

TAX CHANGES FOR NON-UK DOMICILIARIES AND THEIR OFFSHORE TRUSTS

JUNE 2017 UPDATE



Following the announcement of the General Election, a reduced Finance Act 2017 was passed which omitted the proposed amendments to the non-dom tax regime and those for inheritance tax (IHT) on UK residential properties held in offshore structures.

TAX CHANGES DELAYED

The changes were dropped as there was insufficient time for parliamentary scrutiny on the Finance Bill before Parliament was dissolved in readiness for the General Election.

It is very likely that the omitted parts will be passed in a future Finance Bill in the new Parliament. Whilst it is difficult to predict, we believe it unlikely that there will be substantial changes to the original proposals. It is also quite likely that the changes when legislated would be backdated to take effect from 6 April 2017. However, it does seem sensible that where possible any actions are put on hold until there is further clarification.

We will of course provide further information as it arises but as a reference point set out below the previously proposed changes.

A REMINDER OF THE PROPOSALS AND THEIR IMPACT ON OFFSHORE TRUSTS

- ▶ Certain protections will be afforded to non-dom individuals who settled an offshore trust prior to 6 April 2017.
- ▶ Existing excluded property trusts with non-UK assets will retain this status for IHT purposes even where the settlor becomes domiciled under the 15 out of 20 year rule or under general law.
- ▶ Excluded property status will be lost for trusts set up by an individual with a UK domicile of origin who was born in the UK, if they become UK resident again ('formerly domiciled resident') and were resident for at least one of the two tax years prior to the year in question.
- ▶ UK residential property held by offshore companies held by trusts, will no longer be excluded property exposing it to IHT.
- ▶ No de-enveloping relief of trust owned companies holding UK residential property potentially resulting in multiple tax charges on restructuring (IHT, ATED, CGT, SDLT).
- ▶ Loans to trustees, individuals or partnerships used to acquire UK residential property will now be deemed to be a UK sited asset for the lender.
- ▶ Loans made by trustees to help beneficiaries acquire UK residential property (including structures already in place) will be within the IHT regime.
- ▶ Guarantees for borrowing in respect of the UK residential property may also be subject to IHT.
- ▶ For CGT, protections will remain unless property is added at a time when the settlor is deemed UK domiciled under the 15/20 rule.
- ▶ Tax on gains within trusts would continue to be deferred but would be chargeable as and when capital benefits are received by a UK resident beneficiary which is matched to trust capital gains.
- ▶ Where trust distributions are made offshore to a non-resident beneficiary and within three years the payment is passed on to a UK resident beneficiary then they will be treated as if they received the original payment and taxed accordingly (this had already been dropped from the original Finance Bill with the caveat that it may be introduced at a later date).
- ▶ For income tax, protections will also be offered to settlors unless the trust is added to at a time when the settlor is deemed UK domiciled under the 15/20 rule.

CONTACTS

ANDRÉ TREBERT

Director
BDO Limited, Guernsey
+44 (0)1481 741610
andre.trebert@bdo.gg

JOHN BRADLEY

Tax Director
BDO Limited, Guernsey
+44 (0)1481 741609
john.bradley@bdo.gg

MARK SAVAGE

Tax Director
BDO Limited, Guernsey
+44 (0)1481 748450
mark.savage@bdo.gg

- ▶ In cases where protections apply, non-UK income arising in offshore trusts and their underlying entities from 6 April 2017 will be taxed when matched with income distributions to the settlor or beneficiary or where a capital benefit is received.
- ▶ UK source income in a trust would continue to be taxed on an arising basis on the trustees and/or settlor. Underlying UK income in companies will be taxable on the settlor, subject to any commercial/non-tax avoidance motive defence.
- ▶ For both CGT and income tax, there is to be a restriction on 'washing out' gains and income to non-resident beneficiaries after 5 April 2017.

BEST PRACTICE FOR TRUSTEES GOING FORWARD

The taxation position for offshore trustees, settlors and beneficiaries combined with their reporting obligation is growing in complexity and now more than ever, there is a compelling need for trustees to observe good governance and best practice in their demanding role. BDO can carry out status reviews to establish:

Governance

Whether settlors/beneficiaries are still domiciled outside the UK prior to any large offshore distributions.

When the settlors/beneficiaries become deemed domiciled under the new rules - particularly relevant to years not determined under the statutory residence test.

Financial and compliance obligations for Trustees

- ▶ Keeping full and accurate records
- ▶ Preparing annual accounts for trust and underlying companies/entities
- ▶ Calculating income pools pre 5 April 2017 and post 6 April 2017
- ▶ Calculating capital gains pools
- ▶ Provide information to UK resident settlor and beneficiaries to comply with their reporting requirements.

Tax Assurance

- ▶ HMRC have proposed a statutory obligation 'The Requirement to Correct' (RTC). This obliges a UK tax payer with any offshore financial connection, including trustees to review their UK tax obligations to ensure that the relevant disclosures are made and to correct any issue with their historic tax position, within a specific time frame (The RTC period).
- ▶ Trustees should be compliant with the OECD Common Reporting Standard reporting disclosure requirement.

HOW BDO CAN HELP

Accounting

BDO can provide a trust accounting service to assist with the preparation of trust and company accounts, including bringing the trusts accounting records up to date. The accounts can be in BDO's standard format or tailored to suit the trustees' needs.

Our newly developed cloud based accounting service provides trustees with the opportunity to have access to current accounting information at any time.

We can assist with all UK tax compliance for offshore structures including preparation of the different UK returns and calculations of the relevant tax liabilities arising.

We can calculate the income and gains pool within trusts and advise settlors/beneficiaries regarding the distributions in the current tax year in relation to CGT and income tax treatment versus the inheritance tax risks. Where no accounts have been previously prepared, we can discuss how we approach the updating of records.

Planning

- ▶ Review loans made to trusts - interest free loans to trusts are likely to be considered as additions to the trust post 5 April 2018 thus 'tainting' the trust. A commercial rate of interest may have to be paid from 6 April 2018 to retain trust protections.
- ▶ Review whether historic capital payments have been made which are unmatched to capital gains.
- ▶ Review trust lending to beneficiaries for UK residential property.
- ▶ Review IHT position in the light of loans and interests in UK residential property.

We can advise on the tax implications of making capital payments to beneficiaries as well as separating mixed funds, rebasing assets and settling further assets into trust.

Tax Assurance

We can carry out a Forensic review of your structures as required and as regards to the RTC we can assist with a 'Health Check' of the trustees position during the RTC period and approach HMRC as appropriate.

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Our award winning Private Client Team offers a range of tailored services to trustees and high net worth individuals who want their global tax affairs managed proactively and seamlessly.



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