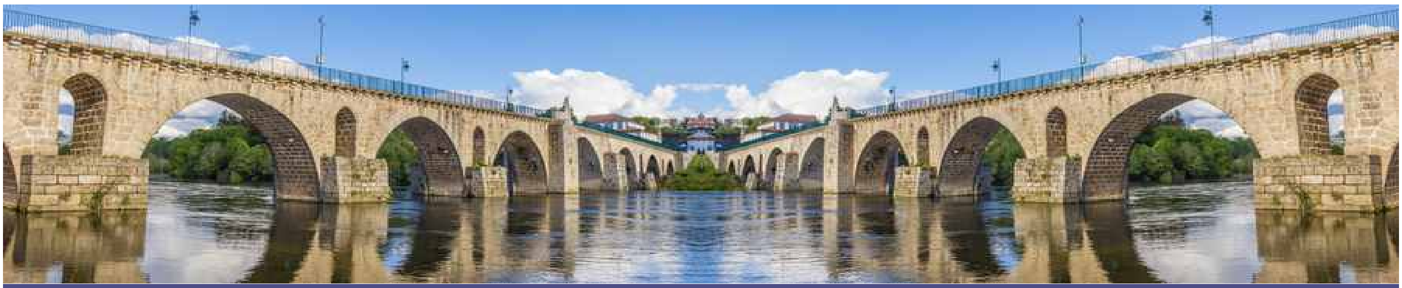



# TAX TECHNIQUES

nº 18 - Autumn 2017

an *e*Publication from ***euro*FINESCO*s.a.*** FISCAL & EXPATRIATE SERVICES


## THE DELAWARE PAPERS

### *Delaware Companies in a World of Change*

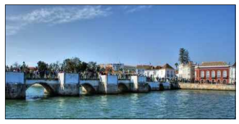
The European Commission has decided to replace the 28 individual EU country offshore blacklists with one common register, based on adherence to the new *Common Reporting Standard*. The United States (aka "*America first*") still refuses to sign this broad-based international information sharing agreement, thereby excluding Delaware from general acceptance. Meanwhile, once tainted tax havens now progress to the top category as compliant "early signatories".

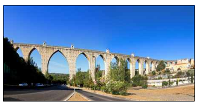
In 2018, Portuguese properties belonging to these reclassified Delaware Companies may be faced with Property Rates ("IMI") assessed at 7.5% of their updated Rateable Value ("VPT"). To make matters worse, the new Additional IMI ("AIMI") levy will also be assessed at 7.5%, leading to an annual total tax of 15%. In plain English, this means annual Portuguese Property Tax, previously paying just a few hundred Euros a year, will soar to the tens of thousands of Euros per annum for unwitting Delaware Company owners.

Our "Delaware Papers" newsletter clarifies this looming situation and explains how you can still take timely steps to avoid the unwanted consequences of this "inevitable" change.

### AUTUMN NEWS BRIEFS

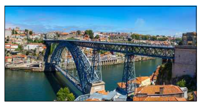
- NHR: *Potential minimum tax on pensions*
- *Ageing & expensive rent rob young adults*
- Golden Visas: *delays force move to other offices*
- *Distinction proposed between LL businesses*
- Golden Visas: *only 8 created jobs since 2012*
- Golden Visas: *blocked until November*

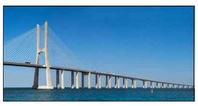




**a. *Delaware classified as opaque jurisdiction*** - Delaware has the dubious honour of being classified amongst the least transparent tax havens by the Tax Justice Network. Tax authorities around the world lose hundreds of billions of Euros each year in tax revenues.

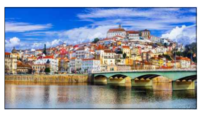
**b. *Why move a Delaware Company to Portugal*** - When a company redomiciles to Portugal, there is no asset transfer: no crystallisation of CGT, no "*I.M.T.*", no Stamp Duty. Only the headquarters and management move. The assets remain safely within the Company.





**c. *CGT and Redomiciliation to Portugal*** - Historically, many offshore jurisdictions had lax accounting, when financial statements were not required. At best, practices were *pro forma*. Upon entry to Portugal, we must now begin with an accurate balance of accounts.

**d. *Buying a Property in a Delaware Company*** - Annual property tax for black-listed companies is now set at 7.5% of "VPT", some 20 times the Rates on domestically held property. The new AIMI also doubles this levy. Rateable Values ("VPT") are also updated.

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## THE DELAWARE PAPERS

### *Autumn News Briefs*

**NHR:** ***Potential minimum tax to be assessed on pensions***
Government is studying a basic levy to Non-Habitual Resident pensions with possible introduction in the 2018 State Budget. According to the *Jornal de Negócios*, the step under consideration is applying a potential tax rate of 5-10%. Currently, NHR beneficiaries enjoy a 10-year tax holiday. The measure is said to be in the name of "good fiscal relations" with other European countries.

**Local Lodging:** ***Proposal to distinguish between types of "AL" businesses***
The Left Block, a partner in the governing coalition, proposes changes to current Local Lodging legislation. Under the soon-to-be recommended plan, holiday letting not exceeding 90 days per year should continue to benefit from the current tax regime. Year-round operation – without a limit of days and designated as "tourist accommodation" (*Habitação turística*) - must be equated with a hotel activity and assessed on the same basis.

**"*AL*" & Housing:** ***Ageing and high rents rob young adults from Lisbon***
Lisbon has experienced the greatest decline in the number of young adults within Portugal in recent years. One factor contributing to the drop is the difficulty in finding affordable housing. In 2012, the median rent in Lisbon was €268, according to INE ("*Instituto Nacional de Estadística*"). In 2016, the average climbed to €830. But high rent is only part of the problem. The ageing of the population is at the root of the decrease. In 1991, Lisbon had 138 seniors for every 100 young people (from 0 to 14 years old). By 2016, the number of elderly rose to 182, a proportional increase of 24%, making Lisbon the oldest council in the nation. Provisional population estimates advanced by INE indicate that the number of young people aged between 20 and 34 living in Lisbon went down from 95,830 in 2011 to 67,916 in 2016, a net loss of 29%.

**Golden Visas:** ***Only 8 awarded have created jobs since 2012***
Between 2012 and July 2017, just eight Golden Visas, out of a universe of 5,243, were granted based on the creation of job positions in Portugal. The vast majority of investors (4,945) choose to buy homes costing more than €500,000 in order to qualify for permanent residency programme.

**Golden Visas:** ***Delays move processing to other offices***
The Immigration and Borders Service ("SEF") will authorize Golden Visa applicants wishing to make property investments in the Greater Lisbon region to submit their applications to offices outside the capital area as is currently required. The decentralisation move intends to reduce the current growing backlog of submissions.

**Golden Visas:** ***Processes blocked until November***
The Immigration and Borders Services will not be able to process new applications until November according to APEMIP *(Associação dos Professionais e Empresas de Mediação Imobiliária de Portugal)*. "SEF" continues understaffed and overwhelmed with the backlog of existing requests.

## THE DELAWARE PAPERS

### a) *Delaware classified as opaque jurisdiction*

According to financial standards of opacity, Delaware has the dubious honour of being classified amongst the top *least transparent tax havens* as determined by the Tax Justice Network. Tax authorities around the world lose hundreds of billions of Euros each year in tax revenues due by major corporations as well as high net worth individuals who hide their assets in offshore structures. Compounding the problem are added links to money laundering, financing of terrorism and global drug trafficking networks.

#### *Misleading stereotypes*

In identifying the most prominent providers of international financial confidentiality, the study also reveals that traditional stereotypes of tax havens are often erroneous . The world's most preeminent suppliers of financial secrecy are not quaint tropical islands as is customarily imagined, but rather some of the world's largest and richest countries. Wealthy OECD member states and their satellites jurisdictions are the primary benefactors of or channels for these illicit capital flows.

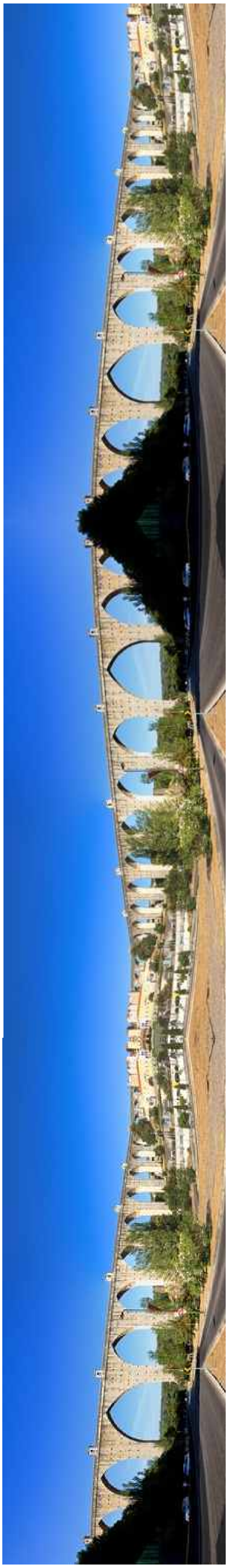
#### *American double standard*

The United States and its second smallest state, Delaware, are glaring examples of duplicitous practices. One illustration is the *Delaware LLP* (Limited Liability Partnership). As a fiscally transparent entity, these "offshore companies" pay no US tax in their own right as their non-resident shareholders have no US-sourced income. Subsequently, money from around the world can be moved to and from these structures tax-free.

The United States, after instigating dramatic international changes in fiscal transparency with the introduction of "FATCA" (Foreign Account Tax Compliance Act), now refuses to be part of the OECD's Common Reporting Standard, leaving states such as Delaware high in the ranking of *Least Transparent Offshore Jurisdictions*.

This example of "*America First*" dates back to policies of the Obama administration and before. It seems highly unlikely that this "*go-it-alone*" approach on the part of the US will change anytime soon under the Trump government.

The implications for global power politics are enormous and help explain why international efforts to crack down on tax havens and financial secrecy in te past have been so ineffective over the years. The reprehensible reality is that the recipients of these "huge" inflows of capital are the very same ones who write the rules of the game.



## *EU agrees on criteria for Tax Haven Blacklist*

Last year, the European Council resolved that it would determine a common EU registry of non-cooperative jurisdictions by the end of 2017. To be considered compliant for tax transparency, a country needs to commit to implementing the Common Reporting Standard (CRS). It must also have agreements in place for the automatic exchange of tax information with all EU member states as well as achieve an OECD rating of "largely compliant". By the end of the year, this EU-wide classification will replace the country-by-country "black lists" that abound throughout the European Union.

Unless the US makes an unexpected reversal in its current uncooperative policies by the beginning of 2018, Delaware will finally find itself amongst the EU classification of attainted black listed jurisdictions. Portuguese properties held in Delaware companies will face a ±20 fold increase in their normal rates bill plus similar amounts again due under the new *"AIMI"* levy. Rather than real estate rates of a few hundred Euros as before, these structures may face annual tax bills of as much as €50,000 per annum or more. Delaware company owners take heed!

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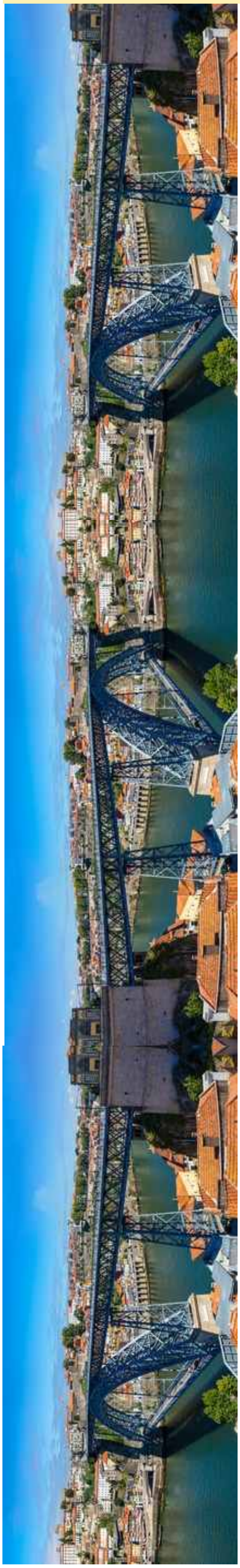


## THE DELAWARE PAPERS

### b) *Why move a Delaware Company to Portugal*

*Offshore* has become a “four-letter word” throughout the EU in recent years. Properties held in Delaware Companies, for example, once a popular solution within the expatriate community in Portugal, will soon become a scourge in 2018. Property tax rates, normally 0.4%, will skyrocket to 7.5% next year for US companies. This means a property valued at €300,000 pays an annual tax of €22,500 rather than €1,200! Coupled with the new AIMI levy, the annual tax due will reach €45,000.

When a company redomiciles to Portugal, there is no asset transfer: no crystallisation of Capital Gains, no “*I.M.T.*”, no Stamp Duty on Real Property. Only the headquarters and effective management move. The assets remain safely within the Company. Thus the alternative term for Redomiciliation: *Continuance*. “Continuance” opens an attractive opportunity for tax mitigation.

### *Updated Basis for Capital Gains Tax*

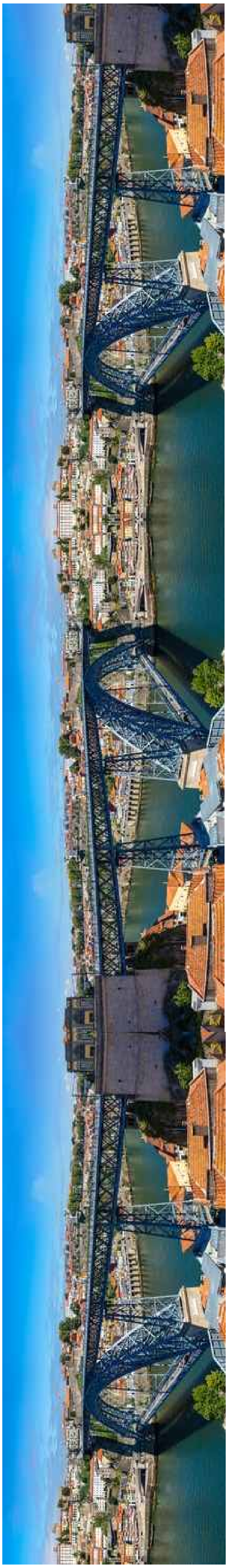
Following Company registration in Portugal, a Balance of Accounts needs to be presented to mark the starting point as a Portuguese resident entity. This Balance Sheet must be based on *current* rather than *historical* values. Thus, the Company’s assets reflect either their book value or the present market value of the property. Any Shareholders’ loans into the Company as well as any mortgages (if one exists) show as “Liabilities”. “Capital” is the paid-up share capital as well as Reserves, reflecting any appreciation in the value of the property. As such, there is a fresh start and many historical problems, such as under-declared deed values or lack of bonafide invoices for capital improvements, can be rendered mute.

The move to Portugal constitutes a *transformation,* not a *transfer of ownership*. The latter is at the core of any chargeable event. However, if a Company moves across the street or resettles to another jurisdiction, it is not seen as a transfer because of the nature of *continuance*, meaning, despite a new permanent establishment in a new jurisdiction, there is no fundamental change seen in the Company.

### *Reduced CGT*

From this new base as a resident Portuguese entity, Capital Gains Tax on the eventual sale of the Company is reduced to 14%, as compared to 28% that may normally be assessed to other Portuguese companies. The combination of these factors alters what is normally a colossal problem into a very manageable inconvenience.

Capital Gains tax mitigation can take one of two forms. With the uplift in share value upon registration of the new Portuguese entity, the shares can be sold at full value with little or no gain. Alternatively, the company can be wound up (liquidation) and the assets distributed to the shareholders. As in the previous instance, with similar documented values, there is little or no tax to pay.



***Potential Transfer Tax Exemption***

If the Company assets include Portuguese immoveable property, the sale of the shares may be exempt from "*IMT*" depending on the circumstances of the eventual buyer of the Company. Under Portuguese law, when one does not exceed a concentration of more than 75% of shares to any one of the shareholders, no Property Transfer Tax (*"IMT"*) is due on the underlying assets. If eligible, the buyers may potentially save many thousands of Euros, thus making such an acquisition more desirable than purchasing in one's own name.

***Reduced Bureaucracy***

When property changes hands, many organs of government get into the act. *Finanças* records the change of ownership and updates the "*VPT*" evaluation (rateable value) in a somewhat cumbersome and laborious process. The Council checks to see that current technical drawings match the building on site. The Land Registry verifies that boundaries and areas are correctly recorded. In short, a sea of bureaucracy that can be both slow and expensive.

A transfer of ownership of shares is normally a simple notarial process. While there is some paperwork involved in amending records to reflect the changes of Company domicile or ownership, the process is normally straightforward and does not trigger reevaluations of the underlying property nor any latent licensing problems inherent in many older properties.

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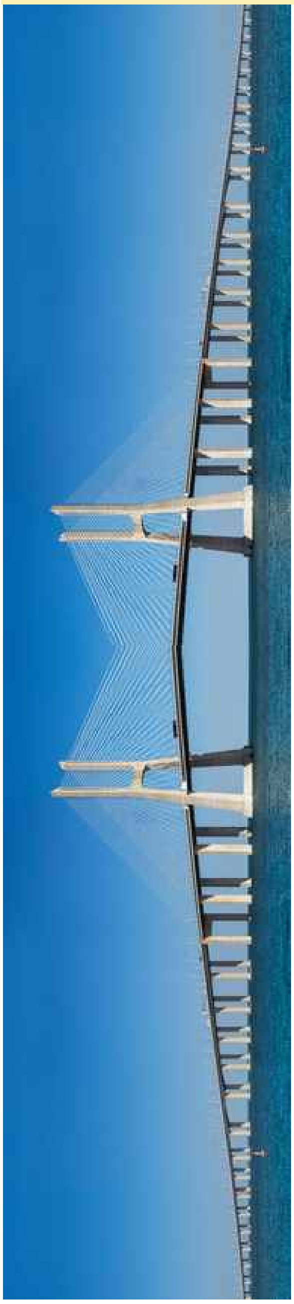
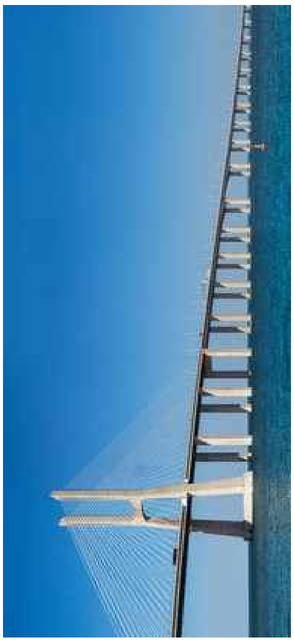




## THE DELAWARE PAPERS

### c) *CGT and Redomiciliation to Portugal*

**Company Redomiciliation: *Non-Resident to Resident***

Historically, many offshore jurisdictions had lax accounting, when financial statements were not required for "exempt" companies. At best, practices tended to be *pro forma*. Upon Redomiciliation to Portugal, we must begin with an accurate, current balance of accounts, so that future declarations will be fully correct and compliant, not merely historical figures that may be a decade or more out-of-date. ("*O valor das quotas ou partes em sociedades ... determina-se pelo último balanço.*" Art. 15º, CIS).

For these and other reasons, we perform a proper appraisal of the company's property, so that the closing balance prior to Redomiciliation, as well as the opening balance once a recognised Portuguese entity, reflect the present rather than the past of the Company and its assets.

**Non-Resident Companies**

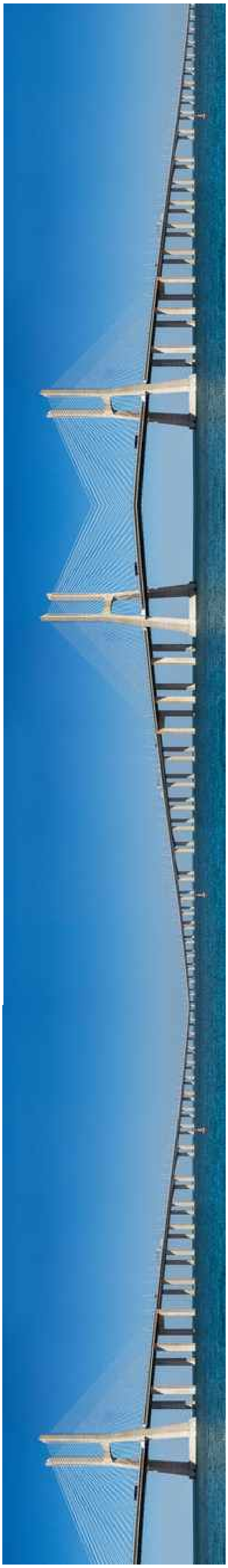
Nonetheless, any uplift takes place while the Company is *non-resident without permanent establishment* in Portugal, still subject to the statutory law of its home jurisdiction. Theoretically, the change from historical to current accounts could constitute a taxable event in that resident territory. However, for most offshore jurisdictions in question (whether blacklisted or not), this rarely proves to be the case. In the instance of Delaware, there is no final assessment.

In Portugal, chargeable events for *non-resident companies without permanent establishment* are determined in accordance with Articles 15º and 51º of the CIRC. Under current legislation, a redomiciliation is not contemplated as taxable income.

Once the move is complete, it is the current value of the shares in Portugal that will be act as the basis for calculating capital gains on the eventual sale of the resident company.

**CGT: *Company* versus *Property* transfers**

Confusion easily arises if the value of a *Company* is mixed up with the worth of its *Property*. Capital Gains on Real Estate is always calculated on the net difference between original purchase and sale price of a property. Any eventual sale of the *Property* by the Company will trigger a CGT assessment to the *Company*, the owner of the *Property*. On the other hand, the sale of the *Company* would normally spark Capital Gains Tax to the shareholders on the difference between recorded values when first registered in Portugal and the eventual sale price of the *Company*. Needless to say, each event is distinct in nature and subject to entirely different fiscal rules.



## Finanças' Position

We, at ***euro*FINESCO**, have always acted with full knowledge of and cooperation from the Portuguese tax authorities regarding Company Redomiciliation. In fact, it was *Finanças* that originally recommended and encouraged us to pursue the strategy of bringing offshore companies to Portugal, rather than moving them laterally to other jurisdictions. They have actively helped us to overcome obstacles that we have encountered over the years, working with us to bring these corporate entities to a fully compliant, resident status here in Portugal.

## *What if the USA signs up for Information Sharing?*

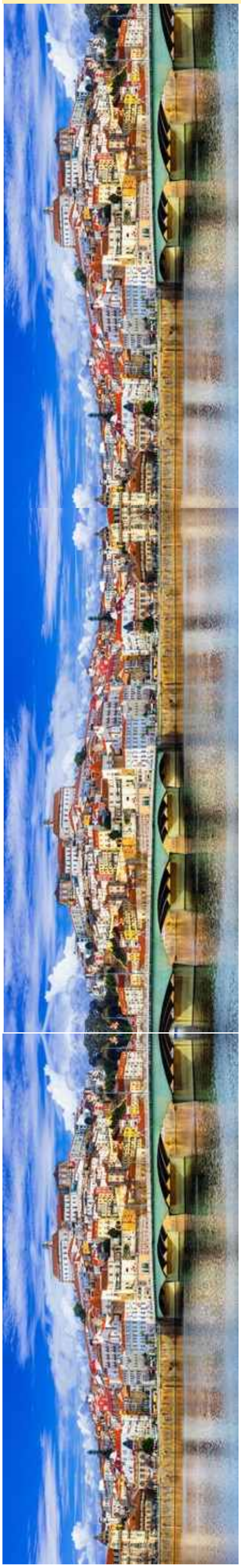
Imagine that Delaware (read: USA) changes its policy at some time in the future and decides to join the *Common Reporting Standard*. What is your situation if you act now to get out of Delaware?

1. You will most likely have substantially reduced your company running costs.
2. You will have uplifted the share value of your company from a token amount to the full market value of your property.
3. You will be in a position to either:
   - a) continue enjoying the benefits of Portuguese company ownership; or
   - b) liquidate the corporate structure altogether and own the property in your own name. In either case, your Capital Gains Tax position will be similar: little or nothing to pay.
4. You will be out of "Offshore": you will be in Portugal, your property will be in Portugal; your company will be in Portugal.

*Isn't that what you wanted in the first place?*



03 September 2017



## THE DELAWARE PAPERS

## d) *Buying a Property in a Delaware Company*

Putting a property Offshore was once considered the sensible thing to do. However, annual property tax for black-listed companies is now set at 7.5% of registered value (“VPT”), some 20 times the Rates on domestically held property. The new AIMI also doubles this levy.

Also important it the fact that rateable values, traditionally understated, have also been updated. As a buyer, what should you look out for when the house of your dreams is in a Delaware Company, once “white-listed”, now soon-to-turn black?

### *Don’t buy the Problem*

Keep in mind Rule nº 1: *When you buy a company, you acquire both the assets and the liabilities*. The first problem, of course, is the Delaware Company structure itself. It can be expensive to maintain, needlessly forcing you to pay Portuguese Corporate Income Tax and, worst of all, can cost you tens of thousands of euros annually in extra Property Rates assessment. All because the Company’s head office is soon to be considered to be in a black-listed jurisdiction.

However, if the owner moves the Company headquarters and management to Portugal, not only will most of the problems melt away but both you, the buyer, along with the seller, will achieve surprising tax advantages.

### *Investigate the History of the Company*

Many companies have a complicated past. Sometimes, there are underlying bureaucratic problems. All too often, improvements have been made without building permission or without registration. Some former owners engaged the property in commercial activity, yet never declared a penny of the earnings.

Remember rule nº 2: *the Company’s liabilities are the responsibility of the current shareholder.*

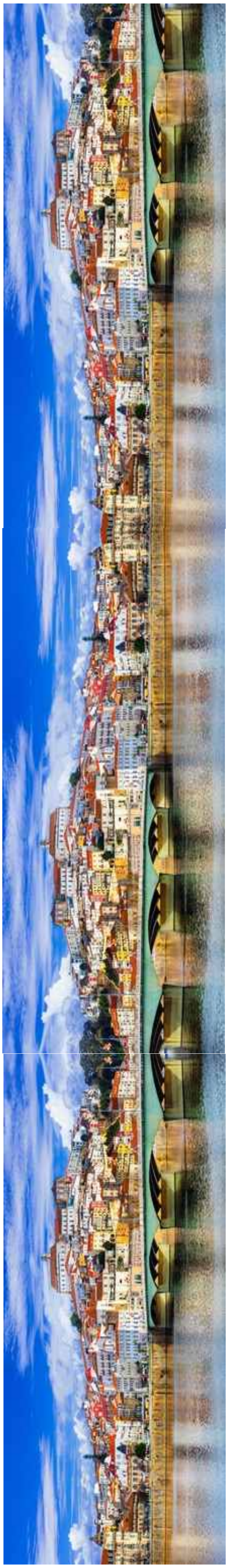
Finally, do your homework thoroughly. Have your lawyer check all registrations, deeds, licences, etc. to make doubly sure that everything is up-to-date and contains no surprises. You, as current owner, will be responsible for any outstanding liabilities.

### *Check out Compliance Requirements*

Another key issue is *Compliance*. Has the Company fulfilled all legal and fiscal requirements? Who is the Company’s Fiscal Representative? Make sure that the Company tax returns have been submitted and that property Rates are up-to-date.

### *“the Triangulation Trap”*

Those with property companies in Delaware are faced with a dilemma: while in the past, they were able to escape the immediate consequences of punitive taxation on black-listed companies, they still failed to resolve a fundamental taxation problem: *the Triangulation Trap*.



No government likes to lose control over a piece of sovereign territory, especially when it means giving up most taxation rights. Portugal is no exception. This is why the OECD introduced measures in the current version of the Model Double Tax Treaty to enable countries to assess Capital Gains on effective property transfers wrapped in a foreign Company.

In a nutshell, the owner/taxpayer may be faced with being taxed twice: once, in the Company, from the *de facto* transfer of rights to the Portuguese property, and also as an Individual, on the gain from the sale of US shares within a worldwide assessment of income in the home jurisdiction.

Under Portuguese law, as elsewhere throughout the European Union, it is your obligation to declare <u>all</u> of your taxable income. It is *Finanças'* job to evaluate and assess income or implement coercive measures if you do not fulfill your reporting requirements. If left undeclared, a liability could remain in the Company as an eventual charge against future shareholders.

### *Buy a "Clean" Company*

The problem is not the Company *per se*. It lies in the fact that the headquarters of the Company is in a black-listed non-resident jurisdiction. If the shareholders transfer the headquarters to Portugal, the Company achieves a "New Beginning":

1) Capital Gains Tax issues can be reduced to a minimum;
2) Buyers may be exempt from "*IMT*" transfer tax (formerly "Sisa");
3) Operating costs are low;
4) Local management can provide an important support structure against eventual property related complications.

### *Get a Bargain*

Finally, rule nº 3: *the difference between a problem and an opportunity is your perception*.

While the current starting place may be less than desirable, simple, relatively inexpensive changes can dramatically reverse the fortunes for all concerned. With sound professional advice and a bit of perseverance, the house that is now a nightmare can become your "dream come true". In other words, buy a bargain, then move the structure safely to Portugal.

 03 September 2017