

# EVERYTHING YOU NEED TO KNOW ABOUT LUXEMBOURG AND LATIN AMERICA

LFF spoke with the leaders of the Latin-America desks of Deloitte, Ernst & Young, KPMG and PwC in Luxembourg about the latest topics in business and finance that shape today's agenda.

*Francisco DA CUNHA,  
Director Cross-Border Tax,  
Deloitte Luxembourg*



## INVESTMENT HUB

Francisco Da Cunha, Director Cross-Border Tax at Deloitte Luxembourg explains how Luxembourg is developing as an investment hub for Latin America.

- **LFF: WHAT KIND OF ADVICE AND SERVICES ARE CURRENTLY MOST FREQUENTLY ASKED FOR?**
- **FDA:** With increased intensity these past three years, Luxembourg has been in the spotlight of LatAm investors.

While more traditional forms of investment structures start to lose their effectiveness (for several reasons but mostly linked to the international context or changes in domestic tax legislation), Luxembourg is appearing more and more as a reliable and compliant jurisdiction for the purposes of establishing an investment platform.

In this context, we are often asked to render advice and services on the establishment of these investment platforms. As we cover the region and not only some investor profiles, this involves a wide range of services and assistance such as establishment of holding companies, incorporation of investment funds, audit, cross-border tax structuring advice, liaison with our regulator, the CSSF, assistance on the incorporation of financial service providers (PSFs), etc.

## ► *LuxembourgforFinance*

### BRAZIL FELL INTO RECESSION IN THE FIRST HALF OF 2014. WHAT IS YOUR FORECAST IN TERMS OF GROWTH?

#### ► *Francisco DA CUNHA*

There are some factors that I believe one should not lose sight of when addressing this issue.

Clearly, if we consider (i) the size of the country, (ii) the (still evident) economic exposure to changes in politics, (iii) the real fluctuations and its macro-economic impact, (iv) the lack of basic infrastructure to connect the interior and north regions with the wealthier ones, (v) the uncertainty in terms of legal and tax stability and (vi) some inefficiencies as regards public servicing, we cannot but conclude that Brazil has done an outstanding job these past 8 to 10 years to keep up with more developed nations.

Many fights need to be fought before Brazil is viewed internationally as a risk-free economy to invest in and for Brazilian investors to comfortably invest overseas. In our view, the country is definitely getting there. Recent news of a recession can of course be seen as a step backwards, but this is part of the "learning curve" Brazil has to pass in order to solve the issues above and eventually unlock and unleash all its resources.

### ► **LFF: HOW HAVE LUXEMBOURG – LATAM RELATIONS DEVELOPED OVER THE LAST TWO YEARS?**

► **FDA:** Since Luxembourg started promoting roadshows involving high-level political and technical delegations to specific countries in Latin America, we have witnessed an outstanding progression on cooperation at an institutional level. From a perspective of cross-border investment, specific cases are the envisaged enlarging of the Double Tax Treaty network between these two regions, and the discussions held for purposes of knowingly removing Luxembourg from "black-lists" radars in several LATAM countries. The reconnection of the embassies of several of these countries with the Luxembourg professional sector (as a mean to monitor and understand Luxembourg's attractiveness for these countries) can also be seen as a positive sign for the future development of economic relations.

### ► **LFF: IN WHICH AREAS DO YOU SEE THE MOST IMPORTANT OPPORTUNITIES FOR COOPERATION BETWEEN LUXEMBOURG AND LATIN AMERICA?**

► **FDA:** There are a number of areas that start being developed between Luxembourg and LATAM, and others yet to be developed. Essentially, Luxembourg is, from all perspectives, an ideal gateway into Europe, and vice versa for professionals willing to invest in LATAM.

This is the case from a fund and investment platform industry perspective (where we have seen more development these past years), but also from a logistic one, given that Luxembourg is ideally located in the middle of Europe and allows to easily and efficiently expand exports for LATAM companies willing to go deeper and wider into European continental markets.

### ► **LFF: WHY IS LUXEMBOURG SOMETIMES STILL UNKNOWN TO LATAM CLIENTS?**

► **FDA:** I believe Einstein once said that *"if you always do what you always did, you will always get what you always got"*. Luxembourg is, slowly but very steadily, appearing in the spotlight of LATAM clients; and this is nowadays always for the best reasons. Reliability, stability, compliance with international standards as well as appropriate and efficient regulation are the main reasons for this. LATAM clients understand it, and the international framework pushes them to this natural outcome. Some may still not know it (and even then I would dare say not many), but once they do, it will come as evident the possibility to use all the resources this country has to offer, and especially in relation to the Latin American region.



Patricia **GUDINO**,  
Partner, Tax Advisory services,  
EY Luxembourg

Patricia Gudino, Partner at EY Tax Advisory services explains how ICT become an important area for cooperation between Luxembourg and Brazil, the challenges countries in America are facing and what it sometimes means to be blacklisted.

## PRIME LOCATION FOR E-BUSINESS GIANTS AND STARTUPS

### ► LFF: WHY IS BRAZIL BECOMING ONE OF THE BIGGEST POTENTIAL MARKETS FOR PLAYERS IN THE ICT INDUSTRY?

- **PG:** Brazil is the fourth largest market of smartphones in the world. As of Q1 2014, it ranks as the second country in the world in number of apps downloaded from Google Play, the top revenue generating app store market in Latin America for iOS and even while the country's economy saw a decrease in growth in 2014, in Q2, mobile devices saw a record growth when compared to the same period in 2013, with an average of 100 smartphones sold per minute to retailers.

Brazil is the second largest country in number of Facebook users (1<sup>st</sup>: US), and frequently the most active in terms of posting. It is the 5<sup>th</sup> most connected country in the Internet in absolute terms, with over 109 million Brazilians connected to the Internet. Additionally, Brazil stands as the biggest gaming market in Latin America in terms of revenues.

The Brazilian government sees this potential and is actively encouraging the development, through initiatives such as the "TI Maior", Project Innovative and Competitive Digital Brazil 2015-22 and Start-up Brazil, all geared towards encouraging the development of the ICT industry, by attracting local and foreign enterprises. There are still points of severe struggle, mainly in the infrastructure to support said development and qualified workforce to support the growing industry. Nevertheless, it is still growing steadily.

### ► LFF: WHAT DOES LUXEMBOURG HAVE TO OFFER IN TERMS OF ICT?

- **PG:** Luxembourg is a state-of-the-art ICT hub and has a well-equipped data center park, with access to the main European data traffic exchange centers. Allied with academic programs aimed at capacitating new professionals, as well as programs such as Europe 4 Startup – of which EY is a partner – Luxembourg can serve as an entry door for up-and-coming ICT companies interested in expanding activities to the rest of the world. As a prime location of e-business giants, Luxembourg can be of great assistance to ICT companies envisaging to access the Brazilian market.

Certainly there is plenty of room for cooperation between Luxembourg and Brazil, to promote the expansion of Brazilian ICT companies to the European markets – and the world –, and also the entry of international companies in the Brazilian market, be it through start-up initiatives or as a center for distribution of digital content to Brazilian consumers.

## STRATEGIES FOR DEALING WITH THE CHALLENGES

Patricia Gudino explains that one of the biggest challenges is high regulatory risk, in view of unstable legislation and taxation rules. *"Quick and often unpredictable changes to the legal and tax framework create uncertainty for investors. Likewise, foreign exchange controls restrict the freedom to repatriate capital. Regulatory risks such as these materialized, for instance, in the drastic devaluation of the Venezuelan bolivar, allied with over 60% inflation this year and strict controls to remove capital from the country, which results in heavy losses for investors who are unable to take their money out of the country unless using official – and disadvantageous – exchange rates, making their investments lose value rapidly"*. Similar phenomenon was witnessed in Argentina, where the dwindling of foreign cash reserves in the country led to the enforcement of stricter controls over the purchase of foreign currency. Not all countries are as strict, with countries such as Brazil, Peru, Colombia and Chile merely monitoring the inflow and outflow of currency (although Brazil may regulate this with a financial operations tax that can be increased to up to 25% if needed).

### POLITICS

Politics also play a role in increasing risk when investing in Latin America. As much as the instability of governments and susceptibility to "coup d'état" have lowered, there are still risks to be taken into account, such as seizing of private companies' operations in times of crisis (as occurred with Repsol two years ago), protectionism, resource nationalism, increased state control over the economy,

among others. Patricia says *"Countries tend to have high levels of bureaucracy and compliance requirements, which are linked to the governments' desire to monitor the flows of income in their territories"*. Corruption, intimately linked with the excess bureaucracy and the relatively high shadow economy in the region, is another risk factor.

### TAX TREATIES

The lack of an extensive tax treaty network and inconsistent application of treaty provisions can also be a concern for investors to structure their businesses in Latin America. Brazil, for instance, had cases where its particular interpretation of tax treaty provisions led to domestic taxation of business income when, under the treaty, Brazil would not have had the right to tax.

### INFRASTRUCTURE

Infrastructure and lack of qualified workforce often can be an issue, but investments and opportunities in these areas are increasing, with professionals investing more and more in their qualification, and in most countries the process for visa is not overly-complex, thus being possible to have expatriate workers when needed.

Despite the challenges, the prospects of a stable and continuous economic growth in Latin America show that it remains desirable to invest in view of the many opportunities. The return can be very attractive to investors who are well-advised to overcome the risks inherent to the region. **LR**

## BLACKLISTING

Countries usually create so-called blacklists or greylists with the objective of imposing barriers for outbound payments made to certain jurisdictions which (i) do not levy taxes or levy low taxes, (ii) are deemed to be uncooperative in terms of exchange of information, (iii) lack transparency and/or (iv) do not impose substance requirements.

The consequences of being in a black or grey list have to be assessed on a case-by-case basis, depending on the country legislation. Countries usually levy higher withholding income taxes on payments made to listed jurisdictions. Furthermore, there may also be harder thin capitalization limits and any transaction entered into with a company domiciled in a listed jurisdiction may need to comply with local transfer pricing rules. Other undesirable effects can be the non-deductibility of expenses (interest, royalties, service fees and other income) paid to beneficiaries domiciled in listed jurisdictions and inclusion in the scope of Controlled Foreign Corporation rules.

The 1929 holding company regime, which allowed investors an exemption from corporate taxes, and the banking secrecy rules contributed to Luxembourg being historically included in certain black or grey lists. Some countries have removed Luxembourg from their lists after the termination of the regime. Others, however, for the lack of specificity in their lists, include Luxembourg as a whole, irrespective of the taxation regime to which the companies are subject to.

Although the 1929 holding regime ended in 2010, it should be noted that the legislation approving the blacklist in certain countries dates prior to 2010.

Patricia explains *"Brazil initially had listed Luxembourg holding companies as preferential tax regimes, with no specific mention of the 1929 regime. Luxembourg has engaged in discussions to clarify that the regime had been terminated in 2010 and, as a result, Brazil has removed Luxembourg from the list"*.





Bastien VOISIN,  
Partner,  
KPMG

Bastien Voisin, Partner at KPMG explains how Luxembourg's introduction of the private foundation will benefit Latam clients and what the automatic exchange of information will mean to them.

## THE LUXEMBOURG PRIVATE FOUNDATION - A NEW TOOL FOR PRIVATE WEALTH PLANNING

With the new private foundation, Luxembourg introduced a flexible and tax efficient vehicle to organize succession planning and preserve family wealth. It is aimed to attract Latin American entrepreneurs and high net worth individuals and families as an alternative to foundations or trusts existing in other financial centers such as Panama or the Bahamas. However, the Luxembourg private foundation is in no way designed to hide information from the tax administration. Indeed, the board of directors of the private foundation will be required to make available to public authorities all documents necessary for identifying its founder and the beneficiaries at the registered office.

*"The use of a private foundation is limited to individuals and patrimonial entities with the objective of managing private wealth. It is suitable for securing private or business assets, for separating economic ownership from the decision-making authority, or for protecting the private sphere" says Bastien Voisin.*

The foundation has its own legal personality and the capital contribution is of minimum Euros 50.000. It can hold movable or immovable properties as well as entities.

Together with the private wealth management vehicle (société de gestion de patrimoine familial) and the family office, the private foundation aims to complete the range of wealth management instruments at the disposal of entrepreneurs and high net wealth individuals in Luxembourg.

It is also intended to preserve the solid reputation of the country in private bank-

ing following the government's decision to abolish bank secrecy by 2015 and to introduce an automatic exchange of information with third party countries.

*"The Luxembourg private foundation could be seen as the "civil law" counterpart of the "common law" based Anglo-Saxon trust. The manner in which a foundation is established and run, however, is quite distinct from a trust".*

The trust is a relationship created through a private writing, where a trustee holds and controls assets for the benefit of beneficiaries. On the other hand, a foundation is an autonomous legal entity. It has characteristics of a company however the foundation has no shareholders and acts more like a trust.

Another main distinction between the trust and the foundation lies in the fact that an instrument of trust is not registered and is kept with the trustee, whilst a Notarial deed must be drawn up for a foundation. **LR**

## AUTOMATIC EXCHANGE OF INFORMATION: LUXEMBOURG TO SHARE TAX INFORMATION IN 2015

### ► LFF: WHAT DOES IT COVER AND WHAT WILL CHANGE FOR LATAM?

- **BV:** The days of information on request look to be numbered after the OECD released its new global Standard for Automatic Exchange of Financial Account Information in Tax Matters last July.

The Standard is based to a large degree on the United States FATCA intergovernmental agreements in that jurisdictions obtain information from their financial institutions and automatically exchange that information with other jurisdictions on an annual basis. It sets out the financial account information to be exchanged, the financial institutions that need to report and the different types of accounts and taxpayers covered.

At the same time, many Latin American countries have adopted Controlled Foreign Corporation (CFC) rules to fight against tax evasion and tax undistributed income of foreign entities located in tax havens and controlled by domestic taxpayers. The development of CFC rules combined with automatic exchange of information should definitely encourage Latin American investors to migrate in the near future their assets from popular tax havens such as British Virgin Islands, Bahamas or Cayman Islands towards compliant financial centers that are not blacklisted.

### ► LFF: WHAT HAS CHANGED SO FAR?

- **BV:** End of 2012, Mexico has entered into a FATCA Model I Intergovernmental Agreement with the US. For Mexican residents, the agreement provides for automatic reporting and exchange of information in relation to their US financial accounts.

In 2013, Brazil has entered into a tax information exchange agreement (TIEA) with the US and Cayman Islands.

Over 66 jurisdictions including Argentina, Brazil, Colombia and Chile have now publicly committed to implement The Standard and more are expected to follow.

Luxembourg is part of a group of early adopter jurisdictions that have committed to a specific timetable leading to the first exchanges of information in 2017.

Bringing the new global standard into force will still require a lot of work and it is unclear when all of the pieces of the jigsaw will be in place. However, the G20 countries at least expect to be exchanging information with each other automatically by the end of 2015. **LR**

### ► *LuxembourgforFinance*

WHAT DOES IT MEAN FOR  
LUXEMBOURG? WHAT  
WILL LUXEMBOURG BE  
ABLE TO OFFER TO LATAM  
CLIENTS IN THE FUTURE?

#### ► *Bastien VOISIN*

With the new Standard, a new way of doing business is emerging that is based on being globally compliant and tax transparent.

Being at the forefront of these changes, Luxembourg has already paved the way for its compliance with automatic exchange of information.

In this ever-changing environment, Luxembourg will be able to provide the right answers to Latin American clients in need for certainty. By adopting the new global standards, Luxembourg's attractiveness to foreign investments would remain unaffected and even grow. In this regard, the main advantages of Luxembourg are the diversity in financial products, investment vehicles and solutions, a strong tradition in private banking, an extensive double tax treaty network and the access to the European market via the European passport for alternative investment fund managers.

# IN THE SPOTLIGHT: CFC RULES

The Brazilian tax environment is constantly evolving. However, despite the recent attempts of the Brazilian government to introduce changes in the taxation of national residents ("Investors"), as per MP 627/2013 issued in November 2013 ("CFC rules", among other changes), the cash basis system is still in place. How long this is going to last remains unclear. Based on said system, only the Investors' effective receipt of income from their participation in a foreign company would by itself lead to taxation in Brazil.

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*Monica TIUBA,  
Senior Manager,  
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In this context, if the proposed introduction of CFC rules is approved, an annual basis system will henceforth apply to three situations as from 1 January 2015. Either:

- ▶ the CFC is to be located in a low-tax jurisdiction or subject to a privileged tax regime; or
- ▶ the CFC is to be subject to a sub-taxation regime (i.e. a regime which taxes resident companies at a nominal tax rate below 20%); or
- ▶ the Investors will not make the relevant documentation on the CFC available (e.g. certificate of incorporation identifying the other shareholders and subsequent amendments, registered with the relevant public offices).

These proposed rules would apply in case the Investors' participation in a CFC exceeds 50%, regardless of whether the latter is held alone or jointly with another individual or corporation located in Brazil or abroad and considered to be related.

Accordingly, the profits of said CFCs would be made available but not effectively distributed to Investors, and consequently be taxed in Brazil at a progressive tax rate of up to 27,5%.

Therefore, the widespread use of low- or nil-tax jurisdictions to avoid an immediate taxation in Brazil could soon become inefficient. This could be particularly relevant considering both changes in the future and the evolution of Investors' mind-sets remain uncertain. Any fiscal strategy should take into account the economic reasoning underlying the investment structure in question.

Finally, although MP627/2013 was converted into Law 12.793/2014 without including the CFC rules for individuals, one may consider it only a matter of time before the latter are adopted. With this in mind, Brazilian investors are poised to get acquainted with new investment structures. Combined with genuine business objectives, such an approach could justify their international structuring and investments and ensure efficiency in the long term.

Being a well-developed financial centre with a wide range of alternatives (SIF, Soparfi, SPF, etc.) which is white-listed in Brazil and home to a very significant Portuguese-speaking community, Luxembourg offers solutions that aim at ensuring compliance with similar types of rules. As such, the Grand Duchy is definitely the right jurisdiction to consider.

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