The Private Wealth & Private Client Review

Fourth Edition

Editor
John Riches

Law Business Research

The Private Wealth & Private Client Review

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The Private Wealth & Private Client Review

Fourth Edition

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EDITOR'S PREFACE

There is no doubt that the twin recurring themes for 2015 at a global level in private wealth planning are those of transparency and regulation. The zeal of policy makers in imposing ever more complex and potentially confusing sets of rules on disclosure of beneficial ownership information seems unabated.

i Common reporting standard (CRS)

The centrepiece of cross-border automatic information exchange is CRS. This FATCA equivalent for the rest of the developed world is set to come into effect from 1 January 2016. At the last count just over 90 countries had committed to CRS. Its principal effects will be felt in two waves – among the so-called early adopters group the rules will take effect from 1 January 2016 and first information exchanges will apply in September 2017. For the second wave, there will be a year's delay.

What is interesting about CRS is that the OECD has taken a central role in producing coordinated guidance on its interpretation. The draft guidance initially published in July 2014 was somewhat sketchy in nature and we can expect, as we move towards the beginning of next year, revised and more detailed guidance on a number of key issues.

Deep concerns exist about the extent to which information exchange between tax authorities under CRS will remain secure in the hands of the 'home' countries of beneficial owners. While the 'normal' way of signing up to CRS is via the multilateral convention that provides for exchange with other signatory nations, there are indications that some jurisdictions (at this stage the Bahamas, Hong Kong and possibly Switzerland) may seek to adopt a more 'bilateral' approach implementing CRS. If this approach becomes more widespread, then the practical implementation of CRS could be significantly delayed by jurisdictions who negotiate treaties on a one-by-one basis with 90 other countries.

While CRS is often compared to FATCA, there are some material differences that emerge from closer scrutiny. Whatever the shortcomings of FATCA, the ability to issue a global intermediary identification number and to sponsor entities on a cross-

border basis somewhat lessens the bureaucratic excesses of its impact. What is distinctly unclear about CRS at this point is whether equivalent mechanics will emerge. As CRS is currently written as a series of bilateral treaties between jurisdictions with no domestic law 'anchor' (as is the case with FATCA) concerns are being expressed about the potential duplication for complex cross-border structures of reporting. In this context, the July 2014 introduction to CRS notes that the rules as to where a financial institution (FI) will be deemed resident differs between jurisdictions – in some cases this will be based on the place of incorporation whilst in others it may be based on the place of effective management.

There are concerns as to how non-financial entities (NFEs) will be dealt with under CRS. There is anecdotal evidence emerging already in the context of FATCA that financial institutions, driven by concerns about fines from regulators for NFEs and the related ownership structure are subjecting bank account applications for NFEs to additional enquiries that generate very significant costs and delay.

It is noteworthy that there has been a significant crossover from the anti-money laundering (AML) or terrorist financing regime coordinated by the Financial Action Task Force (FATF). This is expressly provided in the CRS model treaty that imports into CRS the FATF concept of beneficial ownership. In the CRS world, this is known as 'controlling persons'. By expressly linking the definition of controlling persons to that of beneficial ownership employed for FATF purposes, there is the prospect of the beneficial ownership definition evolving over time in accordance with principles adopted in that domain. It is noteworthy that, as well as looking to ultimate legal and beneficial ownership of an entity, these definitions also look to the capacity to exert influence and control in the absence of any formal legal entitlement. Thus the expanded definition is as follows.

Beneficial owner refers to the natural person who ultimately owns or controls a customer or the natural person on whose behalf a transaction is being conducted. It also includes those persons who exercise ultimate effective control over a legal person or arrangement.[1]

It is completely appreciated that, in a law enforcement context, criminals and terrorists do not typically advertise their involvement in ownership structures where they are liable to be detected by the appropriate agencies. Transporting this definition wholesale, however, into the world of tax information exchange where domestic tax authorities may draw unfair and adverse implications from an attribution of being a 'controlling person' is more questionable. It is not a complete response to this concern to say, in the final analysis, if someone has no ability to enjoy the benefit of assets held within a particular structure that they can demonstrate this – the potential costs and bureaucracy of an unwarranted tax audit that may arise from such a misunderstanding will be more difficult to quantify.

Another area of concern is the capacity for banks who have, in the past, misclassified or misunderstood information about ownership structures. If this information is simply

1 http://www.fatf-gafi.org/pages/glossary/a-c/ – The Recommendations were adopted by FATF on 16 February 2012. (emphasis added).

'copied over' from AML records for CRS purposes then there is scope for false and misleading information to be exchanged in circumstances where the 'beneficial owners' may be completely unaware of such mistakes or misclassifications.

What follows from this is an increased importance for professional advisers to actively engage with clients to discuss the implications of these changes. Taken together, the combined impact of these changes is likely to be seen in years to come as a 'paradigm shift' in international wealth structuring. It is therefore critically important that the advisory community equips itself fully to be able to assist in a pro-active manner.

ii Public registers of beneficial ownership

On 20 May 2015, the EU published the final version of its fourth anti-money laundering directive (4AMLD). This commits the EU Member States to providing a public register of beneficial ownership within the next two years. What is noteworthy about the terms of the regulation is the fundamental distinction that has been drawn between ownership information about 'legal persons' (including companies and foundations) on the one hand, and 'legal arrangements' (including trusts) on the other. There is an obligation for information on legal persons to be placed in the public domain while information relating to trusts and equivalent arrangements will be restricted so that it is only made available to competent authorities.

The acceptance in the drafting of these regulations that there is a legitimate distinction to be drawn between commercial entities that interact with third parties, primarily in the context of business arrangements, and private asset ownership structures that are primarily designed to hold wealth for families is an encouraging one.

It should not, however, be assumed that the emphasis on privacy that underpinned this particular distinction will necessarily be a permanent one. There is a very strong constituency within the EU that still argues that a public register of trusts should be introduced at some stage in the future.

Turning to the UK, 2016 will see the introduction of a public register of beneficial ownership for companies in the UK. This legislation, to a large extent, anticipates the impact of 4AMLD although it is not completely symmetrical. The centrepiece of UK domestic legislation is the public identification of persons with influence over UK companies, known as 'persons exercising significant control' (PSCs). There are significant penalties for non-compliance. In particular, in circumstances where a PSC does not respond to the request for information from a company, not only can that refusal generate potentially criminal sanctions, it can also result in any economic benefits deriving from the shares as well as the ability to vote being suspended.

While it is appreciated that there are reasons why sanctions need to be applied to encourage people to comply, the harsh economic penalties may be seen as totally disproportionate to non-compliance. It is interesting to note that the PSC concept analogous to that of the 'controlling persons' in the context of CRS. As with CRS, the most complex area here is the extent to which those being seen to exert 'influence' without formal legal entitlement may be classified as PSCs.

One further interesting issue that needs to be considered as matters move forward is whether the impact of the EU public register for corporate entities will result in a 'back door' trust register in many cases. One of the categories for disclosure of PSCs in

the UK register is 'ownership or influence via a trust'. In circumstances therefore where a trust holds a material interest in a company, this can result in not only the trustees and protectors of the trust, but also family members with important powers (such as hire and fire powers) being classified as PSCs and having their information placed on a public register. While this register will not give direct information about beneficiaries as such, in many cases it will provide a significant degree of transparency about family involvement. It seems likely that, over time, the EU will also look to 'export' a requirement for beneficial ownership information on public registered companies to be incorporated in many of the international finance centres. While IFCs have indicated that they are sceptical about the adoption of such registers in circumstances where there is not a common standard applied to all jurisdictions, it remains to be seen how long this stance can be maintained once 4AMLD is in full force.

iii Position of the United States

The United States stands out as having secured a position for itself in the context of cross-border disclosure that many feel is hypocritical. Specifically there is a carve out from CRS on the basis that the US has implemented FATCA. The constitutional position in the US where measures of this nature would tend to be introduced at a state rather than federal level also complicates the picture. In the absence of any comprehensive regime to regulate trustee and corporate service providers, the US appears to have achieved a competitive advantage in administering 'offshore' structures because it has exempted itself, in practical terms, from reciprocation on automatic information exchange. This is already leading to many considering the US as an alternative base from which to administer family structures in a more 'private' setting than is possible in IFCs once CRS take effect.

iv Global legal entity identifier system (GLEIs)[2]

A development flowing from the 2008 financial crisis is the introduction of GLEIs. In December 2014 a regulatory oversight committee relating to GLEIs introduced a task force to develop a proposal for collecting GLEIs information on the direct and ultimate parents of legal entities. The policy is to ensure financial intermediaries can track who they are dealing with as counterparties in investment transactions. The underlying policy that drives the creation of the GLEIs is to create transparency in financial markets. In the current phase 1 of the project, the information required to be collected is limited to 'business card information' about the entities concerned and will therefore be limited to a name, address and contact number. However, the 'level 2' data that is likely to be required will extend the reference data to relationships between entities. This could result in beneficial ownership information being required in due course. This proposal is likely to see some development in the course of the next six months but is yet another illustration of overlapping regimes for collecting beneficial ownership information that are likely to have a substantial effect on the operation of family wealth holding structures in the years ahead.

2 http://www.leiroc.org/.

v Conclusion

The challenges of keeping abreast of changes in the regulatory and transparency arena are significant. These issues look set to be a significant driver in wealth strategy in the next three to five years. Navigating these issues will increasingly become a required skill set for professional advisers.

John Riches
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London
September 2015

Chapter 22

INDIA

Joachim Saldanha and Megha Ramani[1]

I INTRODUCTION

The World Wealth Report 2015 estimates a 104 per cent increase in India's ultra-high net worth individuals (HNWI) over a period of 10 years beginning in 2014.[2] Following an increase in its HNWI population at the meagre rate of 2 per cent in 2013, the year 2014 saw India's HNWI population grow at a rate of 26.3 per cent, outstripping the global average. India now occupies the 11th position in globally in terms of HNWI population.[3]

There are several factors contributing to the rise of wealth creation in India – globalisation, the growth of the Indian economy and the rise of educated first-generation entrepreneurs. The new Indian government voted in by an overwhelming majority in 2014 has also been vocal about making it easier to do business in India and boost the economy, heartened by the growth of a new class of entrepreneurs who are harnessing digital platforms to open up and connect Indian customers across the vast country. While almost 90 per cent of Indian businesses are family run, a significant majority of HNWI promoters do not have personal or business succession plans in place. This trend has slowly begun to change – in fact, the Indian securities regulator has also made it compulsory for certain companies to have business succession plans in place.

The trend also requires insight into the very culture-specific requirements of planning for Indian HNWIs. For example, saving for the often-lavish weddings of their children, caring for dependants from their extended families and religious endowments

1 Joachim Saldanha is an associate and Megha Ramani is a senior member at Nishith Desai Associates.

2 http://articles.economictimes.indiatimes.com/2013-05-11/news/39186852_1_ultra-hnwis-millionaires-india.

3 Available online for download at www.worldwealthreport.com/download.

to a family deity can be a driving force for some structures. As businesses and families have grown, family members are taking up residence in foreign countries, which means that Indian businesses and Indian families are 'going global'. At the same time, we are seeing a reverse migration of sorts of Indian-origin HNWIs, who are not only shifting their physical presence to India but also consolidating their asset bases in India. Such movement creates much complexity when it comes to questions of maintaining and preserving personal wealth, ensuring the sustainability of such wealth, and passing it on to future generations, particularly keeping the Indian succession laws, regulatory, tax and exchange control regulations in mind.

Cultural challenges continue to drive structures, however, for example, the idea of giving up ownership and control is not acceptable to the Indian patriarch. Further, since India does not have hybrid planning vehicles, this remains a key challenge while setting up trusts or other structures. Indian families also prefer centralised and seamless decision-making by the family, possibly with a more conservative mindset than in Western countries. Generational differences in the interpretation of family and business values has led to more and more family businesses having much-publicised family feuds because of parties having differing interests and ambitions for the business. Families are increasingly looking to minimise the impact of these issues on the business through wealth and succession planning. Later generations, being savvier and more educated, favour such planning and have made it more acceptable to implement wealth-planning measures. Slowly there is greater acceptance of institutional trustees, protectorship structures and even the process of will writing than ever before (traditional Indian families continue to consider it inauspicious to discuss the death of the patriarch).

An additional point is the place that philanthropy has had in Indian culture for several centuries. India has a long history of family and corporate philanthropy by the rich and a recent development in this area has been the stipulation of guidelines by the government on corporate social responsibility (CSR). Introduced in 2009, these guidelines aim to provide an effective regulatory framework for Indian corporates to enable them to contribute to the overall growth of society. Now, under the Companies Act 2013 (the 2013 Act) (which replaced the Companies Act 1956), the government has implemented a more robust CSR regime, with specified companies expected to allocate 2 per cent of their average net profits in previous three preceding financial years towards CSR. Activities that fall under CSR have also been detailed in the 2013 Act, and include eradicating hunger and poverty, promoting education and employment-enhancing vocational skills. The ambiguity surrounding whether CSR expenses would be a deductible expense for the company was clarified by a provision introduced by the Finance Act 2014, which allowed CSR expenditure to be deductible only in very limited circumstances.

II TAX

i Taxation of individuals

The Income Tax Act (ITA) provides for chargeability to income tax on the basis of residence. Determination of residence is on the basis of a day-count test of physical presence in a given fiscal year or over a specified number of past fiscal years (or both)

depending on the circumstances (with a relaxed test for non-resident Indians and persons of Indian origin).

India provides for differential rates of tax on ordinary income and capital gains. The benefit of a lower rate on capital gains is linked to the period for which the capital asset is held as specified for different asset categories.

ii Clubbing of income

The ITA provides that income of any person on transfer in certain situations may still be considered as income of the transferor and taxed as his or her income. This would occur where there has been a transfer of income without a transfer of assets or where the transfer is revocable (as statutorily defined). Such consequence would not apply if the transfer is irrevocable during the lifetime of the beneficiaries (in a trust scenario) or of the transferee, unless the transferor derives direct or indirect benefit from the income arising by virtue of such transfer.

iii Other levies

The Finance Act 2015 has abolished the levy of wealth tax from 1 April 2016. In lieu of wealth tax, an additional surcharge (i.e., tax on tax) of 2 per cent has been levied on individuals with an annual income of over 10 million rupees.[4]

There are also state-specific stamp duties that may be levied at the time of executing documents such as trust instruments, release deeds or sale deeds. Some states impose a fixed duty while in other states the duty is a percentage of the value of the property.

iv Recent developments

Currently, India does not have inheritance tax, estate duty or gift tax.[5] A quasi-gift tax was, however, introduced into the ITA by Finance Act 2009. While the outgoing government had contemplated reintroducing estate duty, the new government does not seem to have found any merit in the same.

Under the ITA (amended by the Finance Act 2009), any sum of money (exceeding 50,000 rupees) received by individuals without consideration from any person or persons would be considered as income in the hands of the recipient and chargeable to tax at ordinary income tax rates. A similar provision also covers properties received for zero or inadequate consideration. Monies or properties received from a relative (as defined statutorily) or under a will or by way of inheritance are, however, exempt from these provisions.

---

4 Under the Wealth Tax Act 1957, certain non-business assets of a company, an individual or a Hindu undivided family (HUF) was chargeable to wealth tax at the rate of 1 per cent of the value of such assets above 1.5 million rupees. Net wealth is calculated by aggregating the value of all specified non-productive assets, less the debts that have been specifically secured on or incurred in relation to these assets.

5 Gift tax was in force from 1958 but ceased to apply on gifts made on or after 1 October 1998.

To enhance transparency in real estate transactions, the Finance Act 2013 introduced a provision in the ITA to take effect from June 2013 mandating the purchaser of immoveable property (other than agricultural land) worth over 5 million rupees to withhold tax at the rate of 1 per cent of the consideration payable to a resident transferor.

Similar to the efforts of other nations to make the super rich contribute more through taxes, the Indian government too, in pre-budget discussions in 2013, had considered different options: introducing a higher tax slab, increasing the effective tax rate on dividends to HNWIs or imposing a surcharge (a tax on tax). While the first two proposals were not enacted, a 10 per cent surcharge had been imposed on persons whose total income exceeds 10 million rupees (this measure is applicable only for one year). Budget 2014 did not alter this position. On the contrary, the income exemption granted under the ITA was increased by 50,000 rupees for individuals across slabs. Budget 2015 has kept the surcharge in place and continued the levy of surcharge on qualifying individuals.

A development with far-reaching implications is the adoption of a general anti-avoidance rule (GAAR) in the ITA. Initially introduced under the Direct Taxes Code Bill,[6] GAAR was separated out and inserted into the ITA in 2012. The implementation of the GAAR has been deferred by successive budgets. The GAAR provisions which were set to trigger on 1 April 2015 are now deferred to 1 April 2017. Further, all investments prior to 1 April 2017 would be grandfathered, thereby providing significant relief to investors using popular investment structures including Mauritius and Singapore based structures. The GAAR has been widely criticised on account of ambiguities in its scope and application, lack of safeguards and possible misuse by tax authorities. GAAR gives tax authorities considerable discretion in taxing 'impermissible avoidance arrangements', disregarding entities, reallocating income and even denying tax treaty benefits to a non-resident investor. Further, GAAR shall apply only if the main purpose of an arrangement is to obtain a tax benefit. Presumably the new GAAR provisions may not apply if an arrangement is backed up by sufficient business purpose. There needs to be more clarity on how GAAR would operate in a private wealth planning context, especially since structures are not motivated only by commercial considerations and may involve intervening steps or stages in order to effectuate an individual's or family's wishes.

v Cross-border structuring

India has entered into double taxation avoidance agreements (DTAAs) with various countries under which Indian residents may claim double tax relief. The ITA provides that it will apply to the extent that its provisions are more beneficial to the person

6 A Direct Taxes Code Bill was first proposed in 2009 to amend and consolidated the law relating to all direct taxes in India (i.e., income tax, fringe benefit tax and wealth tax). A revised Direct Taxes Code was released on 31 March 2014. However, with the dissolution of India's 15th Parliament, the bill lapsed and in his 2015 budget speech, India's Finance Minister stated that in light of the amendments made to the existing ITA, the new government did not see any merit in going ahead with the introduction of a Direct Taxes Code.

assessed to tax. Further, the ITA grants unilateral relief to residents in the event that they derive income from a country with which no DTAA exists. For an entity to benefit under a DTAA, a tax residency certificate from the country of residence and the filing of tax returns in India is mandatory. In order to benefit from the lower rate of tax under the DTAA, it is also essential for the said entity to obtain an Indian permanent account number (i.e., a tax identification number).

vi Regulatory issues

India imposes exchange control regulations mainly addressed through the Foreign Exchange Management Act 1999 (FEMA) and the rules and regulations issued under FEMA. Due to the absence of full capital account convertibility, capital account transactions are not permitted unless otherwise specified. Therefore, offshore investment by resident Indian individuals through India-sourced funds is possible but only to a limited extent and in specified situations.

In line with the amendment to the Citizenship Act 1955, the definition of non-resident Indian (NRI) (from the perspective of exchange control regulations governing foreign direct investment) is modified to cover non-residents who are either Indian citizens or overseas citizens of India cardholders. An individual who has registered as a person of Indian origin (PIO) cardholder under the erstwhile Issuance of PIO Card Scheme, 2002 is also deemed to be an overseas citizen of India cardholder. The change is to bring in consistency between exchange control regulations and the Citizenship Act, thereby bridging disconnect currently existing between the two laws. The change in definition is expected to apply to a broad range of transactions by NRIs, particularly, investment in Indian companies, partnerships and proprietary concerns, lending to Indian companies in Indian rupees and acquisition of immoveable property in India.

Further, a change to the investment norms for NRIs and PIOs has been approved such that non-repatriable investments by such individuals will be treated as domestic investments and will not be subject to foreign direct investment caps. The expectation is that this will result in greater inflow of NRI investment.

vii Outward gifts and donations

There are restrictions on outward gifts amongst family members. Previously, the Liberalised Remittance Scheme (LRS) (a scheme under which Indian-resident individuals can undertake permissible capital and current account transactions) restricted cash remittances to up to US$250,000 per individual per financial year for such transactions; initially pegged at US$200,000 this threshold was reduced to US$75,000 per financial year in August 2013 due to adverse macroeconomic conditions, brought back up to US$125,000 in June 2014 and has been increased to US$250,000 as of 26 May 2015.

viii Ownership of immoveable property

General permission is available to NRIs and PIOs for purchasing immoveable property in India but only for residential and commercial property. The purchase by such persons of agricultural land, plantation property or a farmhouse in India is not permitted unless it is inherited from a person resident in India. A foreign national of non-Indian origin,

resident outside India, cannot purchase any immoveable property in India unless such property is acquired by way of inheritance from a person resident in India.

ix Trusts

For repatriation from Indian trusts with NRI beneficiaries, all income that is dividend, interest, rent and pension can be repatriated entirely (without prior approval) to offshore beneficiaries, either directly in their offshore accounts or by way of credit to their non-resident accounts in India. Capital repatriation, however, is restricted to a limit of $1 million per person in every financial year.

On settlement of a trust by an NRI, the foreign direct investment policy expressly states that foreign investment in a trust (other than a venture capital fund) is not permitted. Indian residents are permitted to settle offshore trusts under the LRS.

x Loan arrangements between relatives

A resident Indian individual can borrow sums of up to US$250,000 or its equivalent from close relatives staying outside India subject to certain conditions. An individual resident can lend money within the overall limit of US$250,000 (as per the aforementioned notification) per financial year under the exchange control scheme referred to above, to meet the borrower's personal or business requirements in India, subject to certain conditions.

xi Issues affecting entrepreneurs at the proprietor level

Till date, offshore companies have been treated as 'non-resident' in India unless wholly controlled and managed from India. The consequence of this is that the income of such offshore company is not taxable in India unless distributed to an Indian resident shareholder. Further, even in situations where the offshore company is 100 per cent owned by Indian residents and has majority Indian directors, it has been held that there should be no residence in India if board meetings are held outside India. The Finance Act 2015 has moved to a more subjective test of place of effective management (POEM), and considers a foreign company resident in India if its POEM is in India in the relevant financial year. POEM is to be applied taking the relevant financial year as a whole into consideration.

POEM has been defined to mean 'a place where key management and commercial decisions that are necessary for the conduct of the business of an entity as a whole are, in substance made'. For example, in the situation described above, where an offshore company has 100 per cent Indian resident shareholders, majority of Indian directors and one director offshore, the company could now be considered Indian resident under the POEM test. In that case, the worldwide profits of the offshore company would be taxable in India. Even if the shareholding is less than 100 per cent, with some portion held by non-Indian investors, Indian promoters may still want ownership and management control, which could create exposure. This could impact a range of structures, including outbound investment structures by Indian business families and personal wealth/carried interest structures such as personal holding companies.

To improve corporate governance and protect minority shareholders, the Securities and Exchange Board of India (SEBI), India's capital markets regulator, directed

that all listed companies must have a 25 per cent minimum public holding, failing which stringent action would be taken on promoters or promoter groups, such as the freezing of voting rights and corporate benefits and suspending trading in relevant securities. To ensure compliance with this 25 per cent minimum public holding, a period of three years had been provided, which expired in June 2013. The SEBI has been taking strict action, including suspending the trading of the shares of the company in question. Additionally, the SEBI has notified new corporate governance norms for listed companies in India by amending the listing regulations. According to the new rules, the board of directors of every listed company shall necessarily have to 'satisfy themselves that plans are in place for orderly succession for appointments to the Board and senior management'. These rules, which have applied from 1 October 2014 are expected to have substantial implications for companies, especially closely held, family-run companies.

Another important consideration in the context of listed companies is the SEBI (Substantial Acquisition of Shares and Takeover) Regulations 2011 (the Takeover Code). The Takeover Code prescribes certain threshold limits in respect of the acquisition of shares or voting rights or, in other words, change of control of the company that would trigger disclosure and public offer requirements. The Takeover Code provides for disclosures to be made when the acquirer (along with persons acting in concert with it) holds more than the stipulated percentage of shares in such company; and an open offer to be made when the acquirer acquires more than the stipulated percentage of shares or voting rights in, or acquires control of, a public listed company.

Under Indian trust law, a trustee is the legal and beneficial owner of trust property and this status continues under the Takeover Code. Where a trust holds shares in a listed company on behalf of the beneficiaries, the trustee would be the legal and beneficial owner. In a situation where there is a change in trustee without any change in the beneficiaries, the trustee would have to transfer shares held in its name to the new trustee, who would then hold the shares on behalf of the beneficiaries. In such a situation, a change in trustee would effectively result in transfer of shares from one trustee to another and may create issues under the Takeover Code.

Recently, the SEBI considered the application of the Takeover Code in a situation involving the settlement of shares of a closely held company (which held a 70.3 per cent stake in a listed company) in several family trusts. To understand whether a settlement might result in an indirect transfer of shares or control in the target company, thus triggering a mandatory offer requirement under the Takeover Code, the promoter, in his capacity of trustee of the family trusts, approached the SEBI for an exemption from the application of the Takeover Code. The SEBI granted an exemption order as the transaction was merely a family arrangement involving a restructuring of shareholding and did not necessarily result in a change in control of the underlying company.

Such orders are, however, fact-specific and the provisions of the Takeover Code must be considered before making a settlement of shares in a trust.

In March 2015 with a view to facilitating the easier delisting of companies from recognised stock exchanges, SEBI introduced changes to the SEBI (Delisting of Equity Shares) Regulations 2009 (the Delisting Regulations). Earlier only promoters could initiate the delisting process. However, by virtue of a simultaneous amendment to the Takeover Code, an acquirer may delist the company pursuant to an open offer in accordance with the Delisting Regulations provided that he makes a statement upfront

declaring his intention to delist at the time of making the detailed public statement. This has greatly simplified and reduced the take private process to a single step mechanism. This has proved extremely helpful to those acquirers who acquire large stakes in listed companies with the intent of taking the company private in future.

III SUCCESSION

i Personal laws in India

Indian society is composed of different groups having their own personal laws, some aspects of which have been codified. The presence of both statutory and customary law has led to personal laws being complex and unsettled in some aspects.

The colonial British government attempted to harmonise succession laws by enacting the Indian Succession Act, but this attempt was not completely successful. The post-British era government made another attempt by including in the Directive Principles of State Policy in the Indian Constitution, a directive to implement a uniform Civil Code that would apply to all religious groups. This was difficult because of the reluctance of various religious groups to compromise on their customary practices. Consequently, Hindus have their own personal law (part codified, part customary); Muslims have their own textual law of inheritance (the Islamic Law on Succession), while Parsees, Christians and others are covered under the more secular Indian Succession Act 1925. All wills (except Muslim wills) are, however, governed under the Indian Succession Act 1925 for the purposes of execution, probate, etc. The only exception to this is the state of Goa, which is governed by the Portuguese Uniform Civil Code (which also provides for community property rules). There are also regional differences within certain personal laws.

It has been observed that when it comes to personal laws, courts are usually reluctant to impose a public law standard to adjudge personal law matters. This attitude is well-reflected in a judge's observation in a case challenging the constitutional validity of divorce provisions under the Hindu Marriage Act 1955 when he said: 'Introduction of constitutional law in the home is most inappropriate. It is like introducing a bull in a china shop.'[7]

The difficulty faced in harmonising succession laws and constitutional directives on uniform personal laws is demonstrated by the decision of the Supreme Court in *Mohd Ahmed Khan v. Shah Bano Begum*,[8] pertaining to a Muslim woman's right to maintenance. The court expanded the scope of such a right (otherwise limited under Muslim personal law) holding that if a divorced Muslim woman is not capable of maintaining herself, she is entitled to claim alimony as provided under the Code of Criminal Procedure 1973, a code that is applicable to all, irrespective of caste or religion; however, following societal criticism of this judgment, the government enacted the Muslim Women (Protection of Rights on Divorce) Act 1986, which had the effect of diluting the above judgment and restoring the position under Muslim personal law.

7 *Harvinder Kaur v. Harmander Singh Choudhry*, AIR 1984 Delhi 66.

8 1985 SCR (3) 844.

ii Developments in succession law

Succession law has largely remained static since there have been few initial codification and recent high-impact developments.

A noteworthy development that took place in 2005 was the admission of daughters to the coparcenary system (i.e., the right by birth to an interest in family property). Under Hindu law, an HUF consists of a common ancestor and all his lineal male descendants and their wives and unmarried daughters. A coparcenary is a narrower institution within an HUF. Traditionally, the coparcenary consisted only of male members, but through the 2005 amendment to the Hindu Succession Act 1956, daughters now have the same rights and liabilities in the coparcenary property as sons.

HUFs have been faced with a common issue of demonstrating whether property bequeathed is ancestral or self-acquired property. The Hindu Succession Act 1956 permits a coparcener (family sub-group comprising lineal descendants of the ancestor) to dispose of his or her undivided interest in HUF property under a will. The Supreme Court of India seems to have put to rest the debate for the time being by stating that the Karta had no right to change the character of joint family property by transferring it under a will without the consent of other co-parceners.[9]

As per the ITA, gifts between specified relatives are not taxable and Indian capital gains apply differential rates for assets held for a short-term (up to 40 per cent tax) and long-term period (up to 20 per cent tax). Gifted assets are allowed the benefit of the predecessor's holding period in determining the applicable right while transferred assets are not. Family settlements by which assets, especially shares, are distributed or allocated among the members of the family or family-held companies are a common feature under Indian law. The Allahabad Bench of the Income Tax Appellate Tribunal had held that if a closely held company receives shares from shareholders who belong to the family pursuant to a family arrangement among such shareholders, the receipt will not be considered a gift but a transfer, since it would not satisfy the two essential conditions: the transfer must be without monetary consideration; and the transfer must be voluntary. However, the Mumbai Bench of the Income Tax Appellate Tribunal has recently held that amounts received by an individual under a family settlement cannot be taxed as capital gains. The Tribunal held that such a family settlement does not involved a transfer of title, but is akin to a partition of family assets among family members, which is not regarded as a transfer under the ITA.[10]

The Bombay High Court in a recent judgment[11] has reiterated that that the nominee of a share or financial instrument is only a custodian and the legal heirs have ultimate right as per the relevant succession law. The Insurance Amendment Act of 2015 has introduced 'beneficial nominees', where if a person in a life insurance policy for his life names the spouse, parents or children as the nominees, such nominees will be entitled to receive the amount to the exclusion of other legal heirs.

9 *V.K. Surendra v. V.K.Thimmaiah* ((2013) 10 SCC 211).

10 *Urmila Mahesh Nathani v. Income Tax Officer*, TS 396 ITAT 2015 (Mum).

11 *Jayanand Jayant Salgaonkar v. Jayshree Jayant Salgaonkar*, 2015 SCC OnLine Bom 1221

iii Relevant cross-border developments

India gives due regard to private international law, where, in the event of intestate succession, the inheritance of moveable property is governed by the law of the deceased's domicile, while inheritance of immoveable property is governed by the law of the place in which the property is situated. Therefore, on the demise of a foreign citizen domiciled in India or an Indian citizen domiciled abroad the following rules should be applicable:

Domicile	*Immoveable property*		*Moveable property*	
	India	Abroad	India	Abroad
India	Indian law	*Lex situs*	Indian law	PIL rules applicable
Outside India	Indian law	Law of domicile	Law of domicile	Law of domicile

Where the law of the nation to which the deceased foreigner belonged at the time of death refers the inheritance issues back to India (i.e., the place in which the estate is situated), the applicable law that governs the deceased's estate in India takes precedence. An offshore Will should be enforceable in India as long as it has been certified by an appropriate authority in the jurisdiction.

iv Execution of foreign divorce decrees

Foreign judgments are conclusive under Section 13 of the Code of Civil Procedure 1908 (CPC) if they are in accordance with the conditions set out in it.[12] These may broadly be said to be conditions ensuring that the foreign decree was procedurally and substantively valid and not in breach of Indian law. Foreign judgments (including foreign divorce decrees) passed in reciprocating territories[13] are enforceable by way of execution proceedings in India. Courts in India may refuse to enforce them, however, if they fail to comply with any of the conditions set out in Section 13 of the CPC.

v FATCA obligations

Indian HNWIs who are US taxpayers, trustees or financial institutions who maintain accounts of such persons have taken heed of their compliance obligations under the

12 Under Section 13 of the CPC, the court may refuse execution of a foreign judgment as inconclusive and unenforceable in the following circumstances:
a not pronounced by a court of competent jurisdiction;
b not given on merits;
c based on incorrect view of international law or a refusal to recognise the law of India;
d opposed to natural justice;
e obtained by fraud; and
f breach of any law in India.

13 'Reciprocating territory' means any country or territory outside India that the central government may, by notification in the Official Gazette, declare to be a reciprocating territory for the purposes of this section; and 'superior courts', with reference to any such territory, means such courts as may be specified in the said notification.

Foreign Account Tax Compliance Act (FATCA), the US legislation that targets tax non-compliance by US taxpayers with foreign accounts. An agreement to implement FATCA was signed between India and the United States on 9 July 2015 to take effect from 30 September 2015. Because of this, financial institutions in India are now required to make FATCA disclosures (through the Central Board for Direct Taxes) to the US Internal Revenue Service – this would primarily relate to investments by account holders liable to tax in the United States. Due to the broad definition of foreign financial institutions, FATCA obligations will apply to family trusts and possibly even HUFs (if considered a trust or a non-financial foreign entity).

vi Classification of Indian entities offshore and offshore entities in India

Classification of entities across jurisdictions assumes importance in many private wealth-planning structures, especially in a cross-border context.

For example, a HUF is considered to be a distinct taxpayer in India but may not be accorded the same treatment in other jurisdictions. Close approximations for a HUF under foreign law may be a trust or a partnership – the manner of characterisation would have implications on non-Indian estate tax consequences, or FATCA consequences, for example, on account of other jurisdictions not understanding the role of the HUF manager (who is known as the Karta). Similarly, hybrid entities such as LLCs, S-corps or foundations are not recognised in India and use of such entities may create characterisation issues. A foundation may be considered either as a company or a trust under Indian law – this leaves the issue open of whether membership interests in a foundation should be considered the 'moveable property' of a deceased and subject to Indian succession laws. Such cross-border differences in characterisation of structuring vehicles affect the tax and regulatory benefits available to the structure and subtle differences must be carefully considered.

vii Applicable changes affecting personal property

The Indian government set up a panel to review alimony and maintenance laws that had not kept up with the changes in societal and economic conditions. The government's initiative was spurred on by the decision of the Bombay High Court in 2011, which had held that 50 per cent of the husband's assets should be transferred to the wife under a divorce. The review panel proposed that in order to provide legal recognition to women as equal partners in a marriage and to recognise their contribution to the household, all assets acquired by a couple post-marriage should be viewed as joint property, regardless of who bought it. It also proposed that such joint property should be divided equitably in the event of separation or desertion. These proposals were incorporated in the Marriage Laws (Amendment) Bill 2010.

These amendments resulted in more debates both within the government and in the wider society, forcing the government to refer the matter to a group of ministers (GoM). The GoM had given its recommendations proposing that instead of a 50 per cent share, the courts should be empowered to decide the compensation amount from the husband's inherited and inheritable property for the wife and children upon finalisation of divorce proceedings. Although these recommendations were well received,

the Marriage Laws (Amendment) Bill 2010 has now lapsed in the parliament in India.[14] In order for the new government to propose the amendment, it has to undergo the entire process of proposing a bill all over again.

IV WEALTH STRUCTURING AND REGULATION

i Wealth-planning vehicles

Because of limited options available for wealth-planning vehicles in India, the private trust has become popular because of its flexibility and adaptability. It assists in achieving a wide range of objectives of the Indian HNWI, by providing:

a separation of ownership from actual control and management over the assets and consolidation of assets;
b professional management and guidance on onshore and offshore passive investments;
c business and family governance, and avoidance of family and business disputes;
d the chance for family members to pursue other professional interests while providing for their personal needs;
e the accumulation, management and disposal of an estate as per the desires of the estate owner without going through time-consuming and litigious probate procedures;
f contributions to religious and charitable causes; and
g other financial, tax and business planning.

India gives due recognition to foreign trusts. Foundations are not recognised in India and there are few precedents on how an offshore foundation would be treated for Indian-resident beneficiaries.

The Indian concept of trust is similar to that of many common law jurisdictions. Private trusts, not being public charitable trusts or private charitable trusts, are governed by the Indian Trusts Act 1882 (the Trusts Act). In India, a trust is not a separate legal entity but an obligation. The Trusts Act defines a trust as being a legal obligation annexed to the ownership of property and arising out of a confidence placed in the trustee by the settlor, for the benefit of the beneficiaries as identified by the settlor including or excluding the settlor himself or herself. Under the Trusts Act, the trustee of an Indian trust is the legal and the beneficial owner of the trust property. India does not recognise 'beneficial ownership' in its trust laws and the beneficiaries (regardless of whether they are Indian residents) to such a trust only have a beneficial interest in such trust property.

Family (private) trusts may be set up either during one's lifetime or under a will (in either case, orally or under a written instrument). A trust encompassing immoveable

14 Under the Indian parliamentary process, any bill that is pending in the 'House of the People' (i.e., the Lok Sabha) lapses on the dissolution of the Lok Sabha. Due to the elections in 2014, all bills pending in the House of the People, including the Marriage Laws (Amendment) Bill, 2010 have lapsed.

property must, however, be declared by a registered written instrument.[15] A trust may be set up either as a revocable trust (that is, a trust that can be cancelled by its settlor at any time); or as an irrevocable trust (that is, a trust that will not come to an end until the terms of the trust have been fulfilled); and each of the above may be either of the following:

a a discretionary trust: an arrangement whereby the trustee may choose, from time to time, who (if anyone) among the beneficiaries is to benefit from the trust, and to what extent; or

b a determinate trust: an arrangement whereby the entitlement of the beneficiaries is fixed by the settlor, the trustees having little or no discretion.

For the purposes of taxation, trusts in India are not considered to be separately taxable entities – and the income of the trust is taxed either in the hands of the trustee or in the hands of the beneficiaries. The obligation of the trustee to pay tax would be in the capacity of a representative assessee.

For determinate trusts, the trustee would be assessed to tax to the same extent that would be recoverable and levied upon the beneficiary. At the same time, the trustee is entitled to recover the tax amount from the beneficiary. If the income of the trust includes the profits and gains of a business or profession, then such income would be taxed in the hands of the trustee at the maximum marginal rate (now 30 per cent).[16] For discretionary trusts, income would be taxable at the maximum marginal rate.

Given the dated trust laws, the Supreme Court of India recently stated that income of a discretionary trust cannot be taxed in the hands of a beneficiary unless distributed to the beneficiary.[17] Accordingly, the beneficiaries of a discretionary trust should not include any part of the trust's income in their individual returns unless it is actually received by them.

ii Disclosure and transparency

The Black Money (Undisclosed Foreign Income and Assets) and Imposition of Tax Act (the Black Money Act) has come into effect from 1 July 2015. The Black Money Act requires Indian residents to file returns in respect of their undisclosed foreign income and assets in a bid to identify and bring to tax such income which may have escaped being taxed in India. The Black Money Act also applies to Indian-sourced income of non-residents that has been the source of investment for assets abroad. The Black Money Act contains provisions under which the failure to disclose foreign income and assets is punishable with a tax of 30 per cent and penalty of 90 per cent and in some cases, with imprisonment. The government has also introduced a compliance scheme, available till 30 September 2015 under which a taxpayer may declare his undisclosed foreign assets.

15 The trust deed has to be registered under the Indian Registration Act 1908.

16 Maximum marginal rate means the rate of income tax (including surcharge) applicable in relation to the highest slab of income in the case of an individual, association of persons or, as the case may be a body of individuals.

17 *Commissioner of Wealth Tax, Rajkot v. Estate of Late HMM Vikramsinhji of Gondal*, 2014 (6) SCALE 529.

Under the compliance scheme a tax at the rate 30 per cent, along with penalty of 30 per cent will be imposed on the value of the assets declared.

The Finance Act 2015 passed by Parliament modifies the current disclosure requirement such that all resident individuals who are either beneficial owners or beneficiaries of foreign assets (including financial interest in any entity) or who have signing authority in any account outside India are covered. The term 'beneficial owner' has been defined to mean 'an individual who has provided, directly or indirectly, consideration for the asset for the immediate or future benefit, direct or indirect, of himself or any other person.' The term 'beneficiary' has been defined to mean 'an individual who derives benefit from the asset during the previous year and the consideration for such asset has been provided by any person other than such beneficiary'.

A person who is responsible to pay a non-resident any interest or any sum chargeable to tax under the ITA is mandatorily required to withhold tax on such interest or sum. Until recently, any person responsible for paying to a non-resident any sum chargeable to tax was required to furnish information relating to the payment of such sums. The Finance Act 2015 has extended this requirement to sums which are not chargeable to tax as well. This obligation will come into effect from 1 June 2015.

In India, the anti-money laundering regime is governed by the Prevention of Money Laundering Act 2002 (PMLA). The PMLA criminalises money laundering and provides for confiscation of property derived from, or involved in, money laundering. The PMLA and the rules framed under it provide that whoever directly or indirectly attempts to indulge, knowingly assists, is a party to or is actually involved in any process or activity connected with the proceeds of crime (i.e., property, value of such property derived or obtained, directly or indirectly, as a result of criminal activity) and presents it as untainted property shall be guilty of the offence of money laundering. Every banking company, financial institution and intermediary is required to maintain records of prescribed transactions, furnish information of transactions to the specified authority and verify and maintain records of the identity of all the clients in a prescribed manner. Further, in the PMLA (Amendment) Act 2012, the definition of money laundering has been expanded to cover mere 'possession' of the proceeds of a crime. Further, the minimum threshold for initiating money laundering cases has been removed. Due to the Black Money Act, 'wilful evasion of tax' is a new scheduled offence under the PMLA. However, those declaring offshore assents under the Compliance Scheme of the Black Money Act will not be considered to have committed the above offence under the PMLA.

The time limit for an issue of notice for reopening an assessment (under both income and wealth tax) was increased from six to 16 years if the income is in relation to any offshore asset (including financial interest in any entity) is chargeable to tax and has escaped assessment.

India has also entered into tax information exchange agreements (TIEAs) with most of the offshore island jurisdictions to expand its information collection system. Further, the Indian government has allowed for the blacklisting of countries that do not cooperate in sharing information about suspected tax evaders.

There have been concerns in recent years that foreign direct investments into India routed through Mauritius were a means of money laundering and round tripping of illicit funds. To address this concern, India has been trying to renegotiate the DTAA to

have checks and balances in place on foreign investments into India through Mauritius. A major focus of these negotiations has been insertion of a 'limitation of benefits' clause under the DTAA with Mauritius and a revised agreement is expected shortly. To facilitate exchange of information, India has also been pushing for a TIEA with Mauritius.

The Central Board of Direct Taxes had issued the Income Tax (14th Amendment) Rules 2013 on 2 September 2013 with respect to the payment of taxes to non-residents (not being a company or to a foreign company). Under these Rules, additional disclosures were to be made by any person responsible to make payments to a non-resident. The Reserve Bank of India, the central bank regulating exchange control in India, has by way of a circular informed authorised dealers (dealers or banks authorised to deal in foreign exchanges) to comply with the provisions of the Rules notified by the Central Board of Direct Taxes.

Additionally, in a move to ensure greater disclosure, the Ministry of Corporate Affairs released a circular in January 2014 stating that the views of, *inter alia*, the Income Tax Department need to be taken in case of any arrangement or compromise, or reconstruction or amalgamation.[18] For this the Income Tax Department shall be given 15 days from the receipt of the notice to file a response in the court.

iii Succession plans for listed companies

As mentioned above, the SEBI has notified new corporate governance norms for listed companies in India by amending the listing regulations, applicable from 1 October 2014. Accordingly, the board of directors of every listed company shall necessarily have to 'satisfy themselves that plans are in place for orderly succession for appointments to the Board and senior management'.

iv Arbitration of trust disputes

Arbitration is used because the resolution of disputes takes years in Indian courts. However, the arbitrability of trust disputes has been questioned, since the beneficiaries to a trust are not 'parties' to the arbitration agreement. The Bombay High Court examined the issue, in the case involving a trust created by a settlor in favour of six beneficiaries, all of whom were minors at the time the trust was created.[19] The trust deed specifically included a clause for the resolution of disputes by way of arbitration 'between the Trustees, or the Trustees and beneficiaries, or the beneficiaries inter se'. The beneficiaries were not signatories to the trust. When a dispute arose between some beneficiaries and the trustee and arbitration was sought, the court considered the issue of whether beneficiaries, who were not signatories to the trust, could be bound by the obligations under the trust deed, particularly when they were minor without the capacity to enter into a contract. It was held that 'the definition of 'party' has to be interpreted harmoniously and the beneficiaries, who were referred in the said trust deed, had to be construed as if the beneficiaries were also parties to the arbitration

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18 Arrangement, compromise, reconstruction and amalgamation are court driven processes where the concerned companies approach the court requesting it to sanction the scheme in question.

19 Unreported case of *Mr. Jayesh Dinesh Shah v. Kaydee Family Trust* (March 2013).

agreement.' However, this issue has not been resolved yet since the Delhi High Court has taken the opposing view in a decision.

V CONCLUSIONS AND OUTLOOK

Despite an unprecedented global recession, India has been one of the fastest growing economies in the world over the last four to five years. However, India's GDP growth has been reducing every quarter, from 4.8 per cent in third quarter of 2013 to 4.7 per cent in the fourth quarter of 2013. The first quarter of 2014 saw this reduce further to 4.6 per cent.[20] However, the new government in India, which took over in June 2014, has indicated that it will implement investor-friendly measures with investment protection playing an important role. These seem to be having the required effect with India's GDP growth expanding to 7.5 per cent in the first quarter of 2015.

As mentioned above, globalisation has brought about a change in attitude in both legislators and wealthy individuals towards wealth planning. That said, a major challenge for wealth planning in India is the complex web of personal laws. Harmonising personal laws or enacting a uniform civil law has proved to be socially difficult and politically unpalatable. Further, in comparison with laws that govern planning for purely commercial ventures, laws that affect private wealth planning have received little attention. This has led to a mismatch in the pace and extent of modernisation of laws that affect the larger universe of wealth planning. Addressing private wealth planning should not be limited to targeted changes in tax law alone. To build a framework conducive to private wealth planning that recognises legitimate concerns motivating inter-generational wealth transfer, what is also required is clarity and flexibility in the types of wealth-pooling or holding vehicles that may be possible. Only time will tell what form these options will take, but it is clear that private wealth planning in India is maturing and more robust measures in this field are expected.

20 Shashi Tharoor, 'How India Survived the Financial Crisis', available at www.project-syndicate.org/commentary/how-india-survived-the-financial-crisis#1z13sJMwhlF27WvG.99.

Appendix 1

ABOUT THE AUTHORS

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Joachim Saldanha is an associate at Nishith Desai Associates. He is part of the private client practice at Nishith Desai Associates.

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