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Private Wealth Newsletter 2023

First Edition

TAX FROM EVERY ANGLE

Editors' note

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We are pleased to share with our clients, friends, colleagues, and readers across the world our first edition in 2023 of the Private Wealth Newsletter, a publication of Baker McKenzie's Global Wealth Management Practice Group. Our Private Wealth lawyers have always covered "Tax from Every Angle", and this issue is no different with contributions from colleagues spanning the globe.

Our feature article by Marnin Michaels (Head of our Tax Practice in EMEA) challenges conventional wisdom and looks at whether we really should engage in estate planning for assets that we hope will appreciate using a variety of recent examples when that might not have been the case. The coming year shapes up to follow the recent past with frequent and often significant changes to domestic tax laws, with new laws and proposals in the United States (at the State level), Spain, and Germany (to name a few). Our articles cover these topics and more.

We also see the OECD continues its push at the global level with Pillar Two, while the United States finally takes a step towards its peer countries with the entry into force of the Corporate Transparency Act only for uncertainty to strike the European Union's beneficial ownership registers. Keeping abreast of it all has never been more important, and our "In case you missed it" and "Around the world" sections are great places to start.

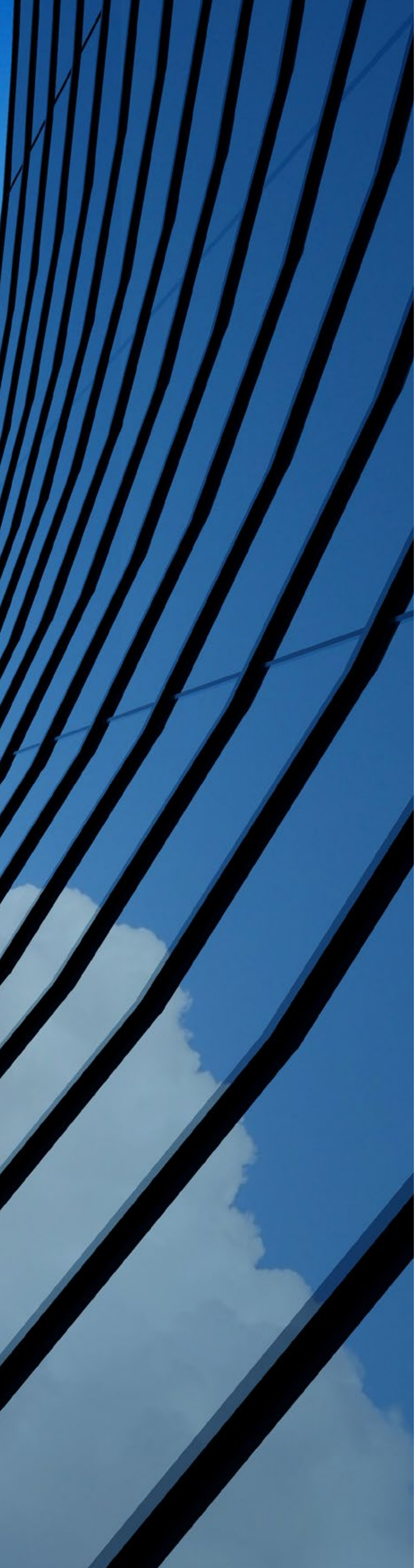
Our editors Elliott Murray and Phyllis Townsend, or any of the authors listed throughout the newsletter, can be contacted with any feedback or questions.

Content

Article

Should We Engage in Estate Planning for Assets we HOPE will Appreciate?

A fundamental estate planning principle frequently discussed when I was a student studying for my LL.M in the Estate Planning program at the University of Miami, and which remains a teaching point to this day, is that it is better to gift assets before they further appreciate in value. I recall professors sharing examples of estate planning benefits that would have resulted if one had gifted certain stock before an IPO or before specific assets had significantly appreciated in value.



The common assumption has been that gifting assets that one anticipates will appreciate in value in the future is a good thing, because it results in a gift tax saving and removes them from the donor's estate. The reasoning for this argument is that the gift freezes the value of the assets (as to the donor) for transfer tax purposes. Thus, if the assets appreciate in value after the gift, the donor or donor's estate will not owe additional transfer taxes on any future appreciation.

As the global markets emerge from the COVID-19 era with some asset values trending lower, coupled with the US federal gift, estate and generation skipping transfer (GST) tax basic exclusion amount set to return to its 2017 level at the end of 2025,[1] many estate planners believe now is the perfect time to transfer to younger generations assets anticipated to appreciate in value. For most of my professional career, I have worked and advised clients along this premise; however, I am beginning to realize that perhaps this common perception is not always correct.

In this short article, I will explore the potential flaws in this line of reasoning. I acknowledge that some readers will find this article somewhat controversial and counterintuitive. And further, in more instances than not, I will continue to advise clients to consider the future appreciation of their assets while planning their estates. However, the point here is to illustrate that anticipated appreciation of asset values does not always occur and, actually, values can decline (and even become worthless) and result in negative economic consequences for the donor (and sometimes the donee).

At the outset of the planning process, I believe practitioners should consider the following points when evaluating whether a client should gift an asset that they believe or hope will appreciate in value:

1. Is the client certain the value of the asset will not decline?
2. Is it possible that the value of the asset could decline significantly or even become worthless after the transfer?

1 In 2017, the basic exclusion amount for US gift and estate tax and GST was USD 5 million (before indexed for inflation). This amount doubled in 2018 to USD 10 million, and increased to USD 11.18 million after indexed for inflation. In 2023, as indexed for inflation, the basic exclusion amount is USD 12.92 million. The USD 10 million basic exclusion amount sunsets on 31 December 2025 and returns to USD 5 million indexed for inflation unless extended or made permanent by Congress.

3. Is the client prepaying a tax now to gift an asset whose current value may be overstated compared to its future value?
4. Are there potential civil law issues that can be triggered by donations during the lifetime that subject the donor to challenges that might not otherwise exist?

Asset values do not always appreciate

Many people who have invested successfully in the last 40 years are biased by the fact that asset values, even with economic corrections, have, for the most part, only moved in one direction: up. However, a closer look at the system in some detail reveals that certain assets have not only declined in value but lost all their value. Additionally, certain external factors beyond the donor's control can cause an asset value to decline or even become worthless. Consider the following real-life scenarios:

Example 1: In 2006, believing that her Bernie Madoff investment account would only continue to increase in value, Ms. F, a UK resident, transferred it to a family foundation, which triggered a UK donation tax. Less than three years later, however, Madoff's Ponzi scheme was discovered, and the investment account is now worthless in the hands of the family foundation. This example illustrates that acting in haste to gift what one believes is a rapidly appreciating asset can result in negative tax consequences if the anticipated growth does not occur or, as was the case with Madoff investment accounts, the asset was essentially worthless before the transfer.

Example 2: In a divorce settlement, H1 and H2 agree to divide the marital assets equally. H1 agrees to take the portfolio assets (all marketable securities) and H2 agrees to take the cold storage wallets containing crypto tokens. One year after the divorce decree is entered, H2's cryptocurrency is now worthless, and H1's portfolio asset values are down 22%.

Example 3: Ms. Jones donated her entire interest in Luna tokens to her favorite charity on 25 February 2022, for which she is then able to claim a charitable deduction for the value of the tokens on the date of the transfer. A few months later, the value of Luna collapsed, and the digital tokens are basically worthless to the charity. The result is a windfall to the donor in the form of a charitable deduction, whereas, unless the charity immediately liquidated the tokens, the charity has lost all the value of its gift. Furthermore, what is the result if the Luna tokens were donated to the charity in exchange for the donor's naming rights to a building? Could the charity rescind its agreement to name the building in honor of the donor if it did not liquidate the tokens before their collapse and lost all value of the donation? Therefore, these value fluctuations also can result in negative economic consequences to the donee.

Examples 2 and 3 collectively illustrate the negative impact that volatile assets, such as cryptocurrency, can have on both donors and donees, as well as domestic matters. These examples also illustrate the negative economic consequences that can result from gifting such assets. Thus, the question becomes, when working with and planning for families (and perhaps when representing a charity), are we working from a flawed analysis with respect to valuation? Is there a flaw in our thinking influencing our decisions? Ultimately, too many mistakes and personal relationships have been based on this assumption. It is especially important to discuss with the client the planning risks associated with volatile assets, and make sure they understand that if the assets decline in value after the transfer, they may not be able to recover the taxes paid on the transfer or restore any exemption used on the transfer. One planning objective should be to ask the client to consider the impact of valuation on a prospective basis.

Assets can and often do decline in value

There seems to be a misconception that assets tend to generally go up in value. However, that is not always true. Even the most stable of assets, such as real estate, have a history of declining in value. For instance, real estate tends to depreciate in value when the general area is no longer viewed as attractive, when the property requires significant improvements, when environmental damage occurs or, as we recently witnessed, from the economic impact of a global pandemic.

Example 4: Ms. Y believes real estate in New York City will always appreciate in value, and she heavily invested in midtown Manhattan for the better part of the last 10 years. In 2020, the COVID-19 pandemic hit, and property values and occupancy rates have never fully recovered even as we enter 2023.

Example 5: In 2015, Mr. Smith began investing heavily in the UK real estate market in prime locations in downtown London. Although the market values of his properties declined as a result of the pandemic, many have since returned to their pre-COVID-19 market value. However, the depreciation of the British pound that has resulted from COVID-19 and Brexit, coupled with recent inflation, has created a situation where there is actually a net negative value when compared to the purchase price.

Various economic factors influence pricing. Thus, even where an asset's fair market value increases, its purchase value can decrease.

It is not always beneficial to prepay tax

Particularly in places like the US, where recently there has been large gift, estate and GST exclusions, and gift taxes are tax-exclusive but estate taxes are tax-inclusive, there seems to be a mindset that paying a tax early is always beneficial. The reasoning is that the donor avoids paying transfer tax on the growth, and it is no longer a part of the donor's estate for estate and GST tax purposes. Although that is true, what if a donor makes a gift, pays the gift tax, but the asset actually declines in value or becomes worthless shortly after the gift is made? The problem then is that there is no corresponding credit system to make the donor whole for transfer taxes paid, or the wasted exemption that cannot be recovered.

Example 6: Believing that her investment in FTX would only continue to increase in value, Ms. C gifted her entire investment in FTX to her children in December 2021 when the market value was USD 50 million. As a result of the transfer, she used up her entire USD 12.06 million basic exclusion and paid over USD 15 million in gift taxes. In November 2022, and after Ms. C paid the gift taxes, FTX collapsed and the children's investment in FTX is now worthless.

This example illustrates that the valuation for a gift is based on the asset's fair market value on the date of the transfer. If the asset's value declines or becomes worthless post-transfer, the donor cannot seek a refund of the gift taxes paid or have any basic exclusion amount restored. In essence, the donor wastes both the money used to pay the tax and the equivalent monetary value of the exemption that could have been utilized for other assets. In contrast, in the estate tax context, however, there is an opportunity to revalue assets six months after death if the assets have decreased in value. Thus, in Example 6, if Ms. C had held onto the FTX stock until it imploded or if it had imploded within six months after her death, then her estate potentially would have an additional USD 27 million in assets.

Example 7: A Swiss tax resident gifts his Tesla shares in November 2021 to his cousins, because he has no other relatives. The cousins, thrilled to have the Tesla shares, are happy to pay the inheritance tax at the third-party rate. Unfortunately, the value of the Tesla shares declined so much that, by the time the taxes are due, the cousins have no choice but to sell the shares to realize the cash to pay the inheritance tax. Certainly, this was not the intended result.

There are nontax reasons where gifting can be important. Tax lawyers love to talk about taxes and money, and families like to think about who gets what and when in the most expeditious way possible. If someone gifts assets to address succession issues or forced heirship issues and those assets significantly change in value from the time the agreement was signed until the donor's death, one runs the risk that someone attempts to reopen the issue. This happens not only in the context of inheritance, but also in the context of divorces and other similar situations. Thus, clients sometimes do not give as much thought as they should to the consequences of a gifting transaction.

Conclusion

As I noted earlier, I recognize that many readers may view this article as controversial and counterintuitive. Yet, in these changing times following market bubbles, Ponzi schemes, crypto implosions and a pandemic, the point here is that practitioners should be mindful that asset values can and do decline, or even become worthless, post-transfer. Thus, when advising estate planning clients to follow the norm of gifting away assets anticipated to appreciate in value, it is also important to counsel them of the potential negative economic consequences that can result if the asset value declines or implodes after the gift is complete. There is no way of going backward to make them whole.

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Article

Substantial Increase in German Inheritance and Gift Tax on Real estate

If you own one or more real estate properties in Germany and plan to bequeath or gift them, you should start planning early. This is because tax and succession laws in Germany can be complex, especially in the case of larger assets that are difficult to divide up.

Moreover, if the tax-free inheritance/donation exemption amount1 is exceeded, significant tax liabilities are quickly incurred. A new law has greatly exacerbated this situation.

The Annual Tax Act 2022, adopted on December 16, 2022, includes notable changes to the German Valuation Act (hereafter, the "Valuation Act"). These changes could lead to an increase in German inheritance tax and gift tax for German real estate assets of 20, 30 or even 50 percent.

While the German Inheritance Tax and Gift Tax Act has not been modified, the amendments to the Valuation Tax will have a direct and tangible impact on the valuation of German real estate in the context of an inheritance or gift. More specifically, the changes to the Valuation Tax will affect German real estate valued using the *real value method ("Sachwertverfahren")* and the *capitalized earnings method ("Ertragswertverfahren")* (e.g., single family homes and rental properties), bringing their valuation closer to fair market values. These changes apply to transfers taking place after December 31, 2022.

In conclusion, the testamentary transfer of German real estate can still benefit from significant exemptions (e.g., exemptions for transfers of family homes or shares of housing companies). However, in many other cases the changes introduced by the Valuation Act will radically alter the tax cost associated with the gift or bequest of German real estate. This will be of concern to German tax residents, as well as non-German residents holding real estate in Germany.[2] Due to the rising land values in many regions, it can already be expected that the real estate values determined on the basis of the Valuation Act will increase significantly.

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1 Children 400'000 Euro /Grandchildren 200'000 Euro - these are quickly utilized, particularly in the case of real estate.

2 As a general rule, inheritance tax treaties that Germany has entered into will reserve to Germany the taxing right over German real estate owned by a non-resident decedent.

Article

States Focus on Taxing High Net Worth Individuals

Lawmakers in eight states are trying to coordinate tax increases on high-net-worth taxpayers in their respective states.

The campaign is called Fund our Future, and it involves legislators from California, Connecticut, Hawaii, Illinois, Maryland, Minnesota, New York and Washington. These states have a large proportion of the country's wealthy individuals. California, New York and Illinois are regularly among the top five US states in terms of estate tax returns filed, which are required for estates in excess of the filing threshold (USD 12.92 million for 2023).

The participants are organizing across state lines hoping that more coordination will make it more difficult for wealthy taxpayers to avoid tax increases by moving out of state. The campaign underscores the increased political and fiscal pressure on states to increase taxes, plug budget shortfalls and ensure that taxpayers are perceived to be paying their "fair share."

Individuals can change their tax status by changing where they live and from where they work. This flexibility has spurred economic activity in many communities. However, the ability to leave behind a high-tax state creates a shortfall in that state's budget that many states are trying to fill. This shortfall has been exacerbated by the pandemic-fueled rise in remote working. Based on the United States Post Office's change-of-address data, the top six states people are leaving are: California, New York, Illinois, Pennsylvania, Massachusetts and Washington.
The top six states people are moving to are: Texas, Florida, South Carolina, North Carolina, Georgia and Tennessee. While warm weather could tell part of the story, increased taxes also appear to be a correlative factor.

New York, which already boasts a high personal income tax rate, recently proposed three bills that would significantly increase its tax base. Senate Bill 2059 would increase tax rates on individuals, with the state's top tax rate moving from 10.9% to an astounding 24% on income of more than USD 20 million. Combined with New York City's tax rate of 3.876% and the federal rate of 37%, the total of the taxes due approaches 65%. Moreover, the lack of a meaningful state and local tax deduction (i.e., the USD 10,000 SALT deduction cap) for federal purposes makes this tax burden even more onerous. In addition to Senate Bill 2059, the New York legislature proposed Senate Bill 2162, which would impose a capital gains tax of up to 15% for top earners. Moreover, the legislature also proposed Senate Bill 2402, which would reinstate the stock transfer tax by reducing the 100% rebate on stock transfers to a 60% rebate (e.g., on stocks selling for USD 20 or more per share, the tax would be 2 cents per share).

A proposal in California would tax individuals based on up to 1.5% of their worldwide net worth. This wealth tax would continue to apply at a reduced rate for a period after the individual leaves California to mitigate the revenue loss associated with migrating individuals. This proposal certainly comes with significant constitutional concerns. Moreover, net worth taxes often come with significant complexities, including how to determine the net worth of an individual.

Proposals for wealth taxes and mark-to-market taxes are not unheard of in the US. These measures have generally had little political momentum, but the fact that these proposals are arising in several states and with a coordinated effort, means that individual taxpayers should consider legislative action as a realistic possibility. However, four of the states participating in Fund our Future are in the top six states that people are leaving. It comes as no coincidence that three of the top six states that people are moving to have no personal income tax. Given some of the aggressive tax proposals in New York, California and other the other states, it would come as no surprise that wealthy individuals may consider other states to live. The million-dollar question is whether the threat of wealthy taxpayers leaving will be enough to curb these onerous tax proposals.

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Article

New Options to Acquire Spanish Citizenship and to Attract Nonresident Individuals to Spain

The new regulations recently approved in Spain regarding the acquisition of Spanish citizenship and the impatriate tax regime applicable for individuals, offer new possibilities to those who meet the requirements and wish to move to Spain.

New term for acquiring Spanish nationality by option for descendants of exiles

Through the recently approved Democratic Memory Law, Spain has opened a new two-year period (in force until 20 October 2024) during which the descendants of exiles will be able to acquire Spanish nationality by option, without the need to prove a previous period of residence in Spain. This measure will benefit those born outside of Spain with parents or grandparents exiled for political, ideological or belief reasons or sexual orientation and identity.

On the other hand, it is also provisioned that Spanish nationality will can be acquired by children born abroad to Spanish women who lost their nationality by marrying foreign nationals before the entry into force of the Spanish Constitution of 1978, as well as children and daughters of legal age of those Spaniards whose nationality of origin was recognized by virtue of the right of option in accordance with the provisions of the Democratic Memory Law or in the seventh additional provision of Law 52/2007, of 26 December, which recognizes and expands the rights and establishes measures in favor of those who suffered persecution or violence during the civil war and the dictatorship.

Thus, the new regulation is applicable to the following:

- Those born outside of Spain whose parents or grandparents had originally been Spanish.
- Those born outside of Spain to parents or grandparents who had originally been Spanish and who, as a consequence of having suffered exile for political or ideological reasons or belief or sexual orientation and identity, have lost or renounced their Spanish nationality.
- Those born outside of Spain to Spanish women who lost their Spanish nationality by marrying a foreign citizen before the entry into force of the Spanish Constitution of 1978.
- Children who were of legal age when their father or mother acquired Spanish nationality by virtue of Law 52/2007 on Historical Memory.
- Children of a father or mother originally Spanish and born in Spain, who opted for Spanish nationality not of origin.
- Minor children of those who acquired Spanish nationality by application of Law 52/2007, who opted, in turn, for Spanish nationality not of origin.

It should be noted that the acquisition of Spanish nationality by option provided for in the Democratic Memory Law will not require the renunciation of the previous nationality.

Residence permits for investors as a way to acquire Spanish nationality

Those who do not meet the requirements established in the Democratic Memory Law for the acquisition of Spanish nationality or who do not wish to follow this path, will have the possibility of applying for Spanish nationality by residence. To that end, among other requirements, they must reside in Spain for a minimum period established according to their nationality or personal situation, so that it is necessary to analyze each specific case to determine the period of legal residence necessary to be able to opt for Spanish nationality.

One of the main ways to obtain legal residence in Spain with a view to subsequently acquiring Spanish nationality is the investor residence authorization (popularly known as "Golden Visa"), which is accessed by making an investment in Spain in any of the cases provided for by the regulations:

a) An initial investment for a value equal to or greater than the following:

- EUR 2 million in Spanish public debt securities
- EUR 1 million in shares or participations in Spanish capital companies with a real business activity

- EUR 1 million in investment funds incorporated in Spain and managed by a management company incorporated in Spain
- EUR 1 million in bank deposits in Spanish financial institutions

b) The acquisition of real estate in Spain with an investment for a value equal to or greater than EUR 500,000 for each applicant.

c) A business project that will be developed in Spain and will be considered and accredited as of general interest, for which compliance with at least one of the following conditions will be assessed:

- Creating jobs
- Carrying out an investment with a significant socioeconomic impact in the geographical area in which the activity is to be carried out
- Making relevant contribution to scientific and/or technological innovation

Once the period of residence required according to nationality or personal situation has elapsed, the process for the acquisition of Spanish nationality by residence can be started based on this investor residence authorization.

It should be noted that investor residence authorizations are granted for a period of three years and allow the holder and their dependent immediate family members to reside and work in Spain without any type of limitation. In addition, holders of this type of authorization will be able to move freely through the Schengen area (an area that includes most of the EU countries and other countries such as Switzerland and Liechtenstein) as visitors.

On the other hand, from a tax perspective, those moving to Spain either as foreign nationals or as Spanish citizens may benefit from the special tax regime applicable to individuals, which has the aim of attracting talent to Spain.

New aspects of the impatriate tax regime

The tax regime for impatriates is a special tax regime that enables foreign nationals who move to the Spanish territory to pay income and wealth tax as if they were nonresidents during the first six years.

This regime allows individuals who reside abroad that want to come to work in Spain to pay a flat fee for salary income of 24% up to EUR 600,000 instead of a progressive tax. However, it will be increased to 47% on the amounts received as salary income in excess of EUR 600,000. On other types of income (including savings income and capital gains), impatriates will be subject to tax in Spain only on Spanish sourced income at the applicable savings income rates up to 28% on the amounts exceeding EUR 300,000. Impatriates will remain subject to Wealth Tax only on Spanish located assets (i.e., Wealth Tax will not be paid on non-Spanish assets).

As of 1 January 2023, the requirements to benefit from the special tax regime for impatriate employees, popularly known as the "Beckham Law," has become easier in the following ways:

- The period of nonresidence prior to moving to Spain to be eligible for this regime is reduced to **five fiscal years** (previously it was 10).
- The law has established a longer lists of reasons that allow the impatriate to qualify for the special regime:
  - Working remotely from Spain through computer, telematic or telecommunication means or systems (**digital nomads**), with no need for the employer to issue a travel order or transfer. This circumstance is understood to be fulfilled in the case of teleworkers with an **international telework visa**.
  - Performing business activities classified as **entrepreneurial activities**.
  - **Highly qualified professionals** who provide services in Spain to startups or who carry out training, research, development and innovation activities, for which they receive a remuneration that represents more than 40% of their total income.

    Regarding the latter two activities, the restriction arising from the fact that the impatriate cannot obtain income that would be deemed as revenue obtained through a permanent establishment located in Spanish territory will not be applicable.

  However, any income obtained from such economic activities will be subject to taxation in Spain, irrespective of its source (worldwide income taxation), which was already the case.

  - Becoming **a director of a Spanish company, regardless of the direct or indirect stake they hold therein.**
  - **Becoming a director of a holding company**, according to the terms of the Corporate Income Tax Act, **if the direct or indirect stake in such holding is less than 25%.**

- The benefits of the regime are now applicable to the impatriate's **descendants** under 25 years old (or descendants of any age if they are disabled) and to the impatriate's **spouse** (or the parent of the descendants, if the partners are not married), if they meet the following requirements:
  - They have **moved to Spanish territory**, either with the impatriate or within the first fiscal year in which the impatriate applies this special regime, provided that they acquire tax residence in Spain as a result of the move.
  - They have not been residents in Spain **during the last five fiscal years**.
  - They do not obtain income through a **permanent establishment in Spain**.
  - The **sum of the net taxable income** for the impatriate's descendants or partners in each fiscal year is **less than the impatriate's**.

To conclude, the current regulation on Spanish citizenship acquisition and the special tax regime for impatriates, offers interesting new possibilities for those who may qualify. Effective pre-immigration advice and tax planning is crucial to determine the option most suitable for each case.

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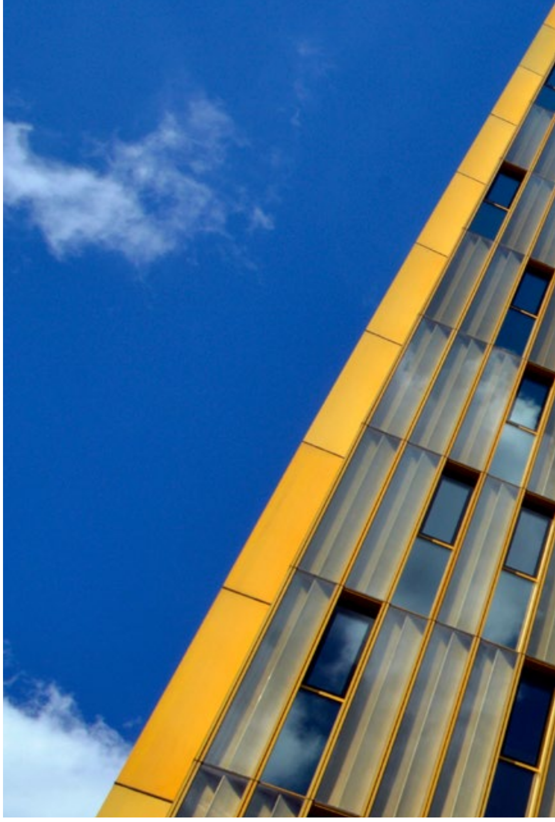

Article

CJEU reveals breaches of fundamental rights inherent in two major EU directives

The Court of Justice of the European Union (CJEU) has historically seemed reluctant to engage in a substantive review of EU secondary law. Recently, however, the CJEU seems to be closely considering the provisions of EU directives that are not in line with the right to privacy.[1]

Echoing this trend, the CJEU recently considered certain provisions of two important EU directives that it found to be incompatible with the general principles of EU law, i.e., with Article 7 of the Charter of Fundamental Rights of the European Union **("EU Charter")** guaranteeing the right to respect of private life.

The CJEU, sitting as the Grand Chamber, rendered two landmark decisions in which it held the following:

- The provision that information on the beneficial ownership of companies incorporated within the territory of the EU member states is accessible in all cases to any member of the general public is in breach of the fundamental rights guaranteed by the EU Charter (CJEU, Joined Cases C 37/20 and C 601/20, 22 November 2022).[2]
- The obligation imposed on a lawyer acting as an intermediary under the EU DAC6 Directive[3] to notify another intermediary is in breach of the fundamental rights guaranteed by the Charter (CJEU, Case C-694/20, 8 December 2022).[4]

1 The public access feature of the Ultimate Beneficial Owner (UBO) register of the Fifth AML Directive is invalid

The Luxembourg law of 13 January 2019 establishing the register of beneficial owners (RBO) **("RBO Law")** and implementing the EU anti-money laundering directives provides that a whole series of information on the beneficial owners of registered entities must be entered and retained in that register. Some of that information is accessible to the public, in particular through the internet.

The RBO Law provides that a beneficial owner may request the Luxembourg Business Registers (LBR), the administrator of the RBO, to restrict upon request access to all or part of the information

1 See for instance CJEU, Judgment of the Court (Grand Chamber), 8 April 2014, Digital Rights Ireland and Seitlinger and Others (C-293/12 and C-594/12, EU:C:2014:238).

2 CJEU, Judgment of the Court (Grand Chamber), 22 November 2022, Joined Cases C 37/20 and C 601/20, WM (C 37/20) and Sovim SA (C 601/20) v. Luxembourg Business Registers, EU:C:2022:912.

3 Directive (EU) 2018/822 dated 25 May 2018 amending Directive 2011/16/ EU as regards mandatory automatic exchange of information in the field of taxation in relation to reportable cross-border arrangements ("EU DAC6 Directive" or "DAC6 Directive").

4 CJEU, Judgment of the Court (Grand Chamber), 8 December 2022, C 694/20, Orde van Vlaamse Balies and Belgian Association of Tax Lawyers v. Vlaamse Regering.

on the beneficial owner on a case-by-case basis if the access to such information would expose the beneficial owner to disproportionate risk, risk of fraud, kidnapping, blackmail, extortion, harassment, violence or intimidation, or where the beneficial owner is a minor or otherwise legally incapable.

The beneficial owner of a Luxembourg company requested that the public's access to the information be limited based on that exemption. The request was rejected. The Luxembourg District Court in charge of the case decided to refer to the CJEU for a preliminary ruling. The main issue here was determining whether Article 30 paragraph 5 c) of Directive (EU) 2018/843 of 30 May 2018, amending Directive (EU) 2015/849 on the prevention of the use of the financial system for the purposes of money laundering or terrorist financing, and amending Directives 2009/138/EC and 2013/36 EU **("Fifth AML Directive")**, which provides for public access to information on beneficial owners, is valid in light of Articles 7 and 8 of the EU Charter (which refer respectively to respect for private life and the protection of personal data).

1.1 Decision in relation to the public access feature of the UBO register

1 The CJEU held that the "public access" feature of the RBO Law constitutes interference with the rights guaranteed by the EU Charter; more specifically, it constitutes serious interference with the fundamental rights to private life and the protection of personal data.

- **The provision constitutes interference with fundamental rights:**
  Article 30 paragraph 5 of the Fifth AML Directive, making personal data available to the public, constitutes interference with the fundamental rights enshrined in Articles 7 and 8 of the EU Charter. The judges reject the argument according to which the public's access to information on beneficial ownership could be justified by the fact that the data is related to professional activities.

- **Seriousness of the interference with fundamental rights:**
  The CJEU also highlights the seriousness of the interference, as the information relates not only to the identity of the beneficiary but also to the nature and extent of the beneficial interest held in corporate or in other legal entities. This allows anyone to ascertain a profile of the beneficial owner, determine its wealth and the economic sectors, countries and specific undertakings in which it has invested. The judges pointed out that unlimited access to such information may lead to abuse, especially when the information is freely accessible on the internet, as is the case in Luxembourg.

2 The interference with fundamental rights may be deemed appropriate to achieve the objective pursued (the prevention of money laundering and terrorist financing) but is unnecessary and disproportionate in light of this objective.

- The CJEU finds that the EU legislature seeks to prevent money laundering and terrorist financing by creating — by means of increased transparency — an environment less likely to be used for those purposes. It holds that the legislature's objective is in the public interest and justifies even serious interference with the fundamental rights enshrined in Articles 7 and 8 of the EU Charter, and that the public's access to information on beneficial ownership is appropriate for contributing to the attainment of that objective. However, the interference entailed by the measure under examination is neither limited to what is strictly necessary nor proportionate to the objective pursued.

- The regime introduced by the Fifth AML Directive amounts to considerably more serious interference with the fundamental rights guaranteed by Articles 7 and 8 of the EU Charter than the former regime. The CJEU recalled that the former version of Article 30 paragraph 5 was limiting access to information on beneficial owners to persons able to demonstrate a "legitimate interest" and contended that the reason for the withdrawal of the limitation was the result of difficulties encountered by the EU Commission in reaching a consensus on the definition of "legitimate interest." The fact that it may be difficult to provide a detailed definition of the circumstances and conditions under which such legitimate interest exists is no reason for the EU legislature to allow the public to access the information.

1.2 Consequences

The optional provisions of the Fifth AML Directive that allow EU member states to make information on beneficial ownership available to those who register online and to provide, in exceptional circumstances, an exemption that prevents the public from accessing that information need to be revisited. According to the CJEU, these provisions do not, in themselves, demonstrate a proper balance between the objective of general interest pursued and the fundamental rights enshrined in Articles 7 and 8 of the EU Charter, or the existence of sufficient safeguards enabling data subjects to protect their personal data effectively against risk of abuse.

Based on the CJEU's decision, EU member states may have to (re)introduce a limitation on the access to information on beneficial owners. To determine the framework of the limitation, the EU Commission is currently reviewing the decision. The situation in the other EU member states should be assessed.[5] The Luxembourg Ministry of Justice, in consultation with the LBR, decided to temporarily suspend public access to the RBO via the internet portal of the LBR services. The Luxembourg government has stated that it will closely liaise with the EU Commission to discuss the consequences of the decision and the solutions that could be envisaged at the EU level. For any beneficial owners residing in the EU or abroad, where applicable, reference to this decision could be made to request an exemption to the public's access to their information. Beneficial owners may wish to take action to protect their personal data and seek an exemption in their case.

2 The system of notification by lawyer-intermediaries subject to legal professional privilege under the DAC6 Directive is invalid

The purpose of DAC6 is to improve the functioning of the internal market by discouraging the use of aggressive cross-border tax-planning arrangements.[6] The DAC6 Directive obliges EU member states to implement rules whereby qualifying intermediaries have to disclose to the competent tax authorities any cross-border arrangements that show signs of aggressive tax planning. Under the DAC6 Directive, the principle is that cross-border arrangements that fall within the scope of at least one of the hallmarks need to be reported to the tax authorities (subject to the main benefit test being met in some cases). The DAC6 report to the tax authorities should contain the name of the intermediaries and relevant taxpayers, their residence for tax purposes, a summary of the content of the arrangement and the value of the arrangement, among other information.

Each member state may grant intermediaries a waiver from the obligation to file a report if legal professional privilege applies. In such circumstances, the intermediary subject to legal professional privilege is, however, required to notify without delay any other intermediary or, if there is no such intermediary, the relevant taxpayer, in writing, of their reporting obligations vis-à-vis the competent tax authorities. In line with these provisions,

5 Access was granted to the public without restrictions according to the national laws in Luxembourg, Bulgaria, Denmark, Latvia and Slovenia. Access was granted to the public with restrictions in Austria, Estonia, Germany, Poland, Ireland; Global Witness, Beneficial Ownership Registers in the EU, March 2020.

6 Recital 19 of the DAC6 Directive.

the Flemish decree transposing the DAC6 Directive provided that, when an intermediary involved in cross-border tax planning is bound by legal professional privilege, they must inform the other intermediaries, in writing and with justification, that they cannot report to the competent tax authorities.

2.1 Decision in relation to the legal professional privilege notification system under the DAC6 Directive

According to the CJEU, the obligation imposed on a lawyer, subject to legal professional privilege and acting as an intermediary to a DAC6 reportable arrangement, to notify another intermediary who is not their client is an infringement of Article 7 of the EU Charter that is not strictly necessary to meet the objectives of DAC6. The DAC6 notification obligation for lawyer-intermediaries interferes with the rights guaranteed in Article 7 of the EU Charter as follows:

- The first interference is when the notified intermediary, who is not a client of the lawyer-intermediary, becomes aware (i) of the identity of the lawyer-intermediary, (ii) of the analysis that the tax arrangement considered is reportable or (iii) of the lawyer-intermediary having been consulted in connection with the arrangement.

- The second interference is caused by the fact that the intermediaries notified are required to inform the competent tax authorities of the identity of the lawyer and of the fact they were consulted as part of the DAC6 reporting.

The CJEU underlines that the information obtained by a lawyer when providing legal advice, both with regard to its content and to its existence, even outside any litigation, remains covered by professional secrecy. As pointed out by the CJEU:

Individuals who consult a lawyer can reasonably expect that their communication is private and confidential. Therefore, other than in exceptional situations, those persons must have a legitimate expectation that their lawyer will not disclose to anyone, without their consent, that they are consulting him or her.[7]

The CJEU then examines whether those interferences may be justified, in particular, in view of the international tax cooperation aimed at contributing to minimizing the risk of tax avoidance and evasion. According to the CJEU, as stated in the UBO register case, among others, it must be analyzed whether the objective pursued could not reasonably be achieved in an equally effective manner by other means less prejudicial to that right, ensuring that the interference is not disproportionate to that objective. This implies a balancing of the importance of the objective and the seriousness of the interference.[8]

With respect to the two interferences outlined above:

- The CJEU considers that the notification obligation on a lawyer subject to legal professional privilege is not necessary in order to attain the objectives of the DAC6 Directive.

- It also does not appear to be necessary for the notified intermediary third parties to disclose to the tax authorities the identity of the lawyer-intermediary and the fact that they were consulted.

7 CJEU, 8 December 2022, C 694/20, para. 27.
8 CJEU, 22 November 2022, C 37/20 and C 601/20, para. 66.

2.2 Consequences

EU member states will have to revisit national provisions to ensure compliance with the ruling. It may be the case that obligations of intermediaries subject to legal professional privilege will be limited to informing only the relevant taxpayer of their respective obligations.

1. For lawyers, the most important takeaway of the CJEU decision is that lawyer-intermediaries subject to legal professional privilege are not obliged to notify the other intermediaries. Therefore, such lawyer-intermediaries cannot be held accountable in case of incomplete, inaccurate or late notification of another intermediary. Legal professional privilege plays a critical role in the protection of fundamental rights of clients. It should be borne in mind that any intermediary who is exempt under legal privilege from the reporting obligation is, in the absence of other intermediaries, still required to notify the client of their reporting obligations.

2. For intermediaries other than lawyers, an important consequence of the decision is that "secondary" intermediaries[9] within the meaning of the DAC6 Directive will no longer be notified of the DAC 6 analysis of the "primary/promotor" intermediary, if the latter is subject to legal professional privilege.[10] A useful effect of the DAC6 notification system was indeed to raise awareness regarding the DAC6 position of the promotors among the other intermediaries and to create a clear reportable/non-reportable expert position that secondary intermediaries could "follow." While the secondary intermediaries will no longer be notified (if the promotor is a lawyer-intermediary), they are still required to carry out the technical DAC 6 analysis by themselves. With secondary intermediaries left on their own, the CJEU decision could potentially result in over-reporting "prudent" positions, or, on the contrary, a breach of reporting obligations.

3. While the case is framed in the context of lawyers subject to legal professional privilege, it is also possible in certain EU jurisdictions for nonlawyer tax advisers or accountants to rely on professional privilege. The CJEU's decision being rendered in the context of lawyer intermediaries, it is unclear whether the judgment applies equally to other nonlawyer exempt intermediaries (such as accountants) who may also claim legal professional privilege. In this respect, the case could have an impact on the position of tax advisers and accountants. These intermediaries could still have an obligation to notify other intermediaries, whereas lawyers clearly now do not have such an obligation following the CJEU's decision.[11] Clarifications in national laws may be necessary in this respect. These intermediaries (who are perhaps at this stage still compelled by national laws to notify other intermediaries) should at the same time consider the compatibility of this obligation with the professional secrecy rules that apply to them.[12]

Please note as a final comment that there are other requests for a preliminary ruling concerning the EU DAC6 Directive currently pending with the CJEU:

- The French Supreme Administrative Court (Conseil d'État) raised similar questions to the CJEU, concerning the compatibility of Article 8ab of DAC6 with the right to a fair trial[13] and the right to respect for private life.

- The Belgian Constitutional Court raised additional and fundamental questions to the CJEU, including whether certain obligations contained in the EU DAC6 Directive infringe the principle of equality and nondiscrimination,[14] and whether the use of key terms and deadlines that are not sufficiently clear and precise infringe the principle of legality in criminal cases and the general principle of legal certainty and the right to respect for private life.[15]

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9 Secondary intermediaries are persons who have knowingly provided aid, assistance or advice in relation to a cross-border arrangement (without having commercialized, designed or implemented it). Secondary intermediaries would typically be financial institutions, banks, life insurance companies, brokers, wealth planners and fiduciary companies.

10 CJEU, 8 December 2022, C 694/20, para. 27.

11 For example, during the Luxembourg legislative process, the benefit of professional secrecy, initially limited to lawyers, was extended to qualified auditors and chartered accountants based on the necessity of equal treatment guaranteed by constitutional rights. According to the Luxembourg State Council, this extension is justified by the principle of equal treatment enshrined in the Luxembourg Constitutional Act. Opinion of the State Council, draft legislative proposal No. 7465 in relation to reportable cross-border arrangements (Avis du Conseil d'Etat), 14 January 2020, p. 7.

12 In Luxembourg, for instance, the criminal code provides that any person breaching professional secrecy will be liable to imprisonment of between eight days and six months and a fine ranging from EUR 500 to EUR 5,000.

13 The right to a fair trial is guaranteed by Article 47 of the EU Charter.

14 The principle of equality and non-discrimination is protected under Article 6(3) of the Treaty on the Functioning of the European Union and by Articles 20 and 21 of the EU Charter.

15 These are protected under Article 49(1) and Article 7 of the EU Charter and Article 8 of the European Convention on Human Rights. These terms include "arrangement"; "intermediary"; "participant"; "associated enterprise"; the qualification of "cross-border"; the different "hallmarks"; the "main benefit test"; and the trigger date for the 30-day reporting period.

Concluding remarks

These decisions are a testimony to the influence that the CJEU can have on acts of EU secondary law such as EU directives. In the tax and wealth management fields, the recent wave of EU regulation (directives) has introduced groundbreaking new rules, including implementing measures against aggressive tax planning or anti-money laundering. The principles and systems established by these directives are, however, subject to the scrutiny of the CJEU, which will assess their compliance with EU primary law and the general principles of EU law. The CJEU is clear: even where the objectives are honorable and abided by in the EU, such regulation should always be proportionate. This is a welcome reminder in an environment of abounded regulation.

This also holds true for any new proposals of EU directives pending approval or transposition. An example that may come to mind is the current draft EU proposal of a directive preventing the misuse of shell companies for tax purposes **("Unshell")**,[16] the provisions of which may one day have to be assessed in detail by the CJEU in light of the EU fundamental freedoms and fundamental rights.

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16 Proposal for a Council directive laying down rules to prevent the misuse of shell entities for tax purposes and amending Directive 2011/16/EU, Brussels, 22 December 2021 COM (2021) 565 final 2021/0434 (CNS).

Article

A thorny issue - the Thistle Trust case creates concerns!

In brief:

The Supreme Court of Appeal issued a judgment on 07 November 2022 dealing with a trust and tax law principle called the conduit pipe principle. Essentially, this principle requires that amounts realized by a trust, where a beneficiary has a vested right to the amount, must be taxed in the hands of the beneficiary and not the trust.

In this case, the Supreme Court of Appeal held that the conduit pipe principle does not apply to income flowing through layered trust structures to beneficiaries, triggering the need for layered trust structures to be tested for continued tax efficiency, without relying on the conduit pipe principle. However, there are a number of technical flaws in the matter, and it is likely that the decision will be appealed to the Constitutional Court of South Africa — the highest court in the country.

Cont'd on next page

Background:

The conduit pipe principle was brought into South African common law from English tax cases in 1938 and it has since been codified into legislation. Under the conduit pipe principle, trusts are not taxed on revenue amounts received or capital gains they realize, where the beneficiaries have a vested right to the trust's income or underlying assets — whether as a result of an exercise of a discretion by the trustees or if they are beneficiaries of a vested trust. Instead, the income or capital gains are taxed in the hands of these vested beneficiaries.

The Supreme Court of Appeal recently issued a judgment that limits the application of the conduit pipe principle in the context of layered trust structures.

The taxpayer in the case is a second-tier trust, which was a beneficiary of first-tier trusts that operated a real estate business and owned certain capital assets. The taxpayer had vested rights to the income and capital of the first-tier trusts and the taxpayer's beneficiaries in turn had vested rights to the taxpayer's capital and income.

Following the disposal of the capital assets by the first-tier trust, the South African Revenue Service (SARS) taxed the taxpayer (a second-tier trust) for the capital gains realized by the first-tier trusts. The taxpayer objected to this, arguing that its vested beneficiaries ought to have been taxed on these gains, which would be taxed at a lower rate.

The taxpayer appealed to the tax court and then to the high court, following these appeals, the SARS appealed to the Supreme Court of Appeal. The case may still be appealed to the Constitutional Court of South Africa.

Case findings:

1. The court held that the amount received by the taxpayer and distributed to its beneficiaries was capital in nature.

2. It was also held that the amount received and distributed by the taxpayer did not constitute an asset, which would be subject to capital gains upon distribution by the taxpayer. Rather, it was an amount received that was capital in nature.

3. Therefore, the taxpayer did not realize a capital gain that could be taxed in the hands of its beneficiaries, because the conduit pipe principle legislative provisions for capital amounts did not make provision for the pass through of capital amounts, but only capital gains realized.

4. Further, as distinct provisions implemented the conduit pipe principle for capital and revenue amounts, and the income provisions expressly excluded application to capital amounts, the taxpayer could not rely on the income provisions to be deemed a conduit of the capital amount it had received.

5. Therefore, the taxpayer's appeal was dismissed and it was taxed on the capital gain realized by the first-tier trusts.

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In case you missed it

Europe

Crypto assets in employee compensation, business and wealth management — points to note in various jurisdictions

Individuals' and companies' increasing interest in crypto assets has led certain employers to introduce cryptocurrencies as compensation, leading to a number of challenges in its implementation and for tax purposes. Individuals holding crypto assets are also facing multiple consequences when holding and transferring such crypto assets.

These topics were discussed during our webinar on 17 January 2023. With the participation of our offices in France, Germany, Belgium, Spain, Italy, Luxembourg, the Netherlands, the United Kingdom and Switzerland, the points worth mentioning for each of the topics are summarized in this alert.

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Spain

The introduction of the new tax: temporary tax on solidarity of Large Fortunes and Wealth Tax

With effect from 29 December 2022, the Temporary Tax on Solidarity of Large Fortunes (TSLF) enters into force, accruing on 31 December 2022.

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Changes on Personal Income Tax (saving taxable base)

From 1 January 2023, the tax rate of the savings income is raised.

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Changes on Beckham Law regime

As of 1 January 2023, the requirements to benefit from the special tax regime for impatriate employees, popularly known as the "Beckham Law", will become easier.

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Around the world

Switzerland

Swiss Federal Supreme Court Affirms Information Exchange with the US

On 2 November 2022, the Swiss Federal Supreme Court **("Court")** upheld the Swiss Federal Administrative Court's **("lower court")** ruling that information can be exchanged to investigate criminal tax matters pursuant to an information exchange request by a foreign tax authority. However, use of the information exchanged for non-tax enforcement purposes is impermissible.

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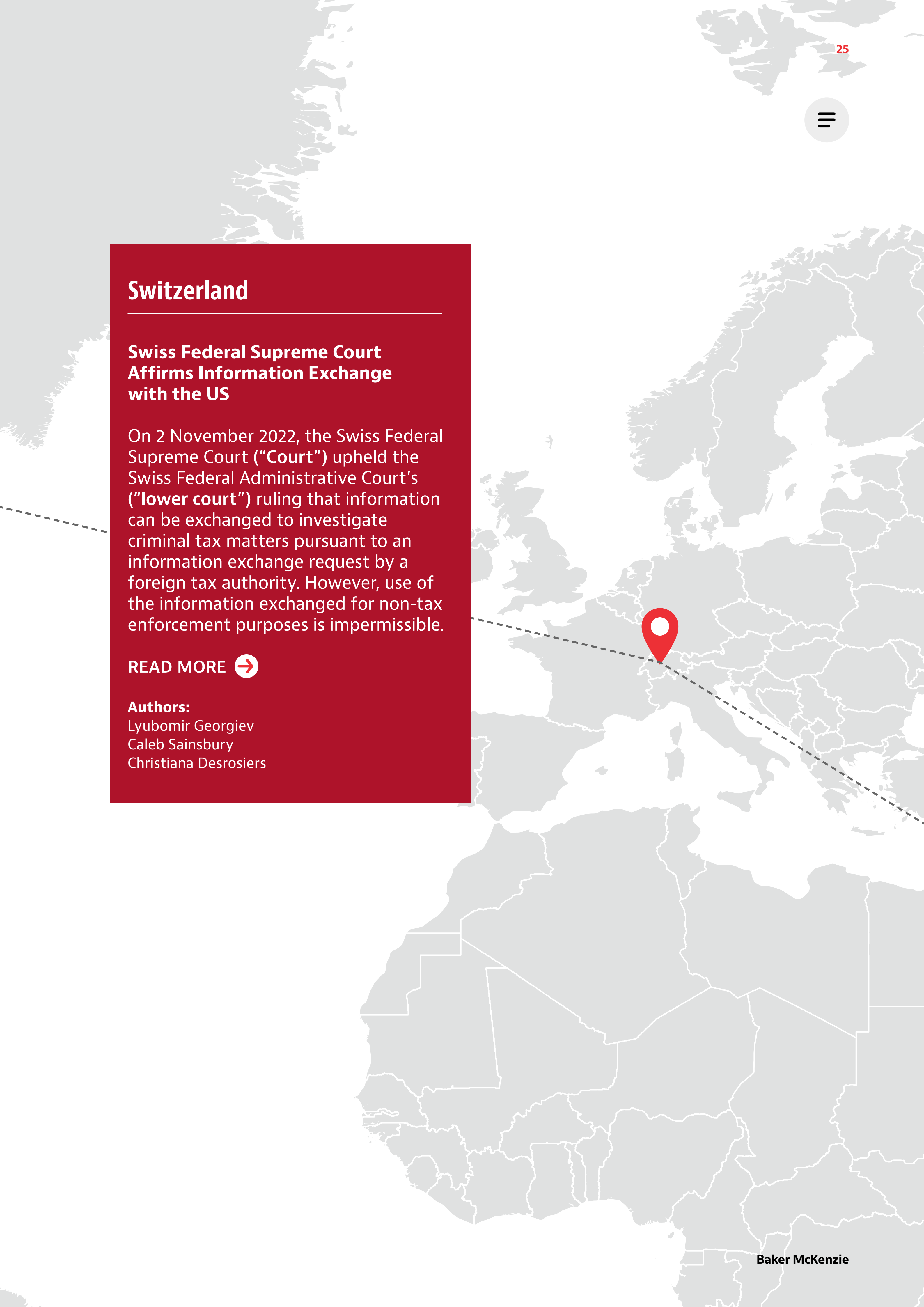

United States

United States and Croatia Sign Their First Income Tax Treaty

On 8 December 2022, the United States and Croatia signed their first convention for the avoidance of double taxation and the prevention of tax evasion with respect to taxes on income ("Treaty"). With this development, Croatia becomes the latest, and the only remaining, European Union ("EU") member state to sign its first tax convention with the US.

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United States

Updates on the FinCEN Renewed and Expanded Real Estate Geographic Targeting Orders

In its press release published on 26 October 2022, The Financial Crimes and Enforcement Network ("FinCEN") announced that its Acting Director renewed and expanded its Geographic Targeting Orders (GTOs) beginning on 27 October 2022 and ending on 24 April 2023 (with certain exceptions).

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France

Changes to the income tax withholding - Reducing the rate and simplification for foreign employers - (Finance Act for 2023, article 3)

Article 3 of the 2023 Finance Act provides for two changes to the income tax withholding (WHT).

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France

Proof of the taxpayer's affiliation with a foreign social security regime to benefit from the exemption of social surtaxes in France (Tax Court of Appeal of Versailles, 8 September 2022, No. 20VE01085)

The Tax Court of Appeal emphasizes that a taxpayer wishing to benefit from a refund of social surtaxes on their French-sourced property income due to their affiliation with a compulsory European social security scheme must provide proof of their affiliation with said scheme for the concerned period.

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France

Reforms relating to wealth management: tax credits for child care, Small and Medium-sized Enterprises (SME) tax reduction, sale of individual enterprises and taxation of foreign capitalization contracts - (Finance Act for 2023)

This article contains reforms relating to wealth management: tax credits for child care, Small and Medium-sized Enterprises (SME) tax reduction, sale of individual enterprises and taxation of foreign capitalization contracts - (Finance Act for 2023).

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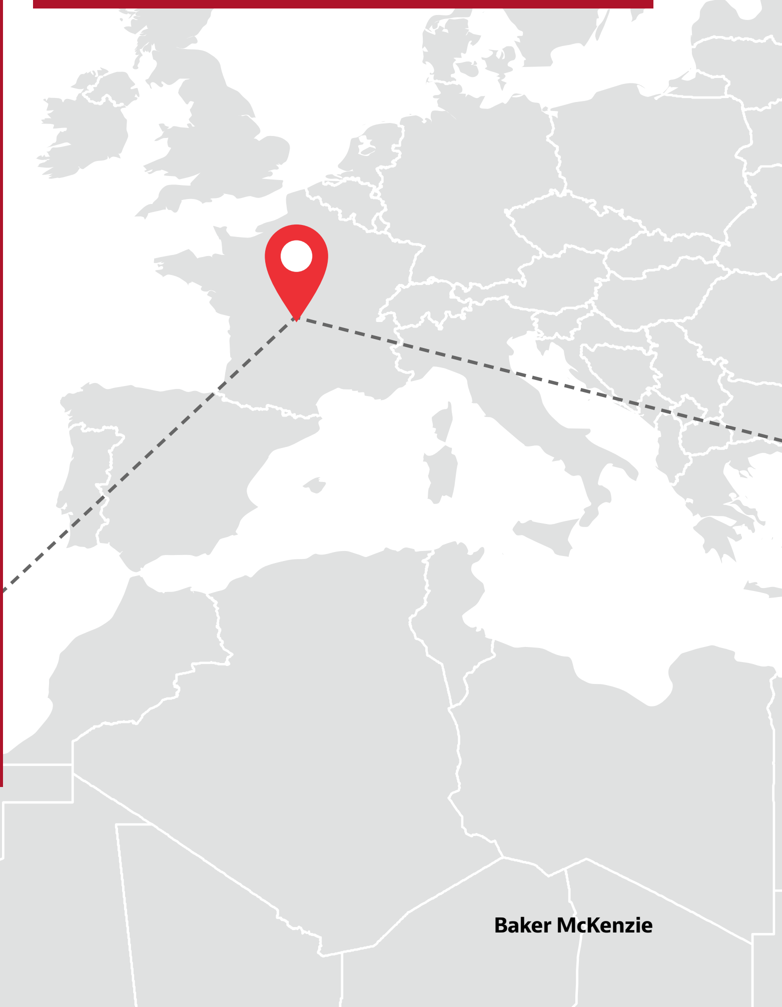

Argentina

Tax on online gambling — rules for the payment of the tax

Through General Resolution (AFIP) 5228 published in the Official Gazette on July 7, 2022 (Resolution), the form of payment of the tax on online betting and gambling (Tax) whose rates were included in Decree 293/2022 published in the Official Gazette on June 2, 2022 (Decree) was regulated.

The Resolution also included the list of entities resident abroad responsible for the organization/operation of online bets and games so that the intermediary resident in the country that enables the payment of each bet can receive the Tax corresponding to said entities abroad from July 2022, inclusive.

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Argentina

Federal Tax Authority implements an advance tax applicable to companies with extraordinary income

On August 16, 2022, Resolution No. 5248/2022 was published in the Official Gazette, by means of which the Federal Tax Authority implemented a one-time advance income tax to Argentine companies and Argentine branches of foreign companies, among others, that have obtained an extraordinary income.

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Argentina

Tax on the Acquisition of Foreign Currency - Extended to new transactions and introduction of new Collection Regime of 25%

On October 13, 2022, Decree No. 682/2022 ("Decree") and Resolution No. 5272/2022 ("Resolution") were published in the Official Gazette. With respect to certain transactions covered by the Tax on the Acquisition of Foreign Currency ("Tax"), the Federal Tax Authority ("FTA") added a new Collection Regime at a rate of 25% to the acquisition of foreign currency for certain payments through the Resolution.

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Argentina

New deadlines for declaration of currency to be invested in Real Estate

On August 22, 2022, Law No. 27,679 ("Law") was published in the Official Gazette, establishing new deadlines for the laundering of foreign currency and / or national currency in the country and abroad to be destined to the "Argentine Federal Construction Incentive Regime and Access to Housing" ("Regime"). The effective date of the Act is August 22, 2022.

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Argentina

Tax Benefits for Disclosing Currency in Argentina and Abroad and Deferral of Inflation Adjustment in the Income Tax

On December 1, 2022, Law No. 27,701 of the Federal Budget ("Law") was published in the Official Gazette, as well as Decree 799/2022 enacting it. The Law contemplates, among others, the following tax benefits:

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Argentina

On December 27, 2022, General Resolution No. 5306/2022 ("Resolution") issued by the Federal Tax Authority ("FTA") was published in the Official Gazette, whereby it established a new Complementary Information Regime for International Transactions ("RICOI").

On 27 December 2022, General Resolution No. 5306/2022 ("Resolution") issued by the Federal Tax Authority (FTA) was published in the Official Gazette. It established a new Complementary Information Regime for International Transactions (RICOI).

Subjects that will have to comply with the RICOI are (i) legal entities registered in Argentina, (ii) permanent establishments of foreign legal entities, (iii) trusts created in Argentina and (iv) sole proprietorships located in Argentina.

The following transactions are subject to the RICOI:

Transactions carried out by Argentine legal entities with related parties incorporated, domiciled or located abroad, and by foreign permanent establishments carried out with other permanent establishments of the same owner or with persons or other types of entities in the country or abroad related to the resident in the country.
Transactions carried out with subjects domiciled, incorporated or located in "noncooperative jurisdictions" or "low or no taxation jurisdictions," whether they are carried out by themselves or through their permanent establishments abroad.
The provisions established by the Resolution entered into force on 27 December 2022 and will apply for the filing of information corresponding to the fiscal years closed as of 1 August 2022. International transactions must be reported on the due date for filing the income tax return.

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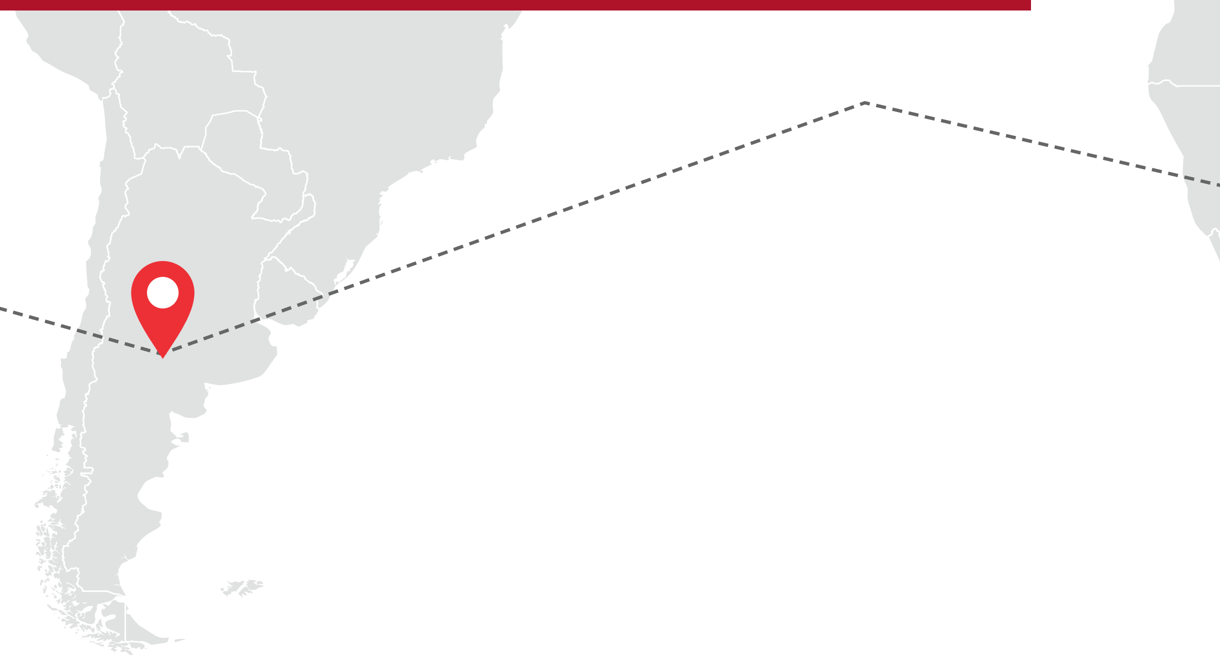

Hong Kong

Hong Kong Proposal to Tax Multinationals' Foreign Income

The Inland Revenue (Amendment) (Taxation on Specified Foreign-sourced Income) Ordinance 2022 (Amendment Ordinance) has come into operation on 1 January 2023 to put in place a new taxation regime for foreign sourced passive income (FSIE Regime) in Hong Kong.

The Amendment Ordinance is substantially the same as the bill proposed by the Government, as amended through the Committee Stage Amendments, the key features of which were discussed in our Client Alert issued in November 2022. In this alert, we outline some clarifications made by the Government during the legislative process and recent updates on the administrative guidance issued by the Inland Revenue Department (IRD) in respect of the operation of the new regime.

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