Liechtenstein and EU Interest Tax on Savings

No Compromise on Liechtenstein Banking Secrecy

In June 2003, the European Union Member States agreed on a directive to harmonise the taxing of cross-border interest payments on private individuals within the Union. The directive which is to be adopted into National Law, after contracts on «equivalent measures» between the European Union and Third Party States have been signed, will finally come into force on 1st January 2005. Liechtenstein, which is one of the Third Party States, is seeking a similar solution to Switzerland, based on the premise that the strict Liechtenstein Banking Secrecy will remain unaffected.

For many years, there have been tough political negotiations on an EU interest tax agreement: In January 1992, the then 12 member states of the European Community, signed a contract in Maastricht (Netherlands) which came into force in November 1993. The Union's most ambitious goal was, without any doubt, the creation of a European Economic and Currency Union.

Long Struggle on EU Common Tax Package

As a direct result of the Economic and Currency Union, the Council of Europe Economic and Finance Ministers (ECOFIN) agreed in June 2003 in Luxemburg after nearly 14 years of debate on a unified tax package.

At the heart of this directive 2003/48/EC is the unified taxation of interest within the European Union. This envisages the mutual exchange of information between EU member states on interest payments paid to an investor whose place of residency is in another EU State.

Gradual Application

Lack of commitment among EU members has, however, led to a step-by-step introduction of the directive. Belgium, Luxemburg and Austria have, at least for the time being, opted for the transitional agreement and have not sanctioned the automatic exchange of information. The three member states fear that an introduction of the automatic exchange of information would affect their financial markets' competitiveness, encouraging investors to move their accounts to Switzerland and other Third Party States, offering more attractive conditions. These regulations do not provide for the reporting of income to the finance authorities of the state of residency. Contrary to the other EU States, Belgium, Luxemburg and Austria, as of 1st January 2005, will place a source tax on interest payments to non-resident EU citizens. Initially, this will be 15% and will increase to 20% and by 2011 to 35% in three-year periods. 75% of the income generated by this source tax will be paid to the financial authorities of the investor's state of residence without further notification, 25% will remain in the depositing country.

As a precondition to joining the automatic information exchange system, Belgium, Luxemburg and Austria demand from the EU that a similar agreement is reached with Third Party States (Switzerland, Andorra, Liechtenstein, Monaco and San Marino) as well as associated territories (e.g. the Channel Islands and the Dutch Antilles).

These Third Party States should commit themselves by contract to introduce a cross-border interest tax based on the EU model. The practical application of this could be by means of reporting of income to the country of residency of the EU investor or by levying a source tax on interest paid.

Only Individuals to be Affected by European Interest Tax

The Movement of Capital to the USA to Be Blocked by Bilateral Agreements

It is still not clear within the EU, how the USA can be persuaded to cooperate with the European directive. In paragraph 24 of the interest tax directive, the danger of the «flight of capital» to the USA is explicitly mentioned.

The USA has repeatedly declared that it is not currently prepared to agree to the automatic exchange of information. For the time being, they would prefer the exchange of information on request. It remains to be seen, as with the Third Party States and Associated Territories, in how far the EU can be successful in negotiating a compromise.

The Swiss Withholding Tax Model to Protect Banking Secrecy

In actual fact, the EU Member States fear the transfer of capital to Switzerland more than to the USA. In the year 2000, the Swiss Government emphatically stated that it was not in the interest of Switzerland to encourage business which would circumnavigate the new EU directive.

That is why Switzerland developed a model for the implementation of the EU directive. The Swiss Model envisages that a withholding tax, equivalent to the source tax in Belgium, Luxemburg and Austria, will be levied on interest payments to individuals resident within the EU.

An automatic exchange of information has been declined in order to protect banking secrecy.

Liechtenstein Negotiations Focus on the Protection of Strict Banking Secrecy

The Principality of Liechtenstein, which holds close economic ties to Switzerland, has followed Switzerland's negotiations with the EU with great interest.

The Liechtenstein Government is currently working on a proposal which in essence is equivalent to that of Switzerland. The proposal provides for the introduction of a withholding tax which will be divided between the country of residency of the EU investor and Liechtenstein. In order to safeguard banking secrecy, which is protected by law and the privacy of the investor, Liechtenstein irrevocably rejects the automatic exchange of information.

What the final agreement with the EU will look like, depends on the results of negotiations between the EU, Third Party States and the USA. Liechtenstein will, without doubt, pursue an agreement which will guarantee its present competitiveness and future prospects as a financial service center.

An absolute precondition, in this case, is the preservation without any compromise of the strict Liechtenstein Banking Laws, in their current form.

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Publisher and Copyright Owner:
ArComm Trust Company Establishment

Responsible for Contents
Law Office of Dr. iur. et lic. oec. Norbert Seeger

Editing and Arrangement
Dr. iur. et lic. oec. Norbert Seeger

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Interest Tax in EU and Selected Countries

National Tax Rates – 2002[1)]

General Rates in Percentage [2)]

	Interest Payments on Fixed-Interest Securities to		Interest Payments on Bank Deposits to		Cross Border Interest Payments to Citizens in (other) EU States[9)]
States	Residents	Foreigners	Residents	Foreigners	
Belgium	15[3)]	–	15[3)]	–	15
Denmark	–[6)]	–	–[6)]	–	AIE
Germany	31,65	–	31,65	–	AIE
Finland	29[3)]	–	29[3)]	–	AIE
France	25[4) 6)]	15[5)]	25[4) 6)]	15[5)]	AIE
Greece	15[3) 5)]	15[3) 5)]	15[3) 5)]	15[3) 5)]	AIE
Ireland	20	20[5)]	20	–	AIE
Italy	12,5/27[3) 5)]	12,5/27[5)]	27[3)]	–	AIE
Luxemburg	–	–	–	–	15
Netherlands	–[6)]	–	–[6)]	–	AIE
Austria	25[3) 7)]	–	25[3) 7)]	–	15
Portugal	20[3)5)]	20[5)]	20[3)]	20	AIE
Sweden	30[3) 6)]	–	30[3) 6)]	–	AIE
Spain	18[6)]	18[5)]	18[6)]	18[5)]	AIE
United Kingdom	20[6)]	20[5)]	20[9)]	–	AIE
Switzerland	35[8)]	35[8)]	35	35	15
USA	–[6)]	30[5) 6)]	–[6)]	–[6)]	–
Japan	20[3) 6)]	15	20[3) 6)]	20[3) 6)]	–

1) In June 2003, the ECOFIN Council reached a political agreement on an EU directive governing cross-border taxation on interest payments to private individuals within the EU. Switzerland and other Third Party States (e.g. Liechtenstein, Monaco etc.) also agreed to introduce a withholding tax on interest gained by EU citizens.
2) General Rates (not double-taxation agreements) without special rates or deviating from the rules on company capital income (parent/daughter company EU directive)
3) Tax payment in lieu
4) Normally taxation on income, unless an option was taken on income tax relief through general taxation
5) Various tax rates and relief for interest gained out of certain investments and accounts offered exclusively to foreigners
6) Automatic Information Exchange (AIE)
7) Income, estate and hereditary tax is covered by this tax
8) Only applies if the person owing tax is resident.
9) The EU directive envisages that the 12 EU Member States as of 2005 will present automatic information exchange (AIE) to the tax offices of the tax payer in other EU States. Belgium, Luxemburg and Austria will levy a source tax at the following rates: from 2005 15%, from 2008 20% and from 2011 35%. These rates also apply to Switzerland.

Source: Deutsche Bank Research

Transfer of Office in Liechtenstein

Hereditary Prince Alois Assumes Executive Powers from Prince Hans-Adam II.

On 15th August 2004 Hereditary Prince Alois will assume executive powers from Prince Hans-Adam II. who, although remaining Head of State, will withdraw from active political duties.

The Prince made this known on 15th August 2003, the Liechtenstein National Holiday. He assumed executive powers in 1984 and became Regent after the death of his father in 1989.

Prince Alois, who is now 35 years old, completed grammar school and entered officer training at the Royal Military Academy in Sandhurst. He served with the Coldstream Guards in Hongkong and London before studying Law in Salzburg. On completion of his studies he worked in an auditing company in London as well as in the Prince of Liechtenstein's Estate Administration.

The Hereditary Prince has, from an early age, been prepared by his father for his role as Head of State. He has regularly attended meetings and discussions with representatives of the Government as well as taking on representative duties.

During the hereditary oath taking ceremony on 15th August 1990, he took the oath of allegiance to the constitution at the side of his father.

In 1993, Hereditary Prince Alois married Her Royal Highness Duchess Sophie in Bavaria. They have four children.

F.L.BULLETIN

The International Monetary Fund (IMF) has given the Liechtenstein Financial Market Place a good reference. In the final assessment procedure report in September 2003, special emphasis was placed on the high quality and modern laws as well as the successful measures in the fight against international money laundering.

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Measures taken by Liechtenstein in the Financial Sector have once again found recognition. Back in June 2001 the Financial Action Task Force (FATF) of the OECD rated Liechtenstein as a State that actively supports the fight against money laundering.