activity not allowed lead to the loss of the PAS status and consequently to ordinary taxation with potential adverse tax impact Probably no double taxation treaty can be used |

| Ordinary taxation - assets | | Private asset structure – commercial activity | |
|---|---|---|--|
| Taxable | Tax exempt | Allowed activities | Not allowed activities |
| <ul style="list-style-type: none"> Cash Short term investments (money market / call money) Long term receivables Derivatives / options / futures Bonds Mixed funds Structured products Precious metals Artwork Loans Real estate Shares in investment undertaking with no investments in shares Securities lending | <ul style="list-style-type: none"> Shares (dividends and capital gains) Pure share funds Shares in investment undertaking with investments only in shares Foreign permanent establishments Foreign real estate | <ul style="list-style-type: none"> Passive exercise of ownership of securities, which means acquisition, possession, management and sale Investment in participations with no control or influence on the management Possession and sale of alternative investments (f.e. gold, pictures, artwork) Free of charge assignment of a real estate to beneficiary Own use of the real estate with no income thereof Grant none interest-bearing loans to beneficiary | <ul style="list-style-type: none"> Any offer of goods or services to the market active exercise of ownership of securities, which means frequent trading Investment in participations with control or influence on the management (particularly on the members of the board) Commercial trading with alternative investments (f.e. gold, paintings, artwork) Lease of real estate Grant interest-bearing loans in general or grant none interest-bearing loans to third parties Partial free of charge lease of real estate or none interest-bearing loans to beneficiary |
| The table is not exhaustive. | | | |