

## **Offshore Aspects of UK Budget**

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Many column inches will, by now, have been devoted to analysis of the UK Chancellor's recent budget. This article intends to focus primarily on the offshore aspects of the budget i.e. the implications for residents in offshore jurisdictions and the implications for UK residents who have investments or investment vehicles in offshore jurisdictions.

#### **Residence Rules**

There have been a number of cases regarding residence in the UK in recent years. These have highlighted the fact that the rules for determining residence in the UK are not contained in any clear statute but rather have to be derived from revenue practice and case law. HMRC consider, as a result of case law, that individuals will be resident in the UK if they visit the UK for an average of 90 days per annum over a period of up to 4 consecutive years. There has been some dispute as to how this period of 90 days should be calculated, it had been proposed that any days present in the UK would be counted for the purposes of assessing whether or not the 90 rule had been breached. Days of arrival and departure would be counted but there was to be a limited relief for "transit days". As a result of much lobbying these proposals have been relaxed. It is now proposed that a day will be counted only if an individual is present in the UK at midnight on that particular day. Furthermore, if individuals are in the UK purely because they are in transit between two places outside the UK, then those days present in the UK due to transit will not be counted even though the individual might be present in the UK at midnight. This relief will apply as long as our travellers do not spend any time in the UK engaged in any activity that is "substantially unrelated" to their travel through the UK. This effectively means that time spent in transit, such as between airports or ferry terminals will not count but if individuals take time out of their "transit" to conduct business activities or to visit relatives then the "transit days" may count towards the 90 day period.

#### **Non-Domicilairies**

The new provisions relating to individuals who are UK resident but non-domiciled are largely as expected. Where such individuals have been resident in the UK for seven tax years then they will only be able to continue being taxed on a "remittance basis" in respect of foreign income and foreign gains where they pay a fee of £30,000 for each tax year in which they wish to be taxed on the remittance basis. The remittance basis is also tidied up so a number of "devices" which tax advisors used to use to enable funds to be used in the UK without actually triggering a tax charge for a non-domiciled individual who had earned that income are curtailed.

#### **Non-Resident Trusts**

There are significant changes to the taxation of capital gains achieved by a trust created by individuals who are UK resident but not UK domiciled. In the past capital gains achieved by such trusts were not taxed either on the trustees or the UK resident but non-domiciled settlor. This was the case, even if the proceeds of the gains were subsequently distributed to those settlors in the UK.

It had been proposed that the gains of offshore trusts would be taxable upon UK resident and non-domiciled settlors as those gains arose. This has now been modified so that no tax will arise as gains arise but the capital gains of offshore trusts will be added to a notional pool of gains. The gains within those pools will be attributed to beneficiaries when they receive capital distributions and taxed upon on them at that time. If the beneficiaries are non-domiciled and paying the £30,000 fee then when they "benefit" from a trust outside the UK no tax will arise until the "benefit" is brought into the UK i.e. there will be a remittance basis in respect of capital gains taxed as a result of trust distributions to individuals who are non-domiciled and who pay the £30,000 fee.

## **Offshore Funds**

There are a large number of offshore funds located in offshore jurisdictions. These are often constituted as shares in offshore companies or units in unit trusts. Economically these are like UK unit and investment trusts, investors buy units in the funds and the monies are then managed by a fund manager, eventually the investor will en-cash his units and hopefully achieve a capital profit. Many offshore funds do not distribute any income and the ultimate profit is known as an "Offshore Income gain" and is subject to income tax. Going forward the rate of tax in respect of such profits will be extremely important. The rate of tax on profits on disposal of units in funds that produce Offshore Income gains will remain at 40%, whereas the rate of tax on most capital gains will fall to 18%. It is possible for funds that comply with certain criteria to apply for "distributor status", in these cases, the ultimate profit on disposal will be taxed at 18%. Going forward I would expect that more funds will aim to achieve "distributor status".

From 5 April 2009 there will be two principal ways of attaining distributors status. The traditional route will be to adopt a policy whereby the funds distribute 85% of the income that they earn each year. A new proposal is that funds will be able to apply for "distributor status" where they declare, on an annual basis, the amount of income they have earned so that investors can be taxed on that income regardless of whether or not it has been distributed. In either case investors have to accept an on-going income tax charge as the cost of achieving an 18% charge on the ultimate realisation of any capital growth in their units.

## **Conclusion**

The above is a very brief summary of some complex provisions. The exact details of the changes will not be known until the Finance Bill is produced and even then, the draft legislation will be subject to change until it becomes a Finance Act. Tax advisors who advise offshore funds, UK resident but not domiciled individuals or individuals who visit the UK but wish to remain not resident would be well advised to review the detail of the Revenue's proposals contained in the Budget Press Releases and eventually the Finance Bill.

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