Liechtenstein: Protected Cell Company as an instrument for sustainable investment structures?

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With the Segmented Legal Entity or Protected Cell Company, the possibility of segmenting legal entities was introduced in Liechtenstein. This is an organizational form that offers various organizational and liability advantages. This article discusses the extent to which the Protected Cell Company offers solutions for the creation of sustainable structures – particularly with regard to increased substance requirements for the use of double taxation agreements («DTAs»)*.

1 Civil law foundations of the Protected Cell Company (PCC)

1.1 Basic concept of the PCC under Liechtenstein law

Articles 243 et seq. of the Persons and Companies Act (Personen- und Gesellschaftsrecht; «PGR») created the basis for the Segmented Legal Entity (segmentierte Verbandsperson; «SV») as of 1 January 2015, which, according to the will of the legislator, may also appear externally in English under the designation Protected Cell Company («PCC»; cf. Art. 243b PGR). This is not a new, independent kind of entity, but an organizational form that can be applied to the legal entities already available under the PGR. In accordance with the nature of the PCC as an organizational form of corporate law that is based on existing legal entities, the legal entity's own general provisions initially apply. Only where the provisions on legal entities are not sufficient, have separate provisions been created for the PCC. Therefore, mandatory company law standards, in particular those specific to the legal form, take precedence over those relating to the PCC.[1]

The segmentation of a legal entity in the form of a PCC is subject to two main restrictions pursu-

ant to Art. 243 para. 1 PGR. Firstly, it is assumed that the legal entity is obliged to be entered in the commercial register or that it actually voluntarily registers. Furthermore (and for the time being[2]), there is a restriction to the extent that the permissible corporate purposes are reduced to those listed below:

– Non-profit or charitable purposes within the meaning of Art. 107 para. 4a PGR[3]
– Acquisition, management and realization of participations in other companies (subsidiaries)[4]
– Exploitation of copyrights, patents, trademarks, samples or models
– Deposit-guarantee and investor protection schemes in accordance with applicable EEA legislation

This is an exhaustive enumeration, whereby cumulation of these purposes does not preclude segmentation.[5]

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1 Cf. the Government Report and Motion No. 69/2014 concerning the Amendment of the Persons and Companies Act (Segmented Legal Entity/Protected Cell Company), p. 15 f. (hereinafter referred to as «Report and Motion»).

2 Cf. the outlook in Chapter 4.

3 A tax exemption pursuant to Art. 4 para. 2 of the Liechtenstein Tax Act is not required (Report and Motion, p. 29).

4 It is assumed that the management of a commercial, manufacturing or other commercially managed business takes place at the level of the subsidiary, while the activities of the parent company must be limited exclusively to the activities pursuant to Art. 243 para. 1 ciph. 2 PGR (Report and Motion, p. 30).

5 Report and Motion, p. 28.

The PCC consists of a core and one or more segments separated from each other (cells; cf. Art. 243e para. 1 PGR). Although the latter are treated like independent companies, they do not have their own legal personality. Only the PCC (i.e. the segmented legal entity; cf. Art. 243 para. 2 and 3 PGR) has legal personality. The special aspects of segmentation are explained in more detail below.

1.2 Special aspects of segmentation

1.2.1 Assets of a PCC and minimum capital requirements

The core assets and the assets allocated to the individual segments of a PCC each represent independent, separate asset masses, whereby the core assets are defined negatively by law as assets not belonging to a segment (Art. 243e para. 1 PGR). The assets of a segment are allocated only to that segment and not to any other segment or to the core assets. The assets of the individual segments must be clearly identifiable and kept separate from each other and from the core assets. For reasons of creditor protection, transfers of assets between the segments may only be approved by the judge in non-contentious proceedings if objectively justified reasons exist (Art. 243e para. 4 PGR).

The core assets must comply with the minimum capital requirements of the respective legal entity. In addition, each segment must have a legal reserve in the amount of the minimum capital of the PCC (Art. 243 para. 2 PGR).

1.2.2 Determination of the field of activity and representation

The separation of the assets allows the individual segments to conduct their business independently of each other. The segments may perform certain activities that must be described in more detail in the articles of association or the regulations (cf. Art. 243 para. 3 in conjunction with Art. 243c para. 1 ciph. 4 and para. 2 PGR). However, the areas of activity of the individual segments may not contradict either the purpose of the PCC or the area of activity of another segment.[6]

As mentioned above, the individual segments have no legal personality of their own. The question therefore arises as to how the segments can conduct business.

In the absence of their own legal personality, the individual segments do not have their own organs; furthermore, a valid signing right cannot be established for a specific segment alone. Rather, the individual segments are represented externally exclusively by the authorized representatives of the PCC. Consequently, only the PCC appears to the outside with the indication that it is acting for a specific segment. Pursuant to Art. 243d para. 1 PGR, the PCC is managed and represented by the bodies empowered by law or the articles of association. In this regard, the provisions governing the organization of the respective legal form (e.g. public limited company, limited liability company, establishment, foundation) must be observed.[7]

In the absence of other legal or statutory provisions, the provisions governing the trust apply analogously to the relationship between the core and the individual segments (Art. 243d para. 2 PGR).

1.2.3 Contractual and non-contractual liability

One of the main advantages and «core idea»[8] of segmenting a legal entity is the limitation of third-party liability claims to the assets of a single segment. The precondition for this is that the PCC (its authorized representatives) informs third parties in writing of their status as PCC when entering into contractual negotiations and designates to the contracting party the segment (or core) with whose assets the PCC shall be liable for the legal relationship in question (Art. 243f para. 1 PGR).

If these formal requirements are met, only the assets of the segment on whose field of activity the claim is based are liable for contractual claims of third parties. Only if the assets are insufficient to satisfy the claim, the core assets are subordinated (Art. 243f para. 2 PGR). Consequently, the assets of the other segments (if any) remain unaffected. If these information duties are not (sufficiently) fulfilled, the law provides for a personal, but subordinate liability of the culpable body in relation to the segment assets (Art. 243f para. 1 PGR). There is therefore no penetration through the segmented assets. Uninvolved segment assets remain unaffected by the breach of duty of the culpable body and thus the separation of liability of the individual segments as the core idea of a PCC remains untouched.[9]
Non-contractual claims by third parties are limited to the core assets of the PCC. If the core assets of the PCC are not sufficient to satisfy the claim, the assets of the segment in whose area of activity the PCC has caused the claim are subordinated. The management is obliged to provide any claimants with the information required to assert the claim (Art. 243f para. 3 PGR).

1.2.4 Segment shares

If the PCC is organized in the form of a public limited company and if the articles of association of the PCC contain provisions on the issue of own shares and the rights associated with this, own shares may be issued in respect of individual or all segments (so-called segment shares). These shares are those of the PCC. Although the shareholders are shareholders of the PCC, their pecuniary participation rights relate only to the individual segment. Hence, dividends are distributed as segment dividends only in respect of the individual segment. Whilst the pecuniary participation rights relate only to the respective segment, the participation of the segment shareholders in respect of their co-determination rights relates to the PCC as a whole. Consequently, the segment shareholders exercise their voting rights at the General Meeting of the PCC.[10] The legal reference to the provisions on preference shares (Art. 243e para. 5 PGR) is likely to provide an opportunity for very flexible solutions tailored to individual needs.

1.3 The Liechtenstein PCC as an independent solution

As HELBOCK points out, Liechtenstein is a country which, due to its limited financial and human resources, is dependent on the reception of regulations from foreign legal systems in many areas of law. This is accompanied by a reliance on the development of the law in the country of origin (doctrine and jurisdiction). Although the PCC is used internationally in various forms[11], Liechtenstein has introduced its own organizational form, tailored in particular to its own legal system and based on the existing foundations of company law.[12] Against this background, the doctrine and, in particular, jurisprudence

6 Cf. the Report and Motion on the whole, p. 36 f.
7 Cf. the Report and Motion on the whole, p. 45.
8 Report and Motion, p. 52.
9 In this sense also HELBOCK, Besondere Aspekte der Segmentierten Verbandsperson (PCC) in Liechtenstein, in: Liechtensteinische Juristenzeitung (LJZ), 1/2018, p. 23.
10 Art. 243e para. 5 PGR as well as Report and Motion, p. 49 f.
11 With Italy and Luxembourg, for example, EU member states are also familiar with the segmentation of legal entities; furthermore, numerous US federal states (cf. Report and Motion, p. 11 f.) and also jurisdictions such as Bermuda, Guernsey, Gibraltar, Malta, Isle of Man and Jersey (cf. HELBOCK, Besondere Aspekte der Segmentierten Verbandsperson [PCC] in Liechtenstein, in: Liechtensteinische Juristenzeitung [LJZ], 1/2018, p. 23).
12 HELBOCK, Besondere Aspekte der Segmentierten Verbandsperson (PCC) in Liechtenstein, in: Liechtensteinische Juristenzeitung (LJZ), 1/2018, p. 25.

developing into the PCC can be expected with interest.
In Switzerland, Germany and Austria, the concept of a segmented legal entity is not provided for.[13]

2 Tax aspects

2.1 Taxation of PCCs

Liechtenstein legislation does not contain any specific provisions regarding the taxation of a PCC as the PCC does not represent a legal form of its own, but merely an organizational form of existing legal entities. Consequently, as stated by MAUTE, GASSER and WILLI, the actual economic structure of the company must be taken into account when evaluating how it is to be taxed. For example, a segmented public limited company is taxable as a corporation pursuant to Art. 44 et seq. of the Liechtenstein Tax Act.[14]
As the individual segments have no legal personality, only the PCC as a whole is subject to taxation. In accordance with the authoritative principle, only one tax return must be submitted based on the annual financial statements of the PCC. With regard to stamp duties, the stamp duty exemption of CHF 1 million can only be claimed in its entirety for the PCC. In addition, all securities held by the PCC are taken into account for the purpose of qualifying as a securities dealer according to Art. 13 para. 3 lit. d Stamp Act.[15]

2.2 PCC as a means of creating and preserving substance

As shown in Chapter 3 below, the PCC is suitable both for creating[16] and preserving[17] substance.
The substance requirements are important, among other things, with regard to the question of DTA eligibility. The OECD/G20 project BEPS («Base Erosion and Profit Shifting») is particularly relevant here. The latter is an action plan aimed at tackling the problem of base erosion and profit shifting of internationally active companies. The BEPS action plan comprises a total of 15 measures, five of which are devoted to the topic of substance.[18] In the following, BEPS Action 6 on preventing the granting of treaty benefits in inappropriate circumstances will be discussed in view of the importance of substance requirements in international relations. Prior to this, however, the substance requirements will be discussed from a Swiss perspective.

2.2.1 Substance as a prerequisite for DTA eligibility from a Swiss perspective

When a Swiss subsidiary distributes profits to its foreign (e.g. Liechtenstein) parent company, withholding tax is payable. In order to benefit from advantages under the provisions of a DTA, the parent company must, among other things, meet substance requirements.
When assessing a tax relief on the basis of a DTA, it must first be examined whether the receiving parent company is domiciled in one of the two contracting states, which is a basic prerequisite for claiming DTA benefits (cf. Art. 4 of the OECD Model Tax Convention). Since residency cannot only be established by the statutory seat of a company, but is also understood as the place of its actual management[19], the requirement of substance is of importance. In particular, the place of actual management can only be where there is sufficient personnel and infrastructure to fulfil management activities (more on this immediately). If the residency is affirmed, the next step is to clarify the question of the right of use. In this respect, sufficient financial substance is (at least) an indication that the right of use exists. If the right of use is also affirmed, the final step is to examine whether there has been an abuse of the DTA. In this context, a lack of substance is an indication of abuse.[20]
STIEGLER has identified the following three main substance-related categories on the basis of the

case law of the Swiss Federal Supreme Court and the Tax Appeal Commission as well as the criteria of the Swiss Federal Tax Authority:[21]

– Personnel and infrastructural substance: It is examined whether the company has the necessary personnel and infrastructural substance to fulfil its business purpose.[22] In this respect, the question arises in particular as to whether telephone, fax and computer connections etc. are available in one's own offices. In order to check whether the structure is actually lived, regular reference is made to telephone bills, account statements and rental agreements. It is also checked whether the books are kept at the company's registered office.
– Functional substance: It is checked whether the purpose of the company is adhered to and whether the economic structure of the company is lived. This means that an actual business activity must take place. Against this background, it would be particularly advantageous for holding companies to manage several participations.[23]
– Financial substance: The recipient company must be properly financed in order to assert the right to use the dividend. The Swiss Federal Tax Authority is guided by Circular No. 6 on hidden equity and requires an equity ratio of 15 % for pure financing companies and 30 % for holding companies.

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13 As regards this and the taxation of the PCC from a Swiss perspective: MAUTE/GASSER/WILLI, Besteuerung der liechtensteinischen segmentierten Verbandsperson aus schweizerischer Sicht, in: Steuer Revue, No. 7–8/2015, p. 551 f.

14 Cf. MAUTE/GASSER/WILLI, Besteuerung der liechtensteinischen segmentierten Verbandsperson aus schweizerischer Sicht, in: Steuer Revue, No. 7–8/2018, p. 551.

15 BENEDETTER/KNÖRZER, Besteuerung einer segmentierten Verbandsperson in Liechtenstein, in: Zeitschrift für Stiftungswesen (ZFS), December 2015/No. 4, p. 264 ff.

16 In this sense, MAUTE/GASSER/WILLI, Besteuerung der liechtensteinischen segmentierten Verbandsperson aus schweizerischer Sicht, in: Steuer Revue, No. 7–8/2018, p. 550 f. as well as HELBOCK, Besondere Aspekte der Segmentierten Verbandsperson (PCC) in Liechtenstein, in: Liechtensteinische Juristenzeitung (LJZ), 1/2018, p. 25.

17 Cf. the examples of use in Chapter 3.

18 Cf. HUBER/BARTZ/BERR, Blickpunkt «BEPS» Base Erosion and Profit Shifting, in: Steuer Revue, No. 12/2014, p. 846 ff.

19 This criterion is still relevant according to the OECD Model Tax Convention 2017 in the context of the stipulated mutual agreement procedure (cf. Art. 4 para. 3 OECD-MC 2017; OECD, Model Tax Convention on Income and on Capital: Condensed Version 2017, OECD Publishing, 2017).

20 ZITTER/GENTSCH, Substanz von Empfängergesellschaften bei Outbound-Dividenden, Analyse und Würdigung der Schweizer Praxis (2. Teil), in: IFF Forum für Steuerrecht, 2009/4, p. 255 ff.

21 STIEGLER, Substanzerfordernis im Zusammenhang mit der Rückerstattung der Verrechnungssteuer im internationalen Verhältnis, in: Steuer Revue, No. 1/2016, p. 10.

22 Regarding the dependence of the substance requirements on the corporate purpose, see ZITTER/GENTSCH, Substanz von Empfängergesellschaften bei Outbound-Dividenden, Analyse und Würdigung der Schweizer Praxis (2. Teil), in: IFF Forum für Steuerrecht, 2009/4, p. 263.

23 With regard to the departure from the safe-haven regulation in connection with the degree of self-financing of foreign holding companies, see STIEGLER, Substanzerfordernis im Zusammenhang mit der Rückerstattung der Verrechnungssteuer im internationalen Verhältnis, in: Steuer Revue, Nr. 1/2016, p. 10 f.

2.2.2 BEPS Action 6: Measures to prevent abuse of DTAs

BEPS Action 6 aims at international standardization on the issue of the eligibility of DTAs. The agreement-related provisions of BEPS Action 6 are incorporated into existing DTAs through adjustments based on the Multilateral Convention to Implement Tax Treaty Related Measures to Prevent Base Erosion and Profit Shifting (MLI) signed by Switzerland and Liechtenstein on 7 June 2017 and through bilateral amendment protocols.[24]

According to the final report on BEPS Action 6 concerning the prevention of the granting of treaty benefits in inappropriate circumstances, the abuse of treaties, in particular so-called treaty shopping, is one of the most important aspects of the problem of base erosion and profit shifting. The participating states have therefore agreed to include anti-abuse provisions in their DTAs. In particular, these provisions are intended to combat strategies whereby a person not resident in a state tries to obtain benefits in that state (e.g. by setting up a letter-box company) which this state grants to persons resident there under a DTA concluded by it. To this end, the following measures are planned, which have already been incorporated into the OECD Model Tax Convention (2017) and the corresponding commentaries:

– DTAs should include a clear statement that the states concluding the agreement intend to avoid the creation of possibilities for non or reduced taxation through tax evasion or avoidance, including through treaty shopping arrangements.
– Inclusion of a Limitation-on-Benefits («LoB») clause in the OECD Model Tax Convention. This is intended to ensure that there is a sufficient link between a legal entity and its state of residence by virtue of its legal nature, ownership in and general activities of the legal entity. The LoB clause is aimed solely at preventing treaty shopping.
– Inclusion of a general anti-abuse provision that focuses on the main purpose of transactions and arrangements (so-called principal purpose test; «PPT clause»). According to this provision, the granting of treaty benefits shall be denied if one of the main purposes of transactions and arrangements is to obtain those benefits, unless it is established that granting these benefits is consistent with the object and purpose of the agreement provisions. In particular, the PPT clause is intended to cover forms of agreement abuse not covered by the LoB clause.

It is at the discretion of the states whether they include both the LoB clause and the PPT clause, exclusively the PPT clause, or the LoB clause supplemented by a mechanism for taking into account conduit financing arrangements not yet covered by their DTAs.[25]

Both the commentaries on the LoB clause and those on the PPT clause point to the importance of substance for entitlement to treaty benefits. For example, the commentaries regarding the LoB clause state that the term «business» must be given the meaning that it has under domestic law, but they also state that a legal entity is generally only considered to be active in business if the persons through whom the legal entity operates (e.g. the officers and employees of the company) carry out significant managerial and operational activities.[26] The examples of the PPT clause are even clearer:

– Example G: A group is considering establishing a regional company to provide group services to other group companies, including management services such as accounting, legal and human resources services, financing and treasury services such as currency risk management and hedging, and some other non-financial services. The group decides to establish the group service company in state R. This is due, among other things, to skilled labour force, a reli-

able legal system but also the extensive DTA network, including the five states in which group companies are located, all of which provide for low withholding tax rates. The commentary notes the following: «Assuming that the intra-group services to be provided [by the group service company], including the making of decisions necessary for the conduct of its business, constitute a real business through which [the group service company] exercises substantive economic functions, using real assets and assuming real risks, and that business is carried on by [the group service company] through its own personnel located in state R, it would not be reasonable to deny the benefits of the treaties concluded between state R and the five states where the subsidiaries operate […]».[27]

– Example H: This example also focuses on the human and financial resources (in various areas such as law, finance, accounting, taxation, risk management, auditing and internal control) necessary to carry out the activities of a group company.[28]

DANON concludes therefrom that the substance requirement is one of the key elements to prove that obtaining a benefit under a DTA is not the primary purpose of a structure or transaction.[29]

3 Examples of use

As explained above, the PCC has legal personality as a whole. In contrast to the subsidiaries within a holding structure, the segments of a PCC are not assessed individually for DTA eligibility purposes due to their lack of legal personality.[30] Instead, the substance requirements are examined on the basis of the entire PCC. In addition, the overarching support processes can be centralized within the PCC. In contrast to a group structure, it is not necessary to set up and maintain appropriate bodies for each subsidiary, which may lead to considerable cost savings. The use of synergies thus makes it possible to increase the personnel, infrastructural and functional substance. With regard to the Principal Purpose Test, these positive aspects of a PCC, and in particular the achievable separation of liability, represent significant economic reasons that speak against a structure implemented mainly for tax reasons. With the help of the organizational structure of a PCC and the scale

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24 Cf. the comments in the explanatory report on the Multilateral Convention to Implement Tax Treaty Related Measures to Prevent Base Erosion and Profit Shifting (MLI) and in an amendment protocol to the double tax treaty between Switzerland and the United Kingdom, Federal Department of Finance (Eidgenössisches Finanzdepartement; EFD), 20 December 2017, in particular p. 7.

25 Cf. OECD, Preventing the Granting of Treaty Benefits in Inappropriate Circumstances, Action 6 – Final Report 2015, OECD/G20 Base Erosion and Profit Shifting Project, OECD Publishing, Paris, p. 9 f. and 18 f.; see also p. 55 f., para. 4 f. on the relationship between the two clauses, if both the LoB clause and the PPT clause apply (hereinafter cited as «Final Report 2015»).

26 However, the execution or management of capital investments for the resident person's own account only counts as business activity if the activity is part of the banking, insurance or securities business of a bank or a similar financial institution or an insurance company or authorized securities dealer; furthermore, a company which exclusively acts as head office is not considered to be actively engaged in business activity (Final Report 2015, p. 37, para. 47 f.).

27 Final Report 2015, p. 62, example G.

28 Final Report 2015, p. 62 f., example H.

29 See DANON, Treaty Abuse in the Post-BEPS World: Analysis of the Policy Shift and Impact of the Principal Purpose Test for MNE Groups, in: Bulletin for International Taxation, 01/2018, p. 48.

30 In this sense also HELBOCK, Besondere Aspekte der Segmentierten Verbandsperson (PCC) in Liechtenstein, in: Liechtensteinische Juristenzeitung (LJZ), 1/2018, p. 25.

achievable as a result, further specific requirements under various DTAs can also be met. For example, some countries require the company to hold various investments of appropriate size. The higher substance thus facilitates the use of the respective DTAs.[31]

In the following, three selected examples of use of the PCC for the purpose of creating or preserving substance are discussed. This is by no means an exhaustive list, but rather thought-provoking ideas designed to highlight possible advantages of a PCC.

3.1 Succession planning

The transfer of assets to the next generation is known to pose many challenges for today's owners. If there are complex asset structures such as group investments, real estate, luxury goods and other assets, these are regularly distributed among the existing descendants. Often a split is only made because there is no viable alternative. The transfer of a group participation to several descendants, for example, exposes the continued existence of the group over further generations to a high risk, as experience has shown. Endowing the assets to a foundation can be a sensible and sustainable solution. The combination of a foundation solution with the organizational form of a PCC (i.e. applied to a foundation) can positively support this solution. Nevertheless, foundations in various jurisdictions are only known to a limited extent or do not exist as their own corporate form under national law and in practice lead to problems in the area of legal recognition and challenges in the area of conflict between asset protection and tax transparency. The corporate form of a public limited company, on the other hand, is an established corporate form of national law in most jurisdictions worldwide or at least exists in a similar form. If the organizational form of the PCC is applied to a Liechtenstein public limited company, the international acceptance of the public limited company as well as the legal structure of the Liechtenstein PCC offer flexible possibilities for making the existing assets accessible to the descendants without fragmentation.

On the one hand, a separate segment can be created for each descendant, to which the assets in which the respective descendant is to participate are allocated (cf. figure 1). On the other hand, the assets can also be allocated to certain segments and the descendants participate proportionately in the individual segments to the extent intended for them (cf. figure 2). Both approaches offer the possibility of holding assets together and concentrating them in a single entity. The consolidation of assets results in synergy benefits and potential cost savings. The core of the PCC takes over the administrative activities of all segments. The existing substance can thus be concentrated in a single entity through consolidation. By preserving the substance and increasing it by expanding its activities, the structure also meets the increased international substance requirements from a tax perspective.

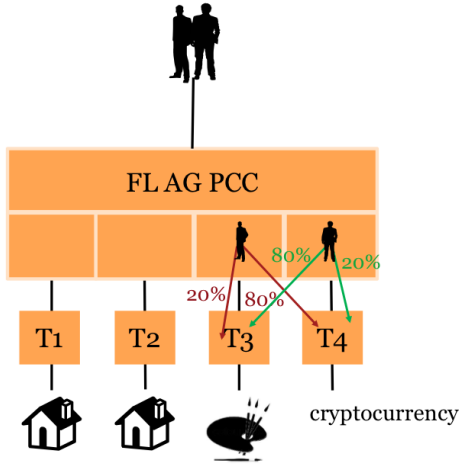

Figure 1: Separate segment per descendant

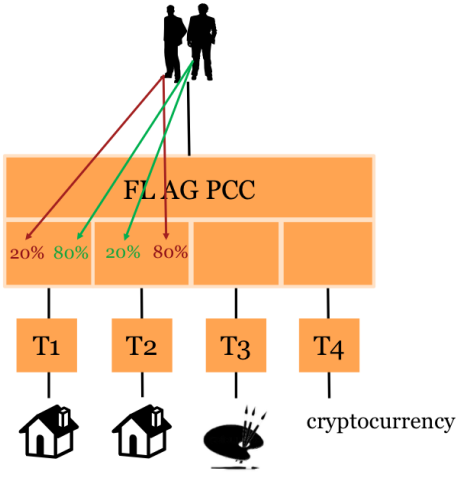

Figure 2: Descendants participate proportionally in segments

3.2 (Multi) Family Offices

Family offices offer a wide range of services for wealthy families. Multi family offices support various families as independent partners in the management of large assets. In both cases, the family office in the form of a company often serves directly as an investment and participation vehicle or separate companies are established and used for this purpose. In the case of a succession solution using a PCC, the focus is on preserving the substance, whereby the use of a PCC offers the possibility of further increasing the existing substance by bringing together additional assets. In contrast to a succession solution, the organizational form of a PCC offers a family office that uses different investment and participation vehicles the opportunity to unify existing structures. Participations and investments can be subdivided and separated into segments that are separated for liability law purposes. The substance formerly divided into different vehicles can be consolidated and thus concentrated by using a PCC. Existing and planned companies as well as structural levels can be eliminated as a result, provided there is no other need for separation of assets under company law. By consolidating the substance in a single entity, family offices can reduce structural costs and exploit synergy advantages in asset management. In the case of multi family offices, economies of scale can achieve additional cost advantages.

In practice, many structures exist today that have grown historically and were set up at a time when the legal, tax, and regulatory requirements and framework conditions were fundamentally different from today's reality. The organizational form of the Liechtenstein PCC offers the possibility to adapt existing structures to the new conditions and to strengthen them sustainably.

3.3 Private Equity

Private equity investments are investments in non-listed companies. Typically, this involves financing for the development and growth of a company. Private equity investors are high net worth individuals or institutional investors such as insurance companies and pension funds. Family offices also regularly count among these investors as part of their activities. Private equity investments can be made directly, provided the investor has the critical size for diversification. Private equity funds can be used to achieve a higher degree of diversification with a lower investment or to supplement the investment portfolio with specific investments for further diversification (e.g. different sectors, geographically different markets or currencies).

[31] Cf. the Government's Statement to the State Parliament of the Principality of Liechtenstein on the questions raised at the first reading on the amendment of the Persons and Companies Act (Segmented Legal Entity/ Protected Cell Company), No. 100/2014, p. 7.

The individual investments are regularly made through independent investment structures.
Figure 3 is intended to illustrate how private equity structures are set up by means of funds (simplified example). In most cases, a fund invests in private equity via a holding company in the form of a public limited company. Depending on the size of the fund and the complexity of the investment strategy, there are subholding companies, e.g. for financing and / or for specific geographical markets.

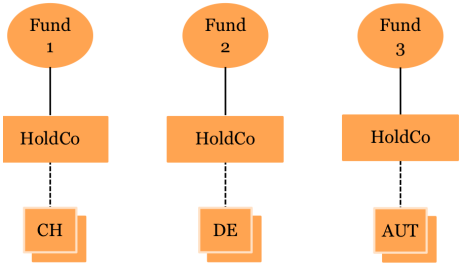

Figure 3: Independent investment structures

Private equity investments are medium to long-term in nature. During the term of the investment, income may be generated in the form of dividends and interest income. In many cases, the intention is to achieve the majority of the return by reselling the investments, i.e. in the form of capital gains on the investments acquired. The choice of location of the holding company is, among other things, influenced by tax considerations, as the withholding taxes on dividends and interest as well as the taxation of capital gains represent a decisive cost factor. In the case of cross-border private equity structures, the tax authorities are focusing their attention on avoiding abusive use of DTAs and in particular on fulfilling substance requirements in financial, personnel and functional terms at the location of the holding company.

In principle, all the above-mentioned considerations with regard to the PCC are also applicable to private equity structures. The disadvantage of existing private equity structures often lies in the dispersion of the substance to separate investment structures. By means of a PCC, different investment strategies can be combined and investments can be separated into individual segments for liability law purposes. Figure 4 below attempts to illustrate what can be achieved by using a PCC. If an investor seeks diversification in various areas of the private equity investment spectrum, he will invest, for example, in various private equity fund products. By designing a PCC accordingly, an investor can achieve the same goal by investing in a single fund vehicle. By issuing segment shares at the level of the holding company (PCC), different funds can participate in different proportions in the individual segments and the underlying investments. In this way, diversification is possible without using separate investment structures. At the holding company level, the substance of several private equity investment structures can be brought together, which makes it easier to meet the increasing substance requirements.

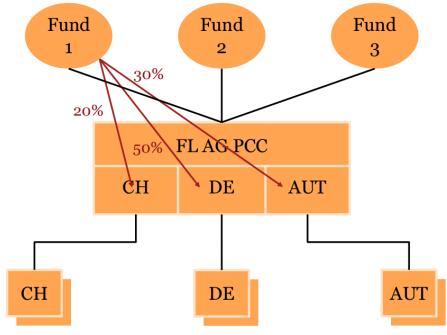

Figure 4: Diversification of investment activity using a PCC

4 Conclusion and outlook

The PCC offers various organizational and liability advantages. It is particularly suitable for setting up sustainable investment structures which, among other things, satisfy the increased substance requirements for the use of DTAs. This, although (for the time being) the permitted corporate purposes are limited.

The government justifies the restriction on the purposes permitted for a PCC by stating that, at present, the use of PCCs should not be permitted in general, particularly for activities regulated under financial market law. In fact, the use of the form of the PCC in the area of activities regulated by financial market supervision is still not permitted, which is why banks, insurance companies, asset management companies etc. cannot be organized in the form of a PCC. On the one hand, the government wants to prevent possible unintended conflicts with the corresponding regulatory requirements. On the other hand, practical experience should first be gained with the legal institute of the PCC. In the event that the PCC proves itself both in theory and in practice, the government has announced the possibility of expanding the use of the PCC – possibly also in areas regulated by financial market law.[32]

The creation of a corresponding legal basis in the regulated area would be very welcome. Especially in the area of so-called captives, in which the Liechtenstein financial center already offers very attractive conditions[33], a segmentation of risks, which could all be managed by the same administration within a single PCC, would favor the creation of substance.

[32] Cf. Report and Motion, p. 14

[33] WÖHRMANN/WILHELMI, Interessanter Standort für Captive-Versicherungen, in: Liechtensteiner Vaterland, article from 9 July 2018 (accessed on 9 August 2018 at http://www.vaterland.li/wirtschaft/region/interessanter-standort-fuer-captive-versicherungen;art198,338466).