



LIECHTENSTEIN



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The taxation of legal entities under the new Liechtenstein Tax Law

On 1 January 2011, the new Liechtenstein Tax Act entered into force. With the new act, Liechtenstein introduced an attractive tax system that complies with European law. In fact, the EFTA Surveillance Authority (ESA) has confirmed that the rules for private asset structures and the new IP box regime are re-garded as compliant with the provisions of the EEA agreement. Below, some features of the new tax law for legal entities are described in detail.

Corporate tax rate and tax base

Legal entities that are taxable in Liechtenstein are now, under normal taxation rules, subject to the corpo-rate income tax on their net income at a rate of 12.5%.

The net income is reduced by income from foreign permanent establishments, rental and lease income of foreign real estate, gains from selling real estate, dividends, and capital gains on the sale of shares. It is noteworthy that the dividend income and capital gains from the sale of shares are tax exempt irrespective of the percentage of the shareholding. As a result, not only income and capital gains from interests in partly or wholly owned subsidiaries, but also income and capital gains from shares held as part of a securities portfolio, are tax-free.

Notional interest deduction

The new tax law introduced a notional interest deduction of currently 4% of the modified equity as a deemed expense to ensure equal treatment of debt and equity.

The modified equity is calculated by deducting the following items from the net equity: shares in legal entities; net asset value of foreign real estate; net assets of foreign permanent establishments; and, assets not required for the company's purposes. The reason for the first three deductions is that they produce tax-exempt income and capital gains and, therefore, cannot be used to create a notional interest deduction.

Private asset structures

As an alternative to regular company taxation and inspired by Luxembourg's Société de Gestion de Patrimoine Familial (SPF), the legislator has devised a new tax privilege for legal entities that are only engaged in the management of their own assets and do not perform any commercial activity. Such private asset structures (PAS) are subject only to the minimum corporate income tax of CHF 1,200 annually without having to file any tax returns.

The main feature with regard to the tax privilege is the lack of commercial activity. Article 64, paragraph 1a of the Tax Act exemplifies, by reference to the Asset Management Act, what is not considered as a commercial activity. This includes the acquisition, possession, management and sale of transferable securities such as bonds, stocks, money market instruments, shares in investment undertakings and derivatives. Likewise, buying, holding and selling of precious metals, artwork and similar assets is generally possible. However, in its decision approving the provisions on the PAS, ESA indicates that transactions in securities when effected "as part of a commercial share dealing activity" constitute economic activity. Regular and active trading of securities (and other assets) is therefore not considered permissible for a PAS unless decisions are delegated to an independent asset manager. The purchase and sale

of securities as part of a long-term investment strategy is allowed in any event.

As the mere exercise of ownership by an entity, and the extension of benefits by the entity to its share-holders or beneficiaries are not considered commercial activities, the holding of a property does not constitute commercial activity as long as the property is used by the PAS, or its shareholders or beneficiaries, and no rent is charged.

When a PAS holds shares in a subsidiary that exercises a commercial activity, neither the PAS nor its shareholders or beneficiaries, are allowed to exercise any control through direct or indirect influence on the management of the subsidiary. Otherwise, the PAS itself will be regarded as commercially active and lose its status as a PAS.

When comparing regular taxation to PAS taxation, it turns out that in some cases there may be only a small difference in the tax burden because even in case of regular taxation the income from the management of the legal entity's own assets tends to be tax-exempt anyway.

The following table shows where PAS taxation has advantages over regular taxation:

Investment	Revenues	Regular taxation (12.5% corporate tax)	Possible advantage of PAS (tax of CHF 1,200 annually only)
Shares	Dividends	Tax-free	
	Realised capital gains	Tax-free	
Bonds	Interest	Taxable if net profit exceeds the 4% notional interest deduction	X
	Realised capital gains	Taxable if net profit exceeds the 4% notional interest deduction	X
Commodities (physical, eg, gold in a safe)	Realised capital gains	Taxable if net profit exceeds the 4% notional interest deduction	X
Real estate (non-Liechtenstein)	Rent	Tax-free	
	Realised capital gains	Tax-free	
Derivatives		Taxable if net profit exceeding the 4% notional interest deduction	X
Investment funds		Treated as transparent; investments of the fund are treated as being held directly by the legal entity	X (except pure stock/property funds)

In summary

The specific features of the new tax system have turned Liechtenstein into an attractive jurisdiction for many purposes. With a corporate tax rate of 12.5%, and the possibility to reduce the effective tax rate even further through the notional interest deduction, Liechtenstein has joined the league of most tax-efficient jurisdictions by European standards. Furthermore, the PAS offers an attractive way for individuals to structure their wealth.

Dr Markus Summer, LL.M, MBA, is a partner of Liechtenstein's oldest and largest law firm Marxer & Partner Attorneys-at-Law.