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Successfully working in foreign countries - Soft Facts of International Assignments

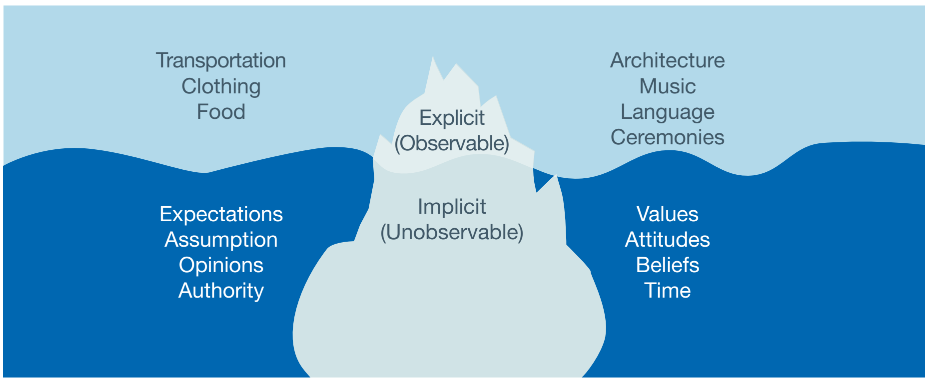
The trend towards international assignments has increased despite the global recession but companies are focusing on short-term assignments in an effort to control costs, says a recent survey by business consultancy Mercer. Mercer's International Assignments Survey 2010 found that international assignments overall have increased by 4% over the last two years. However, to help control costs, companies are focusing on short-term assignments, with over 50% reporting an increase in such assignments. The survey, released on Sept 15, collected data from more than 220 multinational firms across all industries.

Doing business globally and recruiting employees for an international assignment requires careful management and involves concerns such as family adjustment, social and living arrangements, new schedules, costs of moving and settling in, language and cultural training, and personal attitudes, needs, and goals. All of which cannot be truly experienced until your new assignee arrives at their destination and starts working. However, many assignees are surprised at the differences between an earlier visit when they were "shown around" by their hosts and were not introduced to the reality of day to day working and what the reality actually is. In fact, it's very hard to understand another culture unless you've lived there, and that understanding is crucial to business success in a global society.

This article does not deal with administering an assignment. It does not cover social security, health insurance or tax related or visa and immigration issues, relocation procedures or supports you to negotiate an assignment contract. The following deals with the soft facts, such as cultural aspects to an international assignment playing a key role to become successful in business.

Culture

Generally speaking culture can be understood as a shared pattern of preferred values, assumptions, belief and behaviors that define the way of life of a group. And culture can be thought of as an iceberg.



The visible portion of the iceberg consists of the tangible elements, and the invisible, larger part consists of the intangible components. Thus, the tip of the iceberg can be said to consist of observable manifestations of culture, whereas the thick, much more powerful, block of ice below the surface of the water consists of the thoughts and feelings that are associated with and connected to these behaviors. If these thoughts and feelings remain invisible to us, and we have no insight into them, if we see only the behaviors different from our own, then, like any unsuspecting ship, we may run into the iceberg and founder.

And of course there are differences in business. Therefore, the better employees are being prepared, the easier it will be to integrate into the new and unfamiliar which for the company means that the employees will manage business in the new environment much faster.

Stages of Adjustment (Culture Shock)

There are four stages applied to the culture shock, a term used to describe the feelings of alienation experienced when living in a new culture; a state of loss and disorientations predicts in the familiar environment which requires adjustment.

During the "*honeymoon phase*" the differences between the old and new culture are seen with enthusiasm and excitement, anything new or unusual is being mastered with a curious attitude. Like many honeymoons this stage eventually ends as the assignee will invariably experience difficulties with language, housing, friends, transportation, school, work, ...

After some time (3-6 month) differences between the old and new culture become apparent and my create anxiety. This "*regression phase*" will eventually give way to new and unpleasant feelings of frustration and danger as one continues to have unfavorable encounters, feelings of being lonely and not understood. These reactions are typically centered on the language barriers as well as strong differences in quality of food, traffic, safety, ...

During the "*adjustment phase*" things become "normal" again. After usually 6-12 month one grows accustomed to the new culture and develops routines. One knows what to expect in most situations and the host country no longer feels all that new. One starts to develop problem solving skills, interacts with the locals and the new culture begins to make sense.

Mastering the culture is the final stage of adjustment that gives mental stability in different perspectives. The assignee feels comfortable with the foreign way of living an actually begins to enjoy life.

Individuals may differ greatly in the degree in which culture shock affects them. Culture shock can occur directly upon arrival when one immediately begins to miss one´s home country, friends and family, food, ... However, it is at no times advisable to isolate oneself or have anger towards the host people. While it is needless to say that the culture shock will not occur everytime in exactly the same manner or for each individual reacts differently and sometimes a phase lasts longer, it should be mentioned that undergoing a culture shock is absolutely normal.

Cross-Cultural Communication

Cross-cultural communication is simply a strategy for operating successfully in a culture different from one´s own. Spoken language, body language, dress, and customs describe in what areas one can respect a new culture and become interested in working within it. For the spoken language can be considered as window to each culture. Learning a few words and phrases will be the best way to get started. While body language will probably be the most difficult aspect to learn, as it is the least conscious, close observation can help to understand the new culture. A mentor is invaluable, not least because of one´s own unconscious assumptions.

For dress on the other hand is cross-cultural communication made easy. The wise (and trained) newcomer will seek help or advise early in the integration process. Customs are everything else. While some people fear of doing things wrong, others observe closely and pay attention to not behave "just like home".

Some **general guidelines to cross-cultural communication:**

- Be careful with humor and irony. It doesn´t translate well.
- Be careful when using gestures. Certain ones may be obscene in some cultures.
- Learn appropriate nonverbal communication skills.
- What you say may not be what was understood. What you hear may not be what was meant to imply.

Furthermore you might want to consider the following six steps for effective Cross-Cultural Communication:

1. Be aware of your own cultural assumptions and values.
2. Accept the reality of your own cultural conditioning.
3. Accept the reality of the cultural conditioning of the others
4. Don´t assume that what you meant is what was understood.
5. Don´t assume that what you understood is what was meant.
6. Test for understanding.

Start doing business

The company should expect all employees planning for expatriation to be knowledgeable about global business and cross-cultural communication, and the employees should expect support from the company in gaining such knowledge and skills. Apart from the new business environment, the host employer could provide a checklist to help the assignee to better integrate. A mentor to the assignee, who could be a foreigner himself who experienced the cultural change already or a former expatriate of the country, can be very helpful. Furthermore, all parties would add very valuable input to the integration and former experiences would be asked for and appreciated.

A very crucial aspect to the assignee is his new private environment. The worries he has, the uncertainty about the well-being of his family are a critical success factor to the assignment.

Action plan for successful integration with regards to Social Life as well as Business Life:

- What? What actions steps will support me towards a successful integration?
- How? How am I going to do this? What are my next steps?
- When? What deadline should I put on myself for completing this?

Repatriation - Integration

The first day of the assignment is the first day to start thinking of the repatriation. It is essential for a smooth repatriation to continuously stay in touch with the home company and preferred contact person. International Assignments give new perspectives and teaches managers to exploit opportunities that they may not have recognized before. However, an opportunity frequently wasted by companies with foreign subsidiaries is that of using the increased skill and knowledge of an employee returning to the home office after an overseas assignment. Yet it is common for returnees to feel sidelined, as if they have just "missed" the past few years, instead of gaining valuable skills in their work.

Therefore, most returnees appreciate if they get invited to present their "take-aways" in one of the next team or management meetings. Why not arrange a get together between former and current expatriates and re-integrate smoothly. Not only HR managers should give attention to finding ways to use the increased value of the employees whose knowledge of the company's foreign operations may be unparalleled back home.

Conclusion

International assignments have many facets and the management needs to consider them in concert, not piecemeal in order to minimize costs and maximize value from each overseas assignment. Pre-departure selection and planning, cultural awareness and orientation as well as skill-building, and the re-entry phase are all important components for planning. Left to chance, any one of these factors can undermine success and lead to increased costs, but managed attentively, expatriation can significantly improve and increase your global business effectively.

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Withholding taxes amended in Serbia

Recent amendments in corporate taxation in Serbia were introduced on March 23rd and came into force on March 27th. The discrete revision and immediate implementation of the legislation is the outcome of the fact that this reform was pending for more than two years; the proposed amendments awaited the ratification by the Parliament since fall 2007.

The main changes that caused the reaction of the tax advisors community are summarized below:

- The time frame allowed for carrying forward losses is reduced from 10 to 5 years;
- With the permission of the Minister of Finance or Governor of National bank of Serbia the fiscal year of a company, can be different than the calendar year. Such tax year must correspond to 12 months and be maintained for at least 5 years;
- Expenses incurred for sport, humanitarian, educational and cultural are now deductible so long as they do not exceed 3,5% of the total income of a company. Formerly, such allowable expenses could not exceed 1.5% of the total income of a company;
- Deductibility of marketing expenses is now permitted so long as such expenses do not exceed 5% of total turnover of the company.
- The allowance corresponding to entertainment expenses amounts to 0.5% of the overall income;
- Goodwill depreciation is expressly prohibited by the Law;
- Branches of foreign companies preserving double entry bookkeeping are under an obligation to submit their tax returns is the same manner as local companies and are now entitled to any and all tax incentives extended to local entities.
- Capital gains realized in Serbia by a non resident taxpayer will be subject to a 20% withholding tax in unless a DTT provides otherwise.

Notwithstanding the above, special attention should be drawn on article 71 of the corporate income tax law of Serbia, which could significantly impact the business of investors in a number of instances. Most importantly, the law now enables the taxation of the conversion of accumulated interest and/or accumulated profits into capital as analysed hereunder:

- Commonly, Serbian subsidiaries were injected with loan(s) registered with the National Bank of Serbia (NBS). The loan agreements accounted for interest obligations, which generally resulted in an accrual of interest payments at the level of the Serbian subsidiary, considering the fact that such interest payment were not physically made to the overseas parent company. Throughout the course and duration of the loan agreement, such amounts corresponding to interest payments due were accumulated at the subsidiary's level. At the expiration of a considerable amount of time though, the accumulated funds required the necessary attention as to mitigate tax leakage to the extent possible. Assuming that subsidiary in Serbia did not have enough cash flow to account for the payment of the total accumulated interest, the efficient alternative implemented was the conversion of the accumulated interest to capital, leading to an elimination of the obligations of the Serbian company towards its parent company. This action, which was effected by way of an increase of capital, was and still is in full compliance with the Serbian Company law, however, based on the revision of the legislation and the right to tax the conversion of financing into equity, it is no longer a tax efficient alternative to organizations.

- In line with the above, an increase and respective issue of additional share capital was equally considered to be an efficient alternative where companies were accumulating undistributed profits from previous years. Again, as per the aforementioned, such conversion will now trigger Serbian taxes.

In line with the aforementioned, and the changes in the phrasing under the law, taxpayers will be liable to a 20% withholding tax on interest or dividends, on any achieved or paid earnings, unless a tax treaty is in place providing for a more favourable tax treatment.

Therefore, taxpayers are under an obligation to apply and pay the withholding tax on interest or dividends in line with the provisions of the law. Further guidance is available in the case law, according to which the "substance over form" principle is confirmed by the Supreme Court of Serbia, essentially in case U 6573/2006 dated 15 September 2008, where the judge concluded that even the provision for some services could be seen as an interest payment and confirmed the right of the tax authorities to tax it with a withholding tax on interest.

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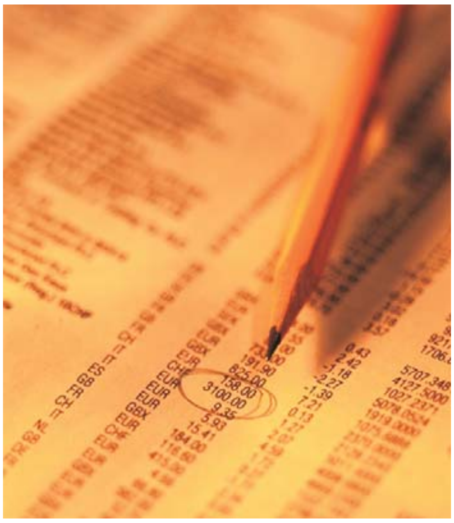
Proposed Direct Tax Code - Important Provisions and controversial Vodafone Case

The Income Tax Act, 1961 having been a bible for the taxation sector, has served the general public, professionals and also the judicial authorities to take the just decisions. But in due course of time, ample number of amendments has made the provisions of Income Tax Act, very much complicated, intricate and obscure.

Hence, a necessity for a new act was felt which could include the amendments in its final touch and could give concise form to the Act. As a result of this Direct Taxes Code Bill, 2009 was released last year. It went through many changes in response to the suggestions received from various quarters including general public and passed in the Parliament in the year 2010.Direct Taxes Code (DTC), 2010 will replace the Income Tax Act, 1961 and shall come into force on April 1, 2012.

DRIVING FORCE OF THE DTC:

- Single Code for all direct taxes and compliances procedures unified.
- Make tax system more efficient
- Simplify the complex structure of the Act by using simple language. Extensive use of formulae and tables.
- Make levels of taxation moderate and enlarge the tax base
- Remove ambiguity to encourage voluntary compliance
- Provide stability In the tax regime based on well accepted principles of taxation and best international practices
- Delegation of power to Central Government / Central Board of Direct Taxes to avoid litigation on procedural issues.



CORPORATE TAX RATES:

Particulars	Current Tax Rates*	Tax rates under DTC
Domestic Company	30%	25%
Foreign Company	40%	25%
Branch Profit Tax	Not Applicable	15% (New tax)
DDT	15%	15%
MAT	15% of the adjusted book profits	To be levied on Book Profit

RESIDENCY TEST:

- A foreign company to be resident even if partial control & management is in India (existing Act requires control & management wholly situated in India)

- Control & Management is held to be situated at the place where "directing power / decision making power" of the company is situated

TAX TREATIES:

- Government is vested with authority to enter into Tax Treaties

- Provisions under DTC as originally proposed-
  - Neither Treaty not DTC shall be given preference
  - Provision that is later in point of time shall prevail
  - Treaty will overrule if subsequent domestic law is inconsistent with treaty
  - Treaty benefits not available until a tax residency certificate is furnished

GENERAL APPROACH TO TAX AVOIDANCE:

- Application of anti-avoidance principles emerging from judicial decisions

- General Anti-avoidance Rules (GAAR)

  - A broad rule that can invalidate an arrangement that has been entered into by a taxpayer for the purpose of obtaining a tax advantage

- Specific Anti-avoidance Rules (SAAR), such as :
  - Transfer Pricing
  - Anti-treaty shopping provisions
  - Anti-deferral/CFC Rules
  - Thin Capitalisation

SAFE HARBOUR:

- Provides a measure of relief to taxpayers
- If the safe harbor provisions are set up at inordinately high levels or ranges, then taxpayers would continue to face litigation
- The global losses and financial crunch faced by the Group as such at present would also need consideration whilst exploring adherence with the safe harbor regulations

CONTROLLED FINANCE CORPORATION:

- Proposal to introduce CFC provisions as an anti-avoidance measure
- CFC provisions to apply to "passive income" earned but not distributed by a foreign company "controlled directly or indirectly" by a resident in India
- Such income to be considered as deemed distribution and shall be taxable in the hands of resident shareholders as dividends

RECENT VODAFONE CASE:

- Vodafone International Holdings BV, Netherlands (.Vodafone..) entered into an agreement with Hutchison Telecommunication International Limited, Cayman Islands (.HTIL.) to acquire 100% share capital of CGP Investments Holding Ltd, Cayman Islands (.CGP.) held by HTIL.

- CGP directly and indirectly through its various subsidiaries owns 52% controlling interest in Hutchison Essar Ltd, India (.HEL.). Further, through contractual arrangements of various companies situated in India, CGP holds 15% in HEL. The combined controlling interest acquired by Vodafone amounts to 67% of HEL.

- The transfer of shares of CGP by HTIL to Vodafone resulted in Vodafone acquiring control over CGP and its downstream subsidiaries, including HEL.

- A significant aspect of the judgment is the strong emphasis on .form over substance of the transaction.- a fundamental principle of taxation

- Courts cannot disregard the form of the transaction or look through legally constituted entities on the basis of any underlying economic motive or outcome

- Also important is the Court.s acceptance of the separate legal identity of a company and the principle that ownership of shares does not imply direct ownership of the company.s assets or any other right such as voting rights or controlling interest that are inextricably linked to the share

- The controlling interest is an incident of ownership of shares and is therefore not an identifiable or a distinct capital asset for the purposes of the Act.

- The High Court has held that the Act has not restricted the obligation to deduct tax only to a resident but chargeability under the Act is mandated before the obligation to deduct arises.

- Once the territorial nexus is shown to exist, income tax can extend to the person. (The court held that the nexus can be based on the situation of the asset; or residence of the person; or business connection.)

- TDS provisions being machinery provisions are not independent of the charging provisions.

- Even though the tax laws of a country may not be enforceable in another country that does not imply that the

Courts of a country shall not enforce the law against the residents of another country within their own territories.

- The High court has clarified that subject to territorial or economic nexus with India, the provisions of section 195 of prevalent tax laws (relating to deduction of tax at source) would apply to transaction ns between two non residents.

- In essence, this ruling will provide the tax authorities a basis to investigate all offshore transactions which derive any value from underlying Indian assets.

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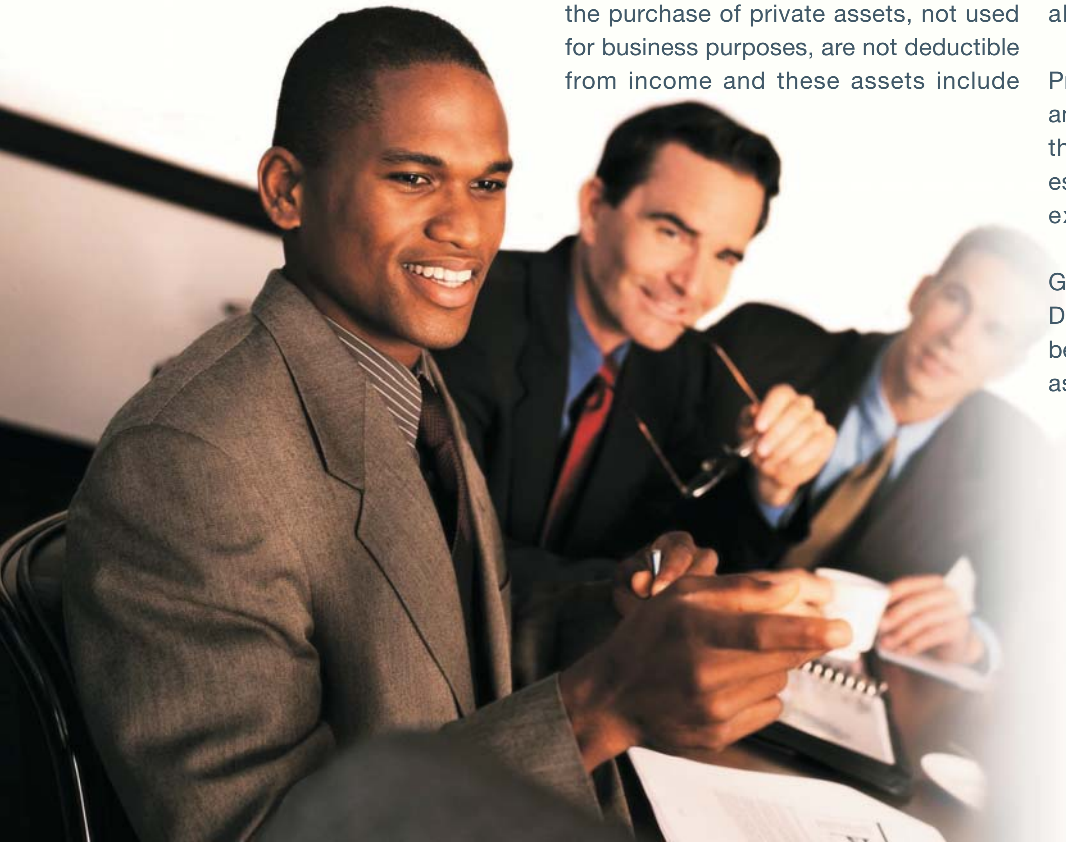
Allowable expenses provided by the Income Tax Law of Cyprus

The 2002 Cyprus Income Tax Law 118(I) lay down some principles which must be observed for the preparation of computation of chargeable income.

The main principle is that for an expense to be deductible from profits/income, it must have been incurred **wholly and exclusively** for the production of income. These are running expenses for carrying out the company's business.

Such expenses deducted from income/profit reduce the tax payable.

Having in mind the favourable nature of the Tax Law, international business companies and locally operated companies treat payment of interest as part of their expenditure.



Interest payable by a company is treated as expense in some circumstances. For example interest payable for the purchase of assets to be used by the company for its business purposes is clearly stipulated on section 9(1) of the Law as a deductible expense.

Recently the Tax Authorities in Cyprus circulated clarifications to all professionals to facilitate how companies treat interest.

Section 11 of the Law provides for certain restrictions on interests and expenses whether they can be deductible. Accordingly expenses that are not wholly and exclusively incurred for the production of income are classified as non-deductible.

Interest as well as all expenses concerning the purchase of private assets, not used for business purposes, are not deductible from income and these assets include investment in shares of public or private companies, land and buildings, leisure boats, works of art.

Irrespective of their use, interest paid for the acquisition of private motor vehicle is not a deductible expense. Such restriction is extended for seven years from the acquisition of the asset.

Interest derived from titles or other securities such as bonds and debentures do not fall under the restrictions of section 11(15) of the Law. However where interest derived from related company dealings is established the arm's-length principle is observed.

Interests relating to the acquisition of shares or other company assets are exempt from the restrictions of section 11 (15) and allowable for income tax purposes.

Provided that the timing between receipt and assignment of the loans is not more than six months, interest payments for established back to back loans are also exempt from the restriction clause.

Guidelines provided by the Inland Revenue Department intent to eliminate disputes between tax payers and authorities as well as aid better understanding of the law.

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Losses of a foreign permanent establishment in the tax computation of the head office

Under the double taxation treaties the fiscal results of foreign permanent establishments generally are due to taxation in the country where the permanent establishment is situated. One of the consequences is that losses of the permanent establishment normally can not be deducted from taxable income in the residence state of the head office.

The European Court of Justice has judged that the deduction of losses of a foreign permanent establishment may not be denied in the residence state of the head office if the deduction of the losses in the state of the permanent establishment definitely is not possible. However, in the decision of the European Court of Justice it was undecided under which conditions the loss of a permanent establishment is "definite".

For Germany this now was decided by the German Highest Tax Court.

The German court said that a loss is not definite when it is not deductible for legal reasons under the laws of the state where the permanent establishment is situated. In this case the loss can not be deducted in the residence state of the head office.

To be deductible in the residence state of the head office the loss of the foreign permanent establishment must be definite in fact, that means that the permanent establishment has in fact no future possibility to match the losses with future profits. This only is given if the permanent establishment has been liquidated or sold or liquidated by restructuring.

A second question is in which year a loss of a permanent establishment can be deducted in the tax computation of the head office: whether in the year when the loss has occurred or in the year when the facts arise that make the loss definite. The German Highest Tax Court decided that a loss of a permanent establishment is deductible in the state of the head office in that year when the loss has become definite (liquidation etc.). That means on the other hand that the loss is not deductible in the state of the head office in the year when the loss has occurred.

Probably also in other countries courts will have to decide these questions. It is interesting how they will be decided by other courts.

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The Use of Pensions and Life Assurance in Tax Planning

1. INTRODUCTION

In the UK's March 2010 Budget the then Labour government increased the maximum income tax rate to 50% for income over £150,000 with immediate effect and restricted the tax relief available for pension contributions to the basic rate of tax of 20% from April 2011. The new Coalition government announced their 'austerity budget' in August 2010 and did not seek to reverse either of these measures.

Last week, on 14 October 2010, HM Revenue & Customs ("HMRC") published a document entitled "Restricting pensions tax relief through existing allowances" ("the Document"). The Document imposes restrictive measures in respect of pensions by decreasing the annual contribution limit by 80% from £255,000 to £50,000 (from April 2011) and further restricting the life time contribution amount from £1.8m to £1.5m (from April 2012). There is a small consolation for the higher earners in that the government, in light of the Document, will reverse the restriction on tax relief for contributions to pensions. This means that for every £1 an individual contributes to their pension they will receive tax relief of £1.

In a time of supposed asceticism the taxpayer is discouraged from saving and with the new pension measures due to be implemented in around six months time - individuals will need to consider alternative arrangements. This article considers some of the options available to individuals considering leaving the UK (of which there are a growing number) and those who are staying put.

2. THE ALTERNATIVES

Under an approved UK pension scheme a tax free lump sum can be drawn upon the beneficiary reaching a certain age. However, the remainder must be used to buy an annuity. An annuity is usually issued by a life insurance company and is essentially income from capital investment in the form of regular payments over a fixed period subject to UK income tax. If the individual does not buy an annuity before death the pension fund is subject to UK pension charges and inheritance tax ("IHT") of up to 82%.

2.1. People who want to leave the UK

2.1.1 Qualifying Recognised Overseas Pension Scheme ("QROPS")

A QROPS is a non-UK pension scheme approved by HMRC. An individual may transfer (without a tax charge or penalty) his UK pension to an overseas scheme where it has QROPS status thus enabling a non-UK resident individual, or an individual leaving the UK, to benefit from the advantages of a non-UK pension arrangement.

Conditions:

To become a QROPS, the scheme must make an application to HMRC and meet a number of specific conditions including:

- be established in the European Economic Area; or
- be established in a jurisdiction with which the UK has a Double Tax Treaty ("DTT") that contains exchange of information and non-discrimination provisions; or
- satisfy the requirement that, at the time of the recognised transfer, the rules of the scheme provide that:
  - at least 70% of the funds transferred must be designated to provide the member with an income for life;
  - the pension benefits (and any associated lump sum) payable to the member under the scheme, to the extent that they relate to the transfer, are payable no earlier than the day on which the member reaches normal minimum pension age, unless member is in ill-health immediately before he became entitled to a pension under the scheme; and
  - membership of the scheme is open to persons resident in the jurisdiction in which it is established.

Benefits:

- No requirement to purchase an annuity or pay UK tax charge (of up to 82%) upon death;
- Ability to leave all unused pension funds to beneficiaries free of tax at source;
- Tax-free lump sum, even if the member has already taken 25% from the UK pension;
- Ability to take income from the pension in a more tax-efficient way depending on where he is resident;
- Ability to take income and benefits in any currency (mitigate currency fluctuations); and
- Protection against possible future creditors (dependent on QROPS jurisdiction).

Restrictions:

- Income or other benefits withdrawn from the QROPS within 5 years of becoming non-UK resident are reportable to HMRC and liable to UK tax;
- Will be subject to UK IHT upon death;
- If HMRC removes QROPS status, e.g. in the case of abusive practices transfers to the scheme may be subject to tax at up to 55%;
- If a transfer to a QROPS exceeds the maximum life time contribution amount (currently £1.8m decreasing to £1.5m in 2012) any excess will be charged at 55%;
- Potential tax under local law of country in which individual is resident.

2.1.2 Qualifying Non-UK Pension Schemes ("QNUPS")

A QNUPS attracts the same benefits as a QROPS. However, a QNUPS is not "approved" by HMRC. This means that a recognised UK pension scheme cannot be transferred to a QNUPS (unless the QNUPS is also a QROPs) without a tax charge of 55%. The key is often to transfer a QROPS to a QNUPS after an individual has been non-UK resident for 5 years. A QNUPS, unlike a QROPS, falls outside the pensioners estate for UK IHT purposes and may also avoid foreign succession laws so that the individual is free to choose exactly who inherits the pension fund and in what proportion.

Conditions:

A QNUPS must satisfy the same conditions as a QROPS except there is no DTT requirement if the scheme is established outside of the EEA. This is because there are no reporting requirements from the QNUPS to HMRC.

Benefits:

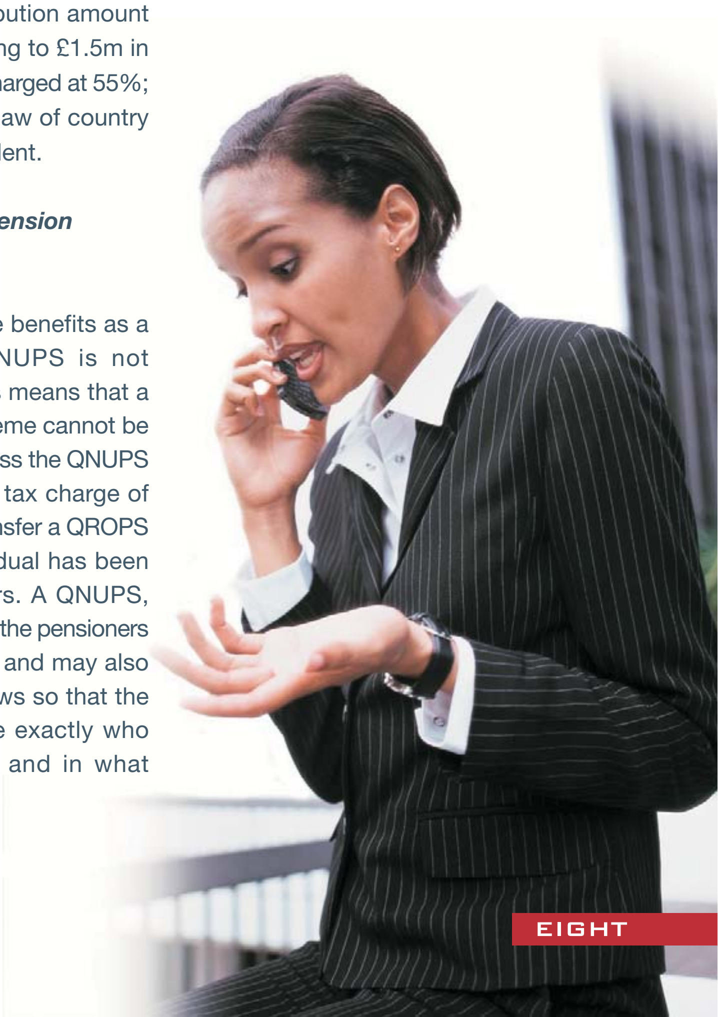
- Same as a QROPS above;
- Contributions can be made from any income not necessarily employment income;
- No maximum contribution limit;
- Can avoid both local wealth taxes during member's lifetime and UK IHT and local succession taxes on member's death; and
- No reporting requirements to HMRC.

Restrictions:

- Transfer from a UK recognised pension scheme will be taxable at 55%.

2.2. People who don't want to leave the UK

QROPS and QNUPS work well for those that know they will leave, or have already left, the UK. For individuals not in this



position other options will need to be considered that allow them to amass their wealth more quickly (i.e. tax deferral vehicles) and pass such wealth to the next generation tax efficiently.

2.2.1. Employee funded retirement benefit schemes ("EFRBS") and employee benefit trusts ("EBTs")

EFRBS and EBTs are essentially offshore trusts established by a UK resident company for the benefit of all or key employees. Both are unapproved for UK tax purposes so that immediate tax relief is generally unavailable in respect of contributions. However, being unapproved they can invest in a wide range of assets and there is great flexibility in terms of timing of benefit withdrawal and succession planning.

Benefits:

- Significant investment ability including shares in listed or unlisted companies, unit trusts, investment trusts, real estate and so on;
- No employers National Insurance Contributions (NIC) for the UK sponsor company;
- Employees NIC only payable when an individual takes a benefit from the EFRBS or EBT;
- Income and gains of the EFRBS or EBT are generally not taxable, rolling up gross for reinvestment;
- Does not form part of the beneficiaries estate for IHT purposes;
- A UK company can obtain a corporate tax deduction equivalent to the contribution it makes to an EFRBS although often only when taxable benefits are paid out from the EFRBS
- Commercial loans can be made to beneficiaries.

2.2.2. Life assurance

Life assurance is a form of insurance where the risk insured is the life of an individual (the life assured) who is generally the policyholder. On the occurrence of the insured event, i.e. the death of the assured, the policy matures and a sum of money becomes payable to the beneficiaries under the terms of the policy. An offshore life company will issue a contract to the policyholder - a UK resident individual - in return for a sum of money - the premium. The life policy will act as an investment vehicle and certain forms of life policy can invest in a wide range of assets including private company shares, unit trusts, real estate and less traditional investment assets such as yachts, fine art and even wine.

Personal Portfolio Bonds ("PPB")

A PPB allows the policyholder to choose the underlying investment which may include a wide range of assets.

Benefits

- Tax deferral on income and gains arising within the policy;
- Falls outside the policyholders estate for IHT when written in trust;
- Commercial loans can be made to the policyholder.

Restrictions:

A PPB is deemed to realise a notional gain (15% of the premium) each year subject to UK income tax. The key is to keep the premium low.

Non-PPBs

A non-PPB is a life policy where the policyholder has limited influence over the underlying investments. The policyholder will pay a premium which is not subject to the deemed gain charge and will provide a mandate to the investment manager of the types of investments he wishes the policy to make.

Benefits:

- Can draw down the capital paid into the non-PPB tax free;
- Allows income and gains to roll up tax free;
- Falls outside his estate for IHT purposes;
- Commercial loans can be made to the policyholder.

Restrictions:

- Policyholder has limited influence over investments.

The income and capital gains tax deferral achieved using life policies may become avoidance in the future if the policyholder becomes non-resident. If the policyholder remains UK resident he may surrender the policy at some point in the future when income tax rates our lower. Alternatively, the policy can be held such that the policyholder realises a capital gain taxable at 28% - this was more attractive when the rate was only 18%!

The use of life assurance is interesting as the tax deferral benefits described can be achieved in other jurisdictions.

3. CONCLUSION

All of the above described planning tools can be used for tax efficiencies and as alternative pension arrangements. The key in determining which is most suitable for a client will largely depend on their circumstances and, in addition, one must ensure there is commerciality to the arrangement.

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Monthly advance on the income tax

Beginning on January, 1, 2011 the "Personas Juridicas" (Companies) must pay a Monthly Advance on the Income Tax (MAIT) equivalent to 1% of the total taxable income of each month.

The definition of taxable income is the result of deducting income that is exempt and/or not taxable and the income from foreign sources from the contributor's total income. This monthly advance of the income tax will be paid on the sworn declaration within the first 15 calendar days following the previous month, per procedure to date which has not been clarified by the DGI or regulated by law.

"*Personas Naturales*" (individuals) and "*Personas Juridicas*" (companies) who as a result of their operations generate income from importing, distributing or trading 91 or 95 octane gasoline, I.P.G., diesel and jet fuel and are duly registered at the National Energy Secretariat, may deduct the amounts corresponding to the consumption of fuel and petroleum by-products, from the total taxable income.

Companies transporting fuel must pay the monthly advance of the income tax equivalent to 1% of the gross profit margin.

The "*Personas Juridicas*" (companies) involved in insurance and reinsurance activities may deduct the income derived from providing insurance and reinsurance products to other companies who are also involved in similar activities from the taxable income.

The general partnerships may deduct amounts distributed to their members from the total taxable income. In other words, general partnerships are exempt from paying the 1% tax because they can deduct the profits distributed to their members for their participation in these societies from their taxable income.

The law also contemplates special treatment for the "*Personas Juridicas*" (Companies) involved in the import and manufacture of nutrients or pharmaceuticals and medicines for human consumption, always and whenever the total product output is traded in the national marketplace, as stated in article 18 of the D.E. 91 of 2010, amended to article 26-A of D.E. 84 of 2005. These "Personas" may avail of the credit from paid ITBM's for services paid in advance or incurred solely for the acquisition of packing material for the manufacturing of nutrients or pharmaceuticals and medical products for human consumption, in the advance payment of 1% of the income TAX.

The "*personas naturales or juridicas*" involved in the farming or agroindustrial sector with a total yearly income in excess of B/. 250,000.00 must pay a monthly advance equivalent to 0.5% of their taxable income.

Adjustment payments between the sworn declaration of 2011 and the monthly advance on the Income Tax of 2011, if favourable to the Government, are made by March 31 of the following year at the latest. If however the company operates a special period, then payment must be made within the three months following the closing of this special period.

In the referred adjustment is in favour of the contributor, it will be booked as a fiscal credit which can be off set against the monthly returns on the income tax for the following years and if the favourable balance persists, said fiscal credit may be off set against the payment of another tax or returned to the contributor if there is no other tax payment to be made.

On the other hand, at the beginning of 2011 the obligation of the "*personas juridicas*" (companies) is to pay the advance of 1%; nevertheless, "*personas juridicas*" showing credits on their sworn tax declaration, may apply same to the monthly returns of 1%.

The monthly declarations of returns of 1% can be filed by way of a specially adapted computer system by the Panamanian Tax Authorities (Direcciòn General de Ingresos or DGI) or otherwise payment can be made through DGI officially appointed agents using the appropriate forms and in the corresponding time frame.

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Labour Reform in Spain: changes made to objective dismissal

The Spanish Official State Gazette (B.O.E. as per the Spanish acronym) dated 18/09/10 published Law number 35/10 of September 17 titled Urgent Measures concerning Reform of the Labour Market, or in other words the much talked of "Labour Reform".

The Law's Statement of Reasons declares that its essential objective is to "contribute to a reduction in the number of people unemployed and to increase the level of productivity of the Spanish economy" and consequently, states that the measures stipulated "are focused on achieving three fundamental objectives":

1."Reduce the dual nature of Spain's labour market, fostering the creation of stable, quality jobs in line with the requirements of a more balanced and sustainable growth model".

2."Strengthen instruments of internal flexibility in the development of labour relations and, in particular the measures concerning temporary reduction in working hours".

3."Increase job opportunities for the unemployed".

Therefore, the First Chapter of the Law titled *"Measures aimed at reducing dual nature and temporality of the labour market"*, includes, among other measures, provisions for limiting the term of duration for temporary employment contracts for specific works and services to a maximum period of three years, which can be extended for a further 12 months when this is provided for under applicable sectoral agreements, after which time the workers acquire full-time staff status within the company. The law raises compensation paid upon dismissal from 8 to 12 days salary for each year worked (even though this increase will be applied successively over several years). This measure, which is obviously aimed at discouraging employers from entering into temporary employment contracts, modifies the regulations that up until the adoption of Royal Decree-Law (RDL) 10/2010 of June 16, establish the regulatory framework covering objective dismissal. However, we cannot understand either how this relates to a reduction in the dual nature of the labour market or to encouraging stable job creation which the Law states as its fundamental objective.

The Law, which came into force on September 19 this year, introduces significant modifications to previous legislation regarding objective dismissal.

Here, we will try to summarize these changes in as brief a manner as possible.

In the first place, the law defines cases which represent a “negative economic situation” (as well as the technical, organisational and productive reasons) which may justify objective dismissal, namely, when the results of the company demonstrate “the existence of current or forecast losses” or otherwise demonstrate “the persistent fall in the company’s level of income”, in such a manner as “that this may affect the company’s viability or its capacity for maintaining the volume of employment”.

This modification to the previous regime is significant insofar as jurisprudence was practically unanimous in indicating that in order to justify dismissal on these grounds the employer must prove the existence of significant persistent and current losses, (i.e.) that these losses were incurred at least in the financial year prior to said dismissal and were ongoing and significant during the current financial year in which dismissal on these grounds was to take place. Moreover, the Courts regularly did not consider a reduction in the company’s income as sufficient reason.

So, when the legislator now refers to current losses, including reference to forecast losses, the Courts should no longer require additional evidence of proof of losses occurring in previous financial years be presented, that is to say, the so-called continuity of losses, even though, if this be the case, they should be presented in order to better justify the negative economic situation of the company.

This continuity is regarded in the Labour Reform as indicative of a decrease or reduction in the company’s income.

But for how long should those losses or reduced income be sustained, and to what extent, so that it is evident that those results or decrease in income “may affect the viability of the firm or its ability to maintain the volume of employment” as required by the Law?

In our opinion, if the losses are significant, but have only occurred during the financial year in which the dismissal occurs, they represent a significant decrease in equity, and are operating losses. The Judge must assess the justification for dismissal on economic grounds, and the same should happen with the loss of income, which at least should be ongoing and persistent, that is, to be continuous for six months. On the contrary, if the loss or decrease in income is slight, or the latter is not persistent, the Judge will consider that there is neither a risk to the viability of the company, nor its ability to maintain employment and therefore will rule that the objective dismissal is inappropriate, unfair or inadmissible.

Thus we face a reform which, in my opinion, is guilty of the same shortcomings as the previous law, its lack of clarity and consequently the broad scope for the discretion of the judge as to the existence or otherwise of the negative economic situation alleged by the employer, especially if we consider that the company must justify "the reasonable nature of the dismissal to preserve or aid the company's competitive position in the market."

In short, although the opportunity for the employer to allege a negative economic situation is extended and based on this claim, to proceed with an objective dismissal, the truth is that it will be necessary to observe caselaw and review case by case in order to comprehend how the Courts are interpreting the new regulations of the aforementioned form of dismissal.

In order to prove the alleged results, pursuant to previous case law, the best solution for an employer is to present the Auditor’s Report, together with the audit of previous years in the event that losses have occurred in these years, taking into account, as has happened on occasion, that a financial report signed by an auditor is preferable to an audit of the results of the current year not yet completed, since in the first case the Auditor will not be as constrained by the Law on Auditing in their responses during the trial.

More importantly however, in my view, regarding objective dismissal, is the new wording of the Law introduced by the Labour Reform for cases in which unfair dismissal should be recognized, given that prior to the reform, a dismissal was always declared null and-void when it did not meet the formal requirements (it was enough to have an error in the calculation of compensation which the Judge deemed "inexcusable" in order for the dismissal to be declared null and void) whereas now, the dismissal will be declared null and void, and if the error is "excusable" and the alleged causes to justify the dismissal are demonstrated, it will be declared admissible.

To sum up, in our view this reform is insufficient, because the courts, we fear, will probably continue regardless of the fact that the purpose of objective dismissal is not to terminate contracts when the company is insolvent (which may also be the case), but rather to prevent the company from becoming insolvent and that, as has been stated by the Supreme Court for several years, it is evident that the reduction of labour costs derived from suppressing jobs by way of objective dismissal always helps to alleviate the situation of the income statement, and in our opinion therefore, helps prevent the dreaded and unwanted corporate insolvency.

Finally, and as the former Minister, Mr. Caldera recently said in an interview, "What is preferable, that the company loses its chance of a future and must close or that the company makes staffing adjustments in a justified manner?”

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Annual accounts and the future fiscal framework in Andorra

Interview with Mr. Vladimir Fernández Armengol, Managing Partner of ALFACAPITAL ASSESSORS · AUDITORS

Good afternoon, Mr. Fernandez, firstly I would like to thank you for giving us the opportunity to have a talk with you about the main aspects of the relevant current economic, accounting and tax situation in recent months in Andorra.

We know that as a partner of the professional services firm Alpha Capital Advisors & Auditors you have a technical and independent standpoint concerning certain accounting, financial and tax issues which affect the current economic situation in Andorra.

In this regard, we would like to know your professional opinion on the fact that 1861 companies have submitted a request to deposit accounts in the middle of last August?

First of all we have to classify the data provided by the Government of Andorra into different groups differentiating between companies (legal persons) and entrepreneurs (natural persons), given that Law 30/2007 concerning business accounting procedures establishes that the obligation to deposit accounts lies with those entrepreneurs with a turnover in excess of €100,000 and, consequently, the obligation to deposit accounts and how many of the companies registered in the register are still active, identifiable and informed by their legal representatives of their obligation to deposit accounts. Once the data has been more clearly defined, we would then know the exact percentage that these 1,800 applications filed in the deposit accounts represent. Even so, a priori the numbers do not appear to be incorrect and it seems that there is some awareness of the situation on the part of the business community in Andorra.

From some quarters and the media there have been comments that these numbers seem very low considering that there are some 7,000 companies registered in the Companies Register and more than 2,600 self-employed, what is your opinion on this?

As I mentioned in my previous answer, I think we would have to analyse further the data, likewise we must consider the fact that there are many companies such as the ski resorts, hotels and professional service firms (as is the case of Alfa Capital), whose financial year-end is later than December 31. Therefore, these companies are not required to deposit their annual accounts until after 31 July and these entrepreneurs and/or companies begin depositing annual accounts with the Mercantile Registry during the following months of the second half. Furthermore, based on the information available and what is common knowledge, many entrepreneurs are filing their annual accounts after the deadline date (July 31), a fact that will increase the statistical data available last 15 August. Finally, we have to bear in mind all those entrepreneurs (natural persons), whose turnover does not exceed €100,000 and are not required to deposit accounts. In light of all these facts, I understand that the number of companies and entrepreneurs required to deposit accounts will be lower than the 7,000 companies and 2,600 self-employed workers registered, which is why I reiterate that in principle, an initial request by 1,800 companies to deposit accounts seems to be a fitting initial figure considering the fact that many companies will be depositing their accounts in the coming months and many more companies will almost definitely unsubscribe from the registry.

As an auditor, what is your opinion about the fact that even though companies are required to deposit their annual accounts, to date there are still many employers who have not fulfilled this obligation?

I am a firm believer in good management and corporate transparency; I think the accounting practices of many Andorran employers are properly organized and appropriate to their business. Even so, my opinion on the matter is that we are still lacking in experience in certain accounting issues, both in reference to technical compliance with the rules, and formal compliance. Andorran entrepreneurs are possibly still getting accustomed to the situation, but I hope that over time any doubts they may have will be cleared up.

In reference to the fact that there are still companies who have yet to deposit their accounts, I firmly believe that in the coming months they will do so, given that legislation for 2010 will bring in a penalty scheme which will mean that practically every company will be depositing their annual accounts. Moreover, bear in mind that depositing annual accounts for 2010 will imply furnishing comparative accounts with those of 2009. For this reason, I recommend companies to deposit their annual accounts at the earliest possible date. In addition, I would like to stress that if a company deposits annual accounts which register losses, I believe that this could be beneficial for future reporting periods (with a view to future Corporate Tax), given that the draft Bill published in October 2009 in the General Council Official Gazette, states that losses originating prior to the publication of the Corporate Tax Law, can be offset against profits obtained in subsequent financial years. Tax credit can be booked in this case, which is why it is even more interesting to have previously deposited accounts and have informed the tax authorities of any losses incurred during the 2009 financial year and when applicable, in previous financial years.

Well, this certainly appears to be quite a complex issue to comprehend, while appearing very interesting at the same time…, how can this be accounted for? And as we are touching on fiscal matters, how can the future corporate tax affect the fact of having presented previous annual accounts? For any companies or entrepreneurs who read this interview and in order to make it easier for our readers to understand, we would have to apply a 10% tax on year-end losses and this would be the amount of tax to be paid?

We should deal with this question is different parts. As the first temporary provision of the Corporate Tax draft Bill establishes, as soon as the aforementioned Law comes into force, if a company has experienced a negative accounting result (losses) pursuant to the definition established under Generally Accepted Accounting Principles, these losses can be offset against positive tax basis obtained in later reporting periods. This fact in Spain is referred to as generating tax credit and is booked as a right the company acquires with the tax authorities to deduct possible future profits. It is evident that if you lose 100€ one year and the next year you make a profit of 100€, you are not required to pay the Government anything because the previous year you lost Money. These losses can be booked as tax credits.

If the question is if depositing annual accounts with a future Corporate Tax can have an effect, well, I am sure that it can (I have explained an example here), although I am in complete agreement with the Andorran Government in the fact that we require certain statistical data in order to fully understand the macroeconomic data for our State. It is not possible that in 2010 we have so much conflicting data from varying sources regarding Andorran GDP and per capita income. This only causes confusion and can bring about an environment of instability.

To sum up and in reference to the question as to whether accounting results are the same thing as fiscal results, the answer is no. One thing are the results as determined by accounting practices and another thing are the fiscal results, which are used as a basis for calculating Corporate Tax. It is true that the figure for fiscal results is obtained by way of the accounting results, however there are certain entries or concepts on the books which have no influence on the fiscal situation but do influence the accounting situation, or visa versa, and these are referred to as timing or temporary differences and long-term or permanent differences. Allow me to give you an example. If I am given a fine for speeding or for having broken a law, in accounting terms a company books this as an expense, although at a fiscal level there is no doubt that the authorities would not allow you to book it as such thereby giving rise to a difference between accounting and taxation. Even so, we can only wait to see how future legislation on Corporate Tax will be passed and subsequently developed in regulations.

If the truth be known, it all seems very complex and highly technical to me. It looks like accounting will have an important role to play in calculating the future Corporate Tax. As such, what recommendations do you have for any members of the business community who read this article?

Above all, my message would be one of calm, I would suggest that they get their accounts in order as is necessary, telling them to seek out professionals capable of assisting them in this process of accounting reconciliation and that they understand accounting procedures as a tool for assisting them in the day-to-day management and running of their companies, rather than seeing it as a revenue collection agent for the State. Likewise, I would recommend them to invest in ongoing training for management level and employees in order to fully comprehend existing legislation and the benefits that its mechanisms can afford their companies.

In reference to training, we know that Alfa Capital provide ongoing training for companies in a broad range of accounting, financial and fiscal issues. Are you currently working on the design of training courses targeting companies to better prepare them for applying tax legislation?

Firstly, I would like to point out that the partners at Alfa Capital have spent the past 10 years providing training for the Andorran

corporate sector, in conjunction with Andorran Chamber of Commerce, Industry and Services and more recently in collaboration with the University of Andorra, we have trained numerous individuals and companies in areas such as basic and advanced accounting principles, balance sheet analysis, application of Andorran Generally Accepted Accounting Principles, how to prepare the annual accounts, or when applicable the practical application of indirect taxation, (ISI, IPI, IAC). We have organised numerous training courses that have been successful and which have been attended by many professionals and where we have always sought to highlight the Andorran aspect of the courses and their trainers, by way of applying practical case studies from the country itself and which have always been well received by those attending.

In a similar vein, last year we published a comprehensive summarised collection of all accounting laws and regulations in one single publication, an accountancy textbook titled, “Practical Handbook for Application of Andorran Generally Accepted Accounting Principles”, which is used as a practical reference book for the application of the GAAP and was distributed to every company in Andorra by the Andorran Chamber of Commerce, Industry and Services and the network of Crédito Andorrano branches.

We are currently working on the technical aspects of the draft Corporate Tax and VAT Law; however we cannot as yet begin training courses in this area until the laws in question have been passed. The draft Bills allow us to observe trends or technical impact but we will have to wait for the definitive text in order to prepare the upcoming training courses.

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Hidden Profit Distribution: Change of definition

Usually amendments and supplements to tax acts and regulations are stipulated annually with the aim to introduce certain policies, new rules taken from the EU legislation, to illustrate the undertaken engagements before European partners, including regarding penal procedures, the upgrading of the legislation structure and correction of any inaccuracies that have been located in the process of the real application of the Acts.

In this regard at the end of last year the Bulgarian Corporate Income Tax Act was enriched by several amendments one of which refers directly to the hidden profit distribution. The change itself is in the definition for hidden distribution of profit, and with the new interpretation it also includes amounts not connected to the business activities or such that surpass the usual market levels not only for expenses accrued, but also for amounts paid or distributed, regardless the form, to shareholders, partners or persons related to them. Until now the hidden profit distribution was an issue related only to the accrued expenses. As from this year this goes for all amounts accrued, paid or distributed in any form by the legal entity. The new definition is highly distinctive than the previous one and it covers all cases of distributions paid to the entity owner/s that have not been inserted in the profit and loss accounts but are directly reported in the owners' equity. Never the less, the distribution of dividends, when performed according to the requirements of the Law, does not fall under the category of hidden profit distribution.

Other cases of hidden profit distribution as stipulated in the Corporate Income Act and in force as of January 2010 are:

- accrued expenses for interests (with the exception of the cases when the credit terms are not agreed upon as per the requirements set forth in the Act) when three of the following cases are identified:

  a) When the credit exceeds the own capital of the income payer as at 31 December of the previous year;

  b) When the redemption of the credit or its interests is not limited to a fixed period;

  c) When the redemption of the credit or of its interests or when the amount of the interest depends on the availability or on the amount of the profits of the income payer;

  d) When the redemption of the credit depends on meeting the requirements of other creditors or on the payment of dividends.

The purpose of the expanded definition is to provoke the attention that in the cases of such hidden profit distribution is identified and proved that the fiscal consequences are extremely severe and heavy as amounts, such as:

- the expense is not recognized (if such is reported) but at the same time income qualified as hidden profit distribution is recognized and the company that received it is taxed respectively
- a 5% tax is imposed on dividends in the case of distributions to EU/EEA persons

when such distribution is identified as hidden profit distribution.

- the administrative penalty measure is a property sanction, decreased from 50% to 20% of the relevant reported expense that represents hidden profit distribution.

In 2009 Bulgaria adopted an unconditional relief for distributed dividends from local subsidiary companies to parent companies in EU/ EEA. Up to now the hidden profit distribution was treated as dividend and thus was covered by this relief. As from 2010 each profit distribution to a parent company, local entity of an EU/EEA country or to other related persons from these countries, that according to the Bulgarian tax legislation is qualified as hidden profit distribution, is taxable with a 5% tax at the source. A very limited number of DTT's will provide the tax relief.

With regards to the aforesaid, there are still grey areas that are yet to be clarified , among which the issues if the granting of a free of interest credit or an unlimited credit to the owner of the capital or if a granted prepayment that is not reported for say some years, could these be treated as a hidden profit distribution after the abovementioned amendments as of January 1st 2010. We have yet to expect more amendments on this field.

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Government incentives support in Turkey

In June 2009, the Turkish government announced an incentive plan to encourage investment in Turkey. This incentive plan contains topics including tax, strategic consulting, education, training and full granted funds for domestic and foreign investors. The main objectives of the governmental incentives programs are to bring saving capital into the economy, encourage the use of technological innovations, create employment opportunities, and, to minimize the current economic imbalance between the regions in Turkey. However, more important is to create an more competitive market structure.

The plan sets out certain incentives which apply to "large-scale" investments in certain sectors, and some others which are only applicable on a regional/sector-specific basis. Moreover, free trade zones (FTZs) have been designed to encourage trade to and from Turkey. The FTZs mainly function for taxation and customs duty purposes. For example, companies do not have to pay corporate income tax nor do they have to pay income tax on employees' salaries, VAT or customs duties.

For some of the regulations on incentive programs established in 2009 an Investment Incentives Certificate shall be obtained by the investor from the Ministry of Commerce and Trade to be able to benefit from the incentives. Incentives should not be confused with cash grants to companies, but are rather given in the form of tax discounts and exemptions. The number of incentives a company can make use of depends on the region it is established in and branch of operations. Turkey has been divided in to four incentive regions. Each region has its own regulation regarding the height of the incentives, however, they all give incentives in the field of: Tax discounts, Social Security Premium discounts, Site Selection, Interest support, Value Added Tax support, and Customs Tax support.

Besides the abovementioned incentive regulation, the State started offering Research & Development ("R&D") incentives to encourage innovation and competition since 2008. R&D support comes in various ways, through all stages of the business process - from idea development to final sales. The only requirement to make use of R&D incentives is that the company possesses a R&D department. Some of the support mechanisms are tax discounts, Social Security Premium discounts, Personal Income Tax reduction, and, Grants for entrepreneurs in technological areas.

The Turkey's government has successfully passed through a number of regulations in recent years, contributing to its boosting economy, increase in foreign investment and the country's credibility. Despite of the recent economic crises, Turkey has shown strong economic stand. Also for the coming years, new incentives plans will be introduced and are warmly welcomed by domestic and foreign investors.

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