

International investment

Stick with this abiding rule in wealth management and you will have nothing to fear in this safe harbour □

By Martin Crawford, CEO of Labuan IBFC Incorporated, the marketing and promotional agency for the Labuan jurisdiction

Wealth, like a good reputation, takes a long time to build but can also disappear with one false step, one bad moment, or even an unexpected economic crisis similar to the one the world is digging itself out from.

Couple that with the giant spot lights the OECD is turning on in search of illegal activities like tax evasion or money laundering. A dilemma consequently comes into focus for those law-abiding wealthy individuals or families who, in most cases, are less concerned about tax evasion than the simple wish to perpetuate their wealth for generations to come.

At the heart of the dilemma for the wealthy community is the question of whether to sit it out or move on to another jurisdiction. This decision requires a clear-sighted, hard headed assessment covering service support, the regulatory environment and the ability of the tax planning structures to withstand scrutiny from tax authorities while ensuring an individual's right to privacy.

For the truth of the matter is that in the new world order of the OECD with its Exchange of Information standard, secrecy will not be tolerated, nor will obfuscation. In their place, confidentiality (as in 'need to know' which rules out 'fishing expeditions' and unauthorised prying eyes) and transparency will be the rules of the day.

Nothing will be lost for those who conduct legitimate business activities or wealthy individuals who use Labuan International Business and Financial Centre (Labuan IBFC). The domicile has been sticking to its guns over the last 18 years that only real, legitimate business would be welcome. In other words, only substance makes good business sense.

Even though there is no exhaustive definition of 'substance' it is worth checking out some of the criteria normally associated with the term. From a Malaysian tax perspective, these criteria include the following:

Effective place of management should be the country of residence. This means business activities such as management or commercial decisions are actually conducted in the jurisdiction. So too are the main activities of the entity.

Similarly, accounts should be maintained in the jurisdiction.

While the legal entity's registered office could be located in Labuan, it must not also be regarded as a tax resident in another country. (The advantage of this sole residency will be elaborated below).

All relevant requirements pertaining to submission of tax returns should be complied with, when due.

Shareholding needs to be adequate based on the functions performed, taking into account the assets used and the risks assumed.

But as substance becomes increasingly the focus, so will the cost of establishing substance go up and this is where Labuan IBFC can offer real savings. As a low risk, low tax jurisdiction with a full complement of service providers supported by modern infrastructure, operational costs in Labuan IBFC can often be up to 40% lower than its nearest neighbour, Singapore.

Furthermore, for HNW individuals or family offices whose country of origin is outside Malaysia, setting up a trust or foundation in Labuan IBFC brings with it the benefits of access to the country's double taxation agreements network (DTAs) with 69 countries, one of the largest in the world.

The principal advantage of Malaysia's DTA network is under the Article 4 tie breaker rule. This deems 'sole residence' for both a company and the individual tax payer who would otherwise be dual tax residents, if they have a permanent home in Malaysia but not in the other contracting state.

In addition to the DTA access, Labuan IBFC's tax benefits under the Labuan Offshore Business Activity Act 1990 (LOBATA 1990) include 0% tax on passive income (a boon for the expatriate with a pension or retirement plan); tax exemptions on distributions; no tax on gifts, inheritance, estate or capital gains; no exchange controls or stamp duties.

Depending on the individual's wishes, Trust structures in Labuan IBFC can take various forms such as interest in possession trust; discretionary trust; accumulation and maintenance trust; protection or 'spendthrift' trust.

The trend of setting up a Family Office is catching on and Labuan IBFC provides for those who desire wealth accumulation to be managed professionally under its soon-to-be-passed new Trusts Act and Foundations Act. The provisions clearly spell out the role of the professional advisers as providing investment functions which are separate from the custodian role of Trustees. Should a settlor desire greater or more direct control over assets in the Trust, he has recourse through another provision.

This separation of roles balances the inter-generational needs of the family members, acknowledging the contribution of each as being beneficial. The older, more conservative generation that built the family fortune has sway in managing the family legacy while the younger, next generation can make investment decisions to maximize returns.

In achieving the latter goal, the younger generation may choose to become more involved in managing the investments or appoint a professional investment adviser, whether located in Labuan IBFC or in some other global city.

For Muslim families, trust structures such as discretionary trusts, charitable trusts, trading trusts and testamentary trusts (Inter Vivos) can easily be made Shariah compliant by ensuring the Shariah Adviser approvals are obtained certifying that Shariah principles are met. Labuan has specific laws governing Shariah-compliant structures while the Malaysian judicial and arbitration system is well versed in Islamic finance matters.

When all these considerations have been weighed, other points to consider are the infrastructure support and the regulatory environment. Labuan's telecommunications system includes fibre optic cable, voice and data links, air services, highways with a well developed services sector comprising legal, tax, accounting and secretarial professionals.

As for regulating the jurisdiction, Labuan Offshore Financial Services Authority (LOFSA) has been the one-stop agency since 1996. The regulator is committed to, and practices, international standards set by the various international multilateral bodies of which it is a staunch member.

In keeping with its stringent entry policies, extensive due diligence is conducted and no bearer shares or cash transactions are allowed as part of the operational restrictions.

The regulatory framework in Labuan IBFC, while robust, is nevertheless business-friendly and totally supportive of the OECD standards which, more and more, stress substance as the way of the future.

For more information on Labuan IBFC's wealth management or other estate planning services, please visit www.LabuanIBFC.my.