



BANQUE  
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**WEALTH PLANNING NEWSLETTER:  
ON THE UTILITY OF WEALTH  
STRUCTURES**

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# ON THE UTILITY OF WEALTH STRUCTURES

**Personalised services have always been at the heart of Eric Sturdza Bank's proposition. In order to deal with increasingly complex situations, the Bank relies on its expertise in Wealth Planning to meet the ever more specific expectations of its clients. Wealth Planning is an essential part of our holistic approach. In this new issue, we asked our expert to shed light on the various types of wealth structures, their relevance in a context of increased transparency, their advantages and the traps to avoid when using them.**

As an individual, you have the option of holding your financial assets directly on a bank account in your name, or indirectly through a wealth structure.

When considering the appropriate holding structure, it is important to be advised by product neutral professionals whose only compass will be the most appropriate solution for the situation.

When we start a business relationship, our holistic approach leads us to question at the outset the best ownership structure for the needs and circumstances: Does direct ownership allow the owner to achieve his objectives? If not, what type of structure should be considered? If a structure already exists, we question its relevance: Is it still useful in light of the developments that have occurred since it was put in place, whether in terms of regulations, taxes or family circumstances?

Establishing the optimal ownership structure before you begin the investment process also avoids the complications and costs associated with subsequent changes.

**How you hold your financial assets is important because it impacts your ability to**

**achieve your goals in terms of protecting, growing and ultimately transferring your wealth.**

## INDIVIDUAL ACCOUNT OR ACCOUNT IN THE NAME OF A STRUCTURE?

Over the past 15 years, developed countries, under the leadership of the OECD, have taken numerous initiatives - BEPS, CRS, DAC, among others - aimed at preventing the use of wealth structures for tax evasion or criminal purposes.

Therefore, only those structures that are based on sound economic rationale, have substance through their own staff and offices, pay taxes and operate in full compliance with their by-laws can hope to achieve their objectives in a sustainable manner.

These "new generation" structures are often complex and costly. They often expose their owners to a foreign and therefore unfamiliar legal system. They require the involvement of professionals - trustees, directors, insurers - in whom the owners will have to place their trust.

**Given this new landscape, direct ownership of financial assets is more than ever the preferred option. Structures should only be considered for legitimate reasons, when the objectives sought cannot be achieved otherwise and when the cost/benefit analysis is favourable.**

## WHAT ARE THE DIFFERENT TYPES OF OWNERSHIP STRUCTURES?

We can mention in particular :

- **holding companies or domiciliary companies** designed to hold a portfolio of securities or a stake in an operating company.
- **family investment funds or private funds** used to consolidate the investments of a generally small circle of investors.
- **life insurance policies** that allow the contractual transfer of assets (outside of probate) to designated beneficiaries upon death.
- **pension funds such as “libre passage” and 3rd pillar in Switzerland**, intended to finance an annuity or a capital for retirement.
- **trusts and private foundations** often used as governance tools and/or for the planning of complex successions.

Many jurisdictions - onshore and offshore - offer these different structures. To hold assets outside the country of residence, preference is generally given to structures located abroad, i.e. in recognized international hubs. We will come back to this point later.

## WHAT ARE THE CONSEQUENCES OF CONTRIBUTING ASSETS TO A WEALTH STRUCTURE?

Indirect ownership means that the individual no longer owns the financial assets, but the structure. In return, the individual owns shares or units in a company or fund, rights in a trust or a claim on an insurer, as the case may be.

**Setting up and financing a structure requires professional advice to assess the legal and tax consequences : Is the structure recognized in my country of residence and possibly in that of my heirs?** Are there any taxes or fees associated with the transfer to the new entity? Is it preferable to transfer the portfolio or to sell it and have the structure buy it back?

For tax purposes, the structure is either considered as a separate entity or transparent. In the latter case, it is the shareholder's responsibility to reflect the company's assets in

his tax return and bear the tax. In the event of the death of the owner or shareholder of the structure, the legal representatives - directors, trustees or insurers – handle the estate, in accordance with the applicable laws and taxation.

## WHAT ARE THE REASONS AND MOTIVATIONS FOR SETTING UP WEALTH STRUCTURES?

To name but a few of the needs frequently expressed by private clients:

- asset protection
- confidentiality / privacy
- tax efficiency
- simplification of tax reporting
- estate planning
- co-investment with third parties

Some of these needs can be met without a wealth structure. For example, most successions are planned through last wills. Using the services of an accountant allows foreign assets to be properly reflected in the tax return.

However, in some instances, a structure, alone or in combination with other measures, will be necessary to achieve the desired goal. Below are a few examples.

## ASSET PROTECTION

- **I live in a politically unstable country. I would like to mitigate my country risk with my foreign assets.**
- **As entrepreneur, I want to protect my loved ones in case I go or become bankrupt.**
- **The wealth of my family should be protected in case my marriage would fail.**

With asset protection planning, you mitigate the risk of unwanted parties gaining access to

your assets.

**Trusts, foundations and life insurance policies are frequently used to enhance asset protection. This planning is based on a simple principle : once transferred into the structure, the assets can no longer be seized by your creditors as they no longer legally belong to you.**

The effectiveness of an asset protection plan depends on multiple factors such as the jurisdictions involved (that of the investor, of the structure and of the underlying assets), the features of the structure and the timing of its implementation. For example, a plan designed to defeat an existing claim is likely to fail and to expose its initiator to legal action.

## CONFIDENTIALITY / PRIVACY

- **I live in a country where holding assets puts my physical safety at risk.**

Opening an account in the name of an entity will take the banking correspondence out of your name and improve your security. However, the confidentiality offered by the structure is limited: the tax authorities of your state of residence will, for example, be informed of the existence of the foreign entity and its assets, thanks to the exchange of information in place between the countries.

## TAX EFFICIENCY

- **How can I legitimately defer taxes on the income and gains generated by my portfolio?**
- **How can I take advantage of the tax benefits available in my country of residence (life insurance, pension funds, special tax regime for holding companies, etc.)?**
- **The taxation of financial investments is complex in my country of residence. How can I avoid being penalised by unwise tax choices?**

**Tax deferral is beneficial because it allows your portfolio to grow faster. Bringing your portfolio to an ad hoc structure will allow you to defer taxes and to no longer bother about the tax treatment of each individual investment. Instead, you will be mindful of the tax treatment of your structure.**

Holding companies have long been the preferred vehicle for maximising the after tax return on a portfolio or participation. Many countries attract holding companies to their territory by offering them favourable tax treatment.

Today, holding companies, even when established in European jurisdictions such as the Grand Duchy of Luxembourg, the Netherlands or Malta, do not offer their shareholders with the desired tax deferral if they do not have the required substance or do not comply with the multiple anti-abuse provisions in force.

As for companies established in "blacklisted" jurisdictions (countries with low taxation or without information exchange agreements with other states), they generally expose their shareholders to punitive taxation (heavier than that which applies in case of direct ownership). The constraints imposed on holding companies have led to the emergence of unit-linked life insurance policies : With these, the premium paid at subscription is invested in a securities portfolio managed by the bank of the policyholder.

In many countries, particularly in Europe, policy-holders benefit from tax deferral: the income from the portfolio is only taxed when the policy is surrendered or at death. However, **this treatment is reserved for genuine policies, those that are part of an estate plan.** In other words, contributing a significant portion of your wealth, at an advanced age, into a policy is a strategy that is likely to fail in many countries.

The Grand Duchy of Luxembourg, Ireland and Liechtenstein have become key jurisdictions for cross-border life insurance, thanks to their European passports and the protection afforded by their laws, particularly in terms of segregation and deposit protection.

It is common for individuals, particularly in Europe, to use foreign (rather than domestic) insurance policies to hold foreign assets. If this is the case, we recommend that you check deposit protection, restrictions on surrender, compliance of the policy with the rules applicable in your country of residence and tax treatment.

## TAX REPORTING

- **How can I simplify my country's tax reporting obligations for my foreign bank account?**

Countries tend to impose stricter reporting rules on their taxpayers for foreign bank accounts than for domestic accounts. Foreign wealth structures are also sometimes subject to specific disclosure rules. This is for example the case for life insurance policies and foreign trusts set up by Belgian, Italian or French taxpayers.

In general, the tax reporting takes place once a year when you file your tax return. Some countries require additional ad hoc reporting on specific tax events, for example when a dividend is paid or a trust is dissolved. Without the help of an accountant or tax specialist, meeting your tax reporting obligations for your foreign assets can be challenging.

**Holding your portfolio through a non-tax-transparent structure will make this task easier. Instead of reporting the value of each individual investment and the income it generates, you will provide the tax authorities with a consolidated figure reflecting the value of your company, trust or insurance policy and the amount of distributions paid to you.**

In most cases, the consolidated figures to be reported in your tax return are provided by the professionals in charge of your structure.

## ESTATE PLANNING

- **I would like to protect the children from my first marriage.**
- **I want to balance the share that my wife and daughters will have against what is required by the Sharia law.**
- **Ensuring the continuity of my business after my death is as important as allowing my heirs to benefit from it.**

Most often, when you plan your succession, you draw up a last will. However, a will may not be appropriate if you are pursuing one of the following objectives :

- limiting the effects of the forced heirship rules applicable in civil law and Sharia law countries.
- to organise the transmission of wealth over several generations ensuring that your values and principles are applied beyond your death.
- to ensure the sustainability of a company through appropriate governance.
- to carry out charitable missions.

The use of life insurance, trusts or foundations, to name the main estate planning structures, may be considered in these cases.

Life insurance policies discussed above are, per se, estate planning tools: through their beneficiary clause, the assets pass to the designated beneficiaries on the death of the insured person.

For complex cases due to the family situation or the nature of the assets and for multi-generational planning, trusts and foundations are often preferred because of their ability to adapt to changing circumstances such as birth, premature death, sale or disappearance of an

asset, relocation of a family member to a new country, family conflicts, etc.

The trust is a concept that originates from common law countries, whereas the foundation originates from civil law countries. Many jurisdictions have introduced the trust into their legal systems. Although Switzerland is a civil law country, it is in the process of adopting a trust law in order to remedy shortcomings in its domestic law. In addition to the United Kingdom and the United States, the Channel Islands, the Bahamas and the Cayman Islands are among the leading trust jurisdictions.

For foundations, the choice of jurisdictions is more limited. Jersey, Liechtenstein, the Netherlands and Panama are some of the main options.

There are multiple types of trusts and foundations (revocable, irrevocable, fixed or discretionary). Their legal and tax treatment depends not only on the type of trust or foundation but also on the country of residence of the respective stakeholders and the powers they exercise within the structure.

**Some countries do not recognize trusts and foundations from a legal point of view or restrict their application. Their tax treatment is sometimes uncertain or even unfavourable. For this reason, alternative structures (e.g. civil companies, testamentary pacts or life insurance policies) better suited to the country of domicile of the deceased or his heirs are sometimes used as substitutes to trusts or foundations.**

## CO-INVESTMENT WITH THIRD PARTIES

- **I need a professional framework to co-invest with family and friends in a private equity project.**

The interposition of a company can be useful where assets are held by multiple owners. For example, two family members may each own a share in a company. The shares will pass to the heirs in due course, in accordance with the respective last wills. A life insurance policy can also be used to consolidate assets held by multiple custodians or even to jointly manage the assets of different family members to achieve economies of scale or enhance portfolio diversification.

**However, when it comes to consolidating multiple asset classes and/or investors, the investment fund is the most suitable structure because of its variable capital, a clearly defined asset valuation process, and a more institutional framework where the client's family office can play a central role if necessary.**

From a regulatory standpoint, there is a wide range of funds, from highly regulated funds (UCITS) available to unsophisticated investors to lightly regulated or unregulated funds (often referred to as private funds or family funds) reserved for wealthy and sophisticated investors.

Well-known jurisdictions for private funds include the British Virgin Islands, Cyprus, Malta, Ireland, the Grand Duchy of Luxembourg, etc. The level of regulation, the security they offer to investors, the quality of their local infrastructure and their costs are the main differentiators between fund jurisdictions.

If you are a resident of the European Union, a private fund located in a tax haven will probably not be recommended for tax purposes. Similarly, your shares in a fund with only a few investors may not be treated as favourably as those in a truly collective fund, as we see in Switzerland and Spain.

Investment funds are sophisticated and expensive structures that involve an ecosystem of professionals (administrators, custodians,

investment managers or advisors, accountants, auditors, etc.). It is sometimes possible to mutualize costs by "renting" a compartment in an "umbrella" fund rather than creating your own independent fund.

### **WHEN SHOULD A STRUCTURE BE DISSOLVED? WHAT ARE THE RISKS OF NOT DOING SO?**

Given the numerous domestic and international initiatives to curb their misuse, most structures, even those that have been established recently, no longer (or soon will not) comply with current standards: they have no staff or offices of their own, their main purpose is to hide the identity of their shareholders, they are established in low or no tax jurisdictions or in "blacklisted" countries.

Holding assets through a non-compliant structure is inappropriate not only because of the high risk that it will be detected by the relevant authorities, but also because of the consequences to which the owner is exposed: In the least serious cases, the non-compliant entity will be treated transparently by the tax authorities. Its income will be assigned to its shareholder. In most cases, however, the shareholder is exposed to higher taxation than would have applied in the absence of the structure, sometimes penalties, longer statutes of limitations, more burdensome reporting duties and, in the most serious cases, to criminal sanctions and reputational damage.

Let's not forget that obsolescence of a structure can also result from a change in personal circumstances such as the relocation to a new country, the birth or death of a person, or the sale of an asset.

**Changes in family circumstances, regulations and taxation may impact the nature, validity and efficacy of your structure. For this reason, it is essential to have your structure regularly reviewed by your tax and legal advisors.**

## **TRENDS AND CONCLUSIONS**

How you and your family own your assets can be just as important as what you own. Using the right structure for your situation is essential for successful planning.

Holding assets directly in a bank account in your name is the preferred option whenever possible.

However, certain objectives or situations may require the use of a structure. This is illustrated by the fact that we continue to see new structures being put in place, even in sophisticated countries.

The landscape for wealth structures has changed dramatically over the past decade. Compliance requirements, particularly with respect to tax, have increased sharply. If you hold your assets through a structure or are considering creating one, you should take this into account.

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We hope that you will find interesting our Newsletter dedicated to wealth structures. We are at your disposal to deepen the topic.

In the meantime, please do not hesitate to send your suggestions for future newsletters to

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