Liechtenstein

Branch Reporters
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Summary and conclusions

Until the tax reform of 2011, the Liechtenstein tax provisions exhibited the peculiar structure of having one SAAR but no GAAR.[3] Accordingly, Liechtenstein did not have a GAAR in its Tax Act before 2011. Therefore, the Liechtenstein tax authorities and the Liechtenstein tax jurisprudence had to rely merely on a teleological interpretation and the substance-over-form doctrine.

With the general revision of its tax law in 2011, however, Liechtenstein introduced a GAAR. Most of its SAARs, which especially refer to close relationships between persons – such as between companies and their shareholders – were also introduced with the same tax reform.

The tax law covers economic facts and determines their tax implications. Even with the greatest legislative care, it cannot be ruled out that taxpayers will take advantage of the opportunities available to them to attain domestic tax advantages. The purpose of the GAAR set out in article 3 of the Tax Act is, in fact, not to limit the right of taxpayers to choose the best option from among several economically reasonable structures in order to achieve the lowest possible tax burden. If the taxpayer, however, is unable to provide evidence of an economic purpose or other significant reasons for the legal or actual structure chosen, but instead the structure can be explained only with reference to the desired tax advantage, and it would violate the object and purpose of tax law to grant that advantage to the taxpayer, then the structure must be considered abusive.[4]

According to the Liechtenstein legislature, the GAAR is further to be understood as being only of a clarifying nature.[5] Although no discussions are currently taking place in Liechtenstein on how to deal with the GAAR from a theoretical standpoint, it seems evident that the GAAR wants to emphasise the systematic and teleological interpretation of the tax provisions. It does not aim, however, to create fictions in order to enforce an adequate taxation and it cannot lead to a separate tax liability. The GAAR is thus based on the substance-over-form doctrine and is clearly led by an economic perspective.

Due to this high material hurdle, the GAAR has hardly been ever applied since its intro-

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[3] Wenz Knörzer & Busch, "Chapter 19: Liechtenstein" in Lang et al. (eds.), *GAAR – A Key Element of Tax Systems in the Post-BEPS Tax World*, IBFD Vol. 3 (2016), p. 409.

[4] Liechtenstein Government Report no. 48/2010, pp. 62 et seq.

[5] Idem.

duction in 2011. The interpretation of the GAAR is up to the tax authorities and the courts, and this process is still at an early stage.[6] While there are no specific "safeguard clauses" in this regard, Liechtenstein law still provides taxpayers a comprehensive regime of procedural rights.[7]

Although the GAAR is not the sharpest tool for tackling tax abuse in itself, the combination of the GAAR with the different SAARs and the implementation of anti-abuse clauses in tax treaties according to the minimum standards of the OECD/G20 on Base Erosion and Profit Shifting (BEPS) leads to an effective protection of taxation rights in Liechtenstein and in other countries.[8]

1. General anti-avoidance rules and doctrines

1.1. General overview

In Liechtenstein, article 3 of the Tax Act[9] contains the following GAAR with the aim of ignoring abusive structures for the purposes of taxation:

"*Legal or actual structures that appear inappropriate to the financial circumstances and the sole economic purpose of which consists of achieving tax advantages shall be considered abusive, if:*
a) *the granting of this tax advantage would be counter to the object and purpose of this Law; and*
b) *the taxpayer is unable to present any economic or other significant reason for the choice of this structure and the structure does not produce any separate economic consequences.*"

This is a cumulative list of preconditions, all of which must be met for a structure to be considered abusive. Apart from this GAAR, the Tax Act also contains individual SAARs that refer, in particular, to close relationships, such as the one that exists between a company and its shareholders. The GAAR and the SAARs must, of course, always be seen and interpreted in the light of prevailing case law. As will be illustrated below, however, hardly any judicial decisions have been issued in this regard so far.

Besides the Tax Act, anti-avoidance rules can also be found in Liechtenstein tax treaties. In this regard, it is interesting to see that, during the legislative process of the new Tax Act in 2010, a renowned Liechtenstein law firm and the Liechtenstein Chamber of the Association of Professional Trustees and Fiduciaries argued that abusive fact patterns should be governed by double taxation treaties only, and therefore article 3 of the Tax Act should be deleted without substitution. The parliament did not follow this proposal, holding that while double taxation treaties do indeed take account of abuse, such agreements can "only" deprive treaty benefits from a specific person. But the attribution of income to a specific

[6] Liechtenstein Government Report No. 48/2010, p. 63.

[7] See Benedetter & Wytrzens, "Liechtenstein", in International Fiscal Association (ed.), *The practical protection of taxpayers' fundamental rights*, Cahiers de Droit Fiscal International Vol. 100 B (2015), pp. 495 et seq.

[8] Wenz Knörzer & Busch, "Chapter 19: Liechtenstein" in Lang et al. (eds.), *GAAR – A Key Element of Tax Systems in the Post-BEPS Tax World*, IBFD Vol. 3 (2016), p. 409.

[9] Law on National and Municipal Taxes (Tax Act, *Gesetz vom 23. September 2010 über die Landes- und Gemeindessteuern*, LR 640).

person, especially, is subject to national tax law, not a double taxation treaty.[10]

1.2. The tax avoidance scheme

The comprehensively revised Liechtenstein Tax Act entered into force in 2011. The goal of the revision was to modernise the existing tax law by taking international developments into account. In this regard, a GAAR has also been introduced that defines the abuse of structuring options. This is a special manifestation of the economic perspective that has already been used as a decision aid in several judgements of the Constitutional Court and that is also included in a similar form in article 2(2) PGR.[11] According to this doctrine, the legally relevant tax facts are examined according to their economic background, not their external appearance. Such an economic perspective on facts relevant to taxation is considered only if a structure is abusive and does not violate the object and purpose of the Tax Act.[12]

The GAAR ensures that taxpayers cannot abusively rely on the Tax Act. Accordingly, a proper legal structure is always relevant to economic facts and circumstances, as well as to the model of the tax system, even if this is not formally provided in the law. Consequently, certain tax advantages are not permissible if the transaction or structure does not have an economic substance or purpose.[13]

According to the wording of article 3 of the Tax Act, the GAAR tackles abusive structures. Necessarily so, the definition of an abusive fact pattern is broad, since an overly narrow definition of the fact pattern would be easy to circumvent. The precise delineation should arise through practice and case law. In order to facilitate an autonomous development of the law that takes into account Liechtenstein's special circumstances, the legislative power refrained from using Swiss or Austrian law as a model, as is otherwise often the practice.[14]

The GAAR applies to all national and municipal taxes governed by the Tax Act. Pursuant to article 1 of the Tax Act, this includes the property and income tax on natural persons, the corporate income tax on legal persons, the tax based on expenditure, the real estate capital gains tax, and the formation tax and insurance premium tax. There is no GAAR in the value-added-tax legislation.

1.3. The tax advantage

The focus of article 3's treatment of the GAAR is on attaining tax advantages through abusive structures. No further definition of such tax advantages was included. This rule accordingly does not prohibit the right of a taxpayer to choose the option among several structures that results in the lowest tax burden. Pursuant to article 3 (1) (b) of the Tax Act, the legislative power's intention with the GAAR was instead to prevent the granting of tax advantages that would violate the object and purpose of the Tax Act.

[10] Liechtenstein Government Report No. 48/2010, p. 63.

[11] Idem, p. 62.

[12] Liechtenstein Administrative Court (VGH) No. 2016/090 of 5 August 2016 (LES 2016,227).

[13] Wenz Knörzer & Busch, "Chapter 19: Liechtenstein" in Lang et al. (eds.), *GAAR – A Key Element of Tax Systems in the Post-BEPS Tax World*, IBFD Vol. 3 (2016), p. 398.

[14] Liechtenstein Government Report No. 48/2010, p. 63.

1.4. The taxpayer's intent

Even with the greatest legislative care, it cannot be ruled out that taxpayers will take advantage of the opportunities available to them to attain domestic tax advantages. As indicated above, the purpose of the GAAR set out in article 3 of the Tax Act is, in fact, not to limit the right of taxpayers to choose the best option from among several economically reasonable structures in order to achieve the lowest possible tax burden. If the taxpayer, however, is unable to provide evidence of an economic purpose or other significant reasons for the legal or actual structure chosen, but instead the structure can be explained only with reference to the desired tax advantage, and it would violate the object and purpose of tax law to grant that advantage to the taxpayer, then the structure must be considered abusive.[15]

1.5. The consequences of applying the GAAR to a given case

In general terms, the object of the Tax Act is described in article 1 of the Tax Act. According to that article, the law governs the levy of property and income tax, the tax based on expenditure, the real estate capital gains tax, the corporate income tax, the formation tax, and the insurance premium tax. It follows that, if the GAAR is applied in accordance with article 3 of the Tax Act, consequences are primarily relevant in those tax areas, including the penal provisions according to articles 135 et seq. of the Tax Act. The question of whether abuse gives rise to more far-reaching consequences – such as under the public law, law of obligations or company law – is not covered by tax law and so the applicable provisions must be examined accordingly.

Specifically, article 3(2) of the Tax Act sets out the legal consequences when an abuse arises. According to that provision, the taxes shall be levied in the way they would be if the legal structure were appropriate to the economic processes, facts, and circumstances.[16] In other words, the legal or actual structure is then not recognised by Liechtenstein tax law and is replaced by a structure that is appropriate for the purposes of taxation (recharacterisation), followed by a reassessment.

Due to the high material hurdle for the application of the GAAR, in particular, no judicial decisions have been issued so far with regard to the application of article 3(2) of the Tax Act.[17] Against this backdrop, no principles, according to which a recharacterisation is undertaken by the Fiscal Authority, are available.

1.6. Conflicts between domestic and treaty GAAR or between domestic GAAR and SAARs

Currently, Liechtenstein has concluded roughly 20 double taxation treaties and numerous other tax treaties.

According to some observers, Liechtenstein principally strives not to include GAARs in its double taxation agreements. They hold that specific rules shall only be included if the other

15 Idem, pp. 62 et seq.

16 In the case of abusive structures, taxation is carried out as if the legal structure were appropriate to the economic circumstances. The economic approach is applicable (see *section 1.2 The tax avoidance scheme*).

17 See also s. 2 *Case law on statutory and court-developed GAARs.*

party to the agreement insists.[18] This view, meanwhile, contradicts the continuous efforts of Liechtenstein to comply with the OECD standards.

For an illustration of this, on 7 June 2017 Liechtenstein signed the MLI which was developed by a working group of 95 jurisdictions. Liechtenstein has also actively participated in this process. The purpose of the MLI is to incorporate the standards developed by the OECD/G20 countries within the framework of the BEPS project into the existing double taxation agreements of the participating jurisdictions. Liechtenstein will use the MLI to implement the minimum standards for the prevention of the misuse of agreements and the improvement of dispute settlement. To illustrate, the double tax treaties shall be modified to include the following preamble text:

"*Intending to eliminate double taxation with respect to the taxes covered by this agreement without creating opportunities for non-taxation or reduced taxation through tax evasion or avoidance (including through treaty-shopping arrangements aimed at obtaining reliefs provided in this agreement for the indirect benefit of residents of third jurisdictions).*"[19]

Moreover, Liechtenstein, as required by the OECD, henceforth includes the principal purposes test in its double taxation treaties. The wording according to the OECD Model Convention is:

"*Notwithstanding the other provisions of this Convention, a benefit under this Convention shall not be granted in respect of an item of income or capital if it is reasonable to conclude, considering all relevant facts and circumstances, that obtaining that benefit was one of the principal purposes of any arrangement or transaction that resulted directly or indirectly in that benefit, unless it is established that granting that benefit in these circumstances would be in accordance with the object and purpose of the relevant provisions of this Convention.*"[20]

Following the ratification, which is expected in 2018, the Liechtenstein double taxation treaties, which do not now fully comply with the minimum standards, will be adjusted. This concerns the double taxation treaties with the following 15 countries: Andorra, Czech Republic, Georgia, Germany, Guernsey, United Kingdom, Hong Kong, Luxembourg, Malta, San Marino, Singapore, Switzerland, Hungary, Uruguay and the United Arab Emirates.[21]

In 2016, Liechtenstein further ratified the OECD Convention on Mutual Administrative Assistance in Tax Matters. Based thereon and the fact that Liechtenstein is a Member of the OECD's Inclusive Framework on BEPS, Liechtenstein has committed itself to the spontaneous exchange of information in accordance with the international minimum standards. The corresponding Government Report[22] regarding the change of the Administrative Assistance

[18] Wenz Knörzer & Busch, "Chapter 19: Liechtenstein" in Lang et al. (eds.), *GAAR – A Key Element of Tax Systems in the Post-BEPS Tax World*, IBFD Vol. 3 (2016), p. 406.

[19] Art. 6(1) Multilateral Convention to Implement Tax Treaty Related Measures to prevent Base Erosion and Profit Shifting, 24.11.2016.

[20] OECD (2015), *Preventing the Granting of Treaty Benefits in Inappropriate Circumstances, Action 6: 2015 Final Report*, OECD/G20 Base Erosion and Profit Shifting Project, OECD Publishing, Paris, p. 55.

[21] Liechtenstein Government, *Liechtenstein unterzeichnet das multilaterale Übereinkommen zur Umsetzung steuerabkommensbezogener Massnahmen zur Verhinderung der Gewinnverkürzung und Gewinnverlagerung*, retrieved 18 September 2017 from http://www.regierung.li/de/mitteilungen/154766

[22] Liechtenstein Government Report No. 51/2017.

in Tax Matters Act[23] was recently discussed by the Liechtenstein Parliament in the first reading and is expected to be ratified in 2018 as well.

So far, there has been no known conflict between the GAAR set out in article 3 of the Tax Act and any double taxation treaty concluded by Liechtenstein. This certainly has to do with the fact that treaties do not provide treaty-specific GAARs, but rather the domestic anti-avoidance rules and provisions to prevent tax avoidance and tax evasion apply. In the tax treaty between Liechtenstein and Germany, for instance, the relationship between national GAARs and provisions of the agreement is expressly clarified.[24] According to article 31(4) of the treaty, the parties are not prohibited by the treaty from applying their domestic anti-avoidance rules or their legal provisions to prevent tax avoidance or evasion. The parties may refuse to grant treaty benefits, in whole or in part, in order to prevent structures that, if they were able to enjoy the benefits, would violate the object and purpose of the agreement. This includes, in particular, non-taxation in both contracting parties (double non-taxation) or multiple enjoyment of treaty benefits. Nevertheless, the current double taxation agreement between Liechtenstein and Germany will be adjusted in light of the MLI.

With respect to the relationship between the GAAR set out in article 3 of the Tax Act and the SAARs,[25] it is of note that the Liechtenstein Administrative Court (*Verwaltungsgerichtshof*, VGH) applies both anti-avoidance rules simultaneously, i.e. the GAAR is not given precedence over the SAARs. Both provisions are applied independently from one another in the same case.[26]

Finally, it should be mentioned that despite not being part of the EU – whose members have to comply with tax directives such as the EU Anti-Tax Avoidance Directive – Liechtenstein is part of the European Economic Area and therefore has to meet the requirements under the EEA Agreement. Compliance with these requirements, especially regarding the fundamental freedoms and the prohibition of state aid, was further identified as a main goal of Liechtenstein's tax reform, which entered into force in 2011.[27] In any event, Liechtenstein's GAAR has so far never been contested before any European court.

1.7. SAARs in uncommon areas of application

Liechtenstein's GAAR is supplemented by just a few specific anti-avoidance rules. These provisions do not refer to classic areas of taxation in which SAARs are most likely to be found in other countries. Instead, they are primarily concerned with close relationships between persons, such as between companies and their shareholders. This is in part due to the neutral impact of the Liechtenstein tax system in accordance with the notional interest deduction set out in article 54 of the Tax Act in the amount of the uniformly defined, standardised

[23] Gesetz vom 30. June 2010 über die internationale Amtshilfe in Steuersachen, LR 353.

[24] Treaty between the Principality of Liechtenstein and the Federal Republic of Germany on the avoidance of double taxation and the prevention of tax evasion with respect to taxes on income and property, enacted 17 November 2011.

[25] See *s. 1.7 (SAARs in uncommon areas of application)*.

[26] See ss. 1.7.2 (Restructuring measures) and 1.7.3 (Depreciations and value adjustments in the case of a permanent fall in value of holdings).

[27] Liechtenstein Government Report no. 48/2010, pp. 7 et seq. and pp. 21 et seq.

projected income on the balance sheet equity adjusted for certain factors.[28] The tax treatment of this fictional expense is adjusted to that of equity financing or borrowing, or if the interest rates are identical, the two are treated equally. The goal of this rule is to achieve financing neutrality and allocation efficiency.[29]

Moreover, the intentions relating to the tax burden are not relevant and are not required in cases falling under a SAAR. The SAAR is applied if the fact pattern referred to in the provision is met, irrespective of the goals and intentions of the taxpayer.[30]

1.7.1. *The arm's length principle between shareholder and company*

One SAAR deals with the arm's length principle between shareholder and company. According to article 14(2)(d) of the Tax Act, an owner of a company (legal entity) who is employed in that entity must declare an appropriate salary. This provision also applies to persons working in such businesses who have a substantial interest in the capital of the legal entity that enables them to exercise a decisive influence over its management. The appropriate salary takes into account the scope of the work, the position held and the associated responsibility, the professional skills, the size of the operation, and the other salary arrangements in the business. In determining the appropriate salary, the Fiscal Authority relies on salaries of comparable businesses as well as various indicators, developments over time and industry-specific wage statistics. An internal administrative guideline is used to make sure that the discretionary implementation of these provisions is as uniform as possible.[31] An appropriate salary for employed (as a rule: managing) partners is required because income from dividends, unlike income from employed work, is not taxable.[32]

The Liechtenstein Administrative Court (VGH) issued a judgement in this connection on 27 June 2013.[33] In that case, the court adjudicated the salary of a medical doctor who was employed by his own limited company. The question of how high an appropriate salary should be that the doctor should pay taxes on as an employee of his own company was resolved using the legal concept of tax avoidance (*Steuerumgehung*). In doing so, the Liechtenstein Administrative Court examined what salary conditions would have to be met for the doctor to accept employment from another doctor. The court found that neither the formation and operation of a medical limited company nor the employment of the doctor in his own company were abusive. But the unusually low salary that had been agreed between the complainant and his own limited company did constitute tax avoidance for purposes of the SAAR.

28 Wenz Knörzer & Busch, "Chapter 19: Liechtenstein" in Lang et al. (eds.), *GAAR – A Key Element of Tax Systems in the Post-BEPS Tax World*, IBFD Vol. 3 (2016), pp. 401 et seq.

29 Hosp & Langer, *Steuerstandort Liechtenstein* (Wiesbaden, 2011), p. 109.

30 Wenz Knörzer & Busch, "Chapter 19: Liechtenstein" in Lang et al. (eds.), *GAAR – A Key Element of Tax Systems in the Post-BEPS Tax World*, IBFD Vol. 3 (2016), pp. 405 et seq.

31 Liechtenstein Government Report no. 82/2010, p. 31.

32 Hosp & Langer, *Steuerstandort Liechtenstein* (Wiesbaden, 2011), p. 66.

33 Liechtenstein Administrative Court (VGH) no. 2013/067 of 27 June 2013 (LES 2013, 108).

1.7.2. *Restructuring measures*

Another SAAR is included in article 52(10) of the Tax Act. This provision contains a specific anti-avoidance rule for restructuring measures.[34] It further specifies the general anti-avoidance rule set out in article 3 of the Tax Act without, however, superseding it. The covered fact patterns generally relate to avoidance; in certain cases, these fact patterns can also be covered by the general anti-avoidance rule. But a specific provision was set out in order to ensure uniform development of the law in these areas and in order to balance the legitimate interests of the state in maintaining uniformity of tax collection with the interests of taxpayers, who need a higher degree of legal certainty for their planning, especially where restructuring measures are concerned. Structures are covered in which the taxpayer takes advantage of the tax neutrality of restructuring measures. If a taxpayer liquidates a sole proprietorship, taxes must be paid on the liquidation gains (release of undisclosed reserves). But on the other hand, article 16(6) and article 52 of the Tax Act allow the taxpayer to transfer the sole proprietorship to a legal person without giving rise to taxation. If the taxpayer sells shares after the conversion is complete, tax-free realisation of any part of the profit that has not yet been assessed would be possible, given that profit from the sale of shares is generally tax-free. A sale that takes place too soon after such a transfer raises the suspicion of abuse. Nevertheless, it cannot be ruled out that the sale was motivated by economic considerations. For that reason, paragraph 10 stipulates that undisclosed reserves that existed at the time of the transfer shall be taxed retroactively if the sale occurs within five years after the transfer.

At the same time, of course, the values used to calculate the corporate income tax of the accepting company are increased in order to prevent double taxation. Because with time, the probability decreases that the suspected tax avoidance was the motivation, one-fifth of the transferred, undisclosed reserves are permanently considered tax-neutralised for each year that has passed since the transfer. This means that, after five years, no retrospective taxation occurs.

1.7.3. *Depreciations and value adjustments in the case of a permanent fall in value of holdings*

In a manner that is symmetrical to the treatment of capital gains after restructuring measures, article 53(4) of the Tax Act covers avoidance through fact patterns that aim to take advantage of the tax effect of depreciations on holdings. In certain cases, these structures may also fall under the GAAR set out in article 3 of the Tax Act. But a specific provision was set out in order to ensure uniform development of the law in these areas and in order to balance the interests of the state with the interests of taxpayers. This does not defeat the application of the GAAR, however, if the taxpayer is trying to circumvent the application of the specific provisions by abusing structuring options. Article 53(4) of the Tax Act becomes necessary due to the possibility of tax-relevant depreciation combined with the tax exemption of gains achieved through the sale of holdings. Full tax exemption of capital gains makes it possible to sell holdings tax-free. For the buyer, this results in new acquisition costs if the value increases in the meantime, which would then be the basis for any depreciations. This would make it possible within the corporate group to generate higher acquisition

[34] See Liechtenstein Government Report no. 48/2010, pp. 134 et seq.

costs tax-free on a depreciation basis (tax-free step-up). To prevent this, paragraph 4 stipulates that the acquisition costs are adopted immediately as the depreciation basis only if the acquisition is made by an independent third party. If the acquisition is made by a closely associated person (such as a group company), however, the depreciation basis does not change at first, i.e. a tax-relevant depreciation is possible only when the value of the holding falls below the acquisition costs of the closely associated person.

1.7.4. Low-interest loans

A further SAAR according to article 54(3) of the Tax Act takes account of low-interest loans that are granted by a legal person to closely connected persons such as shareholders or – in the case of a foundation or trust – to beneficiaries. If the interest rate of such a loan falls below the notional interest rate that is currently four per cent, the company must pay taxes on the (low) interest income from the loan, but it may also deduct four per cent of its modified equity capital. This would allow the company to reduce its operating result by providing loans with low interest rates to connected persons. To prevent this tax-reducing effect, the deduction must be reduced by the difference between the actual interest and the interest calculated according to the notional interest rate, unless the loan is part of the operating activity of the legal person.[35]

1.7.5. Correspondence principle for dividends within corporate groups

In accordance with the Action Point 2 of the BEPS project, the correspondence principle for dividends within corporate groups was implemented in article 48(1)(e) of the Tax Act. As a result, dividends arising from holdings in Liechtenstein or from foreign legal persons shall not be counted as taxable net income for taxpayers with unlimited tax liability in Liechtenstein. This shall not, however, apply to dividends arising from holdings in legal persons, insofar as the holding amounts to at least 25 per cent of the votes or capital and the dividends can be applied as expenditure for tax purposes by the person making the payment. Therefore, if the holding amounts to at least 25 per cent of the votes or capital and the dividends are claimed as an expense by the person making the payment and are not subject to taxation, then these dividends will be taxed.[36]

1.7.6. Assets not essential to business operations

As already mentioned at the outset,[37] article 54 of the Tax Act provides for an equity capital interest deduction in the amount of the uniformly defined, standardised projected income of currently four per cent on the balance sheet equity adjusted for certain factors. This notional interest deduction constitutes a commercially justified expenditure, which reduces

[35] Wenz Knörzer & Busch, "Chapter 19: Liechtenstein" in Lang et al. (eds.), *GAAR – A Key Element of Tax Systems in the Post-BEPS Tax World*, IBFD Vol. 3 (2016), p. 405.

[36] Liechtenstein Government Report No. 91/2016, pp. 30 et seq.

[37] See para 1.7. (SAARs in uncommon areas of application).

the basis for the assessment of the corporate income tax and thus the effective tax rate.[38] The starting point for the application of article 54 of the Tax Act is modified equity capital. This includes paid-up nominal capital, share capital or equity capital, and the reserves representing own assets. The amount is reduced by several items, in particular assets that are not essential to business operations. This reduction serves to prevent cases of abuses in which assets are brought into the company for the sole purpose of achieving a higher national interest deduction.[39] A general rule applies in this context: if certain assets can be sold without diminishing the operating activity of a company, those assets are considered not essential to business operations. In this regard, article 32a of the Tax Ordinance clarifies that assets not essential to business operations are assets that do not primarily serve the actual business objective; in particular luxury items and works of art, land reserves and excessive liquidity reserves.

2. Case law on statutory and court-developed GAARs

2.1. General overview

According to the principle of legality in Liechtenstein, legislation is the primary source of law. Law-making and legislation are thus the prerogative of the legislative power, i.e. of the Liechtenstein Parliament (*Landtag*). In contrast, Liechtenstein courts are responsible for interpreting the law in specific cases. There is thus a clear division of labour between making and interpreting the law. The decrees issued in individual cases and the judgements rendered by courts in specific legal disputes never have the power of law and cannot be extended to other cases or other persons.[40] But one of the characteristics of laws is that they are never perfect or complete. It may happen that the wording of a provision is ambiguous or that simply no legal rule exists to cover a particular fact pattern (loophole). Legislation therefore needs to be interpreted and in some cases loopholes must be closed. When courts, especially the highest courts, flesh out unclear or indeterminate norms and, in doing so, claim not only to decide specific cases but also to guide practice and legal interpretation in future cases, this is referred to as case law. In practice, the role of this law should not be underestimated. Moreover, specific court judgements may serve as an incentive for the legislative power to act and to solve an issue differently than the solution found through judicial practice.

2.2. Noteworthy cases on the operation of the GAAR

The GAAR enshrined in article 3 of the Tax Act entered into force in 2011. Since then, hardly any disputes have arisen referring to this norm, so that only a few court decisions have dealt with the anti-avoidance rule.

Paragraph 1.7 (SAARs in uncommon areas of application) already dealt with one of these

[38] Liechtenstein Government Report No. 91/2016, p. 138.

[39] Hosp & Langer, *Steuerstandort Liechtenstein* (Wiesbaden, 2011), p. 111.

[40] See § 12 of the General Civil Code (*Allgemeines bürgerliches Gesetzbuch vom 1. June 1811*, LR 210).

decisions. At issue was the legal question of what salary a taxpayer should pay income tax on as an employee of his own limited company. The Liechtenstein Administrative Court (VGH) decided that this question should be solved using the Swiss legal concept of tax avoidance (*Steuerumgehung*), given that this prohibition was derived, in general terms, from the prohibition of abuse of law, which applied in all areas of tax law and – with reference to article 3 of the Tax Act – was set out and applied the same way in Liechtenstein as in Switzerland. *"Accordingly, tax avoidance should be assumed if, firstly, a legal construct chosen by the persons involved appears to be unusual, unreasonable or peculiar and, in any event, fully inappropriate to the economic circumstances; secondly, it must be assumed that the legal construct was chosen abusively for the sole purpose of saving taxes that would be owed if the circumstances were arranged appropriately; and, thirdly, the chosen approach, in fact, would lead to a significant tax savings if it were to be accepted by the tax authorities. With this in mind, the legal question at issue here – namely how high an appropriate salary for taxation should be that the complainant, as an employee of his own limited company, must pay income tax on – can also be resolved using the legal concept of tax avoidance (Steuerumgehung), and thus taking account of Swiss case law."*[41]

Another important decision was issued by the Liechtenstein Administrative Court (VGH) on 5 August 2016.[42] At issue here was the allocation of the Liechtenstein real-estate capital gains tax. The decision arose from a dispute in which a real property, equal shares of which had previously been in the possession of six co-owners, was transferred to an establishment in order to realise a new development with seven condominium units. Consequently, three of the former co-owners acquired one condominium unit each by way of their status as beneficiaries of the establishment. The remaining four units were sold to third parties. A tax ruling was sought in regard to this fact pattern. But this tax ruling was not concerned with the attribution of the purchase price or the resulting real-estate capital gains. A tax was consequently assessed on the real-estate capital gains generated by these sales and charged to the establishment. The establishment contested this assessment, arguing that an economic perspective should be taken, which would indicate that the realised purchase price should be attributed economically as acquisition costs to the four condominium units sold to third parties. Disputing this, the Fiscal Authority argued that an allocation of the purchase price should be undertaken according to material criteria, namely according to the value share of all seven condominium units. The Liechtenstein Administrative Court (VGH) issued the final ruling on this case.[43] The Administrative Court found that, according to article 3 of the Tax Act, *"an economic perspective must be taken in regard to facts that are relevant to taxation, but only if the legal or actual structures are abusive. Conversely, it follows that no economic perspective shall be taken if the structures are not abusive, i.e. if they take account of the object and purpose of the Act. This is at the very least the case when the Fiscal Authority approves the legal and actual structure in advance by way of a tax ruling, as in the present case."*

2.3. Judge-made general anti-avoidance doctrines and concepts

As already mentioned in paragraph 2.2, the courts in Liechtenstein have so far dealt with only a few cases involving the abuse of structuring options. For that reason, other than the

[41] Liechtenstein Administrative Court (VGH) No. 2013/067 of 27 June 2013 (LES 2013, 108).

[42] Liechtenstein Administrative Court (VGH) No. 2016/090 of 5 August 2016 (LES 2016, 227).

[43] See para. 3 GAAR and taxpayer safeguards.

judicial treatment of the question of abuse as held in paragraph 1.2 (The tax avoidance scheme), there have been no doctrines or concepts derived from court decisions dealing with anti-avoidance.

3. GAAR and taxpayer safeguards

Liechtenstein tax law is based on a large number of different national and international legal sources. For instance, article 24(1) of the Constitution of the Principality of Liechtenstein[44] sets out that, through the enactment of legislation, the state shall provide for equitable taxation that exempts a minimum subsistence level and draws more heavily on high assets and income. Based on these principles, the Tax Act was enacted as the key norm for formal and material tax law. Moreover, Liechtenstein has been a member of the European Economic Area (EEA) since 1 January 1995. Although the common tax policy of the European Union is not part of the EEA Agreement, the EEA Agreement does have a major impact on Liechtenstein tax law due to the fundamental freedoms and the prohibition of state aid contained therein. There are no "safeguard clauses" for taxpayers relating to the GAAR. However, it is possible at any time for taxpayers to contact the Fiscal Authority and to request a relevant advance ruling.[45] The newsletters and information documents of the Fiscal Authority likewise serve as safeguards, facilitating uniform interpretation and application of the provisions of the Tax Act. Taxpayers also have several general rights in the context of the assessment procedure, during which abuse of structuring options is examined. In any case, the GAAR will be applied as a matter of last resort.

3.1. Procedural rights and obligations in the assessment procedure

Pursuant to article 93 of the Tax Act, the tax authorities, together with the taxpayer, are *ex officio* responsible for establishing the actual and legal circumstances relevant to full and accurate taxation as part of the assessment procedure. Despite this inquisitorial principle[46] and the associated extensive burden placed on the public authorities to determine the material truth, only relatively limited investigative means are provided to those authorities. In order for the tax authorities to meet their investigative obligation, taxpayers are subject to procedural obligations requiring them to cooperate in the tax authorities' investigations.[47] Information provided by the taxpayer in this context may be used by the tax authorities as the basis for their decisions, without further verification, if there are no reasonable doubts as to its correctness. But if asserted facts are disputed and there is a specific reason for the tax authorities to doubt the presentation of the facts, then they will have to undertake a more detailed review.[48]

44 *Verfassung des Fürstentums Liechtenstein vom 5. Oktober 1921*, LR 101.

45 See Benedetter & Wytrzens, "Liechtenstein" in International Fiscal Association (ed.), *The practical protection of taxpayers' fundamental rights*, Cahiers de Droit Fiscal International Vol. 100 B (2015), pp. 495 et seq.

46 This internationally recognised principle governing the remit and responsibility of the tax authorities ensures the postulate of uniformity of taxation, which is also enshrined in the Liechtenstein Constitution (Hosp & Langer, *Steuerstandort Liechtenstein* (Wiesbaden, 2011), p. 147).

47 Liechtenstein Government Report no. 48/2010, pp. 183 et seq.

48 Hosp & Langer, *Steuerstandort Liechtenstein* (Wiesbaden, 2011), p. 147.

The counterpart to these provisions is the taxpayer's obligation to cooperate according to articles 94 et seq. and also articles 97 et seq. of the Tax Act. The main responsibility of the taxpayer is to file a tax return so that a standard assessment procedure can be undertaken. Taxpayers who are subject to property tax and income tax or to corporate income tax are invited to send in a tax return by public announcement and by delivery of a tax form for this purpose. Pursuant to article 94(1) of the Tax Act, non-delivery of the form does not release the taxpayer from the obligation to submit a tax return or from tax liability itself – regardless of why the tax form was not delivered. Beyond this, pursuant to article 97(1) of the Tax Act, taxpayers must cooperate in the investigation by the assessing authority and take all reasonable action to ensure lawful – i.e. full and accurate – assessment. When requested to do so, taxpayers must, in particular, provide verbal or written information and present business accounts, vouchers, and other certificates and documents relating to their business transactions pursuant to article 97(2) of the Tax Act.

Apart from these procedural obligations, taxpayers also enjoy several procedural rights. Under article 88 of the Tax Act, taxpayers are entitled to inspect documents they have submitted or signed. Similarly, article 89 of the Tax Act grants taxpayers the right to request evidentiary measures, while the assessing authorities are required to examine evidence that has been provided in a timely manner and is of legal relevance to the facts. Finally, article 90 of the Tax Act permits taxpayers to arrange for representation before the tax authorities, unless personal involvement is required.

Pursuant to article 101 of the Tax Act, the assessment of the taxpayer is conducted by the Fiscal Authority with the support of the municipal tax offices. The tax authorities examine the tax return and conduct the necessary investigations. If the taxpayer has not submitted a tax return or the basis for the assessment of tax cannot be properly determined in the absence of reliable and complete documentation, then the Fiscal Authority conducts the assessment according to its due discretion based on article 102 of the Tax Act. This discretionary assessment consists in an estimate of the tax factors or of individual property, income and earnings components, and it aims to achieve the most probable conclusion regarding the facts that corresponds as closely as possible to reality. In performing this assessment, the Fiscal Authority may take into account historic figures based on experience, asset trends and the living expenditure of the taxpayer.[49]

So, although the tax authorities are responsible for determining the actual and legal circumstances that form the basis for full and accurate taxation, taxpayers are involved significantly in the process for establishing the facts. Through their disclosure and cooperation obligations, taxpayers can actively substantiate their intended tax advantages by presenting relevant economic facts from the outset, thus helping to prevent potential abuse in accordance with article 3 of the Tax Act. When taxpayers fail to cooperate in the establishment of the truth, thus giving rise to discretionary decisions and estimates, they have to accept the imprecisions inherent in such discretionary assessments.

If the tax authorities do identify abuse in accordance with article 3 of the Tax Act, then, pursuant to article 3(2) of the tax Act, taxes are levied in the assessment on the basis on which they would have been levied if the legal structure had been appropriate to the economic events, facts and circumstances.

[49] Liechtenstein Government Report No. 48/2010, p. 196.

3.2. Appeal proceedings

The assessment procedure ends with the service of the assessment decree by the Fiscal Authority. If the Fiscal Authority has identified an abusive structure and adjusted it in accordance with the GAAR set out in article 3 of the Tax Act and if the taxpayer does not agree to this adjustment, then article 116 of the Tax Act allows the taxpayer to raise an objection with the Fiscal Authority within 30 days from the service of the decree. Such an objection can be used by the taxpayer not only to contest misapplication of the GAAR, but also to assert any other shortcomings; including in the case of a discretionary assessment, albeit only for obvious inaccuracies. The objection itself must be submitted in writing and must contain the petitions and the justification for them, with an indication of the evidence (e.g. completed tax return, accounting records), as well as the signature of the objector or his or her representative. If these requirements have been met, the Fiscal Authority reviews the matter and may amend the decree in full or in part. The objector has the right to present the objection to the Fiscal Authority in person.

Pursuant to article 117 of the Tax Act, the taxpayer may appeal to the National Tax Commission against an objection decision of the Fiscal Authority within 30 days from its service.[50] Again, all shortcomings may be asserted, but in the case of a discretionary assessment or discretionary decision, only for obvious inaccuracies. As was the case for an objection to the Fiscal Authority, the appeal must be submitted in writing and must contain the petitions and the justification for them (including evidence), as well as the signature of the appellant or his or her representative. The appeal is then presented to the Fiscal Authority to allow it to respond. Upon conclusion of the investigation, the National Tax Commission reaches a decision and communicates it to the parties.

If the taxpayer still believes the assessment is incorrect, an appeal may be lodged with the Administrative Court against the decision of the National Tax Commission within 30 days of service in accordance with article 118 of the Tax Act. This right of appeal is also granted to the Fiscal Authority. The appeal may be used to assert violations of the law or contend that the contested decision of the National Tax Commission is based on facts that contradict the records or were incompletely established.

A further appeal of the decision of the Administrative Court is not possible under the ordinary procedure. Article 15 of the Constitutional Court Act[51] merely provides the possibility of submitting an individual complaint to the Constitutional Court if the complainant believes his rights have been violated with respect to a constitutionally guaranteed right or a right guaranteed by international conventions where the legislative power has expressly recognised an individual right of complaint.

3.3. Changes to legally binding assessments

Finally, articles 119 et seq. of the Tax Act provide the possibility of subsequent corrections to legally binding assessments. The available procedures differ according to whom they benefit: the back tax procedure benefits the tax authorities by correcting assessments that

[50] If the objection concerns a fully substantiated decree, the Fiscal Authority may also forward the objection as an appeal to the National Tax Commission upon application or with the consent of the objector (art. 116(4) of the Tax Act).

[51] *Gesetz vom 27. November 2003 über den Staatsgerichtshof*, LR 173.1.

are too low, while the review procedure benefits the taxpayer by remedying overtaxation. In doing so, pursuant to article 123(1) of the Tax Act, a legally binding order or decision may be reviewed on request, or ex officio in favour of the taxpayer, if significant facts come to light or conclusive evidence is produced, or the decision-making authority failed to take significant facts or conclusive evidence of which it was aware or should have been aware into account, or otherwise if it violated significant procedural principles.

Two further possibilities exist to correct assessments:[52] by means of article 124 of the Tax Act, the implementation of mutual agreements and arbitration awards is ensured. According to this provision, an assessment order shall be issued, reversed or amended, insofar as this is required for the implementation of a mutual agreement or an arbitration award under an international tax agreement.

Pursuant to article 125 of the Tax Act, accounting errors and typing mistakes in legally binding orders and decisions may be corrected within a period of five years from delivery, at the request of the taxpayer or ex officio, by the authority that made the errors. In this context, the same legal remedies may be adopted against the correction or rejection of a correction as are adopted against the earlier order or decision.

These two correction possibilities occupy a middle position and may act in either direction, i.e. for the benefit of the tax authorities or for the benefit of the taxpayer.

[52] Liechtenstein Government Report no. 48/2010, pp. 215 et seq.