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Emergency Report

To: Clients, friends and other interested parties

From: Mark van Gelderen, Jean Kauffmann, Reinhard Damberger, Zhi Zheng

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Re: **How to prevent being financially checkmated**

Part 2:
Understanding the critical role of Custodians

Initial concepts

As indicated in Part 1, it is critical that anyone with some wealth keep their money in more than one country. One needs to keep money and investments in the country where they live, plus probably keep assets in other countries, depending on the size of the wealth they have and the relative strength and attributes of the country of residence. Everyone's situation is slightly different.

Before dealing with finances, resolve two primary issues.

- Legal Considerations

In order to know what types of custodians and services are needed, first resolve all legal and inter-personal related issues . Begin by consulting with lawyers, accountants and Financial Advisors with plenty of experience in estate planning related topics. With their help, decide what is the best 'form' for holding assets for both legal and tax considerations. Should some or all assets be held: individually or in joint tenancy? Should at least part be inside a corporation, a trust, a foundation, an insurance policy or some other form of shelter? Organize assets properly, for estate planning considerations, as well as to protect business partners, heirs, etc.

After the issues are outlined, resolve them with the involvement of. family, trusted friends, associates, and the same outside advisors. Review/develop business plans, succession plans and estate plans. Wills, Disaster Plans (Living Wills/Trusts) and similar fundamental documents and concepts, should at least be in final draft form before beginning asset transfers to new custodians or investments.

The best custodians and investments can easily be a disaster without a well-defined road map charting the future, including the chain of control, tax reduction strategies, asset management and distribution guidelines.

- ## Taxes

Simultaneously, one’s tax profile needs review. Exploring tax mitigation possibilities often helps decide how to organize legal documents and relationships.

Given that most countries are technically bankrupt, an unprecedented phenomenon has occurred in the last three years. For the first time, most countries are beginning to cooperate with each other in order to track every citizen's financial profile. Hardly any Western citizen is exempt from the responsibility of paying at least minimal taxes.

Most jurisdictions grudgingly agree with the 1947 court decision of Judge Learned Hand, who held that "there is nothing sinister in so arranging one's affairs as to keep taxes as low as possible".[1] An actual U.S. Supreme Court ruling said: “The legal right of a taxpayer to decrease the amount of what otherwise would be his taxes, or altogether avoid them, by means which the law permits, cannot be doubted”. [2] Therefore, it is important to concentrate on legal Tax Avoidance before beginning to allocate assets.

Learn to legally reduce your tax footprint. Tax Evasion rarely worked well for sizable assets. From now on, Evasion is increasingly impossible. Doing your tax planning homework could be your single greatest income producer of the year, and for decades to come. What follows is a proven, inexpensive, technique to quickly research your tax situation. The results have very low risk of criminal attack from tax authorities.

I. Describe your income and tax situation in a hundred words or less.

Use your current tax advisors, friends, and colleagues to help you put together a summary statement of your tax situation. Get it down to less than a half a printed page. On the second half of the page you will put down your key questions that need resolution. Ask about risks, and present your own tax saving ideas. Also, ask about how to clean up any outstanding potential tax infractions. While preparing your overview and questions, collect recommendations of experienced international Tax Strategists (not Tax Preparers) to be consulted. Consult at least 5 advisors. (Financial Advisors like ourselves have no trouble finding suitable Tax Consultants, no matter where you live.) Do not be afraid to spend significant money in order to get these opinions, as they will in the long run probably save you many times what they cost.

II. Meet each of the recommended tax advisors with your printed up page.

Let each consultant read the page without any interruption, then begin a discussion with him/her and take copious notes. Immediately after each meeting do two things. (1) Review, correct and amplify your notes so you have not lost key ideas and suggestions. (2) Modify your presentation page with improved wording and better questions before going to the next Tax Advisor.

III. Analyze the results.

Once at least 5 interviews are completed, sit down with appropriate family members, partners or advisors to review the results. Since some Tax Advisor meetings will be followed-up by a written report from the Tax Advisor, delay the review sessions until all data is received. Compare both these reports and your notes, to evaluate what seem to be the best ideas. You will generally receive several

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[1] He was referring to reporting of individual income through corporate tax forms for legitimate business reasons. In tax decisions, as in all statutory cases, Hand studied the intent of the original legislation. His opinions became a valuable guide to tax administrators. Source: Griffith, Kathryn (1973), *Judge Learned Hand and the Federal Judiciary*, Norman: Oklahoma University Press, ISBN 978-0-8061-1071-4, pp. 26–30. Also see Chirelstein, Marvin (January 1968), "Learned Hand's Contribution to the Law of Tax Avoidance", *Yale Law Journal* **77** (3): 440–474, doi:10.2307/794940, JSTOR 794940. (JSTOR subscription required for online access.). Source: Wikipedia.

[2] **U.S. Supreme Court Justice Sutherland, Gregory vs. Helvering, 293 U.S. 465, 1965: Source: http://www.vernonjacobs.com/tax-quotations.htm**

very different great ideas from these Advisors. Expect to go back to one or two of the top professionals met to help analyze and amplify the best ideas and to put together a final plan.

IV. Always get the solutions you will be using spelled out in writing from the Tax Advisors who offered them.
Important Opinion Letters are kept as a protective shield, in case the relevant authorities challenge your tax avoidance techniques.

V. Once your plan is defined, you will know how to move forward.
Not only will you have defined which type of custodian you want, but you will know what types of investing or financial parameters you need to use in order to successfully accomplish your financial goals. All will be accomplished without committing illegal activities and without unnecessarily high taxation for yourself, your colleagues, and your heirs. Only at this point are you truly ready to begin considering both long-term custodians and the investment ideas in these reports. Asset Management must be synchronized to your unique situation, but also be realistic in terms of the harsh realities already discussed in Part 1.

This investigative process works in all areas of professional research, including estate planning and investment research.

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Custodians - A plethora of possibilities

With the background work completed, you can seriously look at how the investment world is organized. 'Custodianship' is the first step. The term describes how Assets are owned. The specific institutions used must match your needs and not be a source of unreasonable risk.

There are five categories of Custodians that *21*CA affiliates generally encounter:

1. Direct ownership. Investments are bought in the Investor's own name.
2. Broker Bonds. A Life Insurance policy that pays perhaps 102% of the value of the underlying assets upon the insured's death (to hopefully legally avoid taxation). These policies are 'wrappers' over a brokerage type platform. The Investment options range in variety and complexity, depending on the policy type and the size of the 'premiums' paid in
3. Custodial organizations. Either an onshore or an offshore financial organization specializing in holding assets for individual investors, trusts, foundations, corporations, retirement programs, etc. Such regulated custodial firms, including traditional stock brokers, often can buy virtually anything that is legal and hold it in trust for the underlying Client.
4. Banks. Banks the world over have asset management divisions that mainly cater to higher net worth clients, and can buy virtually anything that is legal, via their proprietary brokerage/trust/wealth management division.
5. Cash Management Accounts. A uniquely American hybrid Banking/Investment account that is unique in the financial world.

To aid you identify the pros and cons of each category, the following graphics are being used:

A Negative feature

A Positive feature

1. Private Ownership:

Direct Ownership of Investments involves the most paperwork (👎A) compared to the other categories. Since 9-11, and especially since the current worldwide financial crises began, the KYC (Know Your Client) information that is needed when an individual or small corporation opens an account, is difficult and frustrating. Individual Investors have to provide each Investment House with a complete set of unique documentation, to satisfy local regulators, the US government, Interpol, and others. Various forms of proof of identity for each owner or corporate officer involved, needs to be collected and certified, then verified as acceptable against various databases for criminal, civil or tax problems. Unfortunately, you will rarely find out why paperwork did not go through smoothly, but instead will be repeatedly requested to provide additional information to attempt to bypass roadblocks, until the Applicant and his Advisor give up!

Besides significantly more initial work, down the road, the Investor and his Advisor are likely to face (👎B) additional speed and time problems per investment. In this fast moving world, *21*CA has found, from experience, that most Investments have a life of approximately 3 years. Investments are sold because:

- Investors have changing needs, need cash, or even become bored with their portfolio.
- Investments no longer do what was expected, display 'counterparty risk', fail to be reliable, etc..
- Advisors, doing good portfolio management, see better and safer opportunities elsewhere.
- There is a major economic change/jolt that makes it prudent to sell quickly.

Situations can change very fast. Advisors need to help Clients sell in a timely manner. With Direct Ownership, the Advisor needs to track down the Client in order to complete paperwork. Plus, if moving to a new investment, a new set of initial paperwork for the replacement investment has to be completed. This often becomes a time-consuming mess.

Thus, unless it is an unusual circumstance or each individual investment is for well over $100,000, *21*CA discourages using Direct Ownership.

In summary, Direct Ownership definitely has its advantages by (👍A) providing the Investor with an additional sense of security and (👍B) one less layer of costly management. However, this may only be cosmetic compared to the reality that almost inevitably needs to be faced. It does not pay to do multiple sets of paperwork and admin, as they will take too much of everyone's time and resources, both when buying and when selling. Often this is also the most inefficient way to hold an asset in terms of (👎C) taxation.

Each of the following 3 types of custodians often provide superior Tax Avoidance, Estate Planning and Asset Protection (protecting the Client from asset seizure as a result of lawsuit, regulatory actions and tax obligations).

2. Broker Bonds:

Major insurance companies around the World offer these investment 'wrappers'. The best known players in this field are in Europe: Royal London, Royal Skandia, Friends Provident and others, have onshore and offshore platforms for managing client assets. Insurance-based Annuities and similar plans in most western countries are onshore Broker Bonds.

Broker Bonds often make the portfolio (A) tax efficient and allows relatively (B) easy management of assets. Only an initial (C) set of documentation needs completion. The paperwork requirements are more standardized and processing more reliable, so you will probably get it right the first time and rarely have to redo paperwork again.

The disadvantages are related to a (A) lack of flexibility for the Investor and the Advisor, and (B) potentially high operating costs. The policyholder:

(i) may not be able to buy everything needed for a dynamic portfolio;

(ii) usually cannot move money in and out without incurring significant fees;

(iii) often incurs very significant penalties for early withdrawal within the first 5 to 8 years, depending on the charging plan being used (although no-load alternatives are often available onshore for the knowledgeable - contact *21*CA for more details).

Broker Bonds had two traditional significant advantages:
They were (A) unquestioned tax shelters. However, this has been diminished in recent years. Offshore Broker Bonds are very questionable tax shelters for Americans and increasing so for Europeans, particularly if the Investor moves back to their home country. Before usage, tax advantages should be carefully investigated by each Investor, including understanding the potential affects for heirs or other eventual beneficiaries. Since the playing field seems to be rapidly changing, the longer one procrastinates, if interested in a Broker Bond type product, the less chance of being grandfathered into new tax laws.

Since the insurance company owns Broker Bonds' assets, they are (D) outstanding Asset Protection vehicles.

More on Costs and administration. Broker Bonds often provide the Seller with high rates of initial sales commission in return for selling this product (which has much to do with its popularity). The insurance companies are also often hoping that sellers who do not supply them with regular significant new business will disappear. To assist in the process, the insurance companies are known to use mergers or similar corporate events as a legally defensible excuse to eliminate paying commissions. This increases profitability for the insurance company, freezes out the Seller, and decreases accessibility to service for the underlying Clients. The insurance companies, like most businesses, look out for their corporate interests first and foremost. This phenomena is not uncommon to all areas of the Financial Services industry.

In summary, Broker Bonds are the biggest and most standardized way for holding assets offshore for medium-sized to lower High-Net-Worth Investors. In many countries, onshore Broker Bonds are popular. *21*CA has active Terms of Business with several of the leading insurance companies, which can be accessed by our Affiliates. Broker Bonds are a good alternative for many Clients, particularly if they are not regularly modifying their holdings on short notice. There are hundreds of plans available to match specific needs, both onshore and offshore. Due diligence should always be done before making a final decision. *21*CA can assist at all stages of the process.

However, *21*CA believes that the next way of doing business is often significantly better, because it is generally fairer to the Investor, allows the Advisor to provide more responsive management, and ultimately shows superior financial results.

3. Custodial organizations:

Merrill Lynch, E-Trade or any of thousands of their competitors worldwide are by definition custodial organizations. *21*CA works with one relatively small international custodian, on the Isle of Man, that is worth examining in order to understand the possibilities.

The pros for using such a custodian in a leading offshore financial centre like the Isle of Man, is that (A) the Isle of Man is on everyone's white list (as are more recently, many other low-tax jurisdictions). Activities conducted from there are not considered de facto questionable by any tax authority. The Manx government has made peace with the US, the UK, the OECD and all related entities. Assets properly domiciled on the Isle of Man, particularly in 'Discretionary Trusts' or similar structures, can provide a legal tax shelter for most Clients. Americans are generally the big exception, but can declare they have a Grantor Trust and pay US taxes on the Trust's growth. Americans who also have tax exposure in other countries will generally be able to simultaneously use their Manx structure as a legal tax shelter elsewhere.

Authorities on the Isle of Man, unless ordered by a local court, never know who are the underlying beneficiaries, grantor or settlor. In general, it is very difficult to get a court order to force the trust company to provide details.

The people at the trust company used, have worked with the *21*CA team for a decade and give clients of *21*CA (B) significant discounts for placing business with them. Their Fee Schedule compares extremely favourably to both their competitors and Broker Bonds. The straightforward fees, (depending on the size of the trust or other structure that might be used), are simple to understand and calculate when planning a portfolio. The Client is not dogged by unexpected costs.

For the Client and Advisor, (C) account and fee administration is much easier and can have creative terms, in comparison to Broker Bonds. As long as the Client's wishes are legal and ethical, the Trustees will follow the guidelines given, until changed by the Settlor or his successor. *21*CA has a proven system that simplifies portfolio management for the Client and the Advisor. Ask us for further details.

With these trustees, reasonable Clients, regardless of size, receive treatment and service as if he/she was in the wealth management department of a major Swiss bank or similar entity.

Furthermore, and perhaps the most important reason for using this custodian, is that (C) *21*CA has over 30 great Investments that are already available and used by associated Trusts. Several of the choices normally need a Million Dollars to enter, and are the flagship funds of leading internationally recognized investment gurus, normally only available to the very wealthy or via discounted feeder funds. Since the trust company is the official owner of all the Investments, any new allocation to anything already owned is a 'top-up' that usually only requires sending in a minimum of $10,000. In this way, with as little as $100,000, one can build a portfolio of up to10 Investments providing amazing diversification, lowered volatility and higher returns than traditional portfolios elsewhere.

Alternatively, such custodians, like these trustees can own and operate separate Merrill Lynch and E-Trade type accounts, combining cutting edge efficiency at conventional brokers, with the benefits of offshore tax efficiency and Asset Protection.

In summary, with an offshore asset holding structure, such as an investment company or trust, the Investor completes a single set of paperwork (D). Everything can be created efficiently and has maximum flexibility. Once the structure is created the portfolio can be quickly organized, maintained and updated, There are thousands of similar custodians available both onshore and offshore that may be more suitable for your specific needs. The main issues will be (A) costs, (B) quality/pedigree and (C) service. Due diligence should always be done before making a final decision as to who to use. *21*CA can help you at all stages of the process.

4 Banks

Most banks have wealth management departments. Using your existing banking relationship can be an excellent way to (A) to manage investment assets - as it reduces the 'can I trust the new Custodian or an outside Advisor' issue. Banks are viewed as conservative institutions that don't encourage gambling with assets. Often (B) no additional account opening paperwork is needed.

You can own most traded securities through most commercial banks. The main issues will be (A) costs and (B) service. The level of sophistication in terms of running a custody platform varies widely, and is often less efficient than with a brokerage or trust company account. The Investor and his/her Advisors may have greater difficulty working with Banks that have not fully developed this part of their business model. *21*CA has a working relationship with a number of banks in various countries and can often help individual investors and their advisors.

There are many other types of custodians worldwide, such as stockbrokers, retirement account custodians, specialized banks, mutual fund marketing platforms, etc. They all work along the same guidelines as given here. There are thousands of possibilities, both onshore and offshore that may be more suitable for specific situations. Due diligence should always be done before making a final decision as to who to use. *21*CA can help you at all stages of the process.

There is a specific subset of custodians that is a Hybrid between classical brokerage accounts and a bank account. These Cash Management Accounts can also be used by 'structures' (Trusts, Investment Corporations, etc.), whether onshore of offshore.

5 Cash Management Accounts.

CMAs are hybrid Banking/Investment accounts, unique to the USA. CMA accounts provide very significant (A) efficiencies, including:

i) Simplified maintenance and administration.

ii) Dramatically lower total internal costs to operate, compared to any of the custodians described above, resulting in higher net returns for doing the same portfolio with equivalent securities elsewhere.

iii) Dollar Chequing, Savings, Debit Card and Investments are all in one unified account, instead of separate sub-accounts. The client can follow all transactions real-time.

iv) Potentially no-cost access to all account information, real-time, by phone or internet all day, everyday, from much of the World.

v) Monthly easy-to-read detailed statements, available by mail or the internet.

vi) Margin (overdraft) to cover cheques or card usage greater than the cash available while most of the value is invested; or to buy securities beyond the nominal value of the account.

vii) Access, mainly at very low trading costs and often even free of holding and trading fees, to most of the world's Shares, most ETF's, Bonds and all American registered mutual funds, Certificates of Deposit (Dollar savings plans), even physical precious metals.

As a result, even after taxes, a CMA account can be far superior to using custodians anywhere else. Americans, (particularly once the changes decreed by the 2010 HIRE act go into effect), should seriously look at doing most of their investing via a U.S. based custodian. For non-Americans, all categories of income other than Capital Gains are taxed at source, at Treaty rates, depending on the passport presented when accounts are opened. Treaty rates range between 10% and 30%, and can be easily researched online. Taxes paid in the USA are usually a credit for the client against their home country tax liabilities, regulated by bilateral tax treaty agreements.

(viii) Capital Gains are tax-free for non-Americans.

(ix) These accounts can be opened & operated by corporations, trusts and other entities.

Other than U.S. taxation (A), the main negative is that an American CMA account is (B) not capable of containing a number of important types of securities commonly available elsewhere,. These include: most types of Hedge Funds, Funds of Hedge Funds, Managed Commodity Funds, Capital Protected Investments, non-US registered open-ended mutual funds, and various other securities that do not have a US retail counterpart.

In summary, after all costs a CMA account can often give a higher total return than if similar investing was done elsewhere, plus the accounts have very important features that cannot be found in one package anywhere else. There are dozens of CMA account providers commonly available to Americans. For non-Americans living outside North America, choosing and dealing with the creation of such an account can be daunting. *21*CA can help you explore the possibilities and set up accounts.

These symbols were used above to identify the pros and cons of each category:

A Negative feature

A Positive feature

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Moving Forward

As indicated in Part 1, it is critical that anyone with some wealth keep their money in more than one country. How and what to do are determined, among other factors, by legal and tax needs, size and location of existing and future assets, and the current financial situation of the countries involved. Everyone's situation is slightly different.

The next report in this series, #3, deals with Asset Allocation.

To see or download Report #1, http://www.21ca.eu/ER1.html.

To see or download this Report, http://www.21ca.eu/ER2.html.

Feel free to be in contact with your *21*CA Account Executive if you have any questions. We will gladly provide more details.