

Amendments 51 to 53 to Clause 35 and Schedule 10: Settlements: anti-avoidance etc

Summary

1. Clause 35 and Schedule 10 introduce anti-avoidance provisions in relation to payments and benefits made from offshore trusts. These technical amendments ensure that the provisions inserted in the Income Tax (Trading and Other Income) Act (ITTOIA) 2005 operate as intended by ensuring the onward gift rules apply where appropriate and preventing double taxation.

Details of the amendments

2. Amendment 51 amends new section 643A of ITTOIA 2005 (deemed income because of benefits for settlor or close family member). The amendment ensures that there is no income tax charge on the recipient where a benefit paid to a settlor or close family member is matched to protected foreign-source income at a time when he or she is non-UK resident. However, in such a case, income can be treated as income of the individual for the purposes of subsection 643A(2) (income tax charge on the settlor) and the onward gift rules at sections 643I to 643L. This is subject to subsection 643A(5).
3. Amendment 52 also amends new section 643A. It clarifies that where subsection s.643A(2)(c)(i) and (ii) apply the deemed income is to be treated for income tax purposes as income of the settlor; and that where (ii) applies it is not treated for income tax purposes as income of the individual.
4. Amendment 53 amends new section 643I of ITTOIA (recipients of onward gifts) in consequence of amendment 1.

Background note

5. Chapter 5 of Part 5 of ITTOIA 2005 (Chapter 5) treats income arising to the trustees of a settlor-interested offshore trust as arising to the settlor (irrespective of whether the settlor enjoys the income). Where income is not treated as arising to the settlor it is treated as income of the settlor if it is distributed or otherwise payable to his minor child. Capital sums (such as loans) paid to such settlors in excess of the trustees' undistributed income is also treated as income arising to the settlor. Where the remittance basis applies to the settlor, foreign-source income is taxed in the year in which it is remitted.
6. However, the Chapter 5 provisions no longer apply to the foreign-source income of certain trusts created when the settlor was not domiciled in the UK (protected

foreign-source income) following changes provided by Schedule 8, Part 2 to the Finance (No. 2) Act 2017.

7. As the settlor charges have been disapplied, and to prevent avoidance, paragraph 11 of Schedule 10 to the Finance (No. 2) Bill introduces a new benefits charge into Chapter 5 where benefits paid to the settlor or a close member of his family can be matched against protected foreign-source income. Where the benefit is provided to a close family member of the settlor who is not taxable, a charge can be imposed on the settlor if he is UK resident.
8. In addition, it is possible for an offshore trust to route payments to a UK beneficiary via other beneficiaries who are either not UK resident or who are remittance basis users without the UK resident beneficiary paying UK tax. Paragraph 11 of Schedule 10 tackles this form of avoidance by introducing an onwards payment rule. This ensures that payments made from a trust to a beneficiary who is not UK resident or is a remittance basis user who gives or lends it back to a UK beneficiary within 3 years will be taxed on the UK resident beneficiary.
9. The changes provided by Schedule 10 were announced in December 2016 at paragraphs 2.3.3 (taxation of foreign income in overseas trusts) and 2.3.5 (recycling benefits from protected settlements) of the government's response to further consultation on reforms to the taxation of non-domiciles. The consultation response can be found at: <https://www.gov.uk/government/consultations/reforms-to-the-taxation-of-non-domiciles-further-consultation>
10. Amendments 2 and 5 to 32 to the Bill clarify that the anti-avoidance provisions inserted by paragraph 11 of Schedule 10 apply to both capital and income benefits, ensure that they will not result in income tax charges on non UK resident beneficiaries and that no double charges arise.
11. Amendments 3 and 4 to the Bill also amended paragraph 11 but have been changed and re-tabled as amendments 51 and 52 in response to stakeholder comment. For amendment 51 the only change is the added reference to sections 643I to 643L. For amendment 52 the only change is that reference to paragraph (a) has become a reference to paragraph (b).