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LIFE INSURANCE IN LUXEMBOURG

By Christophe Maulny and Alexane Palide - Anthony & Cie

As part of our International Family Office core business, we often work on interesting creative wealth strategy as well as real estate planning that would have been very difficult to envisage before meeting the person at the source of inspiration.

In spite of being confronted with different diversified situations, which is one of the charms of the profession, one's must find the creativity which is necessary to resolve these kinds of needs.

We were recently approached by a couple of prospective clients, both of Irish nationalities and Abu Dhabi tax residency. They wished to change their way of life. Their concern was providing the best education possible for their three teenagers children. Their wishes were to come back to live in Europe and especially in the sunny South of France. It also has the advantage of well-known universities in a pleasant place to live.

Among their different assets, the couple owned real estate assets in Abu Dhabi and Ireland. They had bank accounts and pension plans. They are also shareholders of a private unlisted company based in Abu Dhabi.

The distribution of dividends from this company brings them approximately € 900,000 per year of income depending on the EURO/AED (dirham of the United Arab Emirates) which brings them their principal revenue.

In Abu Dhabi, the dividend is not liable to any tax, and they are also not subject to social charges. Referring to tax treaties, we quickly understand that changing their tax residence to France would create major tax liabilities.

In French practice, these dividends would be subject to income tax but aren't entitled to any tax credit as it is well known that there is no taxation in United Arab Emirates. If one takes into account the family tax restructuration, it already seems that the € 900,000 of dividend revenue would be taxed for a global amount of € 510,000 and a total of € 371,000 directly subject to income tax and questionably the French tax authorities will try to collect € 139,000 for the social aspects. Welcome to France!

Beyond the disappointment of this situation, we needed to find a satisfactory solution, and this seemed clear to us, and a strategy could be put in place to mitigate this substantial potential liability. It is all about a life insurance policy from Luxembourg which offers solutions for an overall wealth management strategy.

The solution concerns the tax advantages with a partial takeover, in other words, a change of ownership. This obviously needs to take place before changing the residency to avoid French capital gains taxes.

The insurance policy is suitable for all families with International business operations and also residing in multiple tax jurisdictions. The purpose of this interesting mechanism is the right to hold diversified assets and for our client's case, the shares of the Abu Dhabi unlisted Company.

Client's profile allowed them to subscribe to a Luxembourg life Insurance contract type D, which means that the net wealth worth of the subscriber has to be higher than 2.5 million euros and the net value of their life insurance policy contract has to be higher than 1 Million euros. For your information, this kind of specific contract is determined by the Luxembourg Insurance Commission rules and regulations.

Such contract has the possibility to hold any type of assets, including 'Emiratis Private Equity' securities from our clients. The amount is limitless, and the contract can be in multi-currency, which represents an essential criteria for the solution proposed. However, the operation is more complex than it seems, firstly the motivation of the client is essential, with a beneficial growth economic sense.

First of all, this operation requires the shares to be initially transferred to the Luxembourg life insurance company, as stated before and also before French residency, which will then be settled into the client's life insurance policy.

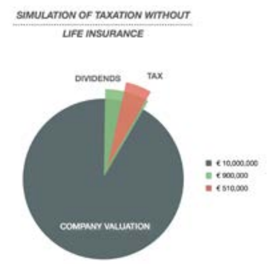
For a successful operation, several obligations remain:

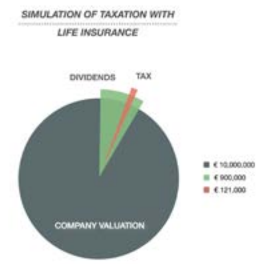
- The insurance company does not want to have an operational role in the unlisted company. If the clients have an operational function conditioned to the possession of the securities being transferred, it is necessary to find a contractual arrangement to ensure that this function is assured with a different shareholder structure.
- Usually, like any buyer, the insurance company will request the normal documentation such as company statutes, the shareholders register, the audited annual accounts, an analysis of the company describing its activity and its market, a local legal opinion confirming the transferability of the securities, plus any documents necessary for a thorough "due diligence".
- Finally, the valuation of the company must be carried out; the justification of the valuation has to be shown to Luxembourg insurance commissioner. It is obviously a critical step.

For our client's case, the valuation has been established by the equivalent of the local auditor. The evolution of the company's turnover over the last ten years is considered, but also the debt, the assets held, the strength of the activity, the market and the gross operating profit GOP. The company valuation was compared with similar companies doing the same activity with an available valuation either through quotation or following transactions.
Without forgetting a discount for illiquidity being applied which takes into account the number of shareholders in the capital and the tradability of the shares of the company.

By respecting these several obligations, the company was valued 11 times the profits (which valorises approximately around ten million euros the shares held by our clients) it may seem a little but fiscal wise, a higher valuation would have been more interesting. Reflecting the French rules of the pro rata income/capital invested in the calculation of the tax on partial redemptions in the context of life insurance. The purpose is being able to justify an undisputed valuation.

After carrying out all these steps, the securities are transferred to the Luxembourg insurance company which will then be lodged in the client's policy.





Indeed, the tax advantage is interesting. Assuming that the amount of dividends and the valuation of the shares will not change for the next 20 years, the total annual tax will be € 172,000 the maximum, and € 36,000 the minimum (which concern the total tax on income and social taxation).The average of the total annual taxation of € 121,000 –Presuming the taxation rate will not change… which seems to be already unrealistic.

However, in case of a tax rate evolution proposed by Emmanuel Macron, French President, it should only slightly affect this type of operation. The government are talking about flat taxation of insurance policies.

Last, but not least, this wealth planning operation should ideally be structured a long time before the change of residence in order to avoid the requalification by the French Tax Authorities into an abuse of rights. It should also be emphasized again this needs to be carried out before being tax resident in France to avoid French capital gains taxes on the transfer disposal of the direct ownership of the company.

As far as we know, we did not see any restrictions, but as always, we have to keep in mind that prudence is the key in tax matters.

This case study and the simulation are for information, illustration purposes only and no advice has been made, or responsibility will be accepted by Anthony & Cie for any action or decisions made from it. We advise readers to take individual professional advice as each person's circumstances are different and the solution made not be appropriate.

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