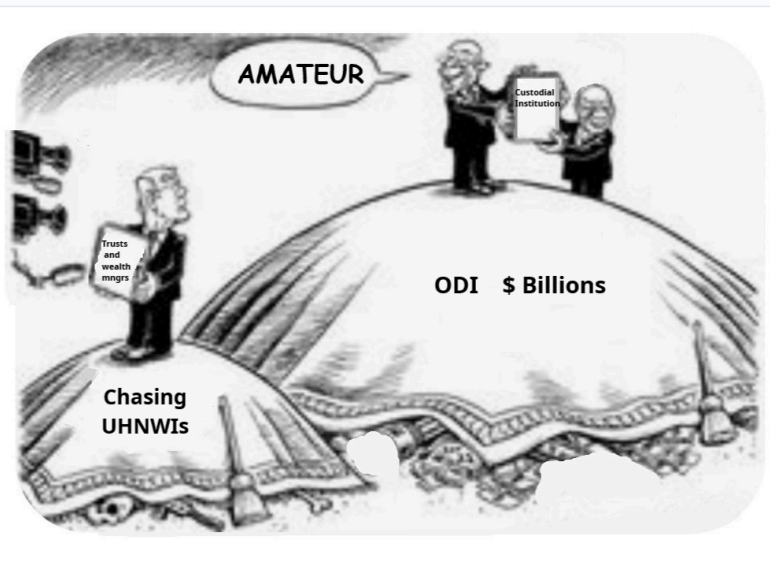

Singapore trusts and wealth managers, get billions under management almost instantly by Chinese sending ODI funds to your privacy structures.

Mark Morris
CRS and CARF expert. No, truly.

August 13, 2024

Comments

Ed Rogers TEP and 2 others

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Messaging

Get untold billions out of China pronto for your wealth management and trust business

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This is an update of my ODI article published in November
2023. It the most read of my publications.
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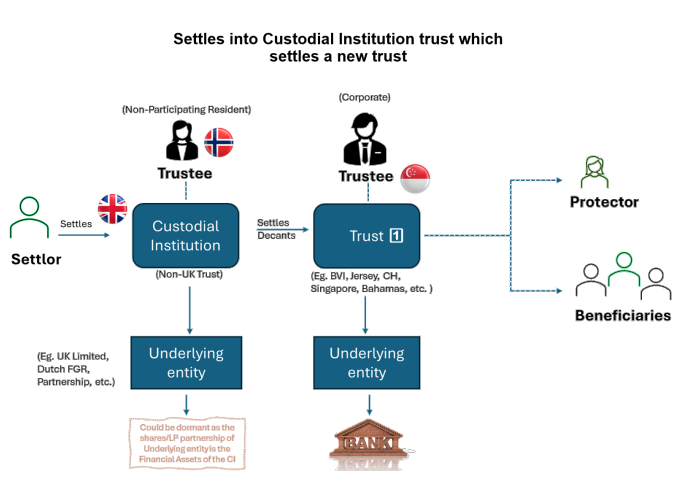
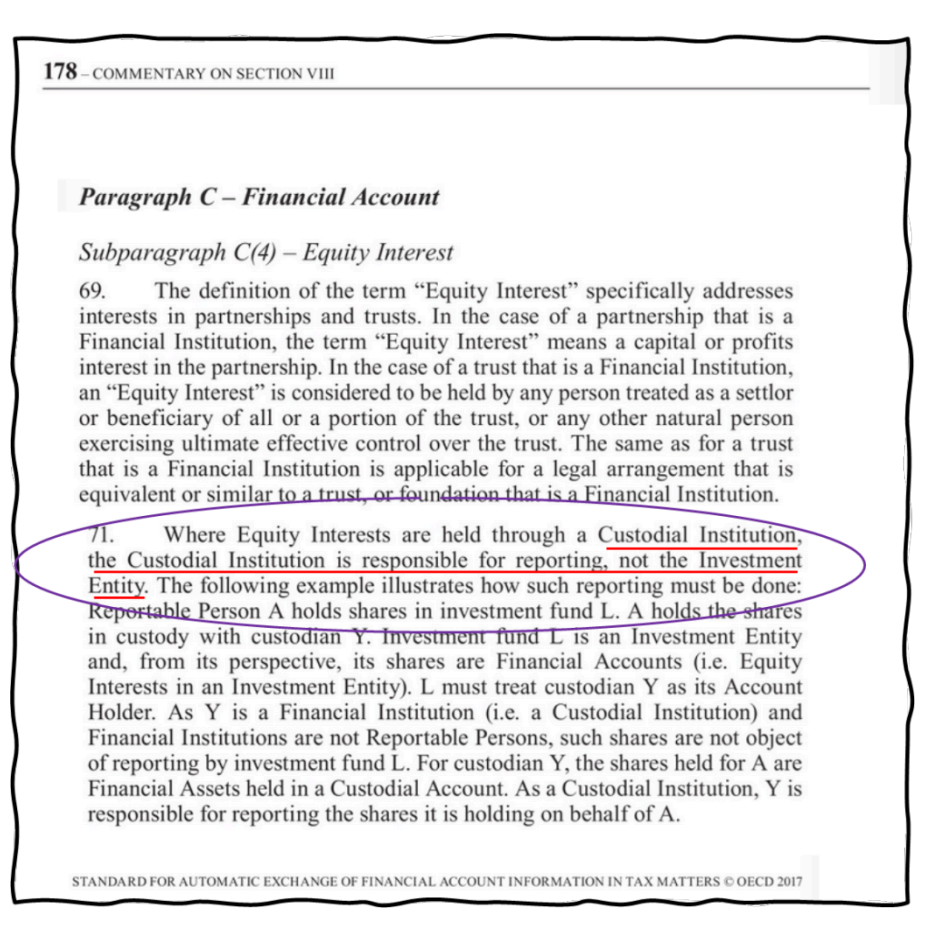

Settles into Custodial Institution trust which settles a new trust
(Non-Participating Resident)
Trustee
(Corporate)
Trustee
Settlor
Settles
Custodial Institution
(Non-UK Trust)
Settles Decants
Trust
(Eg. BVI, Jersey, CH, Singapore, Bahamas, etc.)
Protector
Beneficiaries
(Eg. UK Limited, Dutch FGR, Partnership, etc.)
Underlying entity
Underlying entity
Could be dormant as the shares/LP partnership of Underlying entity is the Financial Assets of the CI
BANK

- Chinese ODI applicant files for ODI and as long as below USD 300 m, it's just a filing procedure.
- Break up larger projects into multiple projects less than $300 m threshold which would require approval.
- China ODI applicant sends his money through a SAFE bank once he has the ODI filing numbers from two state enterprises.
- Applicant sends funds to underlying company (I like UK company as the PSC is only the trustee of the parent Custodial Institution trust) held by a non-uk trust (not registered with HMRC or TRS trust register of beneficial owners)
- Name the Custodial Institution trust "Kazakhstan Cement and Stone Factory" or "Maputo Rail Carraiges", etc. As long as the industry matches China's ODI belt and road strategy.
- Subsequently, the Custodial Institution trust settles a new Singapotre trust.
- As the settlor (equity interest) of new trust is an FI which is excluded reporting person for CRS it is not reported as per CRS page 178, in black and white. No bullshit interpretation by lawyers or ignorant AML-KYC staff.



178 – COMMENTARY ON SECTION VIII

Paragraph C – Financial Account

Subparagraph C(4) – Equity Interest

69. The definition of the term "Equity Interest" specifically addresses interests in partnerships and trusts. In the case of a partnership that is a Financial Institution, the term "Equity Interest" means a capital or profits interest in the partnership. In the case of a trust that is a Financial Institution, an "Equity Interest" is considered to be held by any person treated as a settlor or beneficiary of all or a portion of the trust, or any other natural person exercising ultimate effective control over the trust. The same as for a trust that is a Financial Institution is applicable for a legal arrangement that is equivalent or similar to a trust, or foundation that is a Financial Institution.

71. Where Equity Interests are held through a Custodial Institution, the Custodial Institution is responsible for reporting, not the Investment Entity. The following example illustrates how such reporting must be done: Reportable Person A holds shares in investment fund L. A holds the shares in custody with custodian Y. Investment fund L is an Investment Entity and, from its perspective, its shares are Financial Accounts (i.e. Equity Interests in an Investment Entity). L must treat custodian Y as its Account Holder. As Y is a Financial Institution (i.e. a Custodial Institution) and Financial Institutions are not Reportable Persons, such shares are not object of reporting by investment fund L. For custodian Y, the shares held for A are Financial Assets held in a Custodial Account. As a Custodial Institution, Y is responsible for reporting the shares it is holding on behalf of A.

STANDARD FOR AUTOMATIC EXCHANGE OF FINANCIAL ACCOUNT INFORMATION IN TAX MATTERS © OECD 2017

Background

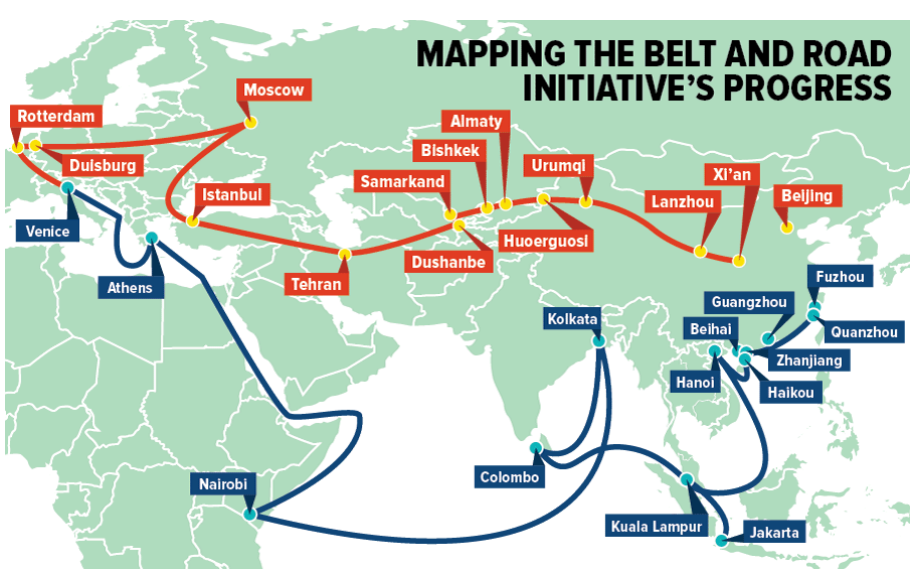
- Most investments out of China are from the Chinese government into the Belt and Road initiative. However, nearly USD 200 billion per year is invested by private enterprises in Outward Direct Investment, now approaching USD 2.3 trillion in total.
- **Note** to portfolio managers, trustees, funds, and banks. There are billions in China waiting to be placed with the wealth industry in Switzerland, Singapore, Liechtenstein, Luxembourg, etc. It's there for the taking.

How to set up privacy structure for ODI funds

- Chinese applicants set up a privacy two tier structure simply by filling in the privacy structure template, signing, and having their signatures attested by local witnesses.
- For those technically orientated, the structure is a non-participating Special Purpose Vehicle Custodial Institution (i.e. persobnally yours) and an underlying owned investment entity. The investment entity legitimately files a "nil report" or "no reportable persons" for CRS because its equity interest is held by a non reportable financial institution (the Custodial institution), and secondly, the parent SPV Custodial Institution has no AEoI reporting obligations as its a non-participating Custodial Institution.
- Chinese applicant files an ODI project (less than USD 300m in value) in the name of the investment entity structure (e.g. AB construction, CD cement factory) with NDRC and MOFCOM
- Register project with a state-approved foreign exchange bank in accordance with the requirements of the State Administration of Foreign Exchange (SAFE).
- Privacy structure is impenetrable as no local person in the jurisdiction of the structure is involved in setting up the Custodial Institution, such as representative agents, local trustees, notaries, lawyers, witnesses, or corporate service providers.
- Privacy is augmented as legally there is no registration for tax or with the beneficial owner register.
- Privacy is guaranteed as the structure is excluded from local and cross-border reporting (Common Reporting Standard, Exchange upon Request).
- Allows client's complete control whilst providing privacy.
- Asset protection is facilitated by privacy.
- Critically, the structure is located in a highly reputed onshore Western European jurisdiction, considered just and fair in the interpretation and enforcement of trusts.

ODI background

Belt and Road initiative (also known as "one belt one road")



- The projects build on the old trade routes that once connected China to the west, Marco Polo and Ibn Battuta's routes in the North, and the maritime expedition routes of Ming dynasty admiral Zheng.
- **Belt** is short for the Silk Road Economic Belt. referring to the proposed overland routes for road and rail transportation through landlocked Central Asia along the famed historical trade routes of the Western Regions.
- **Road** is short for the "21st Century Maritime Silk Road", referring to the Indo-Pacific sea routes through Southeast Asia to South Asia, the Middle East and Africa.
- Some estimates list the Belt and Road Initiative as one of the largest infrastructure and investment projects in history, covering more than 68 countries.
- In the maritime Silk Road, which is already the route for more than half of all containers in the world, deep-water ports are being expanded, logistical hubs are being built and new traffic routes are being created in the hinterland.
- Examples of Belt and Road Initiative: Infrastructure investments including ports, skyscrapers, railroads, roads, bridges, airports, dams, coal-fired power stations, and railroad tunnels.

i). Legal Framework of Chinese Outbound Investments

- With the encouragement of *Going Global Strategy* and the *Belt and Road Initiative*, a growing number of Chinese enterprises have actively implemented Outbound Direct Investment (ODI).
- The Chinese **National Development and Reform Commission** (NDRC) introduced ODI rules in 2004 based on an approval system.
- Updated measures in 2018 complement and expand the reach of the existing 2014 *Administrative Measures for the Verification and Approval and Record-Filing of Outbound Investment Projects* based on a filing system.

II). An Overview of Outbound Regulations

- When a Chinese company plans to invest abroad, various regulatory measures must be taken according to Chinese law: The investor must either:

1. apply to the **NDRC** and the **Ministry of Commerce** (MOFCOM), or
2. register the investment project.

- Once the prospective investor company has successfully completed the relevant procedural steps, the investment project is registered with a state-approved foreign exchange bank in accordance with the requirements of the **State Administration of Foreign Exchange** (**SAFE**).

iii). The Procedure at the NDRC

- Whether the investment project is subject to approval or must only be notified to the **NDRC** largely depends on three criteria:

1. **The investment amount:**

- All investments exceeding USD300 million must submit a project investment report

2. **Indirect or Direct investments**

- For all non-sensitive **direct** investments, an application is sufficient.
- A non-sensitive indirect investment does not require any application.

3. **Sensitive sectors not permitted**

- ·Any project that relates to a sector that has been classified as *sensitive*, a permit will be required, regardless of the envisaged investment volume.

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iv). Procedure at MOFCOM

- The approval and registration procedure with MOFCOM is essentially the same as that of the NDRC.
- The decision on the procedure to be applied also depends on the type of investment as well as the sector in which it shall be made.

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 In 2004, China formally issued regulations on the outbound
direct investment (ODI) of Chinese enterprises based on an
approval regulatory system
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In 2014, China made major adjustments to the ODI regulatory
system, transforming from the approval system to the filing
system· Filing is generally required for normal ODI
projects, and Approval is only required in special cases.
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In 2018, under the principle of the filing system, the
relevant departments further established new sensitive
sectors not allowed.
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Also, a supervision principle based on classification based
on the nature of the projects:  Encouragement, Restriction
and Prohibition
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v). Registration with a Foreign Exchange Bank

- The investment must be registered with a foreign exchange bank that has received the State Administration of Foreign Exchange (SAFE) identification code for financial institutions and has been granted access to the capital account information system.
- Documents to be submitted, inter alia, include the application form for the required currency for the foreign direct investment to be made as well as the company's business license, which contains the "unified social credit number".

vi). New Rules for Chinese ODI 2018

- New measures came into effect in March 2018, relating to the approval and registration procedures with the **NDRC**.
- The reform has broadened the scope of applicability of the **NDRC** rules to include investments:

1. directly
2. indirectly via offshore controlled companies owned by Chinese entities or natural persons.

- Approval no longer constitutes a condition precedent for the validity of the investment agreement but is designed as an enforceable requirement that can be made part of the closing conditions.

vii). New sensitive sectors likely to be blocked

Following a sharp increase in outbound investments and their related capital and currency outflows, the following investments have been classified as *undesirable*, and these sectors have now been included in the catalog of *sensitive* sectors:

1. Hotels
2. Real estate
3. Film
4. Sports (the gambling industry is prohibited)

viii). Encouraged ODI

- ODI projects that are conducive to **Belt and Road** construction and infrastructural connections among neighboring countries and regions.
- ODI projects that may drive the output of superior production capacity, high-quality equipment, and technical standards.
- Strengthen the investment cooperation with overseas high-tech and advanced manufacturing enterprises and encourage the establishment of overseas research and development centers.
- Participate in the exploration and development of overseas oil, gas, mineral, and other energy resources on the basis of prudent assessment of economic benefits.
- Expand the agricultural cooperation with other countries and carry out mutually beneficial investment cooperation in agriculture, forestry, herding, fisheries, and other fields.
- Promote overseas investment in business, culture, logistics, and other services in an orderly manner, and support eligible financial institutions to establish overseas branches and service networks.

ix). Prohibited ODI investments

Chinese enterprises are prohibited from engaging in overseas investment that endangers or may jeopardize national interests and security. The prohibited ODI projects will not be able to obtain the approval or record filing notice from the Commerce Bureau and Development and Reform Commission, which include:

1. Export of core technologies and products of military industries without state approval.
2. Use of technologies, techniques, and products that are prohibited from export by China.
3. The gambling industry, pornography industry, etc.
4. Prohibited by international treaties concluded or acceded to by China
5. Endanger or jeopardize the interests and security of the state.

x). Restricted ODI

1). Exceptions

The first 3 items shall be subject to the approval of the competent department in charge of overseas investment

1. In sensitive countries that have no diplomatic relations with China, subject to war, or shall be restricted by the provisions of bilateral and multilateral treaties concluded by China.
2. In real estate, hotels, movie studios, entertainment, sports clubs and etc.
3. Setting up offshore equity investment funds without specific underlying industrial projects.
4. Involves the use of backward production equipment that does not meet the technical standards of the destination country.
5. Does not meet the environmental protection and energy consumption safety standards of the destination country.

2). Exceptions

The following six types of ODI activities are excluded from the restricted **real estate** investment:

1. Investment in property management and real estate agency businesses
2. Construction or acquisition of properties for self-use, including office premises and employee dormitories
3. Investment in industrial infrastructure construction and development, such as industrial parks, science and technology parks, and logistics parks
4. Construction enterprises in exchange for a minority stake in projects with the purpose of obtaining construction contracts for such projects
5. Uncompleted projects that have been approved by the Development and Reform Commission or have been notified for record filing in accordance with the law
6. Not involving domestic assets or interests or provision of onshore financing or guarantee. The entire capital is raised from overseas.

The following four types of ODI activities are excluded from the restricted hotel investment:

1. In hotel management businesses holding no hotel properties
2. In restaurant businesses without lodging services
3. Uncompleted projects that have been approved by the Development and Reform Commission or have been notified for record filing in accordance with the law
4. Not involving domestic assets or interests or provision of onshore financing or guarantee. The entire capital is raised from overseas.

The following 2 types of ODI activities are excluded from the restricted category of setting up offshore equity investment funds or investment platforms without specific underlying industrial projects:

1. Equity investment funds or investment platforms which involve neither commitment of domestic assets or interest nor provision of onshore financing or guarantee and whose entire capital is raised from overseas
2. Equity investment funds or investment platforms without specific underlying industrial projects formed by domestic financial institutions with the pre-approval of the competent financial regulatory authorities in China.

The 2018 new measures leave some issues unanswered:

1. Without the approval of the competent Chinese authorities, Chinese investors are not really in a position to enter into legally binding agreements, unless the other party to a given transaction is willing to accept that the closing of such transaction will depend on the relevant approval being granted.
2. Even if the investment project only needs to be registered, the investor requires a "record-filing" notice from the **NDRC** in advance.

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Mark Morris
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