Milestone - Question and Answer

Milestone is a boutique international tax practice based in Mayfair. They provide tax advice to a broad range of clients from corporates with international finance activities to investment funds to high net worth individuals.

The examples set out below provide a précis of several client cases Milestone has recently undertaken. The responses and content of this note are general in nature and do not constitute tax advice. We recommend that specific advice is sought for any international finance transaction.

A South American national with significant worldwide commercial interests sought advice on a corporate acquisition together with wealth maintenance and succession planning opportunities for his existing structure. Our client had a preference for a European holding structure.

The client's primary driver was ensuring that wealth (both existing and potential) within the structure could be preserved and passed to future generations. The main restructuring impediment (at least from a tax perspective) was the crystallisation event that would arise on transfer of the assets from the existing structure to a new holding vehicle.

Due to the increasing international antipathy towards offshore tax haven (and similar arrangements) we proposed removing the existing Delaware LLCs and inserting an EU holding company that would be held by a Swiss managed trust. The EU holding company would, in turn, hold the operating assets in Latin America. The client, his children and members of his extended family would be beneficiaries of the trust. We were also able to utilise a bi-lateral investment treaty agreed between the holding and operating jurisdictions. These treaties provide a certain degree of protection for foreign direct investments and are extremely helpful for structuring in Latin American countries.

In addition, we ensured that:

- -profits could be repatriated within (and out of) the structure with minimum tax leakage to enhance internal rates of return;
- -capital gains could be deferred as part of the restructuring to reduce tax leakage;
- -the structure could be 'future-proofed' as far as practicable; and
- -the proposals would be commercially and practically workable for our client on a day to day basis.

The resulting structure allowed our client to benefit from a two-tier holding structure that utilised onshore and offshore entities and struck an appropriate balance between tax optimisation and the one-off tax costs of restructuring.

A London based art dealer asked us to advise on the establishment of an international art trading fund that would provide off market trading, hedging, portfolio management and custodial services.

Our client wanted to target UK and non-UK investors for the fund and base the investment advisory activities in the UK. As with all fund arrangements, the primary driver of the internal rate of return is the asset class itself. In this case, we focussed on the esoteric nature of the underlying asset class in determining the operating structure of the fund.

We proposed a Guernsey fund with a UK limited company to act as the investment manager. We could also have used a UK LLP but our client wanted the ability to 'pool' profits in the UK company.

The display of art created a significant area of concern for the fund. Based on existing contractual arrangements, the fund could be exposed to tax in the local high tax jurisdictions (principally the UK and US). We proposed restructuring the contracts and ensuring an independent third party would take possession of the art to shelter the fund from any potential foreign tax exposure.

In addition, we ensured the structure allowed:

- -the ability to repatriate profits from the underlying subsidiaries and fund vehicle with minimum tax leakage; and
- -sufficient flexibility to create tax enhancements for the individual investors on any eventual exit.

As with most onshore / offshore arrangements, we also highlighted the importance of maintaining the established control and management mechanisms of the fund. This element is critical to the success of any international tax planning arrangement.

A UK family with an extensive property portfolio sought UK inheritance tax advice after the death of the patriarch in whose name the assets were held. The mother had inherited the entire portfolio free from tax but, with ailing health, the family were concerned that 40% of the value of the estate would be lost on her death. We were asked to consider ways in which the portfolio could be restructured to mitigate the tax charge.

The scope of UK inheritance tax is broad and planning needs to be undertaken with care. However, our client allowed us a large degree of scope to restructure the existing arrangements. The first consideration was that on the death of the patriarch, the assets passed to his wife under the spousal exemption. However, this transfer did not allow uplift in base cost of the assets that normally occurs on death. We proposed transferring the property portfolio into a limited liability structure in order to defer a crystallisation of the latent capital gain in the portfolio.

The portfolio could then be partially restructured to take into account the significant rent roll and reduce the impact of the 50% income tax from 2010 through internal debt funding arrangements. The restructuring utilised the available domestic exemptions and allowed our client sufficient structural flexibility to mitigate additional transfers of the portfolio.

A Moscow based matriarch with a substantial art collection (owned by a non-Russian company) engaged us to advise on how the collection could be transferred in a tax efficient manner to her children who were resident in the UK.

We proposed that, prior to transferring the art to her children, the matriarch dispose of her shares in the non-Russian art holding entity by way of gift to a common law trust established on the Isle of Man. The trustees of the trust would be the matriarch's children and any future progeny. This transfer of the foreign shares to the trust could, under the laws of the foreign holding company, be achieved in a tax free manner.

This restructuring step ensured that any future income and gains would only be liable to Russian tax to the extent the matriarch took a benefit from the trust. In addition, due to the current scope and application of the UK non-domicile rules, the matriarch's children could subsequently benefit from the art (provided they have elected to be taxable under the remittance basis and the art is not brought to the UK) without being subject to UK taxation.

The planning took into account the relevant Russian anti-avoidance provisions and utilised the often overlooked, but extremely beneficial tax treatment of common-law trusts for Russian clients.

A South African resident engaged us to undertake a detailed review of a historical holding and trading structure established prior to his immigration from Germany. The European holding structure had evolved organically over 40 years and was engaged in commercial activities in Southern and Western Africa.

Our client was concerned that his $40m investment would be exposed to tax, interest and penalties as no filing position had previously been adopted in South Africa. We undertook a detailed review of each transaction that led to the formation of the holding and operating structure and tracked these developments with the various legislative changes in South African tax law over 40 years.

In particular, we had to consider the 2001 introduction of worldwide taxation in South Africa and the potential exposures to estate tax, capital gains tax and donations tax. In addition, any planning or reporting obligation would need to account for all relevant exchange control provisions and offshore trust reporting rules.

We concluded that our client had a South African reporting obligation but that the potential latent tax liabilities could be successfully mitigated. We proposed restructuring the top holding entity to make the ownership (and control) structure clear, removed a latent estate liability through the use of a non-South African hybrid entity / quasi-trust and restructured the existing financing arrangements.

A UK tax resident individual asked us to advise on his tax position after being seconded by his UK employer to their Paris office. In addition to his employment income and bonus arrangements he sought clarity on how his carried interest in the business would be taxed and where. Our client was born in the UK but his parents were Swedish and

Brazilian and as such he had claim to non-domiciled status.

This case highlighted the difficulty of international secondments and maintaining a beneficial tax status where there is a significant overlap between competing rules. We focussed on his domicile status and explained the case law and tax revenue practice found in the new HMR&C 6 publication. The primary difficulty for our client was that, despite his insistence that his fact situation was simple, the residency rules in the UK and France operated such that he was considered to be resident for tax purposes in both jurisdictions. This finding was compounded by our review of the tie-breaker and employment articles of the France/UK double tax treaty (current and proposed).

On balance, and considering our client wanted to maintain his UK tax residency, we concluded he had a reasonably arguable position that he would continue to be considered a UK tax resident. On that basis, we then had to consider the 'employment related securities provisions' found in the UK tax code that would govern the treatment of his carried interest. Given the sums involved, it was imperative that, post exercise, the units would, at worst, attract 18% capital gains tax. We proposed a structure that would allow the carried interest to be maintained offshore with a resulting tax deferral for our client.

A European property developer engaged us to provide advice on how they should structure a Spanish property development. Our remit was to mitigate Spanish tax on the development profits and to allow UK pension investors to invest without jeopardising the exempt status of their pension arrangements.

Our client wanted a straightforward structure that could be easily explained (and recognisable) to investors. We proposed a UK limited partnership ('LP') structure that included an exempt property unit trust (EPUT) into which UK pension investors would enter the transaction. The fund vehicle itself would be a Luxembourg holding company (established by the LP) that would hold the shares in the Spanish development company. This structure would allow a sale of the development company or distribution of its profits with minimal Spanish taxation.

In addition, we proposed the use of a Dutch finance company (as a sister company of the Spanish company) to provide finance to the Spanish development company. The Dutch and Spanish companies would operate as a silent partnership arrangement. This created an extremely tax efficient structure that increased the internal rate of return for the investors.