PRIVATE CLIENT
GLOBAL ELITE

THE MONTH

MAY 2023

LUXURY ASSETS

2023 - 2024

Private Client Global Elite Celebratory Dinner
Leighton House, London, 26 January 2023

Private Client Forum Americas
Banyan Tree Mayakoba, 12-14 February 2023

International Women's Day Leadership Brunch
London, Thursday 9th March 2023

Private Client Exchange Switzerland
15-16 March, Guarda Val, Switzerland, 2023

Rising Leaders Leadership Brunch
London, 20th April 2023

Private Client Exchange Bermuda
Rosewood Hotel, Bermuda, 9-10 July 2023

Minds of the Future Exchange
Terre Blanche, 14-16 September 2023

Trust & Estates Litigation Forum
La Mamounia, Marrakesh, 20-22 September 2023

Private Client Exchange France
Chateau Saint-Martin, 5-6 October 2023

International Private Client Forum
Villa d'Este, 15-18 November 2023

Private Client Exchange UK
Cliveden House, UK, 30 November - 1 December

Private Client Exchange Cayman
The Ritz, Tuesday 16 - Wednesday 17 January 2024

Private Client Global Elite Celebratory Dinner
Spencer House, London, Thursday - 1 February 2024

Private Client Forum Americas
Wednesday 28 February - Friday 1 March 2024

International Women's Day Leadership Brunch
London, Thursday 7th March 2024

Private Client Exchange Switzerland
Guarda Val, Switzerland, 15-16 March 2024

Rising Leaders Leadership Brunch
London, 18th April 2024

Private Client Exchange Italy
Italy, 21st-22nd April 2024

Please note that events in gold require an are open to all private wealth lawyers, with a membership discount.

The Exchanges in blue are our member-only events.

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EDITOR NOTE

FRANCESCA FFISKE

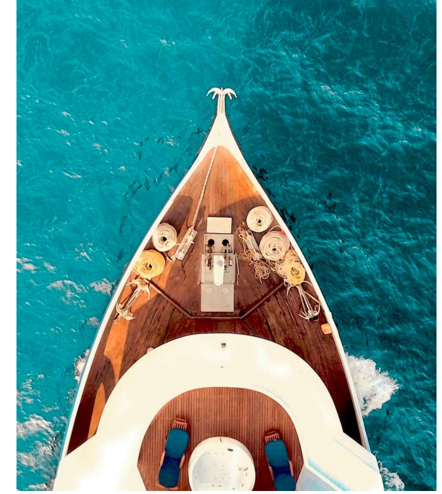
If watching Succession has confirmed anything, it's that the ultra-wealthy love a bit of luxury. As private wealth advisors luxury assets - yachts, wine, cars, homes, jewellery, and watches, are assets which we must be aware of when structuring trusts and estates.

This edition will focus on everything to do with luxury assets. We visit the art world with **Evelyn Sheehan and Lara Levinson** from Kobre & Kim, and with **Philipp Konzett** from Gasser Partner. Next, we discuss it with the Next Generation with **James Campbell,** we visit Italy with **Giorgia Zanetti and Alberto Brazzalotto,** and we even have a peek into the world of insurance - passing down luxurious assets through the generations within a family with **Jonathan Morris**. Finally, **Bethan Waters** shows us how to unlock liquidity within valued possessions, and **Daniel Channing** tells us about how, at the end of the day, good governance is the most important thing to underpin strategies.

We hope you enjoy this edition.

CONVERSATIONS WITH THE NEXT GEN: LUXURY ASSETS - AN EVOLVING LANDSCAPE

JAMES CAMPBELL, OGIER



It is not uncommon for families to hold some form of tangible or luxury assets within their investment portfolios. From vintage and rare cars to fine wines and art, such assets are frequently found within family structures. These assets may be purchased as an investment or simply as a lifestyle choice inspired by a particular interest.

The fact that Sotheby's posted record art sales of US$7.3 billion in 2021 and that sale volumes of fine wine and watches both rose an impressive 16% through the year (Knight Frank Wealth Report, 2022) are testament to the fact that luxury and collectible assets remain a target for private investors. However, with the much hyped 'great wealth transfer' on the horizon – almost US$70 trillion is anticipated to be passed on in the coming years – and the next gen set to assume a greater role in family investment decisions – 70% of families identify a greater role for the next gen in family office activity in the coming years (Family Capital, 2022) – there are question marks over the role and place of such assets.

First, they are often emotionally attached to the family member who originally made the decision to invest, and it is possible – in fact, likely – that future generations may not share the same passions. Or worse, that they may actually conflict with their beliefs.

Second, luxury assets are not necessarily that good at generating returns, and future generations may want to explore how they can leverage more from those assets. However, pure investment return is not the only metric in today's investment world. Of considerable importance is the ESG factor, namely the positive, measurable social and environmental impact of any given investment.

So, what happens when the next gen (with their greater say on family activity and shifting values) are at odds with the values reflected in their family's portfolio of tangible assets? What if fast cars, Picasso, and Burgundy are not to their taste?

Values

Tangible assets can be fashionable and that also means they can become outmoded – what was seen as key to a family's portfolio 20 years ago might seem outdated to the next gen.

Perhaps the biggest macro driver shaping the next gen's behaviours is the onward march of "purpose", incorporating ethical investing, a growing interest in sustainable finance and a weighting towards ESG. While the second is the increasing importance of "impact" in measuring performance and not just monetary value.

Research from PwC, for instance, highlights that 71% of next gen family business members recognise that their family business has a responsibility to fight climate change and its related consequences (PwC Global NextGen Survey 2022). In this light, it is possible to see how a luxury asset such as petrol-heavy vintage cars may not sit easily with next gen values driven increasingly by environmental awareness and responsibility.

However, this is more nuanced than a simple shift away from luxury assets. In fact, between February 2021 and February 2022, Gen Z and millennial luxury purchases made up 60% and 63% of total luxury market sales, respectively.

Equally, the next gen is highly focused on growth – expanding into new sectors and markets is the

single biggest priority for the next gen, according to PwC.

This teases the dual question: how can families balance their growth objectives with their growing focus on sustainability, and what role can luxury assets play in that?

Solutions

Against this backdrop, there has undoubtedly been an increased desire in recent years for advice on how luxury assets can be retained by a family but be "made to work" to fund projects of interest to the next gen, support its growth agenda, and provide an income where previously they had just accumulated a capital value in the family's portfolio of assets.

The reality is that balancing all of this is difficult but not impossible.

One possibility is that such assets can be retained and used as collateral for loans. For example, art collections with a material value can be secured to provide third party lending for the next gen to invest in other assets without selling the unique tangible assets that have meant so much to the current generation.

This takes careful planning and consideration, not least in respect of where the asset, in this case, an art collection, is situated and how it is secured. However, if everything aligns, this can be an effective way to ensure growth in value while preserving the original tangible assets.

A further avenue to explore focuses on redefining what is meant by luxury assets in a digital context.

The emphasis placed on technology by the next gen and their appetite for digital adoption is shifting the dial further when it comes to investment behaviours. A report by Klarna, for instance, revealed that more than six out of ten Gen Z and Millennials who have heard of the metaverse say they are interested in purchasing luxury goods through it.

The tokenisation of digital assets and "non-fungible tokens" (NFTs) go hand in hand here. 23% of millennials are already collecting NFTs, and there is every reason to believe that this provides an obvious route for next gen investors to balance their interest in luxury assets, digital capabilities and ambitions for growth.

From a trust and private client perspective, this is a rapidly developing but still fledgling area. Lots more work and clarity is needed on key legal issues surrounding ownership, succession planning and documentation. However, this is a direction of travel that offers considerable scope within the family and luxury asset investment space.

Trustee investment duties and structuring options

The structuring of luxury assets does not always sit well with long established trustee investment principles, namely to abide by the ordinary prudent business person test.

In Jersey, the general duty of care for trustees is expressed in Article 21(1) of the Trusts (Jersey) Law, 1984. This article provides that a trustee shall, in the execution of their duties and in the exercise of their powers and discretion, act with due diligence, as would a prudent person and to the best of their ability and skill. These duties cannot be contracted out of in the trust and apply at all times. However, a trustee's duty to preserve and enhance the trust fund's value, as stated in Article 21(3), may be carved out by the terms of the trust.

In these circumstances, how can trustees invest in luxury assets which are highly speculative or wasting?

A lot depends on the luxury asset class itself, as this is not always a class with a speculative or wasting nature (for example, the value of fine wine and classic cars has risen considerably in recent times). Diversification of the trust fund will remain a key factor, as will making sure the trust instrument itself recognises that the trust fund may, at least in part, be invested in speculative or wasting assets.

As with any trustee investment, a trustee must also monitor the performance of the luxury asset class. For bespoke situations, it may be appropriate for trustees to seek a specific release and indemnity from the settlor, adult beneficiaries, or both. There is nothing particularly new or novel with this approach. In fact, trustees have long had to deal with settlors and beneficiaries requesting that trust assets are invested in speculative investments or assets of a wasting nature.

Noting these investment duties trustees are often nervous about holding wasting or speculative assets.

As such, foundations may become the preferred vehicle for these assets.

It is possible under the Foundations Law to establish a foundation specifically to hold these types of luxury assets. In doing so, the council (with its qualified member) will not be subject to the same trustee investment duties. Instead, the council's duty (and ultimately, the guardian's) is in these circumstances to ensure the object of the foundation (namely, the holding of the asset) is achieved. Other structuring options for speculative or wasting assets might include a limited liability company or a limited partnership.

Where is all this going?
The evolution of the luxury asset investment landscape poses several legal considerations and pragmatic challenges for private wealth practitioners. They need to ensure these asset classes are structured in a tax efficient way and should not underestimate their ongoing upkeep and maintenance burden.

As the role of luxury assets continues to evolve – whether to leverage finance to create a liquidity event or to sustain a growth trajectory through luxury asset investment in a digital context – from a trustee perspective, the concept of prudence and the need for specialist advice will remain vital.

Some of that will be in new areas, such as digital IP. But some of it will remain fundamentally as important as it is today. Well drafted trust instruments, good governance, well thought out letters of wishes and a robust family charter, for instance, will continue to play a pivotal role in setting out family values and bringing different voices to the table.

For bespoke situations, in particular, where trustees are investing trust assets in clearly speculative or wasting assets, releases and indemnities will likely continue to be valuable to ensure trustees are not exposed to claims for breach of investment duty. We may also see more use of limited liability companies, foundations, or limited partnerships to structure these assets as an alternative to trusts.

Ultimately, by taking a holistic perspective and drawing on the specific expertise of asset experts, families can align the widening interests of the next Fgen with the founding values of the family and ensure that those emotive luxury assets can continue to work for everyone. ■

FROM MASTERPIECES TO MINEFIELDS

NAVIGATING LEGAL RISKS IN LUXURY ASSET TRANSACTIONS

Evelyn Sheehan and Lara Levinson, Kobre & Kim LLP

The luxury market – including the market for art – has always been the target of mischief due in large part to the high stakes and preference for confidentiality. Recent geopolitical shifts have further increased government scrutiny and enforcement actions, increasing the risks for collectors, sellers, buyers and other market participants.

What are some of the long-standing legal risks?
The luxury and art markets continue to face the perennial threat of fraud and money laundering. Luxury and art investors could become the victim of a fraudulent seller attempting to transfer works and goods that they do not own. This ushers in the potential for high-stakes civil litigation over ownership rights and perhaps even related government scrutiny.

Concerns that the luxury and art markets could facilitate the proceeds of criminal activity have prompted the United Kingdom to require most art market participants to register with the tax authorities for money laundering supervision, for example. Government authorities separately could suspect that a seller is attempting to manipulate prices through fraudulent trades. All this could lead authorities to try to disrupt sales, seize goods or bring criminal charges.

How have sanctions risks recently increased?
The conflict in Ukraine has set off a flurry of sanctions activity, with increasing focus on the luxury and art markets. For example, just recently at the May 2023 G7 summit in Hiroshima, the The conflict in Ukraine has set off a flurry of sanctions activity, with increasing focus on the luxury and art markets. For example, just recently at the May 2023 G7 summit in Hiroshima, the member countries pledged to restrict trade in Russian diamonds and to coordinate future restrictive measures, including "through tracing technologies." The United Kingdom went further, banning all imports of Russian diamonds.

United States
These additional sanctions come on the heels of other legal developments in many Western countries. In June 2022, the U.S. House of Representatives voted to include the Enablers Act in the larger National Defense Authorization Act, which would have added "persons who trade in works of art, antiques, or collectibles" to the category of those who must assist the U.S. government in preventing and detecting financial crimes. Although the measure was removed by the U.S. Senate, it had support within the Biden administration and indicates a willingness to bolster efforts to freeze art market assets related to Russian sanctioned individuals and entities.

United Kingdom
The United Kingdom also enhanced its sanctions regime in 2022 to broaden the scope of prohibited services to Russian individuals and those associated with them. In July, amendments were added to provide for new financial sanctions for such activities. Two months later, the Foreign Secretary announced the expansion of banned professional services to Russia, to include transactional legal advisory services and auditing services. These sanctions layer onto existing anti-money laundering regulations applicable to luxury and art market participants.

How can I protect my collection and transactions?
Most industry players have strong due diligence practices, including those addressing sanctions regimes – and proactive measures can further mitigate the risks. These measures can include obtaining legal counsel to assess assets for potential litigation vulnerabilities or preparing a game plan

should a private dispute or even law enforcement issue arise.

Legal counsel can also supplement due diligence through forensic analysis tools, showing the legitimate source of purchase funds by reviewing the funds intended for the sale, or demonstrating that parties have complied with any applicable anti-money laundering regulations. Parties can then deploy these findings if the buyer-seller relationship turns acrimonious, or if a government authority gets involved due to fraud, market manipulation or other concerns.

In addition, experienced counsel can also consider various strategies to protect assets in the face of government action. This may mean aggressively challenging the government's actions, or alternatively working cooperatively to assist with investigations against the fraudsters.

How can I protect my reputation?

A private dispute or government action also often brings unwanted attention and potential damage to one's public reputation. Participants in a dispute or government enforcement action need to consider not only the risk of reputational damage, but also how to preemptively mitigate its potential fallout, including as to ongoing commercial efforts and unrelated investments.

These risks may range from lawsuits over reputational harm to unforgiving news outlets eager to report on transactions by high-net-worth or high profile investors. Experienced counsel can coordinate a team of legal, crisis communications and public relations professionals to tackle these challenges.

Navigating the luxury market

Litigation risks and enforcement issues are landmines in the luxury market. The current regulatory landscape is especially aggressive and may sweep in any party, despite best efforts to comply. Those transacting in the luxury and art markets should remain ahead of the curve to protect both themselves and their clients against potential exposure. ■

A LESSON LEARNT FROM LUXURY

Dr. Philipp Konzett, Gasser Partner

Earlier this year, I was in Geneva to meet a friend for lunch. Apart from a good time with him, a fantastic steak at Chez Philippe (recommendation!) and the surreal crystal-clear water of the Rhône river, I came across something that made me think. I visited the Patek Philippe museum and was blown away by their motto. Proudly, it says “You never really own a Patek Philippe”. What a claim! The essence of luxury put into one simple sentence; exclusive, forbidding, unreachable, yet so reassuring that someone comes after you and that your own transience is not a bad thing – if only you pass on your values to the next generation.

It reminded me of some of my daily work. Probably everyone that works in estate planning has come across the type of clients that are driven by this very idea. More often than not, they could buy almost everything with money. And still, I feel it is usually not the money itself that they are concerned with, or at least it is not the mere numerical figure. There is a deeper layer behind the reason why they seek advice for their estate-planning. They are mainly occupied with passing on what they hold dear instead of the pure monetary value of these things – be it the company that they built throughout their life, be it the art collection that they have put together so passionately, or the family estate that they themselves inherited from their parents and which they want to preserve for future generations.

Liechtenstein offers attractive solutions for all of these cases. Some would claim, estate planning was practically invented here. However, honouring the topic of this issue of “The Month”, let’s focus on luxury assets and look at two use-cases of Liechtenstein structures for luxury assets.

The epitome of luxury is art. What is the value of a canvas with some paint on it, if there is not something intangible to it. Let’s say, a client (we call her Ms Yang), is a passionate collector of modern art and thinking about how her collection can be preserved for the future. In addition to that, she wants to support promising artists and their work. For her, a Liechtenstein foundation provides everything that she needs. Charitable foundations have a long tradition and are subject to close public supervision. Ms Yang could install a supervisory board with experts (including herself, if she wants) who decide on which artists receive a grant payment from the foundation or in which museum her art shall be shown. Charitable foundations are tax-exempt in Liechtenstein. Unlike trusts in certain jurisdictions, a rule against perpetuity does not exist. Ms Yang will be able to set-up a foundation that provides for all her needs and which will make sure that her passion lives on even after her death.

It does not have to be charitable. Some have used Liechtenstein establishments (Anstalts) as single-purpose-vehicle holdings for their family yacht, the family jet or a family domicile. The use-

cases are infinite. The establishment can be set-up like a foundation (i.e. without direct ownership), thus allowing for a separation of ownership from the beneficiaries. As a special feature, the establishment provides more flexibility than a foundation. Unlike a foundation, the establishment can operate a business. It would, therefore, be possible to rent out the private jet or the yacht during the time it is not needed, thus recouping operational costs. It doesn't matter whether the jet is rented out to third parties or rented back to the own company of the beneficiary or the founder.

Establishments (Anstalts) in general are my favourite type of legal entity. While establishing a "Family Anstalt" doesn't sound nearly as beautiful as laying the basis for your family dynasty with a "Family Foundation", it surely lives up to all our client's needs and it is – if set-up correctly – more flexible than a foundation or a trust. The Anstalt works perfectly as a central holding for the family estates, allowing for continuous influence while maintaining a good level of asset protection.

But I am drifting away from my Patek Philippe (then again, such a brand makes you start dreaming, doesn't it?). In the end, there is a lesson to be learnt from my trip to Geneva. A well-planned foundation, establishment or trust incorporates the very idea that this luxury watch teaches us: you never really own it – you set it up for you and your loved ones, and whoever comes after you. ■

PRIVATE WEALTH NOTICEBOARD

O'Sullivan Estate Lawyers, headed by Margaret O'Sullivan in Canada, celebrates its 25th anniversary this month.

You can read more about it in their blog post here.

"We look forward to the future, to our continuing relationships, to new relationships to come, and the challenges of the work we do. At the end of the day, it is a people business for people who enjoy helping people. Barbra Streisand expressed it best in her hit song, "People"."

AI is the next hot topic...

From PWC saying that the threat of AI will drive people into the office, to the Wall Street Journal saying that AI poses a 'risk of extinction on par with pandemics and nuclear war', AI is proving the topic of the moment. What will it be used for? Where will this conversation go?

Firm Moves This Month

Payne Hicks Beach have added two new partners to their private client team - Melissa Solly and Benedict Jennings.

Withers builds its Geneva practice with addition of former Burges Salmon partner Berry Bloomberg.

Stephenson Harwood makes another hire from Macfarlanes - Ross Davidson, as managing associate in Hong Kong.

Boodle Hatfield adds Taylor Wessing partner Nicola Bushby to their practice in London.

McDermott Will & Emery expand their US team with three partner hires.

LIVIN' LA DOLCE VITA

Alberto Brazzalotto and Giorgia Zanetti, Maisto e Associati

Italian real estate market is getting hotter and, for once, it is not about climate change.

The bel paese is becoming more and more an appealing destination not only for a week-or-so vacation in Capri or in the Chianti hills, but also for those who wish to relocate and optimize their tax exposure thanks to one of the tax regimes granted under Italian law for foreign residents who move to our country.

There is definitely a trend, the official statistics published by the Italian Court of Auditors (Corte dei Conti) speak clearly: around 1,000 people moved to Italy only in 2021 (plus 300 accompanying family members) to benefit from the 100,000 Euro flat tax on their foreign income, for a total of 108 million taxes in the State's pockets (without considering the higher revenues generated by consumptions and investments in Italy). Numbers have more than doubled since 2020 and tripled if we look at 2019 figures. We expect the numbers have grown further in 2022. The regime is designed to attract HNWIs who must have been non-resident of Italy in at least 9 out of the previous 10 years and decide to move their tax residence to Italy. Italy does not acknowledge a specific day-count test, so there is not a minimum or fixed number of days to be spent in Italy to be considered resident in a given year.

Indeed, the Italian concept of tax residence is very broad, it being sufficient to meet any of the conditions set forth by the law to be considered resident. For instance, if an individual is enrolled within the Italian Official Register of the resident population (Anagrafe della popolazione residente) for most part of a calendar year and elects a given place in Italy as his or her main abode, this is sufficient to be considered resident for domestic tax purposes. Nonetheless, to ensure that the Italian tax residence is not challenged by foreign jurisdictions, it is generally advisable that the transfer to Italy is supported by a certain degree of physical presence. This is why many foreigners (or Italians who have been abroad for a long time) decided to seize the opportunity to look for a masseria in the countryside near Lecce, a nice villa stile Liberty by Como Lake, a beachfront villa in Sardinia or a penthouse in a Gio Ponti building in Milan where to establish their main abode.

The "super-rich invasion" has an impact mainly on top-level real estate market and has positive effects also on satellite activities (such as concierge, household and maintenance services, luxury home furnishings, etc.). The reason why HNWIs are now considering Italy as a good option lies not only in the beauty of its landscapes and its famous dolce vita. Hence, despite the reputation for instability of its national politics, the 100,000 Euro flat tax regime has now been in force for 6 years and there have never

been any rumors about having it changed or abolished. Moreover, taxpayers have the opportunity to file a ruling request to obtain from the tax administration a preventive green light on their eligibility, avoiding the risk of an audit at a later stage, and to clarify any application and interpretative issue they may have. The main benefit consist of a 100,000 Euro substitute tax (plus 25,000 Euro for any family members who move together with the "principal" taxpayer) that applies on all foreign-source income and gains in lieu of ordinary taxation, irrespective of their amount and even if remitted to Italy, with the only exception of capital gains on shareholdings above certain thresholds realized in the first 5 years of effect of the regime (but a waiver can be obtained through the ruling procedure mentioned above).

A number of additional benefits also applies, e.g. non-application of reporting obligations on foreign assets, non-application of quasi-wealth taxes on the foreign-held financial products and foreign real estate; exclusion from inheritance and gift taxable base of foreign-situs assets (though the Italian ordinary regime in case of inheritance or gift is quite generous, with rates varying from 4% to 8% depending on the proximity of relationship between the deceased/donor and the beneficiary/donee and an allowance of up to 1 Mio Euro applicable to transfers in favour of the spouse and of each descendant). Such benefits are effective up to a maximum period of 15 years (but taxpayers can leave Italy even earlier, without the application of any exit taxes). Another strength of this regime is that existent offshore structures (holding entities, trusts, foundations, etc.) are generally transparent for Italian tax purposes and the regime applies to the underlying foreign assets (confirmation of the tax treatment of foreign entities can be obtained through the ruling procedure).

The regime seemed initially designed primarily to target rentiers. However, it is also very successful among bankers, managers, sportspersons, celebrities, who generate most of their income outside Italy even after their relocation. Because under the 100,000 Euro flat tax regime Italian-source income is subject to income tax under ordinary rules (i.e. progressive taxation with rates up to 43 % plus local surcharges except for most financial income which is subject to 26% taxation), this option is not working for people who would have substantial income sourced in Italy after relocation: for these people, the most efficient regime is the so-called Impatriate regime according to which employment income sourced in Italy is included in the overall taxable income limitedly to 30% of its amount for the first 5 years of Italian tax residence (10% if the individual moves to Southern Italy or Sardinia).

Ordinarily, the regime would terminate at the end of the fifth year; however, if the individual acquires a residential property located in Italy (or has an underage/dependent child) the incentive is extended for another five-year period, with a reduction of the benefit to a 50% exemption (unless there are at least three minor age or dependent children, in which case the exemption is increased to 90%).

The target real estate market for people moving to Italy under the Impatriate regime is slightly different: since they general carry out working activity in Italy they tend to look for apartments in the center of cities, with Milan being the favourite destination, especially after the decision of several banks to relocate there part of their headquarters after Brexit.

It is worth saying that for people relocating to Italy who intend to buy a residential property, it is in general more tax efficient holding the property as private individual rather than via an entity. ■

PASSING DOWN LUXURIOUS ASSETS

FROM GENERATION TO GENERATION WITHIN A FAMILY

Jonathan Morris, John Lamb Hill Oldridge

People purchase luxury items for various reasons. They may be viewed as an investment or a means of future profit; however, often they are acquired purely for the pleasure of ownership. Owning such items can result in a heightened interest and understanding of their history and significance. The sentimental attachment to a specific item or collection can lead to a devastating impact if they are lost, particularly if they were meant to be passed down to future generations. Owning luxury goods can lead to an increased liability to pay inheritance tax due to the significant value they add to the owner's estate.

In order to avoid the possibility of having to sell off assets in a hurry if there is a sudden liquidity crisis, some owners opt to insure their assets against potential losses. This can encompass protection against events such as fire or theft, which are typically covered by standard household insurance, or potential tax liabilities at the time of the owner's death.

What becomes of the assets after a person dies?
When a person dies, their assets will be subjected to an inheritance tax rate of 40% on any amount that exceeds the nil rate bands and reliefs if the assets are in the UK, and on worldwide assets if they are UK domiciled or deemed domicile. The payment for IHT should be made prior to the grant of probate, however, luxury items are easily marketable and could be often sold to cover the bill.

Many owners of valuable artwork or luxury items, often obtained as part of a collection, want to ensure that they are passed down intact to their beneficiaries and need to consider how the IHT will be funded. This can be accomplished by utilising life insurance to provide the necessary funds to pay off any outstanding tax debt owed to HMRC. By purchasing a policy tailored specifically to match the existing IHT liability, owners can secure the financial resources needed to keep their prized possessions within the family.

Tax issues on transferring assets
Assets are transferred to heirs/future generations either on death or during life. Either has tax implications.

Lifetime transfers offer the advantage of experiencing the joy of seeing beneficiaries appreciate and gain expertise in the assets but even with direct gifts there is a 7 year tail of reducing tax. Life insurance to match the tax is a very cost effective and simple solution. Costs for a gift of £1m by a 60-year-old:

	Sum Assured	Annual Premium
Year 1	£400,000	£1,182
Year 2	£400,000	£1,182
Year 3	£400,000	£1,182
Year 4	£320,000	£959
Year 5	£240,000	£735
Year 6	£160,000	£511
Year 7	£80,000	£267
Total Premiums Payable		**£6,018**

Over the course of seven years, only 0.6% of the value of the gift given is required to cover the cost of insurance.

Giving assets as gifts may have various tax consequences, including Capital Gains Tax (CGT). Nonetheless, presenting assets to younger generations while the person is still alive can be an effective planning approach.

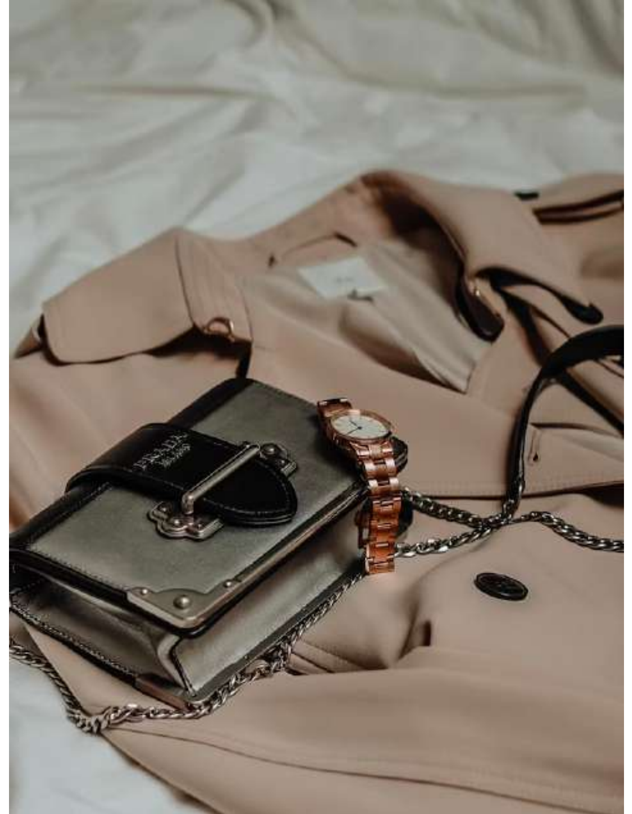
Transfers on death will incur a 40% tax charge, albeit on the probate rather than the open market value of the asset, and the tax on these assets will need to be paid in order to obtain probate. Assets cannot be sold, even if the deceased wants this to happen, prior to probate being achieved and, in any event, high value works of art/luxury assets have limited markets and it is very difficult to obtain full value if there has to be a "fire sale" to realise the funds to pay tax.

If assets are to be retained within the estate, then asset holders need to consider the IHT that will be payable and how it is to be funded. A policy to fund the tax running through to age 90 for a 60-year-old providing £400,000 to cover assets of £1m would cost £3320 per annum – the contract doesn't provide cover for whole of life but it does provide, for most clients, a long enough window for them to be thinking about gifting or sale. A policy that will last for whole of life would cost £9375 per annum.

Funding the tax on art and other luxury assets should only be part of the planning for clients – as HMRC receipts are now running at £7bn a year (to April 2023), up by £1bn from the year before clients need to plan – as they say Fail to Plan, Plan to fail. ■

THE LUXURY OF ASSET FINANCE: UNLOCKING LIQUIDITY IN YOUR VALUED POSSESSIONS

Bethan Waters, Farrer & Co



Superyachts, business jets, art collections, watches, wine cellars, classic cars, prized handbags, jewellery and even the occasional pair of trainers. These assets are often seen as must-haves for high net worth individuals.

Why and how these assets are acquired can of course vary wildly, from inheritance to "passion" acquisitions or speculative investments, through to the simple fulfilment of business needs. It has also long been clear that some "luxury assets" perform very well when compared to other types of investments, sometimes outperforming stocks and shares. This has led to an increasing awareness of the potential to unlock the value of these assets and provide additional liquidity to owners, either through individual asset financing arrangements or as part of a wider banking arrangement.

What is luxury asset finance?

Typically, lenders will offer a lower interest rate on a loan if an asset is offered as security or collateral for the borrowing. This allows the lender, in the event of non-payment by the borrower, to enforce its rights by taking and (in most cases) selling the secured asset in order to recover the outstanding debt. A typical example of this is a mortgage against property, but some lenders will take security in the form of other assets including "luxury assets", such as business jets, art, fine wines, watches or collectible cars.

Can all luxury assets be financed?

In short, no. On a basic level, lenders try to ensure that they will be made whole in the event of an enforcement by only lending a percentage of the value of the asset offered as security. This percentage can vary greatly between lenders and between different asset classes, with higher percentages being lent against "safer" assets which can be valued easily, widely and comparatively (such as real estate, where loan values can sometimes reach as much as 90 or 100 per cent of the value of the property) whose title can be established easily and definitively and which can be protected against disposal whilst secured.

Typically however, much lower loan to value percentages are offered for loans secured by unique moveable chattels such as art or wine, where title can often be difficult to establish and prove, where the asset can physically be moved easily, where value is subjective or intrinsically linked to provenance and / or authenticity (such as handbags), or where comparable values exist only in a small pool of typically depreciating assets (such as cars or business jets).

Similarly, values can differ (often unpredictably) depending on market appetite and the quality of an individual piece, making lenders more cautious about the loan to value they will offer against

some of these asset types. The gaudy interior of a superyacht or imperfect mechanisms of a watch could significantly and adversely affect its value, as could market popularity of an artist at a certain time.

How can you assess whether a luxury asset might be suitable for finance?

A lender will likely only lend against an asset if it (a) has all of the information that it will need to pass to a potential buyer and (b) is confident it will be able to recoup its monies on an enforcement sale. A potential borrower would be well advised take into account the following considerations before approaching a lender for finance secured on a luxury asset.

Location, usage of and access to asset

Before seeking to raise finance against a luxury asset the owner should consider where that asset is, how much access they require to it and what they need to use it for. Often lenders will need to establish or protect their security by housing the secured asset in a specialist warehouse with restricted access. If an individual wishes to keep their valuable watch on their wrist, continue to drive their classic car or store their wine in their own cellar, this could ultimately prevent those items from being offered as collateral.

The borrower should consider whether they or their companies need to use planes, cars and yachts and if so, where they may to want to use them as lenders will have strict rules about where secured vehicles can be taken. Similarly, if an asset is owned by a company, lenders may also have certain stipulations, not only around where the asset itself can be registered or used, but where the company owning it can or can't be incorporated. Lenders will also want reassurance that the asset's tax and customs situation is in order.

If the assets are located or registered outside of England and Wales, or owned by a foreign entity, legal advice will likely be required in each jurisdiction where the asset is located (or vehicle is registered) as well as in the jurisdiction of any ownership companies, trustees and underlying trusts, which can increase documentation and costs.

Title and ownership

It is imperative that whoever offers an asset as security for a loan actually owns that asset. Ownership registers do assist in establishing this for most yachts, cars and aircraft but tracing title can be more complex for personal collectibles such as art, wine, watches, handbags or jewellery. Lenders will typically insist on seeing and verifying unbroken "back to birth" title chains dating from the creation or manufacture of the piece through to the proposed security provider. With registered assets (such as jets and yachts) this is often achieved through registration documents or bills of sale. For non-registered assets, however, where title is often established by a collection of evidence such as invoices, auction records, receipts and catalogues, difficulties can arise. Often the title deduction process reveals questions around ownership, particularly where borrowers have conflated individual with corporate or trustee ownership or where ownership of IP rights has been separated from the asset itself. In order to reduce legal costs and increase efficiency, borrowers contemplating offering a luxury asset as security should ensure that they have clarified and identified the ownership and title of the asset before approaching a lender for finance.

Authenticity, provenance, maintenance and insurance

In addition to establishing title, a lender will require assurance (and will base its lending value on the fact) that the asset offered as collateral is genuine and has been well cared for. Ideally the title chain would always flow neatly back to the original manufacturer or artist but this is often not the case, especially for older assets or assets which may have been transferred several times within a family without any documentation, or where business and personal assets have been intermingled and records lost. A lender would usually appoint their own experts to carry out provenance and title checks and to check for details of any repairs or restoration, as well as asking for things like gem or manufacturers' certifications. With vehicles, the lender will want to check carefully that the asset has been frequently maintained, serviced and insured in accordance with legal requirements, manufacturers' recommendations and market practice and that all documents necessary to the ownership of the vehicle (such as log books, manuals etc) are in place. The assets will need to be adequately insured and the lender's position as secured party must usually be reflected in the insurance documentation.

Value

Establishing the value of any luxury asset

can be difficult as comparators can be rare, sales are often private, and because the true sale value is not always marked on the bill of sale. Certain services such as auction records or the "blue book" for private jets can be helpful, but lenders will always conduct their own valuations (usually at the borrower's expense) before lending. With unique assets such as art, lenders may also require a diverse security pool, requiring more than one asset or assets by different artists to be offered as security in order to hedge against changing market appetites.

Relationship with lender

The luxury asset financing market is quite mixed. Some specialist lenders will lend purely against the secured asset, with recourse only to that asset. Others will only lend against an asset which is consigned to sale (with them) within a certain period of time. Private banks will typically only lend against these types of assets as part of a wider relationship, where the lending is also supported by a personal guarantee from the underlying owner, or where the lender is given certain investments to manage. Borrowers can expect loan pricing to vary in accordance with the type of arrangement they choose to reflect the different risk levels involved.

Confidentiality

Finally, borrowers should be aware that it may be necessary to register certain security on public registries (especially in the case of vehicles or company owned assets) so confidentiality considerations should not be ignored. Similarly, certain luxury asset markets are very small, and values can be prejudiced if an asset is known to be secured. It is important, therefore, to treat security valuations very sensitively and to only approach legitimate lenders who are familiar with lending against these asset types. ■

WHY GOOD GOVERNANCE SHOULD UNDERPIN LUXURY ASSET STRATEGIES

DANIEL CHANNING, CRESTBRIDGE FAMILY OFFICE SERVICES

The indications are that wealthy families continue to hold some form of luxury asset within their investment portfolios. Such assets make up some 5% of investable wealth on average – that's the same proportion as gold and crypto assets combined (Knight Frank Wealth Report 2023).

And possibly with good reason - the latest Knight Frank Luxury Investment Index rose by a healthy 16% during 2022, beating inflation and outperforming most mainstream investment classes. Art was the top performer, growing by 29%, according to the Index, with classic cars rising 25%.

There is, however, some differential within the sector – wine grew 10% (down from 16% the previous year), while whisky was up just 3%.

Often for families, returns when it comes to luxury assts are not necessarily the be all and end all – they are ultimately investments of passion, sentiment, interest and lifestyle. Yachts and private planes, for instance, may meet the lifestyle requirements of a family, but they are notoriously expensive assets to hold, depreciating in value and delivering very little, if any, income return.

But when do non-income generating luxury assets become a problem for the family strategy more widely - particularly with total UHNWI wealth having been eroded by some 10% last year against challenging and high inflation versus previous years market conditions (Knight Frank), and with the nextgen continuing to take more of an interest in driving family portfolios?

Fresh Look

With almost a third of wealthy private investors targeting capital growth this year (Knight Frank), the role of luxury assets within a portfolio may well become part of the conversations between advisers and their clients in the coming months, as they take a fresh look at how hard their investments are working and how they could be put to work harder to generate returns.

Crucial in this scenario is looking at where luxury assets sit within the wider portfolio and the family's wealth strategy holistically.

Often, of course, family wealth creators are emotionally tied to their luxury assets and may well consider them to be part of their family legacy. At the same time, though, those assets may well be at odds with the shifting priorities and values of the increasingly influential nextgen.

In any situation, of course, a family will want to avoid the potential for future disputes – and advisers have a crucial role to play in putting in place measures from the outset that can reduce that risk.

At the heart of this is good governance. Advisers with a focus on nurturing close, positive relationships with their clients are best placed to deliver on that. By understanding their clients, bringing all stakeholders to the table, advisers can establish clearly what a family's fundamental values are and what its shared vision is.

Is there, for example, a mismatch between what a family says its core values are, and what is reflected through its existing portfolio allocation and the luxury assets within it? Does it 'fit'?

Equally, deep conversations with an adviser can reveal whether there is a concentration risk when it comes to luxury assets, which often have high or fluctuating valuations. One piece of art can significantly shift in value, up or down, for instance,

and make a considerable impact on the total wealth valuation – which in turn could impact its risk profile. An adviser can in this instance guide a family as to whether there is a need to think about diversifying to meet its overall wealth objectives.

Indeed, when it comes to luxury assets, families should see it as an opportunity to make sure they have robust, independent, good quality legal and advisory frameworks in place to avoid current and future intergenerational disputes.

All this can subsequently be documented through the family charter, investment strategy, letters of wishes and other documentation, providing a clear framework that should help guide them in an area that is so easily impacted by individual sentimental and emotional preferences.

Practicalities

Balancing the growth, purpose and legacy objectives can be a tricky task but, with a foundation of good governance and sound documentation, there is still undoubtedly a place for luxury assets within a wider portfolio.

There are some practicalities, though, that can help ensure such assets are properly managed and structured.

First and foremost, luxury assets frequently require specialist expertise if they are to be managed effectively. That might mean, for instance, getting specialist insurance advice where family art may be moved across borders, or drawing on yacht management services to administer crew and ensure adequate marine insurance is in place. Bringing in the right expertise early can dramatically reduce risk in the long run.

Taking a view on a family's structures and whether they offer enough, or too much, flexibility in terms of holding assets is another practical point that should be addressed.

Luxury assets are often acquired to be enjoyed by a family – art, jewellery, or vintage cars for example. Others, such as fine wine or whisky, may form part of a collection. Whatever the approach, choosing the right structure is an important factor in achieving the desired and proportionate flexibility - protecting the assets while allowing a family to enjoy those assets too.

Ownership is a key question too when it comes to structuring luxury assets - regrettably there can be instances where question marks over ownership of an asset can lead to inter-family disputes. The case of Robert Tibbles, a collector of contemporary art, and one of his pieces of artwork, a Damien Hirst painting entitled 'Beautiful tropical, jungle painting (with pink snot)', is a case in point. Robert's father, Nigel, and twin brother, Sebastian, sued him over ownership of the piece when it was sold, leading to an unfortunate and bitter family dispute – clear structuring played a key part in resolving that case.

In addition, if structured appropriately, it may well be possible for non-income generating luxury assets such as art to be used as leverage to generate capital liquidity – thereby meeting the needs of both the wealth creator and the nextgen, without directly impacting the asset itself.

Evolution

As families look to a new era of investment, shaped by the need to balance their own growth ambitions with the desire for purpose-driven investment and a need to integrate the values of the nextgen, advisers have a responsibility to ensure luxury assets are managed and structured appropriately as part of a family's holistic wealth management strategy.

Really understanding the needs and ambitions of a family as a whole by cultivating a close relationship with them is critical in establishing a robust governance framework that can cater for the appetite to hold luxury assets on the one hand with the need to generate returns on the other. By taking a number of practical steps -from establishing good oversight models and structuring to seeking specialist expertise where needed – luxury assets can continue to provide both the family enjoyment and legacy they promise, and play a role as part of a wider investment portfolio. ■

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