Remittances
The detail

Although this note looks at some of the more detailed aspects of the remittance rules, because of the complexity of those rules, it can only ever be a general guide.

1 Overview
The remittance regime has been designed with a clear purpose in mind: UK resident non-UK domiciliaries who retain funds outside of the UK and who do not seek to bring those funds to, or enjoy those funds in, the UK will not be taxed on the gains and income that arise from those funds; however, the enjoyment in the UK of funds deriving from non-UK income and gains should be expected to be taxed.

2 Basic qualifications
The remittance basis can be claimed by individuals who are resident but not domiciled in the UK.

Remittance basis users (to use the language of the legislation) who have been resident in the UK for more than seven out of the last nine tax years need to pay a £30,000 additional tax charge, rising to £60,000 for those who have been UK resident for more than 12 years out of the last 14.

The remittance basis cannot be claimed by non-UK domiciliaries who have been UK resident for at least 15 out of the last 20 tax years, nor by an individual who was born in the UK with a UK domicile of origin (irrespective of how long that person has been UK resident).

The mechanics of the payment of the additional tax charge (which can, if handled correctly, be done without triggering a further remittance of the sums used to pay the tax) are beyond the scope of this note. Similarly, the manner in which the additional tax charge applies to "nominated" income and gains (provisions introduced to enable certain categories of non-UK domiciliary – and US citizens in particular – to claim a tax credit in their home jurisdictions for the additional tax) is also beyond the scope of this note.

3 "An individuals income and chargeable gains"
The starting point for analysing the remittance legislation is the concept of an "individual's" income or chargeable gains". It is necessary in each case to identify what type of income and / or chargeable gain is potentially caught by the rules.

In some cases this is relatively straightforward. For example, if an individual's sole source of foreign income is interest arising on a foreign deposit account, then the interest is clearly the individual's foreign income. However, in real life, matters are often more complex.

The concept of income and chargeable gains includes not only income from sources owned by the individual personally, or gains realised from personally held assets, but also income and gains treated as being received by the individual.

The latter categories would include:

- income arising in non-UK corporate structures where the individual is the person who created the structure or, in some circumstances, who added property to it or made loans to it – where the income is treated as theirs;
- income arising in non-UK corporate structures created by someone other than the individual or trusts created by the individual or by any other person – such income can be matched against benefits the individual receives from the non-UK structure (for example, a distribution, use of an asset or interest-free loan);
- gains deemed to be those of the individual by being attributed to him / her through certain closely held foreign corporations – note that these provisions generally only apply where the individual's ability to participate in the gains and income of the company (normally through a shareholding) amounts to a participation of more than 25 per cent;
- gains arising in non-UK resident trusts that can be matched against benefits a UK resident receives from the trust; and
- certain types of deemed income – including on the disposal of non-reporting status offshore funds (e.g. many hedge funds), or income deemed to arise under the "accrued income scheme", or gains from the disposal of other securities, known as deeply discounted securities.

"Income" also includes foreign employment income.

Having identified what constitutes the individual's "income and chargeable gains", it is necessary to track the income and chargeable gains in order to see if they have been remitted.

4 Meaning of remittance – introduction

The scheme of the legislation creates a broad meaning of remittance (see section 5) and a wide class of persons capable of triggering a remittance ("relevant persons" – see section 6) through deeming provisions.

5 Meaning of remittance – money, property or services

A remittance occurs if Conditions A and B are met:

Condition A is that:

- money or other property is brought to, received, or used in the UK by or for the benefit of a "relevant person"; or
- a service is provided in the UK to or for the benefit of a "relevant person".

Condition B is that:

- the property, service or consideration for the service is, or derives from (wholly or in part, directly or indirectly), the income or chargeable gains of the individual; or
- the income or chargeable gains (or anything deriving from them) are used outside of the UK (directly or indirectly) in respect of a "relevant debt" (see section 7).

As will be seen, this definition of "remittance" is exceptionally wide. The purpose of the language is to ensure that if any of an individual's income or chargeable gains are used or enjoyed in any form in the UK, a taxable remittance will occur. There are very narrow exceptions to these remittance rules, and these are explored in more detail in section 9 below. Anti-avoidance rules introduced to counter obvious avoidance techniques are set out in section 10.

6 "Relevant person"

The legislation widens the class of persons capable of remitting funds to the UK by introducing the concept of a "relevant person". A "relevant person" includes:

- the individual (i.e. the non-UK domiciled individual who has the unremitted but potentially remittable foreign income or chargeable gains);
- the individual's husband or wife including of a same sex marriage (including any person living with the individual "as husband or wife");
- the individual's civil partner (including any person living with the individual "as civil partner");
- a minor child or grandchild of any of the above (so the definition also includes minor step-children and even minor children of a long-term but not legal partner);
- a company in which any person who falls within the other categories listed above and below is a "participator" (which broadly equates to shareholder);
- the trustees of a settlement of which any person who falls within the other categories listed above and below is a beneficiary; and
- a company or other corporate body "connected with" such a settlement.

Persons living together in a relationship akin to marriage or a civil partnership are treated as spouses or civil partners for these purposes. The only obvious gap in the definition of what constitutes a "relevant person" is adult children or grandchildren (or indeed adult step-children or step-grandchildren) of "the individual". An individual's parents and siblings are also excluded. Most charities will also fall outside of the definition. However, almost all other likely recipients of funds are "relevant persons".

There will undoubtedly be entities that may appear to fall outside the definition of "relevant persons". Some entities formed in civil law jurisdictions have been promoted as being outside the definition. We would be wary of some of the claims made for these entities. Any planning along these lines is likely to have a rather limited life span.

HMRC does however currently accept that a partnership is not a "relevant person" and that a remittance by a partnership is not treated as a remittance by any of the partners in the partnership (assuming it is not a remittance for the benefit of a particular partner).

7 "Relevant debt"

A "relevant debt" is a debt incurred to purchase, or to finance:

- any money or other property that has been brought to, received, or used in the UK by or for the benefit of a "relevant person"; or
- any service provided in the UK to or for the benefit of a "relevant person".

The most obvious example of a "relevant debt" is borrowing incurred in order to purchase a UK property for the individual; however, the definition is far wider than this.

HMRC treat loans brought to the UK that are secured on offshore income / gains as a taxable remittance of the security, as well as any payment of interest or repayments of principal on the loan made out of offshore income / gains.

8 The remittance rules in practice

The remittance rules are designed to stop the individual and any "relevant person" using unremitted foreign income or gains to finance any item of UK expenditure without a remittance occurring. As a result, and subject to the exceptions outlined briefly in section 9, the purchase of any asset in the UK, the payment for any service in the UK, and the importation of any asset into the UK by an individual or by a "relevant person" using the individual's income or chargeable gains will be deemed to be a remittance.

The scope of the rules is perhaps best illustrated by some examples.

Example 1:
A purchases a picture at an auction in New York. A does not have sufficient clean capital to fund the purchase, so he uses foreign investment income in order to do so. A then brings the picture to the UK to hang on the walls of his house for an extended period. "Property" has been "brought to" and "received in" the UK by A, and therefore the importation of the picture is treated as a remittance of the income used to purchase the picture.

Example 2:
B and C are husband and wife. They have a child, D, who is at school in the UK. The school bills C for D's school fees. B gives foreign investment income to C to finance the payment of the school fees. C is a "relevant person". C has received income which she then spends in the UK by making a payment of D's school fees. A remittance by B is deemed to occur.

Example 3:
The facts are the same as in example 2 above, except the school has a foreign bank account into which it invites non-UK domiciled parents to pay the school fees. In this case, no money or other property is "brought to, or received or used in the UK". However, a service (in other words the education of D) is provided in the UK to D, who is a "relevant person" (i.e. B's minor child). Therefore, the payment of the school fees by C is deemed to be a remittance by B.

Example 4:
F and her two brothers inherit $1m each from their father. F's two brothers live in Dubai, and have no UK tax exposure. The three siblings decide to form an investment company, which is BVI incorporated. The investment company is successful and the initial $3m invested by the shareholders ultimately turns into $9m. The $6m profit is all income or gain from non-UK investments and it is all held in cash in a single account. The investment company decides that it wishes to invest in a commercial property in the UK worth $6m. The property is purchased.

F is deemed to have remitted $2m of income or gains because the investment company will be a "relevant person". (The precise form of any remittance will also depend on the operation of the mixed funds rules discussed in more detail in section 11.)

If a claim for business investment relief is made (see section 9 below), no tax charge arises on remittances to make certain UK investments (including an interest in a commercial property business).

Example 5:
G is a successful hedge fund manager who receives dividends of $10m per annum from his non-UK management company. He wishes to undertake some estate planning and transfers $20m (i.e. two year's worth of dividends) to a trust for his children from which he and his wife are both wholly and irrevocably excluded. The gift is therefore a completed gift for inheritance tax purposes. The gift takes place in 2010. The trustees then decide to retain a UK based investment manager who invests in a range of mutual funds, 50 per cent of which are UK authorised mutual funds.

Notwithstanding the fact that neither G nor his spouse can benefit from the sums in the trust (because they are wholly and irrevocably excluded from the trust), the trustees are "relevant persons" because the beneficiaries of the trusts include G's minor children. As a result, when sums are invested in UK authorised mutual funds, a remittance of G's income is deemed to occur by G.

These few relatively straightforward examples illustrate how non-UK domiciliaries who are resident in the UK (whether on a short-term basis or a long-term basis) need to take specialist advice as to their position. This advice needs to be taken urgently as the rules contain many potential traps for the unwary.

9 Exceptions to the remittance rules

There are a series of exceptions to the remittance basis of taxation. These are as follows:

Consideration for services

Payments for certain services to UK firms are not to be treated as remittances. Such payments will not be treated as remittances if:

a. they are funded out of an individual's non-UK source income or chargeable gains;
b. the service relates wholly or mainly to property situated outside of the UK; and
c. the whole of the consideration (i.e. the payment for the fee) is paid into a foreign bank account of the service provider. There are some anti-avoidance provisions associated with this regime but they are not within the scope of this note.

This provision can be difficult to implement in practice. The key question is whether the advice given relates "wholly or mainly" to property outside of the UK. The rules for determining whether or not property is in or outside of the UK are the capital gains tax rules which can give rise to some anomalous results. For example, a plane located outside of the UK is deemed to be a UK situs asset if its owner is resident in the UK. In practice, many of these anomalies are likely to be irrelevant, but care will be required in making sure that invoices correctly identify the property to which the advice relates; and care will also be required in ensuring that payments are made to the appropriate bank accounts.

Exempt property

Clothing, footwear, jewellery and watches will be exempt property if they are for the personal use of a "relevant person".

Further, property is not taxed where the amount of foreign income or gains (that would otherwise be deemed to be remitted) is less than £1,000. "Property" for these purposes does not include "money" or any negotiable instrument (e.g. a traveller's cheque).

Property brought into the UK for repair, or for the purposes of public viewing (referred to as "public access" in the legislation), or if the property is only "temporarily imported" (which means for a total period of 275 days or fewer, not counting days of public access, personal use or repair) will not give rise to a remittance if the property is purchased out of foreign income or gains.

The public access rule is probably the most important exemption for these purposes. It is designed to exempt, for example, works of art brought to the UK for public display in museums (termed "approved establishments"). The fact that the property in question must be displayed at an "approved establishment" means that individuals bringing works of art to the UK which are not available for public viewing will not benefit from the relief.

Exempt property may be sold in the UK without a remittance occuring as long as the proceeds are promptly removed from the UK. This would, for example, allow a work of art purchased using overseas income to be sold at an auction in the UK.

Business Investment relief

Funds may be invested into UK businesses without triggering a taxable remittance provided that certain conditions are met.

First, the investment must either be for a subscription in newly issued shares, a purchase of existing shares, or in the form of a loan.

Second, the UK business must qualify for the relief. Although the rules are complex, generally a company will qualify if it carries on a commercial trade in the UK (this includes a UK property investment business) and no "relevant person" directly or indirectly obtains a benefit from the company.

The rules are complex and advice is needed to avoid falling into any traps.

10 Anti-avoidance

Because the definition of "relevant person" is not comprehensive, some taxpayers might be tempted to try to use gifts or other transfers made abroad as a method of alienating funds which could then be used for their benefit – for example, a loop structure could be created.

The legislation anticipates this. If an individual's income or gains are received by a "gift recipient" and the gift recipient brings the funds to the UK in a manner which would have been taxable had the individual remitted the funds himself, and if the funds are then used for the benefit of a "relevant person", a remittance is deemed to occur. The legislation goes further than this as it also creates a category of persons other than "relevant persons", who make "qualifying dispositions".

These provisions are all designed to prevent an individual circumventing the new rules by routing his or her income and gains through persons who are not "relevant persons" but who would be willing to return the property to the

individual or a "relevant person" in the UK in a manner which the individual would claim should be tax free. These rules are likely not to have significant application, but they do contain traps for the unwary.

Taxpayers also have to consider the application of the general anti-abuse rule when structuring their affairs. Generally, if a taxpayer undertakes planning, one of the main reasons for which is to obtain a tax advantage, and that planning is deemed "abusive" (broadly something that could not be viewed as a reasonable course of action), they may be caught. There is a high degree of uncertainty about when and how the general anti-abuse rule operates but it is a factor that all advisers must consider when advising non-UK domiciled clients.

11 The mixed funds rules

Specific rules create an order of priority of distributions from "mixed funds" to determine what sums have been remitted to the UK. These rules only apply to funds received after 6 April 2008 – the treatment of pre-6 April 2008 amounts in "mixed funds" remains unclear.

The mixed fund rules are complex. Their purpose is to identify the type of sum remitted. This is done by analysing each account containing mixed funds separately. Funds are also examined year by year, effectively creating layers of distinct income and gains. When funds leave an account, they are deemed to do so from the topmost layer, i.e. from the funds added during the most recent tax year in which the funds entered the account. When those funds have been expended the next layer of funds from the next tax year are considered.

Categories of funds that need to be identified are as follows:

- employment income (i.e. taxed UK employment income);
- relevant foreign earnings (i.e. earnings chargeable on the remittance basis);
- foreign specific employment income (i.e. sums from the disposal of certain types of employment related securities);
- relevant foreign income (i.e. principally investment income);
- foreign chargeable gains;
- employment income subject to a foreign tax;
- relevant foreign income subject to a foreign tax;
- foreign chargeable gains subject to a foreign tax; and
- any other income or capital.

If a remittance is made or is deemed to be made from the account, sums are deemed to be remitted for each year in turn, in the order set out above.

Each layer of income and gains for each year is drawn off in turn, until the remittance is fully franked.

Generally taxpayers will spend significant time in ensuring that they do not need to engage with the mixed funds rules. As a first step to this, it remains essential to segregate income and capital strictly. There is much more that can be done beyond the simple segregation of income and capital.

The maximum number of accounts that a taxpayer could hold in order to separate each category of income and gains is nine, with a fresh set of accounts opened each year.

The complexity that this brings could be mind-boggling and we suspect that many taxpayers will simply have three offshore accounts for:

- capital, from which remittances can be made tax free;
- capital mixed with capital gains – remittances from this account will attract tax at 20 / 28 per cent on a proportion of the sums remitted (with gains being remitted in priority to capital and therefore taxed at the 20 / 28 per cent rate); and
- other sums has including income, deemed income, and capital that has become mixed with sums other than gains.

Certain taxpayers can be expected to see an erosion of their clean capital if this format is followed. They may wish to follow a more complex approach such as the use of trusts or loans in order to preserve clean capital. Some discipline, knowledge and skill must be expected of investment advisers who advise clients seeking to retain clean capital in this context.

What happens if funds are transferred from a mixed account to another non-UK account? The legislation describes this as an "offshore transfer". In that case, instead of the transfer drawing off the constituent layers of the "mixed fund" on an annual basis, the transfer takes a proportionate share of all years' "mixed funds" in the account.

There are anti-avoidance provisions associated with the mixed funds rules because clearly it might be possible to strip out bad funds (i.e. funds subject to a high tax rate) by making a transfer to a foreign account. The anti-avoidance provisions allow HMRC to seek to re-characterise the funds in the transferee account on a "just and reasonable" basis if one of the main purposes of the transfer was to obtain a tax advantage.

Once a mixed fund has been created, it will be difficult for it to be cleansed without the payment of tax. However, any non-domiciliary who has previously paid tax on the remittance basis has a window of opportunity to separate income, gains and / or capital contained in a mixed fund by transferring the relevant part of the mixed fund to another overseas account before 6 April 2019. This is called a "nominated" transfer. The individual must ensure that the nominated transfer does not exceed the amount of income, gains and / or capital in the mixed fund otherwise the cleansing will be ineffective.

The following is a very simple example of the operation of the "mixed funds" rules. A is non-resident on 5 April 2014. On that date, she receives a termination payment from her former employer of £50,000 which she places in her non-UK account, which she designates as her capital account. Assume this sum is accepted as being capital. A becomes resident in the UK on 6 April 2014. For the 2014 / 15 tax year A's account contains the following credits:

- A has her net UK salary of £100,000 paid into the the account;
- A receives non-UK source interest of £10,000 which is paid into the account; and
- Finally, A realises a gain of £100,000 on the disposal of shares in a non-UK company, and the proceeds are paid into the account.

A decides that she would like to remit £220,000 from the account to fund the deposit on a UK house. A is deemed to have remitted the following amounts in the following order:

- her net UK salary of £100,000;
- the interest of £10,000;
- the gains of £100,000; and
- capital of £10,000. The capital of £10,000 is capital of the prior year.

In real life, mixed funds will rapidly become more complex than this very simple example.

Particular rules apply where earnings in respect of which overseas workday relief has been claimed are put into an account together with earnings taxable on the arising basis. These rules are outside of the scope of this note.

12 Other points

A non-UK domiciliary who temporarily becomes non-UK resident can still be treated as remitting funds to the UK unless they remain non-resident for more than five years. If the non-UK domiciliary returns to the UK and becomes resident within five years of his / her departure, non-UK income and gains which arose before the individual left the UK but were remitted to the UK after his / her departure will be taxed. Probably the most likely example of UK expenditure during a period of absence that may involve such a remittance is the repayment of debt incurred when the individual was UK resident.

In addition, dividends from closely held companies, certain employment income, pension income, chargeable event gains from certain insurance policies and loans to participators in close companies will be taxed on a return to the UK after a period of temporary non-residence.

This is an overview of a very complex subject. Specific advice will always be required.

Contact details

If you would like further information or specific advice please contact:

Sebastian Prichard Jones
Partner
Private client
DD +44 (0)20 7849 2829
sebastian.prichardjones@macfarlanes.com

Jennifer Smithson
Partner
Private client
DD +44 (0)20 7849 2891
jennifer.smithson@macfarlanes.com

Robin Vos
Solicitor
Private client
DD +44 (0)20 7849 2393
robin.vos@macfarlanes.com

July 2018

Macfarlanes LLP
20 Cursitor Street London EC4A 1LT
T +44 (0)20 7831 9222 | F +44 (0)20 7831 9607 | DX 138 Chancery Lane | macfarlanes.com

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