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1. Introduction

1.1 In his 2015 budget statement the Chancellor announced changes to the taxation of non-domiciled individuals. A number of these changes affect two groups of individuals who, from 6 April 2017, will be considered deemed domiciled for tax purposes and so will not be able to claim the remittance basis. In the first group are long-term resident non-domiciliaries who have been resident in the United Kingdom for at least 15 of the 20 tax years preceding the year under consideration. In the second group are individuals who were born in, and have a domicile of origin in, the United Kingdom. They will be treated as deemed domiciled whenever they are resident in the United Kingdom, even if they have established a domicile of choice, or have a domicile of dependence, outside the UK.

1.2 It was recognised that many non-domiciliaries living in the United Kingdom hold their wealth in non-resident trusts (often with underlying offshore companies). The removal of the remittance basis for long-term United Kingdom resident non-domiciliaries would result in their being liable to income tax and capital gains tax on all of the income and gains arising in their non-resident trusts and underlying offshore companies without the ability to claim the remittance basis for foreign-source trust income and trust capital gains.

1.3 The government announced that non-domiciliaries who set up non-resident trusts before becoming deemed domiciled in the United Kingdom under the 15 out of 20 year rule would (provided they were not also UK resident, born in the UK and had a UK domicile of origin – see 1.4) not be taxed on the gains and foreign source income of such trusts and their underlying entities provided that such income and gains were retained within the structure. From 6 April 2017 such long-term residents would be liable to pay income tax on the United Kingdom source income arising within a trust structure in which they had retained an interest and would be taxed on any benefits that they received from the trust on a worldwide basis to the extent that

such benefits could be matched with the income and gains arising within the trust. It was subsequently decided that the introduction of this benefits charge should be extended to all non-domiciled settlors of non-resident trusts and that those non-domiciled individuals who were not long-term residents of the United Kingdom would have the opportunity to access the remittance basis charge.

1.4 It should be noted that this treatment is not extended to non-resident trusts created by individuals born in the United Kingdom with a United Kingdom domicile of origin if the settlor is UK resident. While such individuals may have acquired a domicile of choice elsewhere, the trusts they settle while asserting a foreign domicile of choice outside the UK will not be covered by the trust protections referred to in this chapter. Upon becoming resident in the United Kingdom such individuals will be treated as deemed domiciled and the income and gains arising in non-resident trusts that they may have settled and retained an interest in will be assessable on them as they arise under S86 TCGA 92, the settlements legislation and the transfer of assets abroad legislation as appropriate.

1.5 The rest of this chapter looks at the impact the amendments, to the capital gains tax legislation at S86 and S87 TCGA 92 (section 4), the settlements legislation (section 2) and the transfer of assets abroad legislation (section 3), will have on non-resident trusts created by non-domiciled and non-deemed domiciled individuals as well as the special rules which will apply in some cases after a settlor becomes deemed domiciled. There is also a separate section that relates to the tainting of protected settlements, where property is added that can result in the non-resident trust losing its protected status (section 5). The chapter goes on to look at legislation that has been introduced to determine how benefits are valued for the purpose of the benefits charges that arise under the new proposals (section 6). The final two sections deal with rebasing for capital gains tax purposes (section 7) and certain other changes affecting capital gains tax (section 8).

1.6 It should also be noted that whilst all of the proposals around the trusts protections have been legislated in Finance (No.2) Act 2017 other offshore trust matters have still to be legislated and as a result additional changes will be introduced in Finance (No.2) Bill 2017-19. The changes that remain to be addressed are a benefits charge under the settlements legislation, the introduction of a close family member rules for both the settlements legislation and capital gains tax legislation and recycling rules for the transfer of assets abroad legislation, the settlements legislation and the capital gains tax legislation. Readers of this guidance should look out for further HMRC guidance on these changes in due course.

2. Settlements Legislation Trust Protections

2.1 Section 29 and Schedule 8, Paragraphs 20 to 26, of the Finance (No. 2) Act 2017 make changes to the settlements legislation in Part 5, Chapter 5 ITTOIA 2005. Statutory references in this section of the Guidance Note are to ITTOIA 2005 unless otherwise stated. The settlements legislation applies to income arising under a settlement. For the purposes of the legislation the meaning of settlement is extended to include any ‘disposition, trust, covenant, agreement, arrangement or transfer of assets (except that it does not include a charitable loan

arrangement)'. The scope of settlor is similarly extended, and in relation to a settlement means 'any person by whom the settlement was made.'

2.2 The settlements legislation can apply to the income arising under a settlement in three circumstances.

- The settlor retains an interest in property from which the income arises.
- The income is paid to or for the benefit of a minor, unmarried child of the settlor, or it would be treated, apart from the relevant provisions, as income of such a child.
- A capital sum is paid directly or indirectly in any tax year by the trustees of a settlement to the settlor, or such a sum is paid to the settlor by a body corporate in any tax year and an associated payment is made by the trustees of the settlement to the body corporate.

2.3 In the first and second situations above the income arising under a settlement is treated as that of the settlor. Income treated as that of the settlor in the first situation cannot be caught under the second. In the third case, the capital sum is treated as the income of the settlor so far as it falls within the amount of income available up to the end of the tax year. Income treated as that of the settlor in either the first or the second situation will not form part of the income available.

2.4 The basic rules are subject to various exclusions and exceptions. This guidance note is not intended to provide a detailed introduction to the settlements legislation. Further information about the legislation can be found in (TSEM4000) onwards, which will be updated to take account of the provisions of Finance (No. 2) Act 2017.

2.5 The purpose of this Guidance Note is to show how the Finance (No. 2) Act 2017 legislation will affect the existing provisions. The wider changes to the taxation of individuals not domiciled in the UK under common law, which are being introduced through Finance (No. 2) Act 2017, have effect for the tax year 2017-18 onwards. The Finance (No 2) 2017 Act changes to the settlements legislation were to allow the trusts protections. There will be further changes affecting the settlements legislation that will be introduced in Finance (No. 2) Bill 2017-19 (as mentioned in 1.6). The Finance (No. 2) Act 2017 changes include measures to protect, other than in specified circumstances, the income of a non-resident trust settled by an individual who was not domiciled in the UK at the time he or she made the settlement. These measures will often be referred to as the 'trusts protections'. As far as the settlements legislation is concerned there are two concepts that are central to the trusts protections, protected foreign-source income and tainting.

2.6 Protected foreign-source income is defined in S628A. Where income is treated as that of the settlor, the general rules are modified so that they do not apply to income arising under a settlement if it is protected foreign-source income. Where a capital sum is treated as the income of the settlor, protected foreign-source income will not form part of the income available. This principle applies equally to other income tax provisions that might otherwise apply to attribute the income to the settlor.

It is important to appreciate that the term protected foreign-source income does not include all sources of foreign income. Most notably it does not include life assurance gains taxed as income.

2.7 Tainting is relevant because where a trust has become tainted the income arising under that settlement will not be protected foreign-source income after tainting occurs. In this section of the Guidance Note, the words 'tainting' and 'tainted' will be used in relation to a settlement that

has lost the trusts protections because its income has ceased to be protected foreign-source income through a failure to meet condition F of S628A. Further information about this condition can be found in section 5 of this guidance.

2.8 The exceptions to the rules treating the trustees' income as that of the settlor apply with effect from the tax year 2017/18 onwards. They work by providing that the rules do not apply to income arising under a settlement if that income is protected foreign-source income for a tax year.

The guidance below principally considers cases where the settlor retains an interest. The rules relating to sums paid to minor, unmarried children operate along the same lines and are covered more briefly.

2.9 Capital sums paid to the settlor are dealt with in later paragraphs of the Guidance Note, but the information below on protected foreign-source income and tainting are relevant to both income and capital sums that are caught by the legislation.

2.10 S628A(2) sets out the circumstances in which income arising under a settlement in a tax year will be protected foreign-source income for that year. In order for income to be protected foreign-source income six conditions have to be met. These conditions, A to F, are set out in the following paragraphs of this guidance.

2.11 For the purposes of S628A relevant foreign income will be regarded as arising under a settlement in a tax year even if the settlor was using the remittance basis for that year and the income has not been remitted, as the general rule in S648(3) does not apply Where such income is protected foreign-source income it will not be treated as the income of the settlor under S624(1) should the settlor have retained an interest in the settlement. Similar rules apply to relevant foreign income paid to the relevant children of a settlor and treated as the income of the settlor under S629(1). They do not, however, apply where income has been retained or accumulated by the trustees before it is paid to, or for the benefit of, a relevant child of the settlor.

2.12 S628A(3) gives condition A, which is that the income would be relevant foreign income if it were income of a UK-resident individual. Guidance on relevant foreign income can be found at RDRM31140.

Example

Maria is the settlor of the Maria 2019 Discretionary Settlement, in which she has retained an interest. The corporate trustee of the settlement is resident in the Isle of Man. The trustee of the settlement has placed part of the trust fund on deposit in Jersey and has also invested in a portfolio of shares in companies resident outside the UK. The interest on the deposit account and the dividends from the company shares would be relevant foreign income if they were income of an individual resident in the UK. Condition A is met.

2.13 Condition B is given by S628A(4). It is that the income is from property originating from the settlor. Property originating from the settlor is defined by the existing settlements legislation, in S645.

> Example
>
> On 26 June 2019 Maria's father had provided out of his own resources the original £10 for the Maria 2019 Discretionary Settlement. Maria had, on 3 July 2019, given to her father the balance of the intended trust capital, so that he could transfer the funds to the trustee. The vast majority of the trust property originated from Maria, as she had provided it for the purposes of the settlement. For the purposes of this example the original £10 is ignored on *de minimis* grounds, the interest and dividends are income from property originating from Maria and so condition B is met.

2.14 Condition C, in S628A(5), looks at the time when the settlement was created by the settlor. If this was before 6 April 2017 the condition is met if the settlor was not domiciled in the UK, under common law, at that time. Guidance on the law of domicile can be found at RDRM20000 onwards.

2.15 If the settlement was created on or after 6 April 2017, the settlor must not only be domiciled under common law in a territory outside the UK but must also be non-deemed domiciled in the UK at that time if the condition is to be met. For these purposes, deemed domiciled means regarded as domiciled in the UK under ITA/S835BA(2). Further information on this matter is given in paragraph 5.21 of the 'Guidance note for residence, domicile and the remittance basis: RDR1'.

> Example
>
> Maria was born in Spain, which was where her married parents were domiciled at that time and throughout her minority. Her domicile of origin is Spain, she never acquired a domicile of dependence or choice elsewhere, and Spain remained her operative domicile after she reached her majority. In May 2011 Maria came to work in the UK, having never lived here before. She has been resident here since that time, as it was always her intention to live and work in the UK for at least ten years, but she does not intend to remain here permanently or indefinitely. Maria has maintained close links with Spain, and she owns a home there to which she intends to retire within the next decade. Maria has not acquired a domicile of choice in any part of the UK while she has lived here. Maria provided property to the Maria 2019 Discretionary Settlement on 3 July 2019, at which time she was not domiciled in the UK under common law. She had not at that time lived in the UK long enough to become deemed domiciled under condition B of ITA/S835BA, and she could not become so under condition A of that section. Condition C is met.

Example

Nathan was born in the UK. His father was domiciled in South Africa at the time of his birth. Nathan has lived and worked in a number of countries over the years, but he has been resident in the UK since April 2002 when he became the CEO of a company based in London. He does not intend to remain in the UK permanently or indefinitely, as he plans to retire to Switzerland in a couple of years. In August 2017 Nathan settles a portfolio of commercial property, none of which is located in the UK, on the trustees of Nathan's 2017 Family Settlement, the trustees of which are resident in Mauritius. Nathan is subsequently found to have retained an interest in Nathan's 2017 Family Settlement. The rental income from the properties would be relevant foreign income if it was the income of an individual resident in the UK.

Conditions A and B are met, and Nathan is not domiciled in the UK under common law in August 2017. His domicile of origin was not in the UK, so although he was born here he cannot be deemed domiciled under condition A of section 835BA ITA 2007. Nathan was resident in the UK in 2002-03 and has been resident here in every subsequent tax year. The relevant year for these purposes is 2017-18, and Nathan has been resident in the UK for that year and for 15 of the 20 years immediately preceding it. Condition B of section 835BA ITA 2007 is satisfied, which means that Nathan is deemed domiciled in the UK in August 2017. Condition C of section 628A is not met, because Nathan was deemed domiciled when he settled the portfolio of commercial property into trust, and the rental income will therefore not be protected foreign-source income. Had he settled the property in August 2016 however, Condition C would have been met and the income would have been protected foreign-source income, subject to conditions D to F being met.

2.16 Condition D, in S628A(6), looks at the tax year in which the income arises. The condition is met if there is no time in that year when the settlor is either domiciled in the UK, under common law, or deemed domiciled in the UK under condition A of S835BA ITA 2007. The settlor will be deemed domiciled under condition A for a tax year if they were born here, have a domicile of origin here and were resident in the UK in that tax year. The settlor can, however, be deemed domiciled in the UK under condition B of S835BA ITA 2007, due to the length of their residence in the UK, without affecting whether or not condition D is met.

Example

Continuing the example of Maria from previous paragraphs, she is resident in the UK for 2017-18, although she was neither born nor has a domicile of origin here. Also, she is not domiciled here under common law. The relevant circumstances apply throughout the year, so condition D is met. For this purpose it does not matter that for 2017-18 and later years Maria is deemed domiciled in the UK through being resident here for the year and for 15 of the previous 20 years.

Example

Maria has a half-sister, Isabella, who is 22 years younger than Maria and was born in the UK after their father had acquired a domicile of choice here. Isabella provided funds to the Isabella 2012 Discretionary Settlement on 18 September 2012, at which time she had been living and working in New York for some years. The settlement is in the same form and has the same corporate trustee as the Maria 2019 Discretionary Settlement, and the trustee has pursued a similar investment policy. Isabella is married to a citizen of the USA and has two children, both of whom were born in New York. Isabella and her spouse own an apartment in New York and a holiday home on Long Island. She returned to the UK in 2014 to take up a five-year assignment in London. It is accepted that Isabella acquired a domicile of choice in New York State prior to 18 September 2012. Whilst Isabella is in a similar position to that of her half-sister, there is a crucial difference between them; Isabella has a domicile of origin in the UK and was born here so condition D is not met. The interest and dividends arising under the settlement for 2017-18 will not be protected foreign-source income.

2.17 Condition E, in S628A(7), is that the trustees of the settlement are not UK resident for the tax year. Guidance on the residence of trustees can be found at (TSEM10005) onwards.

2.18 Condition F is the most complex of the conditions, and it is the one that relates to tainting. The condition is set out in S628A(8), supplemented by subsections (9) and (10). Subsection (11) provides the link to S628B and the tainting provisions. The conditions relating to the tainting provisions apply for the purposes of the transfer of assets and capital gains tax trust protections as well as for the settlements legislation. The conditions are therefore dealt with separately, in section 5 of this guidance.

2.19 Where foreign income arose under a settlement in the period beginning with the tax year 2008-09 and ending with the tax year 2016-17 it may be transitional trust income. If it is, the meaning of remitted to the UK in the application of S809L ITA 2007 is modified in relation to that income. For that purpose a 'relevant person' will not include the trustees of the settlement concerned. For the avoidance of doubt, as the purpose of this provision is to ensure that trustees cannot remit pre-April 2017 income (which meets the conditions below), it is only necessary to focus on income which has arisen since 2008-09. Due to the transitional rules in FA 2008, trustees have never been able to remit pre-2008-09 income.

Importantly this provision only removes trustees from the definition of "relevant person" in s809L ITA 2007. Underlying companies etc. will all remain relevant persons. Hence a loan of unremitted trustee income from, say, 2010 to an underlying company would trigger a taxable remittance upon subsequent use by the company in the UK. This will also include investing funds in the UK save where Business Investment Relief is applicable.

In order to decide if income arising in that period is transitional trust income it is necessary to consider whether, had the rules on protected foreign-source income applied at that time and conditions A to E above had had effect, the trust income would have been protected foreign-source income when it arose.

If it would have been protected foreign-source income, it must also have neither been distributed by the trustees nor treated as the income of the settlor, under S624(1), to be transitional trust income.

The final condition that must be met is that for the tax year in which the trust income arose under the settlement it would have been treated as the income of the settlor, under S624(1), if the settlor had been domiciled in the UK for that tax year.

In determining whether income arose under a settlement for the purposes of calculating transitional trust income the provisions of S648(3) to (5) do not apply. Consequently, relevant foreign income of the trust for a tax year will be treated for this purpose as arising under the settlement even if the settlor was using the remittance basis for that year and the income was not remitted.

The rules on transitional trust income apply only to income that would for the tax year it arose have been treated as that of the settlor under S624(1) if the settlor had been domiciled in the UK. The transitional provisions do not extend to income treated as that of the settlor under S629(1) or S633.

Example

Uwe is the settlor of the UVW Family Trust. He settled cash and assets valued at the equivalent of around £2 million on the Jersey-resident corporate trustee in late September 2011. The trust is settlor interested as Uwe's wife is a member of the class of discretionary beneficiaries.

Uwe has a domicile of origin in Germany, where he was resident when he made the settlement, and has never acquired a domicile of choice elsewhere. He came to live in the UK in May 2005, to oversee the establishment of a business here from which he draws a salary in the UK. Uwe does

not intend to remain in the UK permanently or indefinitely, but he does not at present have any definite plans to return to Germany. Uwe is claiming under section 809B ITA 2007 for the remittance basis to apply to him while he is resident in the UK.

The trust's income for 2011-12 was £8,000 from UK investments and deposits and ChF16,000 from Swiss investments and deposits. In each subsequent year the income has been £16,000 and ChF32,000.

The UK-source income cannot be protected foreign-source income for the purposes of the trusts protections, and so remains chargeable to income tax on the arising basis. The foreign-source income would be relevant foreign income of an individual resident in the UK, so condition A is met. The trust property originates from Uwe, who was not domiciled in the UK when he settled the trust in September 2011, and the trustees are resident outside the UK. Conditions B, C and E are therefore met. Uwe has not become domiciled in the UK under common law, he was not born in the UK, and he does not have a domicile of origin here, so condition D is met. Uwe provides further property for the purposes of the settlement in July 2020, which means that condition F is met for tax years 2017-18, 2018-19 and 2019-20 but is not thereafter, as Uwe is resident in the UK in the tax year 2020-21 and was resident here in each of the fifteen previous tax years.

It is necessary to calculate the transitional trust income that has arisen under the settlement in the period from 2008-09 to 2016-17 inclusive. In this example the protection period runs from late September 2011 to 5 April 2017.

Any income that could not be protected foreign-source income cannot be transitional trust income, so the UK-source income can be left out of account. The foreign-source trust income for the protection period totalled ChF176,000, ChF16,000 for 2011-12 and ChF32,000 for each of the subsequent five years.

The first stage of the process is to work out the income arising under the settlement during the protection period. Uwe was resident in the UK for the tax years 2011-12 to 2019-20, which means that the foreign-source income would not be prevented from being treated as arising under the settlement for those years by S648(2). The transitional trust income is consequently ChF176,000, this being the foreign-source income for the five and a half tax years 2011-12 to 2016-17. Although this income was not remitted to the UK it can be treated as arising under the settlement as Uwe was resident here for those years, and for this purpose the provisions of S648(3) to (5) have to be ignored notwithstanding that Uwe used the remittance basis.

The second stage is to decide if the income arising under the settlement during the protection period would have been protected foreign-source income if the relevant conditions other than F had been in effect at that time. Conditions A to E would all have been met throughout the protection period, so no further reduction in the figure of ChF176,000 is needed at this stage.

No income was distributed by the trustees prior to 6 April 2017 and none was treated under section 624(1) as the income of the settlor at that time, so the amount of transitional trust income does not need to be reduced to take these factors into account at the third stage.

The final stage again involves the provisions of S648(3) to (5) being ignored, this time in deciding whether the income arising under the settlement for 2011-12 and 2016-17 would have been treated as Uwe's income if he had been domiciled in the UK in those years.

2.20 The changes to the rules relating to capital sums paid to settlors, which have effect for the tax year 2017-18 and subsequent tax years, work by removing protected foreign-source income from the amount of available income. This reduces the amount of income against which capital sums are compared for the purposes of deciding how much, if any, of such sums are to be treated as the settlor's income.

2.21 Before exploring the changes it is probably worth outlining the rules in effect up to and including 5 April 2017. Again, this guidance is not intended to provide a comprehensive introduction to all aspects of the rules. The F(No. 2)A 2017 changes do not alter the pre-6 April 2017 interactions between the settlements legislation and the transfer of assets abroad rules.

2.22 A capital sum paid directly or indirectly by the trustees of a settlement to the settlor in any tax year is treated as the income of the settlor for that year so far as it falls within the amount of available income up to the end of that year. For these purposes, if a capital sum is paid in any tax year to the settlor by a body corporate connected with the settlement in that year, and an associated payment has been, or is, made directly or indirectly to the body corporate by the trustees of the settlement, that capital sum is treated as having been paid to the settlor by the trustees. There are also provisions dealing with payments made to or by associated companies. For the sake of simplicity, these guidance notes illustrate the rules by reference to the basic situation of capital sums paid by trustees to settlors.

2.23 A capital sum arises in two main situations, subject to exceptions similar to those applicable to income by virtue of S625.

- Where any sum is paid by way of loan or repayment of loan.
- Where any other sum is paid otherwise than as income and is not paid for full consideration in money or money's worth.

Example

Dionne is the settlor of the Dionne Family Settlement, in which she does not retain an interest. Dionne has no minor, unmarried children. In January 2017 the trustees of the Dionne Family Settlement lend £500,000 to Dionne. This loan is a capital sum and is treated as the income of Dionne for the tax year 2016-17 to the extent that it does not exceed the available income for that year.

2.24 It also covers any sum which is paid by the trustees of a settlement to a third party at the settlor's direction, or as a result of the settlor's assignment of his or her right to receive the sum. These are treated as sums paid to the settlor by the trustees. Where a sum is otherwise paid, or applied, by the trustees for the benefit of the settlor, that sum is treated as a capital sum paid by the trustees to the settlor.

Example

Enrico is the settlor of the Enrico Discretionary Trust, in which he does not retain an interest. Enrico has no minor, unmarried children. At 6 April 2015 Enrico is owed €200,000 by the trustees. In March 2016 Enrico assigns his right to repayment of the loan to Sophia, his adult daughter. The trustees repay €100,000 of the capital to Sophia in June 2016. This repayment is a capital sum and is treated as the income of Enrico for the tax year 2016-17 to the extent that it does not exceed the available income for that year.

2.25 For these purposes references to sums paid include sums paid to the settlor's spouse or civil partner. They also include references to sums paid to the settlor, or the settlor's spouse or civil partner, jointly with another person.

2.26 Where the capital sum paid in a tax year exceeds the available income for that tax year the excess can be carried forward and matched against the available income of subsequent years, up to a maximum of ten years.

Example

Frank is the settlor of Frank's 2004 Settlement, in which he does not retain an interest. Frank has no minor, unmarried children. In September 2005 the trustees lend Gabriella, Frank's wife, £250,000. The settlement has no available income for 2005-06 and so the whole of the capital sum of £250,000 is to be carried forward to the following year. In each of the next ten years the settlement has available income of £20,000. The capital sum is treated as Frank's income up to the amount of £20,000 each year. The £50,000 balance of the capital sum remaining at the end of 2015-16, the end of the ten years, is not to be treated as Frank's income in any subsequent year, regardless of the amount of available income.

2.27 The amount of any available income is central to the calculation of how much of any capital sum is to be treated as the income of the settlor for a tax year. The changes that take effect for 2017-18 onwards operate through amendments to the rules for calculating available income. They do so by introducing the concept of unprotected income, which means any income that is not protected foreign-source income. The guidance above on protected foreign-source income, in paragraph 2.10 onwards, is therefore directly relevant to the rules relating to capital sums. Prior to 6 April 2017 the calculation of available income included all income arising under the settlement up to the end of the tax year which had not been distributed. The provisions of section 648 applied in determining whether or not income had arisen for this purpose.

2.28 With effect from 2017-18 the calculation of the amount of available income in relation to any capital sum is as follows. Again, for the sake of simplicity this guidance does not deal with the exception provided by S634(3), the special case of trustees for charitable purposes in S636(1)(c) and (6), or with the modifications to the general rules made by S636(3) and (5) and S637.

Step 1

Calculate the undistributed, unprotected income arising under a settlement for the year. This is the unprotected income in excess of the total of the amounts below.

(a) Any sums paid in a tax year, by the trustees of the settlement to any person, as are

(i) treated in that year, other than under the capital sum rules, as the income of those persons for the year, or

(ii) would be so treated if those persons were resident and domiciled in the UK and the sums had been paid to them here.

(b) Expenses of the trustees of the settlement paid in the tax year which, in the absence of express provisions of the settlement, would be properly chargeable to income.

Example

Barbara was born in the UK and has a domicile of origin here. In early adulthood Barbara emigrated to New Zealand, where she acquired a domicile of choice and has lived for nearly fifty years. Barbara's only child, Colin, is currently resident in the UK. Following the death of Barbara's husband in 2015, she decides to try living in the UK again in order to be near her son and his family. Barbara is the settlor of the Colin's Children's 2016 Settlement, which she funded out of what she regarded at the time as her surplus wealth. Barbara does not retain an interest in the settlement. The corporate trustee is in Hong Kong and the trust fund is invested in various assets outside the UK.

Barbara moves back to the UK in August 2017. Acquiring a suitable home in the UK proves to be more expensive than Barbara had anticipated. In February 2018 she asked the trustees for a loan. The trustees are willing to lend Barbara £100,000, at 4.75% interest per annum, with a link to the bank base rate. Barbara and the trustees consider this to be a commercial rate of interest. This would, in itself, lead to the trust becoming unprotected, as it would be a loan from the trustees carrying interest payable at more than the official rate. However, as Barbara was born in the UK and has a domicile of origin here, condition D of S628A will not be met and Colin's Children's 2016 Settlement will be an unprotected trust for 2017-18 onwards regardless of the loan. The making of the loan by the trustees on commercial terms in May 2018 does not benefit Barbara, and is not the cause of the trust being unprotected, but it is a capital sum paid to the settlor.

The income arising under the settlement will not be protected foreign-source income because condition D is not met. Each year the unprotected foreign-source income is £15,000 and the UK-source income is £4,750. From 2020-21 the trustees pay £5,000 of this income to Barbara's eldest grandchild, who started a three-year course of higher education in September 2020. The expenses of the trustees each year are £2,500. The undistributed, unprotected income for each of the years 2017-18, 2018-19 and 2019-20 is £17,250, this being £15,000 unprotected foreign-source income and £4,750 UK-source income minus £2,500 expenses. For 2020-21 to 2022-23 it is £12,250, this being £19,750 income minus £2,500 expenses and £5,000 income paid away.

Step 2

Add together the amount of unprotected income arising under the settlement, in that year and any previous year in which the settlor was UK resident, which has not been distributed or used to pay expenses.

Example

Continuing the example of Barbara, the position up to the end of 2018-19 is as follows.

2017-18	Undistributed, unprotected income	£17,200	Cumulative	£17,250
2018-19	Undistributed, unprotected income	£17,250	Cumulative	£34,500

Step 3

Deduct from the total in step 2 the amounts below.

(a) The income taken into account under the capital sums rules in relation to that capital sum in any previous year or years.

(b) The income taken into account under the capital sums rules in relation to any other capital sum in any previous year or years.

(c) Any income arising under the settlement, in that or any previous years, which has been treated as the income of the settlor under the rules explained in (TSEM4000) onwards and elsewhere in this Guidance Note.

(d) The sum of tax at the trust rate on

(i) the total amount of income arising under the settlement in that year and any previous year which has not been distributed, less

(ii) any income of the kind mentioned in (c) above.

Example

Using Barbara's case again, at the end of 2017-18 there is no capital sum and so the amount of available income is irrelevant. During 2018-19 the trustees pay a capital sum of £85,000 to Barbara. For the purposes of this example it is assumed that tax rates remain unchanged from the tax year 2017-18. At the end of that tax year the figure from step 2 is £34,500. There was no capital sum in any previous year, which means that there is no amount to be deducted at (a) or (b) for 2018-19. None of the income could have been treated as that of the settlor, so there is nothing to deduct under (c). The trustees are resident in Hong Kong and the income has its source outside the UK, so they have had no income tax liability in the UK. The tax at the trust rate on the figures in (d)(i) and (ii) of step 3 is £15,525 (£34,500 @ 45%). The available income for 2018-19 is therefore £18,975, which

falls entirely within the capital sum of £85,000 for the year. This is treated as Barbara's income for 2018-19. £66,025 of the capital sum will be carried forward for use in 2019-20 to 2028-29.

The undistributed, unprotected income for 2019-20 is £17,250 and the total from step 2 is £51,750. The amount at step 3(a) is £18,975, this being the available income taken into account in relation to the capital sum for 2018-19. The amounts at step 3(b) and (c) are nil. The amount at step 3(d) is £23,288 (£51,750 @ 45%), so the available income for the year is £51,750 less £42,263 (£18,975 + £23,288). For 2019-20 an amount of £9,487 is treated as Barbara's income.

Moving forward to 2020-21, the undistributed, unprotected income is £12,250 and the total from step 2 is £64,000. The amount at step 3(a) is £28,462, this being the available income taken into account in relation to the capital sum for 2018-19 and 2019-20. The amounts at step 3(b) and (c) are nil. The amount at step 3(d) is £28,800 (£64,000 @ 45%), so the available income for the year is £64,000 less £57,262. An amount of £6,738 is treated as Barbara's income for 2020-21.

If we assume that the position remains the same in future years, £6,737 or £6,738 will be treated as Barbara's income in each of the years 2021-22 to 2027-28. The available income for 2028-29 will be £6,738, but there will be only £2,638 of the capital sum that has not already been treated as Barbara's income. This latter figure will therefore be the amount treated as Barbara's income for 2028-29.

2.29 Where a capital sum is treated as the income of a settlor for a tax year, it has to be grossed-up by reference to the trust rate for that year in charging it. In Barbara's example there would be a chargeable amount of £34,500 for 2018-19.

A deductible amount is to be set off against the tax due on the grossed-up amount. The calculation of this amount involves consideration of the amount of tax paid on the grossed-up amount of so much of the income available up the end of the tax year, in relation to the capital sum, as is taken into account under S633 in relation to that sum in that year.

The relevant legislation has not changed from 6 April 2017, but it is worth noting that in computing any deductible amount the foreign-source income of trustees resident outside the UK is grossed-up at a rate of 0%.

2.30 For 2017-18 and later tax years, where income of a settlement is paid to, or for the benefit of a minor, unmarried child of the settlor it is necessary to consider whether that income is protected foreign–source income. Such income is not treated as that of the settlor. In deciding whether relevant foreign income arises under a settlement for this purpose it does not matter whether or not the income was remitted.

Where the trustees retain or accumulate income before making a payment to a minor, unmarried child of the settlor, that payment is treated as one of income so far as there is retained or accumulated income available. For this purpose income arising under a settlement does not include unremitted income where the settlor is using the remittance basis. Unremitted income of 2017-18 or a later tax year could be protected foreign-source income that arose under a settlement for a year for the purposes of S629(1) but would not be income arising under that settlement for the purposes of S631.

Example

Paul is the settlor of the Paul 2011 Children's Discretionary Settlement, created for the benefit of his two existing children and any of his future children. He has not retained an interest in the settlement. The trustees are resident in Guernsey and invest in a portfolio of investments located outside the UK that is intended to provide a balance between long-term capital growth and income. Paul was born in the UK and has a domicile of origin here. From an early age he lived in Germany with his parents, acquiring a domicile of choice there some years ago. In July 2012 Paul came to live and work in the UK for just over three years. He did not use the remittance basis during that period. From November 2015 Paul lived and worked in New York, but he returns to the UK in April 2019. For 2019-20 onwards Paul uses the remittance basis. After moving back to the UK, Paul and his wife have two more children.

The Guernsey trustees are permitted by the trusts of the Paul 2011 Children's Discretionary Settlement to distribute amongst those of Paul's children who have attained the age of sixteen up to 10% of the income arising under the settlement in any year. The annual income of the settlement is between £30,000 and £40,000 for the relevant years. Paul's eldest child is sixteen in May 2023 and the trustees make a payment of £500 to her in August 2023, with the intention that they make similar payments annually to her and, in due course, her siblings. None of the children is married. No capital sums are paid to Paul by the trustees of the Paul 2011 Children's Discretionary Settlement.

Paul becomes resident in the UK in 2019-20, and is deemed domiciled here for the year under condition A of S835BA ITA 2007. Condition D is not met and the Paul 2011 Children's Discretionary Settlement is an unprotected trust. Tainting is not, therefore, an issue. For the years 2019-20 to 2022-23 inclusive the settlements legislation does not treat any of the trust income as that of Paul, as there are no circumstances that would cause the income arising under the settlement to be treated as that of the settlor. This changes from 2023-24, with the payments to one or more minor, unmarried children being treated as Paul's income.

Paul has an income tax liability through the settlements legislation only from the point at which income arising under the settlement is caught by the legislation, notwithstanding that the settlement has been an unprotected trust for several years. Payments to Paul's children could result in the trust's foreign-source income for 2012-13 to 2015-16 and from 2019-20 onwards being treated as that of Paul if either income is paid to or for the benefit of the children or a capital sum that is matched by accumulated or retained income is paid to them or for their benefit while they are minors.

Example

Paul's wife, Jane, was born in the UK, but her domicile of origin is the Republic of Ireland. She grew up in the Republic of Ireland before attending university in England and then living and working in Germany. Since 2001 Jane has lived with Paul, and they were married in Germany in 2005.

Jane is the settlor of the Jane 2011 Children's Discretionary Settlement, which is identical in form to the Paul 2011 Children's Discretionary Settlement. The capital and income of the Jane 2011 Children's Discretionary Settlement is about a quarter of that of the Paul 2011 Children's Discretionary Settlement. No capital sums are paid to Jane by the trustees, and there has been no

tainting of the settlement. When Jane becomes resident in the UK in 2019-20 the trust remains protected, as she does not have a domicile of origin in the UK and so is not deemed domiciled under condition A of S835BA ITA 2007.

The trustees of the settlement decide to pay £150 from the current year's income to the eldest child in August 2023. At the time she is studying in Germany and the money is received and spent by her there. The trusts protections still apply to the settlement, so the income from which the payment is made is protected foreign-source income. As it is not remitted to the UK it is not income arising under the settlement for the purposes of the settlements legislation and so cannot be treated as the income of Jane for income tax purposes.

Example

In July 2030 Paul and Jane decide to remain in the UK permanently or indefinitely. The Jane 2011 Children's Discretionary Settlement becomes an unprotected trust from 2030-31, as she is now domiciled in the UK under common law. The trustees reduce the payments out of the income of both the Paul 2011 Children's Discretionary Settlement and the Jane 2011 Children's Discretionary Settlement to £100 a year to each of the two younger children.

Although neither settlement enjoys the benefit of the trusts protections from 2030-31 onwards, the payments to each minor, unmarried child from each trust do not exceed £100 a year. As long as these are the only payments caught by the rules on parental settlements they will not be treated as the income of the parents.

Example

Geoff is the settlor of the Geoff 2014 Discretionary Child's Trust, established in January 2014. The trust is for the benefit of Geoff's only child, Lucy, who was born in March 2012, and any of her issue. Geoff cannot benefit from the trust property. The trustees can pay up to two-thirds of the income each year to Lucy, or for her benefit, while she is a minor.

Geoff was born in Guernsey and he lived and worked around the world before returning there in 2009. He has a domicile of origin in Guernsey, which was operative when he settled the trust. The trustees are resident in Guernsey.

The trust income for 2013-14 was US$2,000 and €2,000, and has been US$8,000 and €8,000 each tax year since. The income arises from US$ and € deposits kept in separate accounts. The US$ income is paid by the trustees for Lucy's benefit, while the € income is accumulated.

Geoff came to live in the UK in August 2014. From February 2020 he became domiciled here under common law, as he decided to remain permanently or indefinitely. Prior to Geoff's acquisition of a domicile of choice in the UK he used the remittance basis.

For 2013-14 Geoff was not resident in the UK. For 2014-15 to 2018-19 he was resident but not domiciled in the UK and used the remittance basis. From 2019-20 Geoff was resident and domiciled in the UK. The trust income for 2019-20 onwards is not protected foreign-source income, as condition D is not met once Geoff becomes domiciled in the UK under common law.

In deciding whether it is protected foreign-source income for the purpose of S629(1) with effect from 6 April 2017, the 2017-18 and 2018-19 trust income arises under the settlement regardless of whether it has been remitted, as S648(3) to (5) do not apply for this purpose.

The 2013-14 US$ income does not arise under the settlement for the purpose of S629(1), as Geoff was not resident in the UK for the year and so S648(2) applies to that income.

The US$ income falls within the scope of S648(3) for tax years 2014-15 to 2016-17. The income was paid for Lucy's benefit outside the UK and was not remitted to the UK. For 2017-18 and 2018-19 the US$ income was protected foreign-source income and so outside the scope of S629(1). From 2019-20 to 2029-30, during which latter year Lucy reaches her majority, the US$ income will be treated as Geoff's for income tax purposes. This is because in 2019-20 Geoff becomes domiciled in the UK under general law and so the trust is no longer protected. The income is all treated as his and the remittance basis cannot apply because of the acquisition of a domicile of choice in the UK.

In May 2025, when Lucy is 13, the trustees pay Lucy €60,000 from the income accumulated to capital up to the end of 2024-25. This payment is remitted to the UK. It is treated as a payment of income arising under the settlement to the extent that it does not exceed the retained or accumulated income available. This latter amount is calculated by deducting the total amount of disregarded income from the total amount of income that has arisen under the settlement since it was made.

No income arose under the settlement for this purpose until 2017-18, as it was all unremitted. In 2017-18 and 2018-19 income arose under the settlement for the purposes of S629(1) even though it was protected foreign-source income. For the purposes of S631, however, the unremitted income is not treated as having arisen for those years. Over the six years from 2019-20 to 2024-25 inclusive, income has arisen under the settlement since Geoff has become domiciled under common law and so S648(3) cannot apply. The US$ income has been distributed to Lucy, to the extent that it has exceeded the trust expenses properly charged against it, and so cannot be retained or accumulated income. The €48,000 that has arisen under the settlement for the tax years 2019-20 to 2024-25 can be retained or accumulated income.

Since 2019-20 all the US$ income has been treated as that of Geoff, which means it would have been disregarded if it had been retained or accumulated income. None of the € income has been treated as Geoff's income up to the end of 2024-25. This is because none of it had been paid to, or for the benefit of, Lucy. There are no living beneficiaries of the trust, other than Lucy, to whom income could have been paid, so there have been no payments to such persons, and there are no such persons as whose income the trust income could be treated. The provision relating to income treated as that of a minor child for years up to 1997-98 cannot be relevant to the facts of this example. The trustees applied €200 each year in meeting the expenses of the trust properly chargeable to income. This has happened for each of the tax years in which income has arisen under the settlement. The retained or accumulated income is the €48,000 of income that has arisen under the settlement for this purpose less the €1,200 (€200 x 6) disregarded income. The payment of €60,000 can be treated as Geoff's income for 2025-26 only to the extent of €46,800.

3. Transfer of Assets Abroad Legislation Trust Protections

3.1 Paragraphs 27 to 38 of Part 2 Schedule 8 of Finance (No 2) Act 2017 make a number of changes to the Transfer of Assets Abroad legislation at Chapter 2 Part 13 ITA 2007 as a result of the domiciled rules that have been set out in other parts of this guidance. The purpose of this guidance is to show how Finance Act (No 2) 2017 will affect the existing provisions; it is not intended to provide a detailed description of the Transfer of Assets Abroad legislation. Further changes affecting the Transfer of Assets Abroad legislation are being introduced in Finance Bill 2018 (see 1.6). Statutory references in this section of the guidance note are to ITA 2007 unless otherwise stated.

3.2 The Transfer of Assets Abroad legislation is wide ranging anti-avoidance legislation. This paragraph provides an overview of the transferor charges with the benefits charge being discussed in paragraph 3.3. In broad terms the transferor charges are aimed at preventing individuals who are resident in the United Kingdom from avoiding a liability to tax by means of a transfer of assets which results in income becoming payable to a person abroad, whilst the individual who made the transfer has either the power to enjoy the income arising (S720 ITA 07) or has received, or is entitled to receive, a capital sum which is connected with the transfer (S727 ITA 07). If the conditions for the charge are met then the transferor will be taxable on the income arising to the person abroad in the tax year and consequently these charges are usually referred to as the transfer of assets (transferor) income charges.

3.3 The legislation also applies where an individual who is resident in the UK receives a benefit provided out of the assets available for the purpose as a result of a transfer of assets made by another person (S731 ITA 07). This is referred to as the transfer of assets benefits charge and the amount of the income subject to tax is the lesser of the value of the benefit received or the relevant income available in the structure to match against the benefit. Unmatched benefits are carried forward to be matched with future income and unmatched income is carried forward to be matched to future benefits.

3.4 In general terms the changes that are made by Finance (No 2) Act 2017 remove certain income of overseas trusts settled by non-UK domiciled settlors from the charge under either S720 or S727 ITA 07 and instead bring them within the scope of S731 ITA 07 (the benefits charge) so that they are assessed on the benefits they received from the trust and its underlying entities. It also removes certain income of non-resident trusts settled by individuals who are deemed UK domiciled by virtue of the length of time they have been resident, provided the trusts were settled before the individual became deemed domiciled, from the charge under either S720 or S727 ITA 07 and similarly brings them within the scope of S731 ITA 07.

3.5 The Transfer of Assets Abroad legislation refers to relevant transactions which includes a transfer of assets and/ or associated operations. The only statutory meaning given to the word transfer is that in relation to rights it includes the creation of rights. In the absence of a more specific definition a transfer under the legislation will carry its ordinary everyday meaning. There are therefore a wide range of actions that may amount to a transfer in the sense of to convey from one place, person, ownership, object group and so on to another. An associated

operation is defined as an operation of any kind effected by any person in relation to any of the assets transferred, any assets directly or indirectly representing the assets transferred and any income arising from them. Likewise the meaning of asset for the purpose of the provisions is very widely drawn as it includes property or rights of any kind. A person abroad can include a body of persons corporate or incorporated and therefore includes companies and trusts that are not resident in the UK.

3.6 It should be noted that there can be an exemption from the charges under S720, S727 and S731 ITA 07 if the relevant transactions were undertaken with no tax avoidance purpose or were genuine commercial transactions (see S737 to S742A ITA 07). The taxpayer must claim the motive defence.

3.7 It can be seen from the foregoing description of how the legislation may apply in paragraphs 3.2 and 3.5 above that it can apply in respect of non-resident trusts established by UK resident non-domiciliaries and also to any non-resident entities that these non-resident trusts may own such as non-resident companies. This means that a deemed domiciled settlor of a settlor interested trust would not be able to access the remittance basis and would be liable to income tax on the income of the trust and its underlying entities in the year that the income arose under a combination of S720 or S727 ITA 07, and the settlements provisions where only an offshore trust was involved. It is, however, accepted that tax on the trust income will only be taken once. Whilst it is not statutory, where the new benefits charge does not apply (in which case the transfer of assets abroad legislation has priority as per the legislation), the settlement legislation has priority. In order to fulfil the governments objectives that individuals who are UK resident but not domiciled and individuals who are deemed domiciled because of the 15 out of 20 year residence rule are only subject to income tax on the UK source income arising in such trusts and the benefits that they receive, it has been necessary to make amendments to the transfer of assets abroad legislation. The remainder of this section looks at the changes that have been made in Finance (No 2) Act 2017 designed to achieve this.

3.8 It should be emphasised that the scope of the transfer of assets legislation goes wider than non-resident trusts and their underlying entities, but the amendments to the legislation covered below only affects non-resident trusts and their underlying entities specifically covered by the new protections. It also includes foreign entities that fall to be treated like trusts under the principle in Memec plc v IRC e.g. certain types of foundations. We look at the non-resident trusts that are covered by the protections in the following paragraphs. For non-resident trusts that are not covered by the protections (i.e. trusts settled by UK domiciled individuals, deemed domiciled individuals born in the UK with a UK domicile of origin, or trusts settled by deemed domiciled individuals after they have become deemed domiciled) or any other entities that come within the transfer of assets legislation, for example a non-resident company owned by a UK resident, the income and benefits charges will remain unaffected by the amendments referred to below.

3.9 Prior to Finance Bill 2017 S720 ITA 07 imposes a charge to tax on an individual if the following conditions are met:

- There has been a relevant transfer
- As a result of the transfer income becomes payable to a person abroad
- The individual is resident in the UK
- If the income had arisen to the individual it would have been taxable in the UK

- The individual has the power to enjoy the income of the person abroad.

If the conditions are met in a particular tax year the transferor will be taxable on the income arising to the person abroad during the year. The Finance (No2) Act 2017 replaces S721(3B) ITA 07 with a new subsection (3B). This new subsection (3B) is what causes protected trusts and their underlying entities to be treated differently from other types of arrangements for the purposes of s720. The new subsection (3B) does this by dis-applying s720 from applying to certain income if broadly speaking that income is foreign income of a protected trust or an underlying entity.

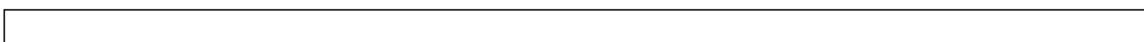
More specifically, it defines the amount of income treated as arising under S720 ITA 07 as either:

- the amount of income of the person abroad if the transferor is domiciled in the UK at any time during the year in which the income arises, or if the transferor is deemed domiciled in the UK in a year when they are resident in the UK because they were born in the UK and had a domicile of origin in the United Kingdom; or,
- if the transferor is not domiciled in the UK or is deemed domiciled in the UK only because they have been resident in the UK for 15 out of the past 20 years then the income of the person abroad is treated as an amount equal to the income of the person abroad that is not protected foreign-source income.

3.10 Protected foreign income for the purposes of S721(3B) ITA 07 is defined in S721A ITA 07 in respect of both income arising in non-resident trusts and in the underlying companies of those non-resident trusts. There is a specific definition of what constitutes an underlying company for these purposes (see S721A(3)(e)).

3.11 Looking firstly at what constitutes protected foreign income in a non-resident trust there are a number conditions that must be met:

- If the income had arisen to the individual then for the purpose of S830 ITTOIA 05 it would have been treated as relevant foreign income. For the purpose of the transfer of assets legislation the person abroad receiving the income is the trustee of a settlement and the trustees are not resident in the UK for the tax year in question.
- When the settlement was created the settlor was not domiciled in the UK and if the settlement was created on or after 6 April 2017 then the settlor was not deemed domiciled in the UK.
- No property or income is provided directly or indirectly for the purpose of the settlement by the settlor, or by the trustees of any other settlement of which the settlor is a beneficiary or settlor at any time in the period beginning with 6 April 2017, or if later the date on which the settlement was created and ending at the end of the tax year in question at a time when the individual is domiciled or deemed domiciled in the UK. This particular condition is referred to as tainting and S721B ITA 07 looks at what constitutes the addition of property. It should be noted that this condition only applies to individuals who have become deemed domiciled and does not apply to non-domiciled individuals who are able to continue to add property to a settlement up to the time that they become deemed domiciled. As the tainting impact is wider that just the transfer of assets legislation this is covered in detail in section 5 of this guidance.



Example

John who is not domiciled in the UK has been resident in the UK for 18 years. He settled a non-resident trust on 6th April 2010 with £1 million of capital. Both John, his wife and children are discretionary beneficiaries of the trust. The trustees invested half of the funds in offshore investments and half in UK investments. Each year the offshore investments generate income of £50,000 and the UK investments generated income of £55,000 for the trustees. The trustees have retained the income and have not made any distributions.
For the purpose of this example it is assumed that the transfer of assets legislation applies and the settlements legislation is ignored.

For the years from 2010/11 to 2016/17 S720 ITA 07 will apply and John will be liable to income tax on the income of the trustees as it arises. However, John is a remittance basis user and will therefore only be assessed on an arising basis on the £55,000 of UK source income each year. John will not be liable on the income from the offshore investments as the income has not been remitted to the UK.

On 6 April 2017 John becomes deemed domiciled in the UK because he is a long term resident. As John settled the trust before he became deemed domiciled (i.e. the trust is protected) the charge under S720 ITA 07 will be restricted to the income that is not protected foreign-source income. John will therefore be liable to income tax under S720 ITA 07 on the £55,000 of UK source income arising in the trust. The income of £50,000 arising in respect of the offshore investments will be protected foreign-source income and so will not be taxed tax under S720 ITA 07.

If in 2020/21 John adds a further £1 million of capital to the trust. John will have tainted the trust and John will be liable to tax on all of the income arising in the trust under S720 ITA 07 from 2020/21 onwards.

Example

Nigel who is not domiciled in the UK has been resident in the UK for 11 years. He settled a non-resident trust on 6th April 2017 with £500,000 of capital. Nigel and his two children are discretionary beneficiaries of the trust. The trustees invest the £500,000 in offshore investments that generate income of £45,000 per year. The trustees retain the income and have not made any distributions. For the purpose of this example it is assumed that the transfer of assets legislation applies.

As the trust was settled on 6 April 2017 it will be subject to the provisions of Finance (No2) Act 2017 from the date it was created. Nigel was not domiciled in the UK when the trust was created and indeed, as he continues to be non-domiciled in the UK, the trust will be protected. As such S624(1) ITTOIA 05 (the settlements legislation) and S720 ITA 07 will only apply to any UK source income arising in the trust. In 2017/18 as there is only protected foreign-source income there will be no liability under either statue since no benefits have been taken.

On 6 April 2020 Nigel settles a further £500,000 of capital into the trust which the trustees use to acquire further offshore investments that generate an additional income of £40,000 per year. As Nigel remains non-domiciled on 6 April 2020 (and has not become deemed domiciled as he has not been in the UK for 15 years) the additional property added to the settlement does not affect the protected status of the trust and S624(1) ITTOIA 05 and S720 ITA 07 will not apply to the income of the settlement as it constitutes protected foreign-source income.

3.12 For the underlying companies of a non-resident settlement, income will be protected foreign-source income for the purposes of S721(3B) if the following conditions are met:

- If the income had arisen to the individual then for the purposes of S830 ITTOIA 05 it would have been treated as relevant foreign income.
- For the purpose of the transfer of assets legislation the person abroad receiving the income is a company
- The trustees of a settlement are participators in the person abroad, or are participators in the first company in a chain of two or more companies where the last company in the chain is the person abroad and where each company in the chain (other than the last one) is a participator in the next company in the chain. A participator for this purpose has the meaning given by S454 CTA 2010 i.e. a person having a share or interest in the capital or income of the company.
- The individual's power to enjoy the income results from the trustees being participators as mentioned in the bullet point above. The trustees are not resident in the UK for the tax year in question
- When the settlement was created the settlor was not domiciled in the UK and if the settlement was created on or after 6 April 2017 then the settlor was not deemed domiciled in the UK.
- No property or income is provided directly or indirectly for the purpose of the settlement by the settlor, or by the trustees of any other of which the settlor is a beneficiary or settlor at any time in the period beginning with 6 April 2017, or if later the date on which the settlement was created and ending at the end of the tax year when the individual is domiciled or deemed domiciled in the UK. This particular condition is referred to as tainting and S721B ITA 07 looks at what constitutes the addition of property. As the tainting impact is wider that just the transfer of assets legislation this is covered in detail in section 5 of this guidance.

Example

Paul who is not domiciled in the UK has been resident in the UK for the last 17 years. In 2009 Paul established a non-resident trust in which both Paul and his wife and two children are discretionary beneficiaries. When the trust was established Paul settled £250,000 into the trust together with shares in his UK trading company P Ltd. The trustees used the funds settled to subscribe for shares in a non-resident company, N Ltd, with a view to investing the £250,000 overseas. The trustees also transferred their holding of shares in P Ltd to N Ltd in exchange for shares.

Solely for the purposes of this example it is assumed that the transfer of assets legislation applies and the possible application of the settlements legislation is ignored.

Until 2017, Paul will be assessable on the income of the trust on a remittance basis because the trustee's income will consist of dividends in an overseas company which will be relevant foreign income. Under the transfer of assets legislation N Ltd will also be a person abroad and Paul will be assessable on the remittance basis in respect of any income arising from the overseas investments. With regard to any dividends paid to N Ltd by P Ltd, as P Ltd is a UK company such dividends will be UK source income Paul will be assessable on this income on an arising basis.

On 6 April 2017 Paul becomes deemed domiciled in the UK because he is a long term resident. In 2017/18 the trustees receive no income from N Ltd. N Ltd receives income from its overseas investments of £20,000 and also receives a dividend from P Ltd of £50,000. The dividend is UK source income. The £20,000 investment income from overseas investments will be protected foreign source income and so will not be treated as income for the purposes of S720 ITA 07, however, as the £50,000 dividend received from P Ltd would not be treated as relevant foreign income if it had been received by the individual this will be assessable on Paul under S720 ITA 07.

3.13 As can be seen from the examples above relevant foreign income may have arisen pre 6 April 2017 in either a non-resident trust or an underlying company of such a trust that will not have been subject to tax under S720 ITA 07 on the settlor/transferor because the income has remained within the structure and has not been remitted to the UK by the trust or company. Under the pre 6 April 2017 rules such income would be assessable under S720 ITA 07 if it was subsequently remitted to the UK. However, S726 ITA 07 which deals with individuals assessable under S720 ITA 07 to whom the remittance basis applies has been amended with the addition of subsection (6). This means that from 2017/18 the position has changed so that S832 ITTOIA 05 will no longer apply to the foreign deemed income in so far as it is remitted to the UK in 2017/18 or a later year and the income is transitionally protected income. Transitionally protected income is defined at S726(7) ITA 07 as any deemed foreign income where the associated foreign income (see s 726(2)) of the person abroad arising from a relevant transfer arose in a tax year that is earlier that 2017/18 and would be protected foreign source income (see paragraphs 3.10 to 3.12 above) had this legislation been in place in the year concerned. Also the income must not have been distributed by the trustees of the settlement concerned prior to 6 April 2017.

3.14 So for example if the trustees were to make a capital distribution post April 2017, then to the extent that that distribution is paid with monies containing pre-6 April 2017 foreign previously unremitted income, that pre-6 April 2017 income cannot be treated as a taxable remittance by the settlor if brought to the UK by a relevant person. Of course, the capital distribution will itself be subject to the anti-avoidance provisions dealing with capital distributions/benefits from offshore trusts which may deem the capital distribution to be income or gains. This would need to be dealt with on its own merits but the issue of remitting the underlying pre-6 April 2017 income referred to above would no longer exist.

3.15 The trustees of a settlor interested trust will from 6 April 2017 also be able to bring trust income (whether arising before or after 6 April 2017) to the UK without the non-domiciled, but UK resident settlor being liable to a charge under S720 ITA 07 on this income. The trustees and their closely held companies can now invest protected foreign income in UK assets sited in the

UK without triggering a charge to tax on the settlor under S720 ITA 07. However. it should be noted that this undistributed income will be relevant income available when calculating any liabilities that may arise under S731 ITA 07 in relation to any benefits that are provided to the settlor or any other beneficiary. The amendments that have been made to the benefits charge are covered in paragraphs 3.25 to 3.36 below.

Example

George who is non-domiciled in the UK has been resident in the UK for the last 20 years. He is a remittance basis user and in April 2010 George settled a non-resident trust in which both George, his wife and son Ringo were discretionary beneficiaries.

The trustees subscribed for shares in G Ltd an offshore company which invested the sums settled in offshore investments and from April 2010 to March 2017 the company's investments generated a total income of £1 million. It is assumed that the transfer of assets legislation applies to the arrangements and in particular the income arising in G Ltd. The income arising in G Ltd is treated as deriving from George's foreign deemed income (which itself is classified as relevant foreign income). Should any of this income have been remitted to the UK prior to 6 April 2017 George would have been assessable to income tax on it. The company did not remit any of the income to the UK before 6 April 2017. In May 2017 the directors of the company identify an investment opportunity in the UK and bring £500,000 of the accumulated income to the UK to fund this. The sums brought to the UK would not be assessable as George's income unless at a later date George received a benefit (or a close family member of `George where he is taxable on the benefit) that was matched to this income under the benefits charge (see paragraphs 3.25 to 3.36 below).

If before 6 April 2017 the directors of G Ltd made a distribution of £100,000 to the trustees who in turn distributed this income to Ringo, George's adult son, this would reduce the amount of the transitionally protected income to £900,000. Ringo may have a tax liability on this distribution in the UK it would depend on his personal circumstances.

If George had not been resident in the UK for sufficient time on 6 April 2017 to become deemed domiciled in the UK on that date then George would still be able to claim the remittance basis in respect of any benefits that he received. So to the extent that G Ltd or the trust provided George with a benefit that could be matched under the benefits charge provisions (see paragraphs 3.25 to 3.36) this benefit would only be assessable to the extent that it was remitted to the UK or matched with income retained within the structure which is remitted to the UK by the trustees or G Ltd.

3.16 So far the guidance on the transfer of assets legislation has considered the situation where an income charge arises to a transferor because they have the power to enjoy the income of the person. There is a further income charge under the transfer of assets legislation where the conditions shown at paragraph 3.9 are in point, but rather than having the power to enjoy the income of the person abroad the individual has received or is entitled to receive a capital sum that is connected to the relevant transfer. Where this condition is met the individual is assessable on the income arising to the person abroad in a tax year under S727 ITA 07.

3.17 The Finance Bill 2017 replaces S728(1A) ITA 07 with a new subsection (similar to the new subsection s721(3B) discussed above) which defines the amount of income treated as arising under S727 ITA 07 as;

- the amount of income of the person abroad if the transferor is domiciled in the UK at any time during the year in which the income arises, or if the transferor is regarded as being deemed domiciled in the UK in a year when they are resident in the UK because they were born in the UK and had a domicile of origin in the UK: or
- if the transferor is not domiciled in the UK or is deemed domiciled in the UK because they have been resident in the UK for 15 out of the past 20 years then the income of the person abroad is treated as an amount equal to the income of the person abroad that is not protected foreign income.

3.18 Protected foreign income for the purposes of S728(1A) ITA 07 is defined in S729A ITA 07 in respect of both income arising in non-resident trusts and income arising in the underlying companies of those non-resident trusts. There is a specific definition of what constitutes an underlying company for these purposes (see s729A(3)(e)).

3.19 Looking firstly at what constitutes protected foreign income in a non-resident trust there are a number conditions that must be met:

- If the income had arisen to the individual then for the purpose of S830 ITTOIA 05 it would have been treated as relevant foreign income.
- For the purpose of the transfer of assets legislation the person abroad receiving the income is the trustee of a settlement and the trustees are not resident in the UK for the tax year in question.
- When the settlement was created the settlor was not domiciled in the UK and if the settlement was created on or after 6 April 2017 then the settlor was not deemed domiciled in the UK.
- No property or income is provided directly or indirectly for the purpose of the settlement by the settlor, or by the trustees of any other of which the settlor is a beneficiary or settlor at any time in the period beginning with 6 April 2017, or if later the date on which the settlement was created and ending at the end of the tax year when the individual is domiciled or deemed domiciled in the UK. This particular condition is referred to as tainting and S721B ITA 07 looks at what constitutes the addition of property. As the tainting impact is wider that just the transfer of assets legislation this is covered in detail in section 5 of this guidance.

Example

Liam who is not domiciled in the UK has been resident in the UK for the last 16 years. He settles a discretionary non-resident trust for the benefit of his son with capital of £100 in 2010, from which Liam is irrevocably excluded. To enable the trust to accumulate funds for his sons benefit he makes an interest free loan to the trust of £500,000 in 2010. The trustees invest £250,000 of the funds in offshore investments that generate income of £10,000 per year and £250,000 in investment in the UK that generate income of £15,000 per year. For the purposes of this example it is assumed that the transfer of assets legislation applies and that the income tax settlement rules are ignored.

Liam does not have the power to enjoy the income of the person abroad, but by virtue of advancing the loan to the trustees he is entitled to a capital sum and as such S727 ITA 07 will apply and as a result the income of the trustees will be treated as Liam's income as it arises. Liam is a remittance basis user and so will only be assessed on an arising basis on the UK source income of £15,000 per year for each of the years from 2010/11 till 2016/17. Liam will not be assessable on the £10,000 per annum of foreign income unless this income is remitted to the UK.

On 6 April 2017 Liam becomes deemed domiciled in the UK because he is a long term resident. As Liam settled the trust before he became deemed domiciled the charge under S727 ITA 07 will be restricted to the income that is not protected foreign-source income (this is on the basis that the terms of the loan are altered to prevent the tainting of the trust (see section 5 of the guidance for further details). Liam will therefore be liable to income tax under S727 ITA 07 on the £15,000 of UK source income arising in the trust. The income of £10,000 arising in respect of the offshore investments will be protected foreign-source income and so will escape tax under S727 ITA 07. It should be noted that if the terms of the loan made to the trustees are not altered prior to 6 April 2018 so that it becomes a loan on arm's length terms as specified in the legislation (see later) and the interest due is not paid the trust protections would not be available as the trust will have been tainted and in this situation Liam would have been liable to income tax under S727 ITA 07 on the total income of the trust arising during the 2017/18 tax year (that is £25,000).

3.20 For the underlying companies (there can be a group structure or a chain) of a non-resident settlement income will be protected foreign income for the purposes of S728(1A) if the following conditions are met:

- If the income had arisen to the individual then for the purposes of S830 ITTOIA 05 it would have been treated as relevant foreign income.
- For the purpose of the transfer of assets legislation the person abroad receiving the income is a company and the trustees of a settlement who are participators in the person abroad, or are participators in the first company in a chain of two or more companies where the last company in the chain is the person abroad and where each company in the chain (other than the last one) is a participator in the next company in the chain. A participator for this purpose has the meaning given by S454 CTA 2010.
- The income has become the income of the person abroad as a result of the particular relevant transaction. .
- The trustees are not resident in the UK for the tax year in question
- When the settlement was created the settlor was not domiciled in the UK and if the settlement was created on or after 6 April 2017 then the settlor was not deemed domiciled in the UK.
- No property or income is provided directly or indirectly for the purpose of the settlement by the settlor, or by the trustees of any other of which the settlor is a beneficiary or settlor at any time in the period beginning with 6 April 2017, or if later the date on which the settlement was created and ending at the end of the tax year when the individual is domiciled or deemed domiciled in the UK. This particular condition is referred to as tainting and S728 (1A) ITA 07 looks at what constitutes the addition of property. As the tainting impact is wider that just the transfer of assets legislation this is covered in detail in section 5 of this guidance.

Example

Noel who is not domiciled in the UK has been resident in the UK for the last 17 years. In 2012 Noel settled a non-resident discretionary trust for the benefit of his son with £1,000. Noel was irrevocably excluded from benefiting from the trust. Noel also advanced an interest free loan to the trustees of £1,000,000. The trustees used the £1 million to subscribe for shares in O Ltd an offshore company. The company used £500,000 of the funds to invest offshore. Noel's son Damian wanted to start up a business in the UK and the directors of O Ltd used £500,000 to subscribe for shares in a UK company B Ltd through which Damian could operate the business. For the purposes of this example it is assumed that the transfer of assets legislation applies and that the income tax settlement rules are ignored.

In the years before 6 April 2017 Noel will be assessable on the income arising in the offshore company under S727 ITA 07 as he meets the capital sum conditions and O Ltd will be a person abroad for the purposes of the legislation. On the basis that he is a remittance basis user he will only be assessable on the income of O Ltd from its foreign investments if this income is remitted to the UK as this income will be deemed relevant foreign income. If B Ltd pays dividends to O Ltd as such dividends will be UK source income Noel will be assessable on these under S727 on an arising basis.

On 6 April 2017 Noel becomes deemed domiciled in the UK because he is a long term resident. In 2017/18 the trustees receive no income from O Ltd. O Ltd receives income from its overseas investments of £20,000 and also receives a dividend from B Ltd of £50,000. The £20,000 investment income from overseas investments will be protected foreign source income and so will not be treated as income for the purposes of S727 ITA 07, however, as the £50,000 dividend received from B Ltd would not have been relevant foreign income if it had been received by Noel this will be assessable on him under S727 ITA 07. This is on the basis that the terms of the loan made to the trustees by Noel are changed prior to 6 April 2018 to ensure that it is on arm's length terms (as specified in the legislation) and that the trustees pay Noel interest for the whole of the year. If the terms of the loan are not be amended then the trust structure would have been tainted (see section 5 of the guidance) and Noel would have been assessable to income tax for 2017/18 under S727 ITA 07 on the total income of £70,000 arising in O Ltd.

3.21 Relevant foreign income may arise in either a non-resident trust or an underlying company of such a trust. It will not have been subject to tax under S727 ITA 07 on the settlor/transferor if the income has remained within the structure and has not been remitted to the UK by the trust or company. Under the pre 6 April 2018 rules such income would be assessable under S727 ITA 07 if it was subsequently remitted to the UK for example as a result of funds being invested in the UK. However, S730 ITA 07 which deals with individuals assessable under S727 ITA 07 to whom the remittance basis applies has been amended with the addition of subsection (6). This means that from 2017/18 the position has changed so that S832 ITTOIA 05 will no longer apply to the foreign deemed income in so far as it is simply brought to the UK and no more in 2017/18 or a later year and the income is transitionally protected income. Transitionally protected income is defined at S730(7) ITA 07 as any deemed foreign income where the income of the person abroad arising from a relevant transfer in a tax year that is earlier that 2017/18 and would be protected foreign source income (see paragraphs 3.18 to 3.20 above) had this legislation been in place in the year concerned. Also the income must not have been distributed by the trustees of the settlement concerned prior to 6 April 2017.

3.22 As a result of these changes the trustees of a trust which is within the capital sum rules will from 6 April 2017 be able to bring trust income to the UK without the non-domiciled, but UK resident settlor being liable to a charge under S727 ITA 07 on this income. This undistributed income will be relevant income available when calculating any liabilities that may arise under S731 ITA 07 in relation to any benefits that are provided to the settlor or any other beneficiary. As such, remittances by the trustees, of income that is not transitionally protected, may result in a tax charge on the settlor just under the benefits charge legislation rather than s 727. The amendments that have been made to the benefits charge are covered in paragraphs 3.25 to 3.36 below.

3.23 So for example, if the trustees were to make a capital distribution post April 2017, then to the extent that that distribution is paid with monies containing pre-6 April 2017 foreign previously unremitted income, that pre-6 April 2017 income cannot be treated as a taxable remittance by the settlor if brought to the UK by a relevant person. Of course, the capital distribution will itself be subject to the anti-avoidance provisions dealing with capital distributions/benefits from offshore trusts which may deem the capital distribution to be income or gains. This would need to be dealt with on its own merits but the issue of remitting the underlying pre-6 April 2017 income referred to above would no longer exist.

Example

Mick who is not domiciled in the UK has been resident in the UK for the last 20 years. In 2010 Mick settles a non- resident discretionary trust for the benefit of his daughter Janet, from which he is irrevocably excluded. He settles £1,000 into the trust, but to provide further capital for investment he also advances an interest free loan of £200,000 to the trust. The trustees use the funds to subscribe for shares in an offshore company J Ltd and the company invests this amount in overseas investments. From 2010/11 to 2016/17 the overseas investments generate total income of £100,000. It is assumed that the transfer of assets legislation applies and that the settlements legislation is ignored. The income arising is treated as Mick's deemed relevant foreign income. Should any of this income be remitted to the UK Mick would be assessable to income tax on it. The company did not remit any of the income to the UK before 6 April 2017. In April 2017, in order to ensure that the trust is not tainted (see section 5 below) the terms of the loan are amended such that it is on arm's length terms and interest is payable by the trustees from 6 April 2017.

In July 2017 the directors of the company identify an investment opportunity in the UK and bring £50,000 of the accumulated income into the UK to fund it. The sums brought to the United Kingdom will not be assessable as Mick's income unless at a later date Mick received a benefit that was matched to this income.

If before 6 April 2017 the directors of J Ltd made a distribution of £10,000 to the trustees who in turn distributed this income to Janet, Mick's adult daughter, this would reduce the amount of the transitionally protected income to £90,000. Janet may have a tax liability on this distribution in the UK it would depend on her personal circumstances.

3.24 From 6 April 2018 the protected foreign income arising in certain non-resident trusts and their underlying companies is l no longer be subject to an income charge on non-domiciled and certain deemed domiciled settlors/transferors under the transfer of assets legislation. The Finance (No2) Act2017 makes amendments to the benefits charge sections of the legislation to bring these individuals within the scope of the benefits charge. The charge has also been expanded so that in in some circumstances the settlor/transferor will be assessable on benefits that have been provided to a person who is a close member of the settlor's family. The paragraphs below begin by looking at the changes that have been made to S731 and S732 ITA 07 to bring settlors and transferors within the scope of the benefits charge and then moves on to the changes that have been made to the calculation of the charge and how the close family members charge will apply.

3.25 In S731(1) ITA 07 the reference to non-transferors has been replaced with term individuals to make it clear that a charge under S731 ITA 07 is not just restricted to non-transferors from 6 April 2017. An additional subsection S731(1A) ITA 07 has also been introduced which states that if an individual is not resident in the United Kingdom in a particular tax year then that individual will not be chargeable to tax in respect of any income arising under this section. The subsection has been introduced to prevent a charge arising on a non-resident individual which was previously covered by S732(1)(b) ITA 07 (see paragraph 3.26 for more information on the changes to this subsection). However, S731(1A) ITA 07 does allow for the possibility of another individual being liable to tax on this income if S733A ITA 07 (settlor liable for section 731 charge on closely-related beneficiary) provides for such a charge. For more information on S733A ITA 07 see paragraphs 3.31 to 3.36.

3.26 In S732 ITA 07 all the references to non-transferors in the section are removed and replaced by individuals. There are changes in S732(1) which will apply the section if-

(a) a relevant transfer occurs,
(b) an individual receives a benefit in a tax year
(c) the benefit is provided out of assets which are available for the purpose as a result of the transfer, or one or more associated operations,
(d) where there is a time in the year when the individual is relevantly domiciled, the individual is not liable to income tax under S720 or S727 by reference to the transfer, and
(e) the individual is not liable to income tax on the amount or value of the benefit (apart from S731).

3.27 In (b) above the reference to the individual being resident in the tax in year which they receive a benefit is removed and is replaced by an individual who receives a benefit in a tax year. This amendment has been referred to in paragraph 3.25 above and the change has been made in order to enable a charge to arise on a settlor if a person who is a close family member of the settlor receives a benefit in a tax year in which they are non-resident.

3.28Point (d) above has the effect of preventing an individual who is liable to an income tax charge under either S720 or S727 ITA 07 from also being subject to a liability under the benefits charge if they received a benefit in the tax year. The replacement paragraph prevents a tax liability arising, under the benefits charge, on an individual if at any time during the tax year they are relevantly domiciled and liable to income tax under either S720 or S727 ITA 07. An individual is relevantly domiciled in the UK if at the time they are domiciled in the UK or are deemed domiciled in the UK by virtue of being resident in the UK, having been born in the UK and with a domicile of origin in the UK.

Example

Dave was born in the UK with a UK domicile of origin. Dave has been living overseas for a number of years and had acquired a domicile of choice in Singapore. Dave is sent to work in London by his employer for a period of three years. Dave took advice before returning to the UK and settled property into a non-resident trust. The trustees use some of the trust capital to purchase a property in London for Dave to live. The trustees invest the remainder of the property in offshore investments that generate income of £100,000 per year.

On 6 April 2017 Dave is still resident in the UK and so will be treated as deemed domiciled in the UK by virtue of his place of birth and domicile of origin. He is not eligible for trust protections given his status. It is assumed for the purpose of this example that the conditions for the application of the transfer of assets legislation are met. Dave is in receipt of benefits i.e. the use of the house, however, he will not be taxed on the benefits arising because he is treated as deemed domicile by virtue of being born in the UK with a domicile of origin consequently S720 ITA will continue to apply and he will be assessable on the trust income arising in 2017/18 of £100,000.

Example

Simon has been living in the UK for 21 years. He is not domiciled in the UK. In 2014 Simon settled a non-resident discretionary trust of which he was a beneficiary with a substantial sum of capital that he inherited from a distant relative. The trustees purchased a property in London for Simon to live in and they invested the remainder of the funds in overseas investments. Simon is a remittance basis user and the trustees have not remitted any of the income arising in the trust to the UK, so no income tax liability arises on Simon in respect of the trust income. It is assumed for the purposes of this example that the conditions for the application of the transfer of assets legislation are met and the settlements legislation is ignored.

In 2017/18 Simon will be treated as deemed domiciled in the UK because he has been resident in the UK for the last 21 years. As a consequence of this Simon will from 2017/18 be assessable under S731 ITA 07 on the value of the benefit provided to him by the trustees (the use of the London property) to the extent that there is sufficient relevant income within the trust to match against the value of the benefit provided.

3.29 If an individual receives a benefit under S732 ITA 07 the amount of income to be subject to tax is calculated using the six steps as set out in S733(1) ITA 07. The steps are as follows:

- Step 1 – the total benefits: identify the amount or value of such benefits received by the individual in the tax year and in any earlier tax year in which the benefits charge could or has applied. The benefits of an earlier year to be taken into account are those of a tax year in which there has previously been a benefits charge or in which there would have been a benefits charge, but for an insufficiency of relevant income to match against the benefits

received. It should be noted that benefits provided to a transferor before 6 April 2017 will not be included in the calculating the transferors benefits for earlier years.

- Step 2 – the total untaxed benefits: deduct from the total benefits the total amount of income treated as arising to the individual under the benefits charge in any earlier tax years, as a result of the relevant transfer or associated operations.
- Step 3 – the relevant income of the tax year: identify the amount of income which arises in the tax year to a person abroad, and as a result of the relevant transfer or associated operations can be used directly or indirectly for providing a benefit for the individual.
- Step 4 – total relevant income: add together the relevant income of the tax year and the relevant income of earlier tax years in relation to the individual.
- Step 5- the available relevant income: from the total relevant income deduct the amount deducted at Step 2 and any other amount which may not be taken into account because of the no duplication of charges provisions at S743 ITA 07.
- Step 6 – the income treated as arising: compare the total untaxed benefits (Step 2) and the available relevant income (Step 5). The amount of income treated as arising for the purpose of the benefits charge for any tax year is the total untaxed benefits or the available relevant income whichever is the lower.

Example

Gary has been resident in the UK for 18 years, but he is not domiciled in the UK. In 2010 Gary settled £5 million into a non-resident trust from which he is able to benefit. The trustees invest £4 million in overseas investments and purchase a holiday home in Spain for £1 million which is made available to Gary all year round. Each year the trustee's income is £40,000.

It is assumed that the transfer of assets legislation applies so Gary will be liable to tax under S720 ITA on the income arising in the trust, but as Gary is a remittance basis user and the trustees retain the income overseas Gary has no liability. In 2017/18 Gary will be treated as deemed domiciled in the UK because he is a long term resident. The income arising in the trust is protected foreign income so will not be assessable on Gary under S720 ITA 07. However, Gary will be assessable under S731 on any benefits that he receives during 2017/18.

Gary has the use of the holiday home in Spain and the estimated value of the benefit is £50,000 per year. Gary's assessable income for the year 2017/18 will be calculated as follows:
Total benefits = £50,000
Total untaxed benefits =£50,000
(It should be noted that benefits arising before 6 April 2017 are not included in the calculation as before this date Gary was not within the scope of S731 (see s733(1) step 1)
Relevant income of the year = £40,000
Total relevant income (£40,000 x 8) = £320,000
(In calculating the total relevant income the income arising in the years prior to 6 April 2017 is taken into account)
Available relevant income = £320,000
The income treated as arising in 2017/18 will be £50,000.

Assuming that the benefit is also provided in 2018/19 and Gary also receives a capital distribution from the trust of £100,000 the assessable income will be calculated as follows:
Total benefits (£150,000 + £50,000) = £200,000
Total untaxed benefits (£200,000 - £50,000) = £150,000

Relevant income of the year = £40,000
Total relevant income (£40,000 x 9) = £360,000
Available income (£360,000 - £50,000) = £310,000
The income treated as arising in 2018/19 will be £150,000 with unmatched relevant income available of £160,000.

3.30 Finance (No2) Act 2017 makes amendments to the step calculation with Step 2 being amended so that for earlier years in which the individual was not resident in the UK the amount to be deducted is restricted to amounts which are taxed on another individual because of the working of S733A ITA 07. The application of S733A ITA 07 is covered in paragraphs 3.31 to 3.36 below.

Example

Louise has been living in the UK for 17 years, but she is not domiciled in the UK. In 2013 she settled a non-resident trust for the benefit of herself and her husband Nigel. Nigel is not resident in the UK. The trustees of the settlement purchase a property in Monaco for Nigel to live in. From 2017/18 Louise is treated as being deemed domiciled in the UK. As the settlor of the trust Louise will be assessable to tax on any benefits that she receives from the trust that she settled. She will also be assessable on any benefits that Nigel who is non-resident receives in 2017/18 in respect of the use of the Monaco property (Nigel is a close family member and will not be liable as he is non-resident). If Nigel becomes resident in the UK in 2018/19 the benefit of the use of the property will be assessable on him (Nigel is UK domiciled). As Louise was assessable on the benefit in 2017/18 by virtue of S733A ITA 07 (see paragraphs 3.32 to 3.37 below) the amount deducted in Step 2 as set out above will include the value of the benefits assessable on Louise in 2017/18.

3.31 The Finance (No2) Act2017 introduces an additional charge on the settlor in respect of benefits that are provided to a closely related beneficiary of the settlor who is not resident in the UK in the year that the benefit is received or where the close family member is a UK resident remittance basis user and the benefit is not remitted to the UK (or only partly remitted to the UK). In this situation the effect of the charge is to assess the settlor to the proportion of the benefit received by the beneficiary that is not taxed on the beneficiary in the UK. The legislation can be found at S733A ITA 07.

3.32 The charge will apply if the following conditions are met:

- The settlor must be resident in the UK at some time in the tax year.
- The settlor is not domiciled in the UK at any time in the tax year.
- The settlor is not regarded as deemed domicile in the United Kingdom at any time in the tax year because he was born in the UK and had a domicile of origin in the UK.
- At no time in the tax year were the trustees of the settlement resident in the UK.
- An amount of income is treated as arising to an individual under S732 ITA 07 in a tax year.

- Under S735A ITA 07 (if it applied for this purpose) the amount would be matched with an amount of relevant income that is protected foreign income for the purposes of rule 2 S721(3B) or S728(1A) ITA 07 and with a benefit received by the individual at a time when the individual was a close member of the family of the settlor of the settlement concerned. Details of who constitutes a close family member is contained in paragraph 3.34 below.

3.33 For the charge to apply the individual receiving the benefit must not be resident in the UK at any time in the tax year concerned or the remittance basis applies to the individual for the year and none (or only part) of the income treated as arising under S732 ITA 07 is remitted to the UK in the year then the settlor is liable for the tax charge under S731 ITA 07 on that income as if the amount was the income of the settlor in that year. The individual who receives the benefit is not liable in any later year for income tax on the amount. If the remittance basis applies to the individual and part of the income that would be treated as income arising under S732 ITA 07 is remitted to the UK in the year the settlor will be liable to tax under S731 ITA 07 on the remainder as if it were income arising to the individual. Once again the individual who receives the benefit is not liable to tax on the income in a later tax year. The amount of income on which the settlor will be assessable under S732 ITA 07 may be the whole, or part only, of the amount treated as arising to the individual. When the remittance basis rules apply in relation to the remittance of income by the close family member receiving the benefit, for the purposes of this section S735 ITA 07 will need to be read as applying.

3.34 For the purposes of assessing a benefit provided to a close member of the settlor's family on the settlor a close member of the family of the settlor is defined at S733A(7) ITA 07 as the settlor's spouse or civil partner or a minor child of the settlor, or a minor child of the spouse or civil partner of the settlor. If two people are living together as if they were spouses of each other for the purposes of the legislation they will be treated as if they were spouses. Likewise if two people of the same sex are living together as if they were civil partners then the will be treated as if they were civil partners of each other.

3.35 It should also be noted that the settlor is entitled to recover any tax paid as a result of a benefit provided to a close member of the family of the settlor from the individual who receives the benefit.

Example

Sue has been resident in the UK for 18 years, but she is not domiciled in the UK. Sue is married to Sam who is both resident and domiciled in the UK. During the year 2017/18 Sam is treated as non-resident in the UK as he is working abroad full-time.

In 2014/15 Sue settles a non-resident trust for the benefit of herself and her husband. It is assumed that the transfer of assets legislation applies to the arrangements for the purpose of the example. The trustees receive overseas income and make a number of wholly capital distributions as follow:

	Benefits		Income
	Sam	Sue	
2014/15	10,000		50,000
2015/16	20,000		40,000

2016/17	0		40,000
2017/18	10,000	50,000	50,000
2018/19	40,000		60,000

The benefits chargeable in 2017/18 and 2018/19 for Sue and Sam will be as follows:

Sue
2017/18
Total taxable benefits received in year (£50,000 +£10,000) = £60,000
Total relevant income = £180,000
Available relevant income (£180,000 - £30,000) = £150,000
Amount of income treated as arising will be the lesser of £60,000 and £150,000 so the amount assessable will be £60,000.

Sam
2017/18
As Sam is not resident in the UK in the tax year he will have no liability, but as he is a close member of the settlor's family Sue will be assessable on the benefit provided to him in the year (see calculation for Sue above). It should also be noted that as Sue has paid tax on a benefit received by Sam she will have the right to recover the tax paid on the £10,000 benefit received by Sam.

2018/19
Total taxable benefits = £100,000
Total untaxed benefits (£100,000 - £60,000) = £40,000
(note that the amendments to Step 2
mean that the £10,000 assessable on
Sue in 2017/18 is deducted)
Relevant income of the tax year = £60,000
Total relevant income = £240,000
Available relevant income (£240,000 - £30,000 - £60,000) = £150,000
The amount of income treated as arising will be the lesser of £40,000 and £150,000, so the amount assessable will be £40,000.

3.36 S735A ITA 07 is expanded by Finance (No2) Act 2017 so that it can apply in situations where a charge arises under S733A ITA 07. An additional section is added S735B ITA 07 such that in relation to income, if:

(a) the income is treated by S732 ITA as arising to a beneficiary in a tax year and

(b) the settlor is liable to tax on the income under S733A ITA 07 (because the beneficiary is a close member of the settlor's family) and

(c) the remittance basis applies to the settlor for the year in question.

The income will be treated as relevant foreign income of the settlor. This is referred to as "transferred-liability deemed income". When considering the application of S735 ITA as it applies to the beneficiary any benefit or relevant income relating to any part of the transferred-liability deemed income for the purposes of the remittance basis as it applies in relation to the

settlor the benefit or relevant income is treated as deriving from that part of the transferred-liability deemed income.

Example

Julian is not domiciled in the UK, but has been resident in the UK for many years. At the end of 2016/17 he settles a non-resident trust in which he and his wife, Amanda, are both beneficiaries. Amanda his wife has been resident in the UK for the last 3 years, but she is not domiciled in the UK. During the years 2017/18 and 2018/19 the following income and capital distributions arise.

Year	Date arises	Foreign income	Benefits to Julian	Benefits to Amanda	Remitted to the UK
2017/18	30 April	10,000			
2017/18	31 May			4,000	2,000
2017/18	31 Dec		5,000		
2017/18	31 Jan	5,000			
2018/19	30 April	10,000			
2018/19	30 June			3,000	
2018/19	30 Nov			10,000	2,000
2018/19	31 Jan	5,000			

As Julian established the trust before he became deemed domiciled the trust protections will apply to the arrangements. For the purpose of the example we will assume that the transfer of assets legislation applies to the arrangements. As all of the income arising within the structure is foreign source income both Julian and Amanda will be assessable under S731 ITA 07 on the benefits that they have received.
The amounts treated as being assessable on Julian and Amanda for the years 2017/18 and 2018/19 will be as follows:

2017/18
Amanda
The benefit of £4,000 will be matched with the foreign income of £10,000 received by the trust in April 2017. Amanda is a remittance basis user and so will be assessable on the £2,000 that she has remitted to the UK.

Julian
Julian has received a benefit of £5,000 and this will be matched with the foreign trust income of £10,000 received in April 2017. Amanda is a close member of the settlor's family and as she is a remittance basis user S733A ITA will apply to any benefit that she has received that has not been remitted to the UK. In this instance £2,000 of the benefit she received has not been remitted to the UK so Julian will be assessable on this as well as on the benefit that he received during the year. Julian will have the right to claim re-imbursement from Amanda in respect of the tax he has paid on the £2,000 of Amanda's benefit.

There is unmatched income during the year of £1,000 of the amount received in April 2017 and the £5,000 received in January 2018.

2018/19

Amanda
The benefit received by Amanda in June 2018 of £3,000 will be matched against the balance of the £1,000 of trust income received on 30 April 2017 and £2,000 of the trust income received in January 2018.

The benefit received by Amanda on 30 November 2018 of £10,000 will be matched with £3,000 of the trust income received in January 2018 and £7,000 of the trust income received April 2018. Amanda will only be assessable on £2,000 of the benefit received as this is the only amount that she has remitted to the UK during the year.

Julian
Julian has not received any benefits during 2018/19 on which he will be assessable. However, as Amanda is a remittance basis user and close member of Julian's family Julian will be assessable under S733A ITA 07 on any benefits that Amanda receives that are not remitted to the UK. It can be seen that Amanda received a benefit of £3,000 that has not been remitted to the UK in June 2018 and a further benefit in November 2018 of which £8,000 has not been remitted to the UK. As a result Julian will be assessable on £11,000 of the benefits received by Amanda during 2018/19. Julian will have a right to claim re-imbursement of any tax paid from Amanda.

4 Capital Gains Tax Legislation Trust Protections

On becoming deemed domiciled under either condition A or B of section 835BA ITA 2007 a non-domiciled individual is prima facie brought within the scope of section 86 TCGA 1992. However section 86 TCGA 1992 will not apply to the gains of a protected trust structure which remains untainted. As discussed in section 3 a trust structure can only be protected where condition A does not apply. An individual who is UK resident, born in the UK and has a UK domicile of origin will always be subject to tax under the offshore settlement capital gains tax legislation under the TCGA 1992 s 86 settlor's charge (meaning he or she will be taxed on the net trust gains for a tax year on the arising basis). Where just condition B applies and the trust is untainted the long term deemed domiciliary will continue to be taxed as a non-domiciliary being subject to the TCGA 1992, s 87 capital payments charge provisions. The long term deemed domiciliary will also continue to benefit from the Finance Act 2008 transitional provisions with respect to trusts.

5 How a protected settlement can be tainted

5.1 In sections 2, 3 and 4 above reference has been made to the situation where a trust that comes within the various protections set out in the relevant sections can be tainted. In broad terms the effect of tainting a protected settlement, from the perspective of a long-term resident deemed domicile, is to bring the trust and its underlying entities back into the scope of S86 TCGA 92, S624, S629 and S633 ITTOIA 05 and S720 or S727 ITA 07 such that the income and gains arising within the settlement will be assessable on the deemed domiciled settlor as they arise. This section looks at how a protected settlement can be tainted. It should be noted that the aim of this section is to provide some general guidance on when tainting may occur and

examples are used to illustrate this, however, it has not been possible to include herein examples that cover all eventualities and it is intended that more detailed technical guidance, including further examples, will follow in due course.

5.2 The tainting provisions can be found at Sch 5 para 5A and para 5B TCGA 92, S628A and S628B ITTOIA 05 and S721A, S721B and S729A ITA 07 for the capital gains tax provisions, settlements legislation and transfer of assets legislation respectively. However, what constitutes the tainting of a protected settlement is the same in each of the respective pieces of legislation. The basic proposition is that no property or income can be provided either directly or indirectly to the settlement by the settlor, or by the trustees of another settlement of which the settlor is the settlor or a beneficiary, at a time in the relevant period when the settlor is domiciled or deemed domiciled in the UK. The relevant period is defined as a period, which begins with 6 April 2017 or, if later, the creation of the settlement. The relevant period ends with the ending of the tax year under consideration. When considering the tainting provisions it is also important to consider whether any property has been provided directly or indirectly by the settlor, or by the trustees of another settlement of which the settlor is the settlor or a beneficiary, to any underlying entities owned by the settlement at any time during the relevant period.

The provision of goods or services by the settlor to the trustees could constitute the provision of property for the purposes of the settlement.

For the purposes above, the addition of value to settlement property is treated as the direct provision of property for the purposes of the settlement.

5.3 A settlor's failure to exercise a right of recovery in relation to settlement property could cause the tainting of the settlement. HMRC's long-established practice, set out in paragraph 24 of SP5/92, will apply for the purposes of the trusts protections. A failure to exercise a power of recovery will be regarded as tainting the settlement unless a genuine attempt to enforce the right has proved unsuccessful.

5.4 Normal exchange rate fluctuations in respect of loans that would not in themselves taint a trust should not cause the tainting of a settlement. However, arrangements involving the use of appreciating or depreciating currency balances or payments designed to add value could well result in income arising under a settlement ceasing to be protected foreign-source income.

Example

Raphael is domiciled under common law in British Columbia, where he was born and has his domicile of origin. He is the settlor of the Raphael 2007 Discretionary Trust. He is also a beneficiary of the trust. The settlement was made in March 2007 and the trustees are resident in the British Virgin Islands. The trust receives income that would be relevant foreign income if received by an individual resident in the UK. Raphael has been resident in the UK since July 2010. Raphael becomes deemed domiciled in the UK by virtue of his long-term residence in the UK with effect from 6 April 2025.

Raphael holds an option to purchase a majority of the shares in a Canadian company, which are currently owned by the trustees of the Raphael 2007 Discretionary Trust, at a substantial discount to their present value. In June 2027 Raphael releases the option. At that time the exercise of the option would have allowed Raphael to acquire the shares at substantially below their market value. By forgoing the exercise of the option Raphael has increased the value of the shareholding of the settlement. Conditions A to E are met, but it is necessary to determine whether or not the provision of property in June 2027 is to be ignored for the purposes of condition F. The release of the option by Raphael plainly does not fall within categories (c) to (g). It is not a transaction entered into on arm's length terms and Raphael does not offer any evidence that he had no intention to confer a gratuitous benefit on any other person. Neither category (a) nor category (b) allows the release to be ignored. Condition F is not met and the settlement is 'tainted'.

5.5 The legislation provides seven categories of property, income or transactions that are to be ignored when considering whether property or income has been added to the settlement. For convenience, the seven categories have been labelled (a) to (g) below, in accordance with their lettering in the relevant sections in TCGA 92, ITTOIA 05 and ITA 07.

It is important to appreciate that tainting will not occur where someone other than the settlor, someone at his or her direction, or the trustees of another settlement of which the settlor is a settlor or beneficiary adds property to the settlement. Where a third party adds property this might constitute a separate settlement and carry with it its own consequences, but it would not taint the settlement made by the original settlor. Similarly, although reference is made in the following example to additions being made to trusts, it is considered that the same consequences will arise where additions are made to companies owned by the non-resident trustees. The tainting rules are not avoided by making additions to such underlying companies rather than to the trusts that own them.

Category (a)

Property or income provided under a transaction, other than a loan, entered into on arm's length terms is to be ignored.

Example

In January 2021 Maria sells a sculpture to the trustees of the Maria 2019 Discretionary Settlement at a price that accords with professional valuations of the asset at that time. The valuations were obtained independently by Maria and the trustees. Maria is deemed domiciled for 2020-21 and has provided property directly for the purposes of the settlement. This property can be ignored, as it was provided under a transaction entered into on arm's length terms. The sale and purchase of the sculpture does not taint the Maria 2019 Discretionary Settlement.

Category (b)

Property or income provided otherwise than under a loan without any intention by the person providing it to confer a gratuitous benefit on any person is to be ignored.

Example

Maria buys an apartment in San Sebastián/Donostia from the trustees of the Maria 2019 Discretionary Settlement. She makes the purchase in November 2021, for an agreed price of €1,500,000. She does not have any intention of providing a gratuitous benefit to the trustees in doing so, as she believes, having taken appropriate measures, the price to be the open market value. Maria and the trustees actively negotiate the price, and the transaction is entered into on arm's length terms. Subsequent enquiries establish that the value was probably closer to €1,400,000 in November 2021. Although Maria has provided property otherwise than under a loan to the trustee, she had no intention of conferring a gratuitous benefit through her actions. She merely made a slightly disadvantageous bargain, from her financial perspective, in agreeing the price of the apartment with the trustee. The difference between €1,500,000 and the open market value of the apartment in November 2021 does not taint the Maria 2019 Discretionary Settlement.

Category (c)

The principal of a loan which is made to the trustees of a settlement on arm's length terms is to be ignored, but see paragraph 5.4 for an exception. For this purpose a loan is on arm's length terms only if interest at the official rate or more is payable at least annually under the loan.

Example

In February 2020 Maria lends the trustees of the Maria 2019 Discretionary Settlement €250,000, repayable in quarterly instalments over ten years. The loan carries interest at 3% per annum, payable quarterly in arrears. The capital and interest are repaid in accordance with the terms of the loan. The loan principal can be ignored and does not taint the settlement, as the loan is made on arm's length terms, for these purposes, by Maria, the interest rate being the official rate in February 2020 and the interest being payable at least annually.

In 2022-23 the official rate rises, but a change in the official rate of interest does not mean that the trust will become tainted.

Category (d)

The payment of interest to the trustees of a settlement under a loan made by them on arm's length terms is to be ignored. For this purpose a loan is on arm's length terms only if any interest payable under the loan is at no more than the official rate.

Example

In May 2020 the trustees of the Maria 2019 Discretionary Settlement lend Maria US$20,000. The loan carries interest at 3.0% per annum, payable six-monthly. This is no more than the official rate in May 2020 and so the payment of the loan interest can be ignored, as the loan is made on arm's length terms, for these purposes, by the trustees. It does not taint the settlement.

In April 2021 the official rate falls to 2.5%. There is no need for the interest rate on the loan to be reduced (unless a relevant event occurs) because the loan was entered into on terms which were arm's length at that time.

Category (e)

Repayment to the trustees of a settlement of the principal of a loan made by them.

Example

In December 2020 Maria repays the loan principal of US$20,000 to the trustees, along with the principal of three earlier loans totalling US$75,000. All these repayments can be ignored and do not taint the settlement.

Category (f)

Property or income provided in pursuance of a liability incurred by any person before 6 April 2017 is to be ignored.

Example

John has been resident in the UK since 2001-02. He has a domicile of origin in Australia, and has not acquired a domicile of choice in the UK. He will, however, be deemed domiciled in the UK from 6 April 2017 due to his long-term residence here. John settled the John 2009 Family Discretionary Trust, which has Jersey resident trustees, in 2009 with £1,000,000. The trustees have invested the funds in long-term overseas investments which cannot readily be accessed.

In December 2016 the trustees are asked to purchase a residential property for the use of John's adult son, Adam, who is a beneficiary of the trust. The trustees do not have the funds available to provide the cash and so John agrees to settle a further £200,000 into the trust to assist with the purchase. John agrees to provide these funds on the date of completion. The trustees enter into a conditional contract to purchase the property in March 2017, but the conditions for the purchase are complied with only in May 2017. Consequently John provides the £200,000 to complete the purchase in that month. As John had already committed to provide the £200,000 before 6 April 2017 the trust would not be tainted by John's action.

Category (g)

Where a settlement's expenses relating to taxation, both UK and overseas and administration for a tax year exceed its income for that year, property or income provided towards meeting that excess is to be ignored provided that the value of such property or income is not greater than the larger of the excess or the amount by which the relevant expenses exceed the amount of the expenses which may be paid out of the settlement's income under the terms of the trust deed. Only the settlement's expenses, and not those of any underlying companies, are to be taken into account for these purposes.

Example

The taxation and administration expenses of the Maria 2009 Discretionary Trust for the 2017-18 tax year are €35,000. Its income is €30,000. The amount of the relevant expenses that may be paid out of the settlement's income is €25,000, the balance of the expenses being capital. Maria gives the trustees €10,000 to meet the expenses. The excess of the income over the expenses is €5,000. The amount given by Maria exceeds this, but it does not exceed the difference of €10,000 between the expenses and the amount of such expenses that may be paid out of the settlement's income. The gift can therefore be ignored and will not taint the settlement.

Where the valuation of benefit rules in section 6 apply and the reimbursement to the trustees is at the level of the benefit that would otherwise arise, this will not be regarded as tainting the trust. An exception would be where acquisition costs have been intentionally inflated over the current value of the property.

For example, the settlor has the use of an asset which the new benefit valuation rules require her to pay £15,750 per annum so as not to have a benefit. And on the other hand the commercial rental value of said asset is £14,000. This would prima facie constitute tainting. HMRC however will not enforce the law in this scenario if the settlor pays the £15,750. However, if there is evidence that trustees are themselves renting assets from a third party for £14,000 so they can rent them to the settlor for £15,750 so as to add property to the trust, HMRC will treat this as a tainting event.

A failure by a settlor to reclaim tax from the trustees could taint a trust, but provided that the settlor claims reimbursement within a reasonable time the trust will not be regarded by HMRC as tainted.

5.6 There are a number of exceptions to the situations in which property, income or transactions can be ignored when considering whether property or income have been added to a settlement by the settlor or the trustees of a settlement connected with the settlor for the purpose of tainting. The first exception is where the following occurs-

(a) a loan is made to the trustees of the settlement by the settlor or the trustees of a settlement connected with the settlor, and

(b) the loan is on arm's length terms, but

(c) a relevant event occurs.

A connected settlement for the purpose of this paragraph is one where the individual is either the settlor or a beneficiary.

In such circumstances the principal of the loan cannot be ignored after the relevant event has occurred and it is to be regarded as having been provided for the purpose of the settlement at the time of the relevant event.

A relevant event occurs in the following situations.

- Capitalisation of interest payable under a loan.
- Any other failure to pay interest in accordance with the terms of the loan.
- Variation of the terms of a loan such that they cease to be arm's length terms.

In respect of bullet point two above HMRC will not seek to apply the tainting provisions for a minor failure to pay interest on time i.e. as per the first example below where the payment was ten days late.

Example

Maria remains in the UK, and the facts are the same as those in paragraph 5.3. In May 2021 the trustees pay the quarterly interest due on the loan ten days late, due to an administrative oversight. This would not be regarded as a failure to pay interest in accordance with the terms of the loan. The settlement would not be tainted and the foreign-source income would remain protected.

Example

Maria remains in the UK, and the facts are the same as those in paragraph 5.3. From February 2022 the trustees do not pay the quarterly interest due on the loan on time. Payments are made between a week and several months late. This would be regarded as a failure to pay interest in accordance with the terms of the loan. The settlement would be tainted and the foreign-source income would cease to be protected with effect from February 2022.

Example

Maria remains in the UK, and the facts are the same as those in paragraph 5.3. The trustees initially pay the interest in accordance with the terms of the loan but in June 2023 they request that the interest is made payable annually with immediate effect. Maria accedes to the request and the terms of the loan are varied accordingly. It is necessary to consider whether there has been a relevant event. There has been no capitalisation of the interest payable and no failure to pay it in accordance with the terms of the loan, but there has been a variation in the terms of the loan. Have the terms ceased to be on arm's length? The interest rate of the loan has not changed at June 2023 and the interest is payable annually. The official rate of interest rose to 3.25% from April 2022. This did not cause the tainting of the trust at that time, but the loan as varied carries interest at below the official rate from June 2023. The principal of the loan is therefore treated as having been provided to the trustees in June 2023. The settlement is tainted and condition F is no longer met. The foreign-source income ceases to be protected.

5.7 The second of the exceptions to the situations in which property, income or transactions can be ignored for the purposes of considering whether property or income has been added to the settlement can apply only where a settlor becomes deemed domiciled in the UK on or after 6 April 2017. Where a settlor does become so deemed domiciled, the time at which this happens is for these purposes called the 'deemed domicile date'. The exception applies, subject to the matters set out below, where:

- a loan has been made to the trustees of a settlement by the settlor or the trustees of a settlement connected with the settlor,
- that loan was made before the deemed domicile date,
- the loan was not entered into on arm's length terms, and
- any amount outstanding under the loan on the deemed domicile date, called the 'outstanding amount', is payable or repayable on demand on or after that date.

In these circumstances the property will be regarded as property directly provided by the lender on the deemed domiciled date for the purpose of the settlement. If, however, the deemed domiciled date is 6 April 2017 then there is are transitional provisions and the loan will not be considered to be property directly provided for the purpose of the settlement if:

(a) the principal of the loan is repaid, and all interest under the loan is paid, before 6 April 2018, or

(b) the loan becomes a loan on arm's length terms before 6 April 2018 and before that date interest is paid to the lender in respect of the period from 6 April 2017 to 5 April 2018 as if the arm's length terms had applied for that period, and interest continues to be payable thereafter in accordance with the terms.

Example – general rule (transitional provision does not apply)

Tracy was born in Massachusetts, although her domicile of origin is the UK. During her childhood her family emigrated to Western Australia, where she has lived for many years. Tracy is married to an Australian citizen with whom she has three children. It is accepted that Tracy acquired a domicile of choice in Western Australia in early adulthood.

In March 2002 Tracy settled on the Hong Kong corporate trustee of the Tracy Children's Settlement two investment properties located in Thailand, an investment portfolio of Australasian and Far Eastern listed shares, and a substantial amount of cash held on deposit in Hong Kong. Tracy retained an interest in the settlement.

The trustees of the Grace 1983 Discretionary Settlement, of which Tracy is a beneficiary, lend A$1,000,000 to the trustees of the Tracy Children's Settlement in October 2008. The loan is interest-free and repayable on demand.

In early 2013 Tracy's husband is offered a senior role at an investment bank based in London. The family move to the UK in March 2013, expecting to be here for about five years. During 2017 Tracy's husband leaves his job in order to start a business with two former colleagues. The business becomes very successful and the family remains in the UK beyond 2018.

Tracy does not become deemed domiciled in the UK for 2017-18, as she was born outside the UK. She does, however, become deemed domiciled here in 2028-29, having been resident in the UK for the tax year 2013-14 onwards. Tracy's deemed domicile date is 6 April 2028, as she is resident in the UK for 2028-29 and has been resident here for 15 of the previous 20 tax years.

The trustees of the Tracy Children's Settlement have repaid to the trustees of the Grace 1983 Discretionary Settlement A$50,000 of the loan principal on each anniversary of the loan being made. At 6 April 2028 there is A$50,000 of the loan outstanding, this balance being repayable on

demand. The A$50,000 is an outstanding amount that is regarded as property directly provided for the purposes of the settlement on the deemed domicile date. The Tracy Children's Settlement is tainted for the tax year 2028-29. The income that was previously protected foreign-source income ceases to be so with effect from 6 April 2028.

If the balance of the loan had been cleared before 6 April 2028 the Tracy Children's Settlement would not have been tainted and, although Tracy would have been deemed domiciled in the UK, the income arising under the settlement would have remained protected foreign-source income.

Alternatively, the terms of the loan could have been varied before Tracy's deemed domicile date of 6 April 2028 so that all future interest would be payable at least annually at the official rate or more.

Example of the transitional provision

Charles was born in Belgium, where he grew up. His domicile of origin is Belgium, and he has never acquired a domicile of choice elsewhere, although he has lived in a number of countries, sometimes for lengthy periods.

In September 1987 Charles settled on the Guernsey corporate trustee of the Charles Property Trust a range of income-generating assets located outside the UK. Charles retains an interest in the settlement.

Charles loaned €1,000,000 to the trustees of the Charles Property Trust in November 2001. The loan is interest-free and repayable on demand, but no repayments have been made.

In early 2002 Charles moved to the UK. Since then he has lived in London, but he does not intend to remain in the UK permanently or indefinitely. He is actively considering leaving in 2019 or 2020.

Charles becomes deemed domiciled in the UK for 2017-18 because he is resident in the UK for the year and has been resident here for 15 out of the previous 20 years. Charles's deemed domicile date is therefore 6 April 2017.

The general rule, see the example above, will not apply if the trustees of the Charles Property Trust repay the €1,000,000 before 6 April 2018. The trustees are not in a position to do so, but there is another course of action open to the parties under which the general rule will not apply. The terms of the loan are renegotiated and the trustees agree to pay interest at the official rate, on an annual basis, with effect from 6 April 2017. The trustees pay €25,000 interest to Charles on 31 March 2018 and continue to do so annually thereafter while Charles remains resident in the UK. The settlement is not 'tainted'. The foreign-source income will continue to be protected in such circumstances, provided all the other conditions are met.

5.8 Where a fixed-term loan whose provisions cannot be varied was not entered into on arm's length terms and was made by the settlor to the trustees of the settlement before the deemed

domicile date of the settlor, the rules will work as follows. The continuation of the loan after the deemed domicile date and up to the expiry of the fixed term will not taint the settlement. If the settlor fails to enforce repayment of the loan at that point, the settlement will become tainted, unless the parties immediately enter into a new loan of the unpaid balance, including any capitalised interest, on arm's length terms.

Example

Joao was born in Portugal, which is his domicile of origin. He lived there until June 2009, when he came to live in the UK. He does not intend to remain in the UK permanently or indefinitely, but he has been resident here since tax year 2009-10.

In October 2014 Joao settled a portfolio of cash and investments situated outside the UK on the trustees of the Joao 2014 Discretionary Settlement. The trustees are resident in Jersey.

Joao made a €500,000 interest-free loan to the trustees in January 2015. This has a fixed repayment date in January 2025, which cannot be varied.

Joao remains resident in the UK and his deemed domicile date is 6 April 2024. Provided that Joao enforces the repayment of the loan in January 2025, the settlement will not be tainted by the existence of the loan during the tax year 2024-25. If Joao fails to enforce repayment of the loan the settlement will become tainted. Joao and the trustees could, however, agree that from January 2025 Joao will lend the €500,000 to the trustees at the official rate of interest plus half a per cent, payable quarterly. This would not result in the tainting of the settlement provided the interest payments are made.

5.9 In relation to what would constitute the addition of value or property to the settlement or any underlying entity the failure of a settlor to exercise a power of revocation in respect of the settlement will not be considered as an addition of value and therefore will not taint the trust. It should also be noted that if the settlement is a life interest trust with underlying companies there is no requirement for the profits of those underlying companies to pay dividends up to the trustees of the settlement. The retention of such profits in the underlying companies will not be considered as an addition of value for the purposes of the tainting rules.

6. The valuation of benefits

6.1 When calculating a benefits charge that arises under either S87 TCGA 92 or S731 ITA 07 the legislation has been silent on how the provision of a benefit should be valued for the purpose of the calculation. With the expansion of these benefits charges due to the changes outlined in sections 2 to 4 above it was thought that a more formal approach was needed to set out how benefits caught under these sections should be calculated. Consequently Schedule 14 of Finance (No2) Act 2017 introduces sections 97A to 97C TCGA 92 to value benefits assessable under S87 TCGA 92 and sections 742B to 742E ITA 07 for benefits arising under the transfer of assets provisions (this feeds into the benefits charge for both the settlor and where a close family member benefit is attributed to the settlor). The calculations of the value of the benefit under the above provisions is the same so what follows in the remainder of this section applies equally to both. It should also be noted that the calculation of the valuation of a benefit also applies for the purposes of calculating a benefit whose value is treated as income of the settlor or a close family member under S97 TCGA 92 and the new settlements legislation benefits charge.

6.2 The Finance (No2) Act 2017 introduces rules for calculating the value of a benefit provided in relation to the following:

- A payment by way of a loan
- The making available of movable property without any transfer of the ownership of the property
- The making available of land without any transfer of the ownership of the land concerned.

This section looks at each of the above benefits and how they are valued in turn.

6.3 For the provision of loans the legislation can be found as S97A TCGA 92 and S742C ITA 07. The value of the benefit conferred on a person by way of a loan is for each tax year in which the loan is outstanding the amount (if any) by which the amount of interest that would have been payable in that year on the loan if interest had been payable on the loan at the official rate, exceeds the amount of interest (if any) actually paid by the person in that year on the loan. The official rate of interest is the rate applicable from time to time under S178 FA 1989. It should be noted that any interest due under the loan must be paid in the year in order for it to be deducted from the amount of interest due under the official rate, if the interest is deferred or added to the capital of the loan it will not be treated as having been paid and no deduction from the interest due at the official rate will be available.

Example
Racheal is the beneficiary of a non-resident discretionary trust. She receives an interest free loan from the trustees on 6 April 2018 of £100,000. The loan is interest free and repayable on demand.
Assuming that the official rate of interest applying during 2018/19 is 2.5% (and that this does not increase in 2019/20 and 2020/21) the value of the benefit that she received during 2018/19 will be £2,500.

If on 6 April 2019 the trustees agree to amend the terms of the loan such that Racheal pays interest at 2% per annum going forward the value of the benefit that she received in 2019/20 will be (£2,500 - £2000) £500 provided that Racheal pays the interest during the year

If on 6 April 2020 the trustees increase the rate of interest that they charge on the loan to 3% the value of the benefit received by Racheal will be (£2,500 - £3,000) Nil, as assuming that she pays the interest the interest paid exceeds the official rate.

6.4 The value of a benefit provided by making movable property available to an individual is covered by S97B TCGA 92 and S742D ITA 07. For this purpose moveable property means any tangible movable property. The value of the benefit provided in these circumstances where there is no transfer of the property is calculated using the following formula:

((CC x R x D) / Y) – T

Where –

CC is the capital cost of the moveable property on the date when the property is first made available to the individual in the tax year,

D is the number of days in the tax year on which the property is made available to the individual (the relevant period)

R is the official rate of interest for the relevant period (but see below for the calculation if there is a change in the official rate during a tax year

Y is the number of days in the year

T is the total of the amounts (if any) paid in the tax year by the individual to the person providing the benefit, in respect of the availability of the property, or in respect of the repair, insurance, maintenance or storage of the property.

6.5 When considering if something is made available this should be interpreted widely. It does not matter if the beneficiary chooses not to use the moveable property. However in cases where moveable property is made available to more than one person at the same time then apportionment of the benefit can be made by reference to use.

Examples

1. Trustees make available a work of art to a beneficiary. The beneficiary holds the art for 300 days in the year and then loans the art to a friend for the remaining 65 days of the year.
   The onward loan is a decision of the beneficiary so the work of art would be regarded as made available to the beneficiary for the 365 days in the year.

2. Trustees make a yacht available to a beneficiary throughout a year. The yacht is only used by the beneficiary for two weeks in the year. Although only used for two weeks it is available for the full year and the benefit is calculated on this basis.

3. A yacht is made available to two beneficiaries throughout the course of the year. A uses it for 3 weeks and B for 2.
   The full years benefit would be apportioned 3/5 for A and 2/5 for B.

6.6 When considering the capital cost of the moveable property this means the amount equal to the greater of the total of the amount or value of the consideration given for the acquisition of the property by the person providing the benefit and its market value at the time of acquisition. If since the acquisition there has been enhancement expenditure this is also brought into account.

Example

A painting which originally cost £30,000 in 2015/16 is made available to an individual on 1/10/18. On 1/12/18 significant restoration work is undertaken on behalf of the trustees. This costs £70,000.

The capital cost would be £30,000 for 2018/19 and £100,000 for 2019/20. The other expenditure will only feature in the amount CC from the next 6 April.

6.7 If the official rate of interest changes during the relevant period then R in paragraph 6.3 above is the average official rate of interest for the period calculated as follows:

Step 1 – Multiply each official rate of interest in force during the relevant period by the number of days in force

Step 2 – Add together the products found in Step 1

Step 3 – Divide the total found in Step 2 by then number of days in the relevant period.

Example

Simon is the beneficiary of a non-resident trust. The trust purchases a classic car in April 2019 for £50,000 and makes the car available for Simon's use. In exchange for the use of the car Simon contributes £500 per year towards the insurance of the vehicle. For the purpose of the example it is assumed that the official rate of interest is 2.5%.

The value of the benefit provided to Simon in 2019/20 is as follows:

$$\frac{50{,}000 \times 2.5\,\% \times 365}{365} - 500 = £750$$

On 6 April 2020 the trustees spend £10,000 on the car to enhance its value. The value of the benefit in 2020/21 is calculated as follows:

$$\frac{60{,}000 \times 2.5\% \times 365}{365} - 500 = £1{,}000$$

On 6 October 2021 the official rate of interest increases to 4%. The value of the benefit in 2021/22 is calculated as follows:

$$\frac{60{,}000 \times (((2.5\% \times 183) + (4\% \times 182))/365) \times 365}{365} - 500 = £1{,}450$$

6.8 The final value of the benefit calculation set out in the legislation relates to the making of land available. This is covered in S97C TCGA 92 and S742E ITA 07. The value of the benefit provided by making land available for the use of an individual for each tax year in which the benefit is provided is calculated as the amount by which-

(a) The rental value of the land for the period of the tax year during which the land is made available to the individual, exceeds

(b) The total of the amounts (if any) paid in the tax year by the individual –

   (i) To the person providing the benefit, in respect of the availability of the land, or

   (ii) So far as not within sub-paragraph (i), in respect of costs of repair, insurance or maintenance relating to the land.

6.9 The calculation in 6.8 above does not apply if the person providing the benefit transfers the whole of their interest in the land to the individual. The rental value of the land referred to above means the rent which would have been payable for the period if the land had been let to the individual at an annual rent equal to the annual value. The annual value of the land is the rent that might reasonably be expected to be obtained on a letting from year to year if the tenant undertook to pay all taxes, rates and charges usually paid by a tenant and the landlord undertook to bear the costs of the repairs and insurance and the other expenditure necessary for maintaining the property in a state to command that rent.

Example

Sarah is the beneficiary of a non-resident trust. The trustees own a residential property in London and in 2019/20 the trustees make the property available for Sarah to live in. In exchange for being allowed to live in the property Sarah agrees to pay for any maintenance work that is needed on the property. The District Valuer states that the annual rent such a property would command would be £25,000 per year.

In 2019/20 Sarah does not have to spend anything on the maintenance of the property and so the value of the benefit provided will be £25,000.

In 2020/21 the property starts to suffer from damp and Sarah spends £5,000 in repairing the property. As a result the value of the benefit is calculated as £20,000 (£25,000 - £5,000).

In 2021/22 an issue is identified with the roof and Sarah pays £30,000 to repair this. As the cost of repairs incurred by Sarah during the year exceeds the value of the annual rent the value of the benefit in 2021/22 will be nil.

7 Rebasing for Capital Gains Tax

An individual that becomes deemed domiciled under condition B of s835BA ITA2007 on 6 April 2017 will be entitled to rebase certain foreign assets to their market value at 5 April 2017 for the purposes of calculating the gain or loss on the disposal of that asset. This is subject to a number of conditions.

For the individual:

i) Section s809H (claim for remittance basis and a charge applies) applied to the individual in relation to 2016/17 or an earlier year
ii) The individual was resident in the UK for 2017/18
iii) For 2017/18 and each year up to and including the year in which the disposal is made condition B of s835BA is met (i.e. he is deemed domiciled under the 15 out of 20 rule) and the individual has not become domiciled in the UK
iv) Condition A of s835BA ITA2007 does not apply to the individual e.g. rebasing is not available where the individual is born in the UK with a domicile of origin in the UK
v) For the year of disposal the individual is not domiciled in the UK at any time in the year under common law

For the asset:

a) The asset was held on 5/4/17
b) The disposal is made on or after 6/4/17
c) The asset was not situated in the UK at any time in the period from 16/3/16 (or acquisition if later) to 5/4/17

Additional points:

- On disposal of an asset an election can be made for the rebasing not to apply to that asset. An election is irrevocable and can be made within normal time limits.
- For a) additional considerations apply where s127 TCGA 1992 applies
- For c) certain periods when an asset was brought into the UK for repair or public access will be discounted when considering whether an asset was UK Situs. In addition certain personal items may not be considered UK situs. The detail of these rules is outside the scope of this material.
- Rebasing of an asset only affects its base cost for the purposes of calculating the amount of the gain (or loss) arising on disposal. It does not act to remove any previously rolled over gains from the calculation of the gain arising.
- Rebasing is available for units held personally in a non-reporting status offshore fund
- Rebasing can apply where assets are held under nominee arrangements or in a partnership that is transparent for capital gains tax purposes.

Examples

1) Mr A first becomes deemed domiciled under condition B of s835BA ITA2007 for 2018/19. Rebasing is not available for Mr A.

2) Mrs B is the settlor of a non UK resident trust that holds non-UK assets. Rebasing is not available for the trust assets.

3) Non UK situs assets are held by a nominee for Mr C. Subject to the other conditions being met, the assets are within the scope of the rebasing rules.

4) Mr D acquires a non UK situs asset on 20/5/15 and transfers it to his wife Mrs D on 21/3/17. She disposes of the asset on 20/12/17. Subject to the other conditions being met Mrs D would be entitled to rebasing for the asset transferred, rather than her acquisition cost being the amount provided by the no gain/no loss provisions for transfers to a spouse. (For Mr D, his transfer to Mrs D is subject to the no gain/no loss provisions as normal.)

5) Mr D acquires a non UK situs asset on 5/3/14 and transfers it to his wife Mrs D on 30/6/17. For Mr D, his transfer is subject to the no gain/no loss provisions as normal. On a later disposal by Mrs D rebasing would not be available as her acquisition of the asset is after 5/4/17.

6) Mr E becomes deemed domiciled under condition B of s835BA ITA2007 for 2017/18 but has not previously made any claims to the remittance basis and s809H has not applied in any year. Rebasing is not available to Mr E.

7) Ms F becomes deemed domiciled under condition B of s835BA ITA 2007 and has owned a UK property for many years. Rebasing is not available for UK situs assets.

8 Capital Gains Tax – other changes

8.1 There are three main areas where other changes are being made:

Temporary non-residence provisions
Foreign Loss Elections

Carried Interest gains

8.2 **Temporary Non-Resident provisions – S10A TCGA 1992**

If an individual left the UK before 17/8/2015 and on return falls within the temporary non-residence rules within s10A then transitional rules apply. These rules allow a claim to be made for the remittance basis to apply to the gains arising in the temporary period of non-residence that are treated as accruing in the year or period of return.

Where a claim is made s890C, s809G and s809H ITA 2007 do not apply and so there is no need to pay any remittance basis charge.

Example

A is non-domiciled in the UK and leaves in 2014/15. He returns to the UK becoming resident in the UK again for 2018/19.

On his return he is deemed domiciled from 6/4/18 and is also within the scope of the temporary non-residence rules.

In 2017/18 while overseas he disposed of an asset he had held for many years realising a gain of £20,000. The proceeds of the sale are retained in a bank account outside the UK.

A may make a claim for the remittance basis to apply to the gains of £20,000 which would otherwise be treated as gains accruing for 2018/19.

8.3 **Foreign loss elections – S16ZA-C TCGA1992**

The rules governing foreign loss elections have been amended.

From 2017/18 losses on the disposal of foreign situs assets in a year will be allowable losses if the individual is deemed domiciled for the year. Losses that accrued while a foreign loss election was in place which have not been used (i.e. losses realised but not offset against gains under the special ordering rules) will be available to offset against gains once the taxpayer becomes deemed domiciled.

An individual who was born in the UK with a UK domicile of origin will be UK deemed domiciled on his or her return to the UK regardless of how many years they spend outside of the UK. Deemed domicile can only be lost by an individual who acquires that status only by virtue of being UK resident in 15 of the immediately preceding 20 tax years. If such an individual loses his deemed domicile status by being non-UK resident for six years or more and later becomes UK resident but not domiciled, then a foreign loss election can again be made. The normal rules apply so this is triggered by the first year in this later period to which s809B ITA 2007 applies. The election is irrevocable but only applies to the later period. See example 1 and 2.

For the years when the election was in force the special rules concerning the allocation of allowable losses are unaffected.

Example 1

Mr A is a non-domiciled individual that has claimed the remittance basis since 2008/09. He made a foreign loss election for 2008/9 onwards. The effect of the foreign loss election will continue up to 2016/17. A is deemed domiciled in the UK from 6/4/17 (only as a result of being a long term UK resident).

In 20019/20 he leaves the UK returning in 2026/27. He is not deemed domiciled from 6/4/26 and he claims the remittance basis for 2026/27. If Mr A wants to be able to claim foreign capital losses he will need to make a foreign loss election. The normal time limit applies. That is four years from the end of 5 April 2027 (so prior to 6 April 2031).

Example 2

Mr B. Facts are the same as A except B didn’t make a foreign loss election in 2008/09. B will have an opportunity to make a foreign loss election for 2026/27 and subsequent years.

8.4 **Carried Interest gains under section 103KA(2) or (3) TCGA 1992**

To avoid difficulties that can arise through double taxation any amount of chargeable gains that are treated as accruing under S103KA(2) or (3) are excluded from the scope of S13, S86 and S87. These changes have retrospective effect.