Private Client MAGAZINE

TAX EDITION

BEYOND BORDERS: YOUR GUIDE TO TAX FOR 2024

INTRODUCTION

"The avoidance of taxes is the only intellectual pursuit that still carries any reward".

John Maynard Keynes

As we pave the way into a new fiscal year, we are delighted to present the 2024 Private Client Tax Special. This special edition will serve as your guide to the latest developments, strategies and insights that have emerged in the realm of tax. Our authors have curated articles that will equip you with the tools to optimise your financial strategies, mitigate risks and cultivate opportunities in the ever-shifting tax landscape.

We would like to thank our community partners and contributors for their support as we kick off 2024 with new events in our Private Client Community.

We hope to see you at our upcoming Landed Estates & Farm Tax Conference in London on Tuesday 19th March 2024.

Enjoy the read!

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THE PRIVATE ASSET STRUCTURE IN LIECHTENSTEIN – OR WHY LESS TAX IS SOMETIMES EVEN TOO MUCH TAX

Authored by: Claudius Müller-Rensmann (Senior Associate) – Gasser Partner

I. General Information

Liechtenstein has been in the process of adapting to the European tax requirements for several years and getting rid of its status as a tax haven. Although taxes are still at a low level, Liechtenstein has adopted much of the European regulation and is not a black list country.

In terms of low taxes, there is one exception in Liechtenstein tax law that is of great importance for the private client sector: the private asset structure or private investment structure (PAS; Privatvermögenstruktur). According to Art. 64 of the Liechtenstein Tax Act (Steuergesetz), legal entities may obtain the status of PAS if they fulfill the requirements. In this case an entity only pays the minimum annual income tax of CHF 1’800.

II. Requirements

Entities with PAS status may hold any kind of assets. This includes financial instruments or bankable assets such like futures, swaps, negotiable securities, liquid monies and shares in other companies. Furthermore, the entity may hold real estate, precious metals and stones, vintage cars and art. A major advantage is that the status is not tied to a special legal form of the entity but neutral in terms of the legal form of the entity. Therefore, limiteds, foundations, trust companies and establishments may opt for the PAS status. However, Liechtenstein trust may not apply for the status as they are not recognised as legal entities.

What sounds good at first, however, is also subject to strict conditions. In particular, the legal entity must not engage in any commercial activity.

This includes offerings of services and goods. Since this is a very broad definition, the European Free Trade Association (EFTA) Surveillance Authority (ESA) has specified commercial activity more precisely. According to the ESA Decision of 15 February 2011 on Private Investment Structures No 44/11/COL and the Liechtenstein Tax Authority (Steuerverwaltung), commercial activity includes renting and leasing of real estate and commercial trading in shares and bonds or investments in leveraged products. Acquiring, holding and selling shares and other tradable securities do not per se constitute an economic activity as long as the trading does not exceed a certain level (such as day trading). In addition, the legal entity must not exercise control by directly or indirectly influencing the management of the invested company.

In order to obtain this status, the articles of association or statutes of the legal entity must provide for the restriction under Art. 64 of the Liechtenstein Tax Act. The Liechtenstein Tax Authority is responsible for monitoring the compliance with the requirements. To this end, the Tax Authority may inspect the minutes of the board of directors or the shareholder’s meeting, resolutions, and other documents appropriate to examine compliance.

III. Relevance

In addition to the advantage to pay only the annual minimum income tax of CHF 1´800.00, private asset structures do not have to submit a tax return. This has considerable advantages, also in terms of costs. Due to its simplicity, the status is often the first reflex for many advisors and an argument which is offered to clients if it comes to Liechtenstein entities.

However, to advise international high net worth individuals, the double taxation agreements with the client's country of residence and invested companies must be carefully examined. It should be noted that many double taxation agreements between Liechtenstein and other countries do not consider the PAS to be an entity resident in Liechtenstein.

This may be illustrated by the example of Germany: a legal entity domiciled in Liechtenstein is recognised as a legal entity under Art. 1 in conjunction with Art. 3 (3)(e) of the double taxation agreement between Germany and Liechtenstein (DTA LIE/GER). However, this does not apply to PAS.

This may have material adverse effect, as the DTA LIE/GER provides extensive relief which, from the perspective of German tax law, leads to considerable tax benefits. For example, a German corporation must deduct the German capital gains tax from a dividend distribution to a Liechtenstein foundation in accordance with § 43 (1)(1) No. 1, § 43a (1)(1) No. 1, § 50c (1) German Income Tax Act (Einkommenssteuergesetz) in conjunction with Art. 30 (1)(1) DTA LIE/GER. The advantage is that the capital gains tax has a final withholding effect from the perspective of a Liechtenstein foundation. Therefore, the Liechtenstein foundation may claim the difference between the tax levied by way of deduction and the reduced tax permitted under the DTA LIE/GER in accordance with § 50c (3) German Income Tax Act.[1]

As dividends from foreign companies are generally tax exempt in Liechtenstein there may be huge tax benefits. However, since an entity with PAS status is not considered as a Liechtenstein resident entity, the entity cannot assert the claim.

IV. Alternative

Although CHF 1´800.00 minimum income tax may sound good, it is often more than the structure would have to pay if it had not received the PAS status. This is because Liechtenstein tax law offers other options where even the minimum income tax can be avoided, and no tax must be paid at all in the end. For example, according to Art. 48 of the Liechtenstein Tax Act, profits resulting from foreign ownership (such as dividends) are exempt from income tax.

However, this tax exemption cannot be granted if an entity is a PAS. This is because a PAS is not obliged to submit a tax return, which is why the tax authorities cannot even see that income has been generated from foreign ownership. Eventually, a PAS may pay taxes even though the income would be fully tax-exempt without the status.

Therefore, it should be carefully examined whether an entity should opt for the PAS. This is because the PAS status can bring tax relief and make tax returns easier, but it can also mean that the entity pays CHF 1´800 more than would have to be paid. In addition, PAS status reduces flexibility and is therefore not suitable for all companies and structures.

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1 HÄRTLING/TOLKSDORF, Besteuerung in- und ausländischer Familienstiftungen aus deutscher Sicht, IStR 2023, 717(734).

US ESTATE TAX AND THE SUNSET PROVISIONS

Authored by: London & Capital

Please note, while we do not provide tax advice, we collaborate with your clients to structure their wealth in the most tax-efficient way possible.

While the terms estate tax and inheritance tax are often used interchangeably, a crucial distinction exists between the two. Estate tax is imposed on the estate of the deceased person, while inheritance tax is levied on the beneficiaries who receive the distribution from the estate.

Part 1 - US ESTATE TAX

Overview

In the United States, the estate tax is a federal levy applied to the estate of a US person if their gross estate exceeds the available exemption, presently set at $13.61 million. This exemption amount, also known as the lifetime gift tax exemption, enables married couples to collectively exclude up to $27.22 million from gift and estate tax.

For those making significant lifetime gifts, these reduce the available estate tax exemption on death. The estate tax is charged on the value exceeding the exemption at graduated rates, reaching a maximum of 40%.

Marital Deduction and Non-US Spouse Gifts: The unlimited marital deduction allows unlimited lifetime gifts to a US citizen spouse. In mixed marriages, a US spouse can gift up to $185,000 annually to their non-US spouse free of gift tax.

Annual Gift Tax Exclusion: US individuals can annually gift up to $18,000 to any number of recipients without impacting their lifetime gift and estate tax exemption. Gifts beyond this exclusion reduce the available exemption on death.

There may also be individual state tax levied depending on your individual circumstances.

The "Use It or Lose It" Provision

Under the 2017 Tax Cuts and Jobs Act (TCJA), the lifetime estate and gift exemption increased to $13.61 million. However, the sunset provision is set to revert to pre-2017 levels by the end of 2025, expected to be around $7 million from January 1, 2026. Planning before 2026 is advised to take advantage of the increased exemption. Gifts made during the increased exemption period won't be clawed back, but it is a 'use it or lose it' provision.

Why should you make gifts prior to the sunset?

Making a gift before the Sunset provisions may have a drastic impact on your estate tax. Below are two examples of someone having an estate valued at $15m.

Table 1 assumes that an individual does not make gifts prior to 2026 and thus their net taxable estate is taxed in full at 40%.

US Estate currently value at	$15,000,000
Less Exemption at 2026	($7,000,000)
Total Estate After Gifting	$8,000,000
40% Estate Tax	$3,200,000

Table 2 shows the effect of gifting prior to the sunset provisions, resulting in giving away $12.5m before 2026 and realising an estate tax saving of $2.2m.

US Estate currently value at	US Estate currently value at
Gifts made prior to 31 Dec 2025	($12,500,000)
2026 Estate Tax Exemption	$7,000,000
As more than 100% of the exemption was used prior to Sunset, none remains	$0
Total Estate After Gifting	$2,500,000
40% Estate Tax	$1,000,000

The estate tax saving would thus be much greater if an individual makes gifts prior to the sunset provisions. It is worth noting that the only meaningful way to make a saving for estate tax purposes is if an individual gives away more than the $7m anticipated estate tax exemption.

Part 2 - UK inheritance TAX

Overview

An individual who is domiciled or deemed domiciled in the UK will be subject to UK inheritance tax on all their worldwide assets. Individuals not domiciled in the UK may be subject to UK inheritance tax on their UK assets.

Domicile is a key inheritance tax concept, you can either be domiciled at birth or become deemed domiciled if you were resident in the UK for at least 15 out of 20 tax years.

In the UK, inheritance tax applies to the estates of UK-domiciled individuals. The nil-rate band is £325,000, with a residence nil-rate band of £175,000 for qualifying residences.

The maximum available residence nil-rate band will be reduced by £1 for every £2 for estates in excess of £2m, meaning that there will be no residence nil-rate band available if the estate is worth over £2.35m.

Transfers between spouses are usually exempt, and unused bands can be added, potentially resulting in a total exclusion of £1 million for married couples.

Annual gifts up to £3,000 are exempt from UK inheritance tax and do not need to be considered when calculating the value of the estate.

Potentially Exempt Transfers (PETs) - Lifetime gifts are generally exempt for UK inheritance tax purposes if the donor survives seven years from the date of gift. If the individual dies within seven years, the gift is known as ‘failed PET’ and will be considered in the individual’s inheritance tax calculation.

Chargeable Lifetime Transfers (CLTs) - a chargeable lifetime transfer is a lifetime gift which is immediately subject to inheritance tax at 20%, provided that the gift is in excess of the nil-rate band

of £325,000. CLTs are cumulative, if an individual makes two CLTs within the same seven year period and the sum of both exceeds the nil-rate band, there will be a charge to inheritance tax on the excess.

Transfers out of surplus income - Individuals can also make gifts out surplus income which are exempt from UK inheritance tax. Such gifts must be made out of an individual's net income and be part of their normal expenditure, i.e. capital cannot be used to fund these gifts.

Part 3 - Opportunities for US/UK people

Lifetime Gifts: Both the US and the UK allow individuals to make gifts during their lifetime, reducing their taxable estate on death.

Trust Planning: Excluded property trusts provide flexibility and control over asset distribution, particularly beneficial for UK individuals not domiciled in the UK.

Mixed Marriages: US spouses can strategically gift assets to non-US spouses, and Qualified Domestic Trusts (QDOTs) offer planning tools for mixed marriages, allowing for the deferral of US estate tax.

Understanding these provisions and planning opportunities is essential for individuals seeking to navigate the complex landscape of estate taxes in both the US and the UK.

There is a specific exemption from inheritance tax where assets are given to charities. If an individual's net estate is given away to a charity, the reduced inheritance tax rate of 36% applies.

Pension funds also receive a general inheritance tax exemption, thus leaving excess pension to the future generation could be a prudent planning point.

Investing in Alternative Investment Market (AIM) stocks for two years or more can be a helpful way to manage UK inheritance tax. These stocks are generally issued by a smaller, more risky companies.

There are other estate tax planning opportunities available to individuals depending on their residency/domicile position, generally these are quite niche and require help from a tax adviser.

INHERITANCE TAX PLANNING, THE 2024 BUDGET AND STEALTH TAX BRITAIN

Authored by: John D. Bunker (Consultant Solicitor and Chartered Tax Advisor) and Laura Colville (Senior Associate Solicitor) – Irwin Mitchell

Kite flying by the Chancellor, or those close to him, has fuelled speculation about a major cut in Inheritance Tax (IHT), even its abolition. Abolishing "the most hated tax", at least in this tail-end of a Parliament, would be hard for 3 reasons:

1. **The "tax take" from IHT is now significant,** rising steeply with the freezing of allowances (a real "stealth tax"). One source in the press scotched the idea of scrapping IHT as it will raise £10bn a year by 2028-29.

2. **It is complex / difficult to abolish IHT, given the interaction with Capital Gains Tax (CGT)** (the current CGT "uplift" on death to wipe out all gains). Some CGT changes might be needed, e.g. introducing CGT on death, to avoid distorting behaviour – such as more people holding onto assets unnaturally until death, if there is then no IHT as well as no CGT.

3. **On a practical level, it will take major Parliamentary time to abolish IHT.** If announced on 6 March 2024, it would clearly not be enacted before 6 April, so would need to be (if Parliamentary time allowed) from a date mid-way through the tax year which may not be easy. It could simply become a Conservative election promise.

Reducing IHT?

Cutting IHT could be easily achieved by increasing the Nil Rate Band (NRB), say to £350K, £400K or even £500K. Such a change could take effect by 6 April, without upsetting the structure of IHT/CGT. However, it is unrealistic to anticipate IHT abolition in March. Clients still need to plan for IHT mitigation e.g. these ideas.

Lifetime planning to mitigate IHT - assuming it's here to stay:

1. **Making lifetime gifts within the available exemptions** is valuable. Especially the use of the normal expenditure out of income exemption, with two key elements to be effective, (i) to ensure there is surplus income available, keep records of income and expenditure needed for the IHT403 form in the event of death; and (ii) to make a written commitment to continue payments to show a pattern of gifting e.g. a letter to parents of a grandchild affirming an intention to pay school fees, or an intention to gift an annual work-bonus to a trust for grandchildren.

2. **Lifetime gifts as Potentially Exempt Transfers (PETs)** that exceed exemptions, or chargeable transfers to trusts, to save tax if you survive 7 years, with appropriate life cover if you die within the 7 year period. The limitation of "taper relief" (it only tapers any tax on the gift, not the gift value itself) doesn't negate the value of making gifts as PETs.

3. **Reviewing assets to ensure they are structured effectively:** especially between spouses, utilising "no gain- no loss" transfers of assets to the right ownership, so that assets aren't liable to unnecessary tax. Also ensuring

that life policies and pensions are written on the right trusts where appropriate.

4 **Reviewing business and farming assets to ensure maximising Business and Agricultural reliefs (BPR/APR) in lifetime and on death.** (i) holding in the best way to secure 100% (or, if not, 50%) relief where possible. Many assume all the assets used in a business get full relief, when it can be only 50% or nothing (e.g. land used by a trading company if you don't control that company!) (ii) to consider lifetime succession planning, passing on interests in a partnership or company, with the benefit of 100% relief; where capital gains allows, or holding over gains for CGT by gifting to a trust. Many are put off considering this, because of the current "double benefit" of 100% IHT and no CGT on death, even if family members might be rewarded for working hard in a farm or business to make it all work. It's at least worth exploring these two areas before it's too late.

5 **Gifting property assets that can be shared or are not needed.** Many people in Britain hold onto property, enjoying the security that land and homes offer, when gifts could be made to individuals or a trust. Second homes might, for example, be held in joint names with others who use them, but proper consideration is needed of both the reservation of benefit and pre-owned assets tax rules.

6 **An estate planning review with a financial planner, with the use of cash-flow modelling,** can be an immense help; to see how much could be gifted, or used in different ways, while still meeting the need for security and comfort. It is great if lawyers and tax advisers/ accountants can work well with financial planners, each bringing their own specialist know-how, on IHT mitigation for clients.

Will drafting - a key planning tool to mitigate IHT, but it is especially important in an age of stealth taxes! Well drafted Wills can help to maximise the value of all these:

1 **NRB:** still £325K, frozen (for 19 years) to 2028, and any transferable NRB (TNRB) from a late spouse.

2 **Residence Nil Rate Band (RNRB):** (frozen at £175K until 2028) if the right property interest is owned in the form to qualify (an appropriate trust on a first spouse's death may enable a second spouse's estate to claim); and the right people "closely inherit", either outright or through a suitable form of trust. IPDI (Immediate Post-death interest) trusts, which can have great flexibility, are important here.

3 **Spouse/ civil partnership exemption:** invaluable for use, at the right time, by outright gifts or life interest trusts. Further advice is needed if either have foreign domicile.

4 **BPR & APR:** which can often be "banked" on a death, by a trust, rather than left to a spouse.

5 **The 36% lower IHT rate** where 10% of a net estate is left to charity – a much under-used relief, especially as the 10% is after deducting any NRB/TNRB, so that in many cases a charity gift can increase the net estate.

All these frozen figures, with another four years at current levels, are designed to increase the amount of IHT raised. The £2m threshold for RNRB (above this, the allowance tapers away) is also frozen until 2028, meaning estates up to £2.7m (and over) can lose out. RNRB for two estates can save £140K IHT (or up to £280K if both a couple are widowed and plan carefully).

Spouses (married couples / civil partners) should consider a Discretionary Trust for the NRB (NRB D/T), any TNRB and RNRB (which can be secured by creating a special fund out of the Will trust within two years of death). By using these allowances on the death of the first spouse; assets are taken out of account on the second death, including for the calculation of the estate considered for the £2m RNRB threshold. The NRB D/T should include BPR & APR assets, to bank any relief, not least in case the farm or business is sold or gifted by the time of the second death.

Flexible Wills or variations? Many want a "simple Will" but risk missing the opportunity to mitigate IHT as well as adapt to changing personal and tax situations. Flexibility in a Will, using trusts, with a separate letter of wishes to guide the executors/trustees in the exercising discretion, can help adapt to new tax opportunities or issues like divorce, entitlement to benefits or health issues among beneficiaries.

Many anticipate doing a deed of variation within two years of death, a great option if things need to be put right or a better option implemented, but it's not sensible to rely on doing this. Circumstances and individual health may make it difficult for some to consent to changes, after the event, and there's always a risk of someone not cooperating!

Anyone leaving a property (or share of one) in trust, e.g. to a co-owner, should carefully consider the options of a life interest, right to occupy, discretionary trust or outright gift with an expression of wish, each with different IHT treatment to consider.

TL4 Private Client

2024 Upcoming Events

The Practitioner's Forum on Trusts in Divorce
15 February 2024 | The Dilly on Piccadilly, London

Landed Estates & Farm Tax Conference: The 3rd Edition
19 March 2024 | Central London

Private Client Circle of Trust Europe
21 - 22 March 2024 | Le Mirador Resort & Spa, Vevey

Private Client Next Gen Academy
23 April 2024 | Central London

Contentious Trusts Circle
25 - 26 April 2024 | Ashdown Park Hotel & Country Club, UK

Private Client Circle of Trust UK
2 - 3 May 2024 | Ashdown Park Hotel & Country Club, UK

Tax for Non-Doms: Annual Review
23 May 2024 | Central London

Private Client Advisory and Litigation Forum: Paris
12 - 14 June 2024 | Waldorf Astoria, Versailles, Paris

Contentious Trusts: Trusts Under Attack
27 June 2024 | Central London

TL4 & ConTrA Private Client Summer School: The Ultimate Insider's Guide
28 - 30 August 2024 | Cambridge, UK

TransAtlantic Tax & Estate Planning
17 September 2024 | Central London

Contentious Trusts Next Gen Summit
18 - 20 September 2024 | The Conrad Hotel, London

Private Client: Jersey
October 2024 | Jersey

Private Client: Guernsey
October 2024 | Guernsey

Mitigating and Managing HMRC Investigations for HNW Private Clients
October 2024 | Central London

Sport Stars, Influencers & Entertainers Tax 2024 3rd Annual Forum
December 2024 | Central London

MAKING USE OF INHERITANCE TAX GIFT EXEMPTIONS

Authored by: Sunir Watts (Partner) – Hunters Law

1. Background

Normally, when an individual (the 'donor') makes an outright gift to another individual this is known as a potentially exempt transfer ('PET') for inheritance tax ('IHT') purposes. The gift is only "potentially" exempt because there may be IHT to pay on the value of the gift if the donor does not survive it by 7 years (and to the extent that any other exemptions do not apply – see below).

If an individual makes a lifetime gift to a trust this is known instead as a lifetime chargeable transfer ('LCT') because the gift is immediately chargeable to IHT at a rate of 20% to the extent that the value of the transfer into trust exceeds the donor's available tax free slice, known as the "nil rate band" ('NRB') (currently frozen at £325,000 until April 2026).

In addition to the LCT, most lifetime trusts are also subject to what is known as the relevant property regime. This means that, subject to any available reliefs and exemptions, the trust will be subject to IHT charges every 10 years from creation (the '10-year charge') to the extent its value exceeds the NRB and also exit charges when capital is distributed from the trust ('Exit Charges').

There are several IHT reliefs and exemptions which can help to reduce the amount of IHT payable on a failed PET.

2. Application of the Nil Rate Band

On death, the NRB is applied first against lifetime gifts. It is often the case therefore that no IHT is payable on gifts made within the last 7 years of the deceased's life because they fall within the NRB.

If there is any unused balance of the NRB after deduction of lifetime gifts, it will be apportioned between the deceased's estate and any trusts under which the deceased had an entitlement to income, to the extent the beneficiaries of the estate and trust are chargeable beneficiaries. If, however, the beneficiary is a surviving spouse or civil partner, no IHT will be chargeable and the balance of the NRB will be

preserved and can be transferred to the surviving spouse's/civil partner's estate and utilised on their subsequent death. This is known as the 'transferable NRB'.

3. Taper relief

Taper relief can be claimed on gifts made at least 3 years before the date of death, but only to the extent that the cumulative value of all the gifts made by the donor within the last 7 years of his/her life exceeds the NRB (£325,000).

The rate of IHT (usually 40%) reduces depending on the time which has elapsed between the date of the gift and the date of death, as shown in the below table.

Years between gift and death	Rate of tax on the gift
3 to 4 years	32%
4 to 5 years	24%
5 to 6 years	16%
6 to 7 years	8%
7 or more	0%

4. The normal expenditure out of income exemption

The normal expenditure out of income exemption is a very valuable, and often underused, IHT exemption on lifetime gifts.

Where a gift qualifies for this exemption its value will immediately fall outside of the transferor's estate for IHT purposes and there is no need to worry about the '7-year rule'.

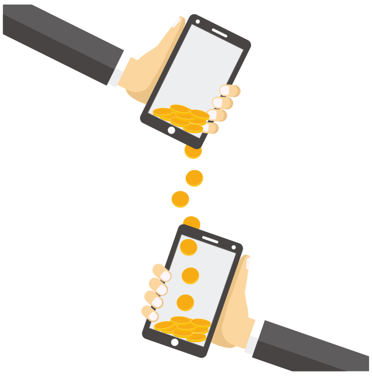
The exemption applies if all the following conditions are met:

1. The gift or transfer of value can be shown to be part of the donor's 'normal' expenditure
2. It must be made from income
3. The donor must retain enough income to maintain his/her normal standard of living.

4.1 What is meant by 'normal expenditure'?

HMRC's interpretation is that for expenditure to be normal, the gifts should form part of a regular pattern of payments. Examples of regular gifts or payments could include gifts on special occasions (such as birthdays or Christmas), the payment of grandchildren's school fees, an annual family holiday, insurance policy premiums, private healthcare arrangements and regular payments into a trust.

If a settled pattern of payments is not demonstrable over a period of time (say, for example, the donor dies before a regular pattern has been established), it can also be evidenced by proof of a prior commitment by the donor regarding future gifts.



4.2 Gifts must be made out of income

Examples of income includes salary, dividends, pensions, bank interest, business profit and rental income.

Ideally the income should be identified in the tax year in which gifts are made to demonstrate that there is sufficient income available. However, if necessary, income from an earlier year can be carried forward.

4.3 Retention of normal income to maintain his/her normal standard of living

To be eligible for the exemption, the income must be surplus income after the payment of tax and other expenses to maintain the donor's normal standard of living.

The donor's normal standard of living is a subjective test which will vary depending upon the circumstances of the donor at different times.

If the donor has insufficient income left to meet their usual expenses after making gifts, the exemption will not be available in full but may still apply to part of the gifts.

4.4 Record keeping

It is strongly recommended that the donor keeps a note/spreadsheet which clearly shows that the regular gifts being made are from surplus income after payment of their usual expenses.

Following the death of the donor, it will be the responsibility of the executors to prove that the gifts meet the conditions for exemption. They will be required to submit details of the deceased's normal income and expenditure, and the gifts for which the exemption is being claimed for each applicable tax year (up to a maximum of 7 years), in the IHT Account.

It is therefore useful to keep a record of your income, expenditure, and gifts in a similar format to that contained in the IHT Account, which should save your executors considerable time/expense when it comes to claiming the exemption on your passing. We can provide clients with a precedent spreadsheet specifically for this purpose.

4.5 Using the normal expenditure out of income exemption to build a tax efficient trust fund

The exemption can be particularly useful when an individual (known as the 'settlor') settles surplus income into a trust during his/her lifetime which accumulates over time. In this way the settlor can build up funds in a tax efficient manner, while maintaining an element of control over the funds (albeit they and their spouse/civil partner must be excluded from benefitting from the trusts).

Provided the payments to the trust are made from the settlor's surplus income and meet the above criteria, they will not be subject to the usual 20% entry charge to IHT for lifetime transfers to a relevant property trust, or the 7-year rule.

5. Gifts between spouses/civil partners

As a general rule, transfers between spouses or civil partners (whether made during lifetime or on death) are exempt from IHT. There is no financial limit on this exemption, provided both parties are UK domiciled and are recognised under the law of England and Wales as legally married or in a civil partnership. However, where the recipient of the gift is not domiciled in the UK but the donor is, the spouse exemption is restricted to the NRB (i.e. £325,000). The rationale for this is that assets moving from a UK domiciled individual to a non-UK domiciled spouse/civil partner are considered more likely to pass outside the UK IHT net, as IHT is charged on the worldwide assets of a UK domiciliary, but only on the UK assets of a non-UK domiciliary.

6. The annual exemption

The 'annual exemption' allows donors to make gifts cumulatively totalling £3,000 in any tax year, without such gifts being treated as a PET. It is possible to carry any unused annual exemption forward to the next tax year, but after that it is wasted.

7. Gifts for weddings/ civil partnerships

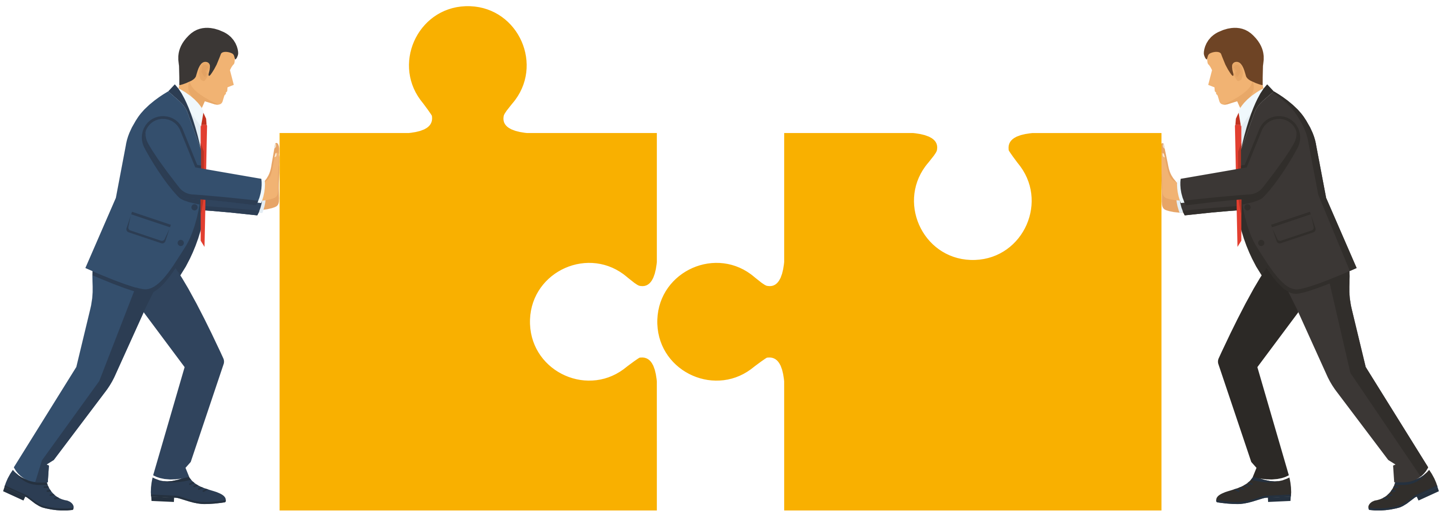
In addition to the above exemptions, an individual can also make a gift to someone who is getting married or entering a civil partnership without such gift being treated as a PET or eating into the other exemptions. The value of the exemption is dependent on the relationship of the recipient to the donor: the donor can give £5,000 to their child, £2,500 to a grandchild (or great-grandchild) or £1,000 to any other person without any exposure to IHT.

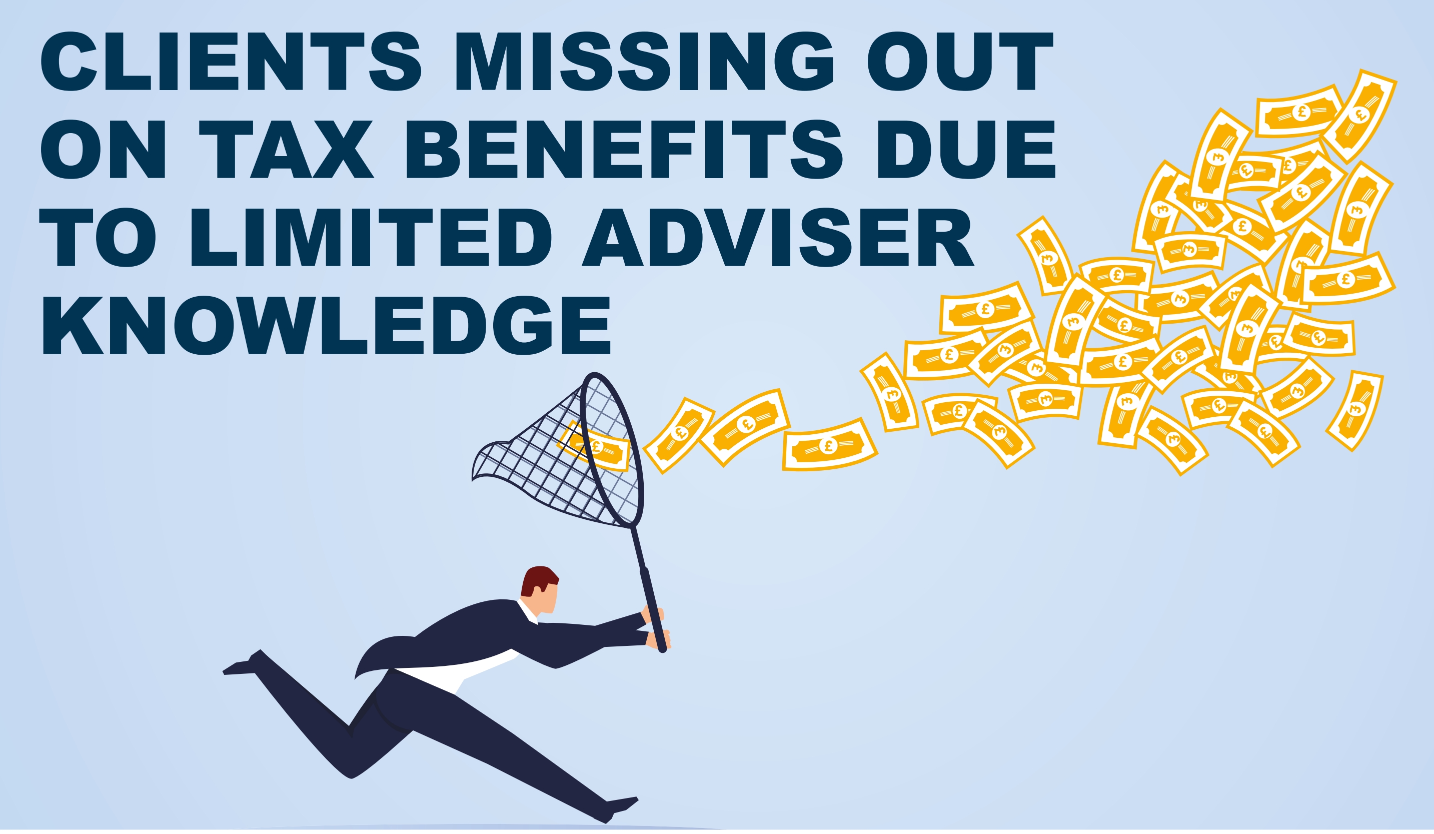
8. Small gift allowance

Finally, individuals can also make as many gifts of up to £250 per person as they wish each tax year, but the exemption cannot be applied to a recipient in tandem with another exemption. For example, if the donor had 9 grandchildren (one of whom was getting married) and had not made any gifts in the previous tax year, he could give the grandchild getting married £2,500, a further £250 to each of his other 8 grandchildren, and still have £6,000 (two years' worth of annual exemptions) available to gift to his children without any of these gifts being considered a PET.

9. Conclusion

Where you or your client have significant surplus income, the normal expenditure out of income exemption remains one of the most valuable IHT exemptions available, not least because there is no statutory limit on the amount of exemption that may be claimed.





CLIENTS MISSING OUT ON TAX BENEFITS DUE TO LIMITED ADVISER KNOWLEDGE

Authored by: Joe Crome (Head of Business Development and CAF American Donor) - CAF

More than one in five financial advisers do not know how to offer wealthy clients support on philanthropy despite its overwhelming potential and the tax benefits and implications associated with charitable giving.

New research by the Charities Aid Foundation (CAF) has found that just 5% of independent financial advisers (IFAs), wealth managers and planners are "very confident" about advising clients on philanthropy and half of all surveyed said the lack of confidence was due to an absence of training in the profession. A significant majority (73%) said they wanted more knowledge on helping their clients to give tax effectively.

We know that there is increasing demand from high-net-worth (HNW) clients for philanthropy advice, especially among younger generations.

A separate CAF survey found more than half (57%) of 18–34-year-old HNWIs and 49% of 35–54-year-old HNWIs believe an adviser could help with their philanthropy. However, it is not common for advisers to raise charitable giving with them - only a quarter (26%) say they have in the past.

Tax incentives for charitable giving have long played a crucial role to encourage individuals and businesses to support charitable causes and in doing so, they also ensure more money goes to charities. It should therefore be an imperative that clients are receiving this advice from professional advisers, consulting with specialist tax advisers where relevant.

The tax implications of giving money to charity may be the most practical reason for advisers to discuss philanthropy with clients, but there are also additional business benefits. Those who regularly give philanthropy advice found it helped to build on existing relationships with clients. Around 56% of advisers saw it as an opportunity to get to know their clients better, and nearly half said it makes them feel closer to their clients. Furthermore, a fifth (21%) drew a direct link between providing philanthropic advice and winning new business.

With advisers considering how to engage with the next generation and grow their business against the backdrop of the 'Great Wealth Transfer', philanthropy could prove to be a key point of difference in a competitive market. The next generation are expected to be the most significant donors in history, and how they approach their giving is expected to differentiate them from previous generations. As philanthropy advisers, we know it is essential to understand the motivations, values, and attitudes of clients, as well as the mechanisms available to them, to ensure philanthropy is as effective as it can be.

Tax Guide to Giving Gift Aid:

Gift Aid is a scheme available to UK charities and Community Amateur Sports Clubs (CASCs) which means they can claim back income tax from HMRC on a taxpayer's donation; effectively an extra 25% for basic rate taxpayers.

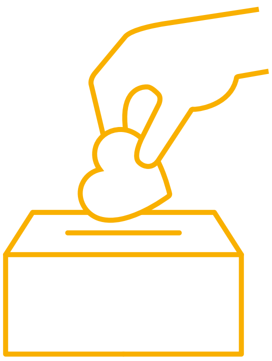
Each time an eligible taxpayer donates but forgets to tick the Gift Aid box, the charity misses out – collectively to the tune of £500 million each year.

A charity can claim Gift Aid when a taxpayer makes a monetary donation from their own funds and have paid UK Income and / or Capital Gains Tax during that tax year and make a Gift Aid declaration.

The amount of tax they pay needs to be at least equal to the value of Gift Aid the charity or CASC will claim on their donation(s).

Non-cash donations:

In the UK you can donate cash, shares, or property to charity and all three have different tax implications. For example, donating shares might be most tax-effective for the client, but the charity won't be able to claim the Gift Aid and could mean they receive less money. It's important to consider a client's personal circumstances and motivations before recommending which method is not only best for them, but also most practical for the charity.



Donor advised funds:

Donor advised funds (DAFs) are the UK's fastest-growing philanthropic giving vehicles. Acting as a one-stop shop for a HNWI's giving needs, donors make charitable contributions and then recommend for the DAF to be invested or make grants to organisations that they suggest over time. DAFs, for which there are a number of providers including CAF, offer several advantages over setting up your own charitable foundation, namely cost savings, tax-efficiency, flexibility, and ease of administrative, fiduciary, and reporting requirements.

When a client gives a donation into a DAF, it crosses the charitable threshold. It is not a bank account and the client can't withdraw money from it - it needs to be used for charitable purposes.

Gift Aid may be applicable on cash gifts to a DAF. In addition, clients who pay tax above the basic rate can reclaim the difference between the rate they pay and the basic rate of tax via their personal tax returns to unlock further benefits.

Legacy giving:

Tax advantages can make a significant difference to the beneficiaries of an estate. A gift to a UK charity in a Will is free from Inheritance Tax, meaning that the money is 'removed' from the value of a donor's estate before tax is calculated. In addition to the donation being tax free, charitable gifts can reduce the amount of tax paid on the rest of the estate. If 10% or more of the net estate is gifted to charity, then the rate of Inheritance Tax paid on the rest of the estate is reduced from 40% to 36%.

Gifts in Wills can therefore make a significant difference to the causes that donors care about the most, whilst having a positive impact on the remainder of their estate.

Payroll Giving:

Payroll giving is a highly tax efficient way of giving because donations are taken from pay or company/personal pension after National Insurance Contributions are removed, but before Income Tax is calculated and deducted. This means the donor gets tax relief, depending on the rate of tax they pay. So, for example, an employee's donation of £20 through this scheme costs a basic rate taxpayer £16, a higher-rate taxpayer £12 and an additional rate taxpayer £11; less if they are a Scottish taxpayer. Because the employee's tax contribution is then calculated on a lower amount, this could change their tax bracket and lower the amount of tax they ultimately pay.

CAF Give As You Earn, the UK's biggest payroll scheme, facilitates over £63 million of donations to charities each year, giving charities a regular income and reducing administration and fundraising costs. Donations made to charity through payroll giving aren't eligible for Gift Aid because they're taken from an employee's wages before tax.

Dual UK and US taxpayers:

Dual citizenship can complicate charitable giving and an adviser with knowledge of this area can be incredibly attractive to many HNWIs. Twenty years ago, CAF launched the CAF American Donor Fund (CADF), a DAF specifically for dual UK and US taxpayers, enabling donors to claim eligible dual tax relief on their giving.

PRACTICE MAKES PERFECT – OR DOES IT?

WHEN CAN YOU RELY ON NORMAL HMRC PRACTICE (IF AT ALL)?

Authored by: Kristina Volodeva (Partner) – Rawlinson & Hunter

Those of us involved in supporting private clients with their annual UK tax return submissions will, by the time that this is published, have finished another undoubtedly rather exhausting campaign culminating in the 31 January filing deadline. Many of the personal tax returns require some quite detailed and complex reporting; this, in turn, often raises the important question of whether a particular transaction or arrangement should be accompanied by a 'White Space Note' ('WSN') explaining what has happened and how it has been treated for tax purposes. It is no exaggeration to say that exercising this judgment call and then preparing a suitably worded note has become one of the most time-consuming parts of a tax practitioner's job.

When considering the tax treatment of any transaction, the first port of call must always be the legislation, supported by relevant case law. However, there is now a huge body of material published by HMRC offering its own interpretation thereof, in the form of Extra-Statutory Concessions, Statements of Practice, HMRC Manuals and the like. It is therefore a sensible precaution to check HMRC's published guidance when advising on a matter and ensuing reporting obligations. Where tax treatment on a tax return is at odds with published HMRC guidance, a WSN explaining this to be the case and why a particular approach has been adopted will provide the first line of defence against a future discovery assessment, in the (admittedly unlikely) event that the WSN itself fails to attract an enquiry into the tax return.

Having said all of this, is it then safe to assume that HMRC will accept the treatment, or reporting, of a transaction which is perfectly in accordance with its own published guidance? The answer to this rhetorical question should be, and in most cases is, 'yes' but on occasions, it is in fact 'no'.

What does HMRC say about it?

One of the reasons for the timing of this piece is that in June 2023 HMRC revised and updated its statement on when taxpayers can rely on HMRC guidance. This includes an explanation of when such reliance might be possible and the bar is set high:

1. It has to be reasonable for the taxpayer to expect HMRC to be

bound by its advice ('legitimate expectation'), and

2. It would have to be 'very unfair for HMRC to act in a different way from the advice and information given' - although the guidance then goes on to say that 'in some cases, there may be a strong reason for HMRC to act in a different way from the advice and information given'.

It is therefore worth elaborating on the inclusion in the updated guidance of the two tests alluded to above.

The meaning of 'legitimate expectation' has been considered in the courts. One example is the 2018 judicial review in the VAT case Vacation Rentals (UK) Limited v HMRC, which concluded that the facts and circumstances of the transactions under review fell within HMRC's guidance on the VAT treatment of card handling services. Although HMRC attempted to distinguish the taxpayer's transactions from the description of those covered in the guidance, these differences were considered to be of no material significance in terms of its intention and purpose.

Once 'legitimate expectation' has been established, it is for HMRC to prove that it would not be an 'abuse of power' if it seeks to apply a treatment different to its published view. The extent to which the taxpayer can be said to have relied on the advice and would suffer significant detriment if HMRC were to apply a different tax treatment are relevant. In the Court of Appeal case Aozora GMAC Investment Ltd, a distinction was drawn between HMRC guidance which simply provides an interpretation of the law (just as a tax adviser can) and guidance which spells out how, where there are uncertainties, HMRC will apply the law in practice.

It is possible to see these principles reflected in HMRC's revised statement, which is understood to be part of a wider review of the subject of reliance on HMRC guidance. So more may well follow.

What is abundantly clear though is that the law has absolute primacy in determining tax treatment.

Materials such as the HMRC Manuals, whilst extremely helpful to practitioners in gauging HMRC views, are likely to be regarded by the courts as simply guidance unless they go further and set out specifically and unambiguously how HMRC will deal with a particular matter in practice.

Frustration abounds……

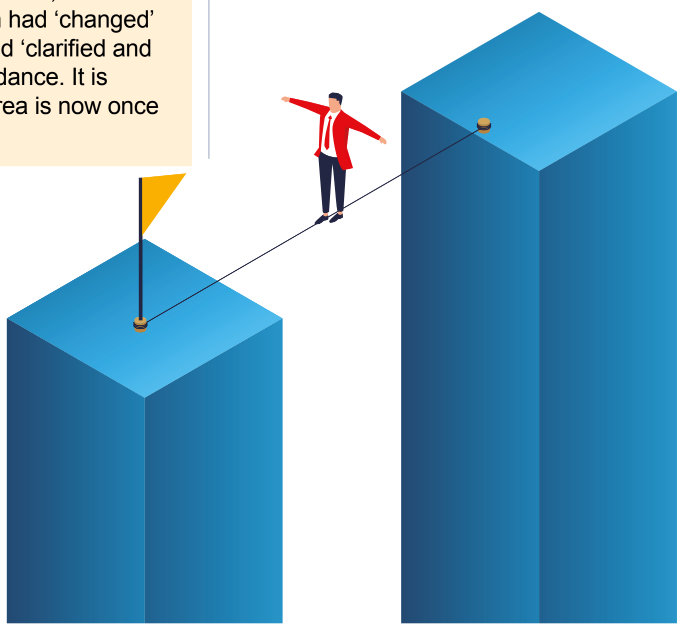
One quite frequent occurrence causing particular frustration for advisers is where HMRC chops and changes its guidance. Often, this will be because its interpretation of a particular matter changes - and it is of course HMRC's prerogative to take advice and come to a different view, just as it is the prerogative of the taxpayer to do the same. This, however, does not detract from the sense of unfairness when consideration has been given to (and comfort taken from) HMRC's published stance in undertaking a transaction or arrangement, only to discover that this has changed some time down the line. We have all been there - for example:

1. The farcical events in the aftermath of the Mansworth v Jelley decision
2. The situs of specialty debts
3. Quantifying the amount of collateral remitted when used as security for a loan used wholly or partly in the UK. At the time of revisions, HMRC denied that its position had 'changed' and asserted that it had 'clarified and corrected' existing guidance. It is understood that this area is now once again under review.

These are just a few examples which spring immediately to mind - there are no doubt more and you will all have your own bugbears.

Guidance on the guidance……

So, what can we usefully conclude from the above? I think the obvious message is to treat HMRC guidance advisedly: the Manuals are undeniably a very useful part of the tax adviser's toolkit, but for the most part only represent HMRC's analysis of the legislation at any given time and may – and do – change with little notice. Be familiar with HMRC's published material but base your tax planning and tax reporting on your own understanding of the law, bolstering this with advice from Counsel in more contentious or challenging circumstances. Establishing 'legitimate expectation' is a tough assignment and even if you get to that point, there is still no guarantee that HMRC will not be able to somehow override it.



UNDERSTANDING DOMICILE AND ITS IMPACT ON UK TAX EXPOSURES

Authored by: Andrew Cardwell (Director) – Equiom

Domicile & UK Taxation

Domicile is a vitally important concept in determining an individual's exposures to UK taxation, if there is some form of connection to the UK, be it their tax residence or assets that they own, for example. Non-UK domiciled tax status confers special UK tax advantages.

The Concept of Domicile

In English law, domicile should be distinguished from tax residence, albeit the two are interconnected. During an individual's minority:

1. First, the child is born with a domicile of origin, which is the domicile of their father (or their mother's domicile in certain circumstances), and

2. Up to the age of 16, their domicile of origin will be displaced by a domicile of dependency if the parent's domicile changes.

Beyond age 16, the individual now has free will to establish their own domicile of choice, which will be determined by two key factors:

1. Where the individual resides on an habitual basis, and

2. Their future intentions.

Based upon case law, if after the age of minority, the individual decides to take up residence in a new territory with an intent of remaining there permanently or indefinitely, then they would establish a domicile of choice in that new territory.

The law relating to the domicile is based in English common law and is inevitably complex and nuanced. The purpose of this article is not to examine that complexity, but rather to focus on the UK tax advantages for non-UK domiciled persons.

UK Tax Advantages

UK tax resident individuals who are domiciled outside the UK are afforded income and capital gains tax ('CGT') advantages under the remittance basis of taxation, namely:

1 Certain forms of foreign income, known as relevant foreign income, are only taxable when remitted to the UK, and

2 Capital gains realised on foreign assets are only subject to CGT when proceeds of sale are remitted.

For foreign domiciliaries who take up tax residence in the UK and who remain there year on year without establishing the intent to remain there permanently or indefinitely, the remittance basis of taxation is available without charge for the first seven years of tax residence. From the eighth year of tax residence there is an annual remittance basis charge which increases over time, up to and including the 15th year of UK tax residence. Thereafter the remittance basis not available due to the application of the deemed domicile rule, of which more later.

What constitutes a taxable remittance is slightly more complex than one might initially imagine. It envisages simple cash transfers that comprise the relevant foreign income and proceeds of capital gains transactions, but there are less obvious cases which we might describe more broadly as constructive remittances.

Great care should be taken, and UK tax advice should be sought if the remittance basis of taxation is to be utilised.

Perhaps the most significant UK tax advantage for the non-UK domiciliary is protection from exposures to inheritance tax ('IHT'). Foreign assets are outside the scope of IHT for as long as an individual remains domiciled outside the UK.

But here we must introduce a further concept of domicile which is enshrined in statute law, the deemed domicile referred to earlier, which is relevant to the individual's IHT position and, indeed, their UK income tax and CGT exposures.

Deemed Domicile

Deemed domicile has, until recently, only had application for IHT purposes. The existing rules were amended and expanded with effect from 6th April 2017, and the key points to be borne in mind are:

1 Long-Stayers - an individual who has been UK tax resident for at least 15 out of the 20 previous tax years, they will be considered to be deemed domiciled (in other words, for somebody who moves to the UK and continues to be UK tax resident thereafter, deemed domicile attaches at the start of the 16th tax year of tax residence);

2 UK Returner – if an individual was born in the UK with a UK domicile of origin, but had managed to shed their UK domicile of origin in favour of a domicile of choice elsewhere, before later returning to the UK to take up residence, they will be deemed domiciled on their return, even if the move is temporary and they continue to retain their domicile of choice overseas; and

3 The UK Leaver – the three-year rule dictates that UK domiciled individuals who leave the UK to take up residence elsewhere will continue to be deemed domiciled for three years after shedding their UK domicile in favour of a domicile of choice.

For a returner, there is one tax year of grace for IHT purposes, but relevant foreign income and capital gains are taxable as they arise from the first tax year of resuming UK residence.

Once a foreign domiciliary becomes deemed domiciled, he or she joins the rank-and-file of UK taxpayers; there are no special tax advantages to their status, even if they continue to be treated as domiciled abroad under common law principles.

Trust Arrangements

For the wealthy and well-advised individual who is approaching the point of becoming deemed domiciled, there are measures that can continue to afford protection against UK tax exposures.

Whilst there might be ideas that can insulate against the imposition of UK tax in the shorter term, such as non-qualifying life policies or IHT insurance, offshore trust arrangements provide a more permanent solution to these issues.

Trust arrangements made by foreign domiciled individuals before they become deemed domiciled, via the transfer of foreign assets onto a settlement, confer these longer-term advantages, viz.:

1 The trust is colloquially termed an excluded property settlement, meaning that the assets held on trust are permanently outside the scope of IHT for the lifetime of the trust, providing:

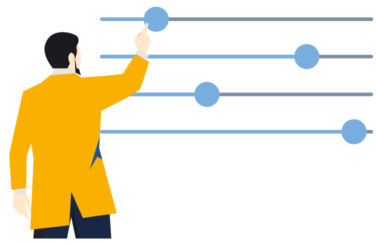
a. The trustees do not hold UK situated assets directly and,

b. With minor exceptions, no further funds are added to the trust by the settlor after he or she has become domiciled in the UK under common law or deemed domiciled under the special statutory rules;

2 Foreign income and all capital gains (other than those arising on disposals of UK real estate) arising to the trustees or underlying companies are not taxed immediately in the UK, which allows for a gross accumulation of funds.

UK income tax and CGT cannot be avoided altogether, these amounts would be taxable in future if UK resident beneficiaries receive distributions or any form of benefit from the settlement, such as an interest-free loan.

These trust arrangements are referred to as protected settlements and their UK tax advantages can live on long after the remittance basis has become unavailable under the deemed domicile rule.



AN OVERVIEW OF THE UK TAX SYSTEM FOR INDIVIDUALS, WITH CURRENT CHALLENGES AND OPPORTUNITIES

Authored by: Natalie Martin (Private Client Director) and Grace Onions (Senior Associate) – PwC

The UK's tax system is highly complex. High Net Worth Individuals (HNWIs) and internationally mobile individuals must comprehend the complexities of this system to ensure their assets are held in a way which both meets their commercial objectives and is compliant with tax rules.

Media coverage of tax in the UK has increased over recent months and we expect to see continued discussion on UK tax policy in the near future. We know one of the most important aspects of any individual's plans, whether in relation to business interests, investment strategy or wider family succession objectives, is certainty. Tax outcomes are, inevitably, an important part of this wider discussion.

The next UK General Election, which must be held by January 2025, inevitably means that there are elements of uncertainty around the future government and tax policy.

It is important for HNWIs to understand the potential areas of taxation which could be subject to change, as well as understanding the current fiscal rules. This brief note aims to provide a high-level overview of a few key areas to consider.

Overview

Individuals are liable to tax in the UK if they are tax resident in the UK, if they receive certain types of UK income or hold UK assets. The UK tax system includes income tax and capital gains tax ("CGT"), Inheritance tax ("IHT"), Corporation tax and Value-added tax (VAT).

Non-domiciled individuals ("non-doms") have a unique position, with access to several tax regimes:

1. The remittance basis of taxation - whilst UK resident individuals are taxedon their UK source income and capital gains, foreign income/gains of non-doms are subject to UK taxation only to the extent they are "remitted" into the UK.
2. The excluded property regime, which exempts non-UK assets from IHT.
3. Business Investment Relief ("BIR") which allows non-doms to bring non-UK funds into the UK to invest in unlisted trading companies.
4. Overseas workday relief ("OWDR"), which allows non-doms to exempt non-UK working days in their first three years of UK residency.

These regimes are not available indefinitely. If an individual is considered to have moved to the UK permanently, they acquire a UK domicile. Alternatively, once they have been UK tax resident for at least 15 years, they are considered deemed UK domiciled for tax. In either situation, they are no longer able to access these regimes.

There is ongoing political discourse around the non-dom regime in the UK and there is a likelihood that the regime may be significantly, depending on the result of the next general election.

Annual considerations for UK-based HNWIs

There are certain well understood tax reliefs that UK taxpayers may wish to consider flexibly on an annual basis. These include the Gift Aid regime which offers income tax relief at up to 25% on donations made to qualifying UK charities and certain incentive schemes. These aim to encourage investment in the UK through income tax and CGT relief. Each incentive has different qualifying criteria.

As there are additional complexities for both of these reliefs, we recommend individuals take professional advice to ensure they are compliant.

There are also a variety of ways for UK based individuals and families to structure their assets for the longer term. Some common examples are briefly discussed below.

Business Property Relief (BPR)

BPR is a relief which reduces the value of certain assets in an individual's estate (by either 100% or 50%) for IHT purposes. Broadly, these assets must relate to a trading company which fulfils certain requirements. In the case of a complex structure, care must be taken to ensure that all assets are fully compliant with rules, as certain categories of assets are ineligible (such as large cash balances, or rental properties).

Family Investment Companies (FICs)

A FIC is a private company which allows families to hold and manage assets collectively, providing flexibility in wealth distribution and potential tax efficiencies. Most dividends received in the FIC are exempt from UK corporation tax, although gains on disposals are taxed at the corporation tax rate of 25% (as opposed to 20% if held personally).

A FIC can be structured in a flexible manner, allowing families to pass wealth to a younger generation, whilst retaining control in the founder's hands.

Placing assets in a FIC is considered a disposal for CGT, so consideration needs to be given to any "dry" tax charge, as well as ongoing running costs. Additionally, due to specific legislation regarding UK property, FICs rarely hold land or property.

Family Trusts

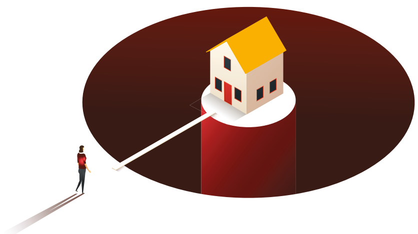
Trusts are a flexible vehicle in which to hold family assets for the long term. A Trust arises when the legal title of an asset and the "beneficial owner" (or "beneficiary") are different persons, so assets (such as company shares or property) can be held by trustees for the benefit of future generations. Again, the trust can be structured flexibly as required, so the beneficiaries may or may not be entitled to receive trust income as it arises.

For UK domiciled individuals, trusts are often established for reasons other than tax, as trusts are seen as useful vehicles to protect family wealth and to ensure an orderly succession.

For non-doms, trusts are often very tax efficient. At a high level, if a non-UK trust is settled with non-UK assets by a non-dom, then this trust is considered "protected" and not within that individual's estate for IHT purposes even once they themselves are considered UK domiciled for tax. The individual (and other UK resident beneficiaries) may be subject to income tax or CGT if they receive trust payments.

Unless the trust is an excluded property (or protected) trust, then there is an IHT charge on creation (unless the assets qualify for BPR, as above), at 20%, and at 6% every ten years. Any trust resident in the UK will also be subject to income tax and capital gains tax on its assets. There are costs associated with running a trust, so there needs to be certainty that the trust will be useful in the long-term.

It is also common for individuals to combine FICs and trusts; for example, a trust which holds shares in a FIC, which then holds the underlying assets.



Conclusion

Individuals navigating the UK tax system face challenges and opportunities requiring strategic thought and professional guidance. Individuals and their advisors need to consider circumstances holistically to ensure that any decisions taken to maximise tax efficiency also takes into account commercial circumstances, changing legislation, succession planning and other considerations. It is also important to note that the UK has a significant amount of anti-avoidance legislation which needs to be considered with any wealth structuring.

ESTATE PLANNING FOR US/UK CLIENTS: TAX TIPS AND TRAPS

Authored by: Camilla Wallace (Partner) – Wedlake Bell

This article considers tax planning issues that UK advisors need to be aware of where they have clients connected to the US. Separate US advice will likely be required but the below should help with issue spotting.

US connections

It may be that a client's US connections are not immediately obvious but when advising on tax or estate planning, it is vital to ask questions to understand the client's and their family's residence/domicile background so as to uncover any US (or other) connections.

A client will have "US connections" if they:

1. Are a US citizen or green card holder;
2. Are tax resident in the US;
3. Are married to a US citizen; or
4. Have US resident or citizen beneficiaries.

Income and capital gains

US citizens are required to file US tax returns in respect of their worldwide income and gains. If a US citizen is tax

resident and domiciled in the UK, they will also be subject to UK income tax and capital gains tax ("CGT") on their worldwide assets. This would ostensibly result in double taxation on the same income and gains but the 2001 US/UK Double Taxation Convention provides relief provided this is claimed.

Coordinated US/UK legal and accounting advice will be essential to make sure the client's tax returns in both jurisdictions correspond, double taxation relief is correctly claimed and full advantage is made of tax exemptions in either jurisdiction.

Tax on inheritances and gifts

The concept of "domicile" determines liability to inheritance tax ("IHT") in the UK, and estate tax and gift tax in the US. The definition is not synchronised so it is possible for a client to be simultaneously domiciled in both the UK and in a US state, and advice will be needed to avoid double taxation (both taxes have a main rate of 40%).

From a UK perspective, it can be useful for a client to have a "domicile statement" which can be kept under review and produced to HMRC as evidence of the client's domicile status when needed. A US advisor may recommend a similar approach.

Where a client with US connections has a UK spouse/civil partner (the word "spouse" hereafter refers to either term), careful planning is needed in respect of the availability of the IHT spouse exemption or federal estate tax marital deduction both of which potentially allow assets to pass between spouses tax-free. In the UK, where assets pass from a UK to a non-UK spouse, the IHT spouse exemption is limited to the IHT nil-rate band (currently £325,000). In the US, where assets pass from a US to a non-US spouse, the estate tax marital deduction is also limited – to $185,000 for US tax year 2024. These limitations can, however, be mitigated with coordinated US/UK Will and succession planning advice as explained below.

Wills and succession planning

In situations where a UK spouse dies before their US spouse, the UK spouse's executors could make an election for the US spouse to be treated as UK domiciled for IHT purposes. This would allow the full IHT spouse exemption to be claimed on the UK spouse's death; however, any assets that remain part of the US spouse's estate on their death will be subject to IHT in full at that point. The US spouse can reduce this IHT liability by carrying out estate planning during the rest of their lifetime. The UK spouse would be advised to leave a letter of wishes addressed to their executors in respect of such an election.

Where a UK spouse is predeceased by their US spouse, the US spouse's Will could include a qualified domestic trust ("QDOT") for the benefit of the UK spouse. A QDOT enables the estate tax marital deduction to be claimed and the tax to be deferred to the death of the UK spouse. Capital distributions form the QDOT trigger estate tax, however, unless made on account of hardship.

The terms of the QDOT should be drafted or checked by a US lawyer as there are key provisions that must be included in order for the trust to qualify as a QDOT, one of which is that there must be a US trustee.

Tax related to home ownership

In the UK, the principal home is often exempt from CGT on disposal; this is not the case in the US where any gain realised by a US citizen in excess of $500,000 (or $250,000 for single taxpayers) is subject to US federal CGT. This is a tax trap that can catch the unwary (Boris Johnson included), but mitigation planning could be put in place if US/UK advice is taken prior to disposal.

Taxation of trusts

Clients with US connections are often advised by their US lawyers to set up a "revocable living trust" or "grantor trust" for their US assets during their lifetime. This serves many functions including avoiding the need for US probate for the assets within the trust as well as allowing details of the assets to remain private and not publicly disclosed as part of the grantor's estate on death. If the client is UK domiciled, advice should be taken prior to set up as the trust could be classified as a "relevant property" trust for IHT purposes. The resulting IHT charges can be circumvented by drafting the trust as a "bare" trust for UK tax purposes.

Clients with US connections who are beneficiaries of a non-US trust need to be aware of the US "throwback rules" for "foreign non-grantor trusts".

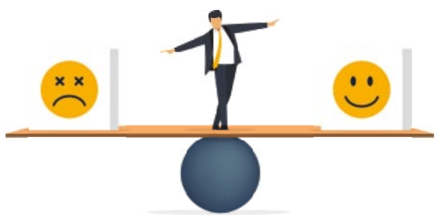
Under these rules, distributions to the US beneficiary could be taxed at penal rates of US tax if the distribution comes from income that has accumulated in a prior US tax year and exceeds the trust's current distributable net income. This can be mitigated but it is essential that the issue is spotted on creation of the trust so that the trustees get specialist US input on this aspect of the trust's management.

Insurance and tax issues

Standard US estate planning can see the use of an irrevocable life insurance trust to shelter value from tax on death. Unless the policy is a "qualifying policy" under UK law, however, UK income tax will be payable on the chargeable event gain triggered upon the death of the insured and when distributions are later made to UK resident beneficiaries.

Closing comment

The above are a few examples of the tax complexities that can plague US/UK clients and why it is a good working assumption that any kind of tax planning in one jurisdiction will always require a tax health-check in the other.



THE UK REGISTER OF OVERSEAS ENTITIES: A CLUNKY TOOLKIT

Authored by: Neil McPartland (Associate Director) – Saffery Trust

The UK Register of Overseas Entities, established under the Economic Crime (Transparency and Enforcement) Act 2022, is intended as a tool to prevent money laundering through UK property.

Implemented in an impressive 109 working days in response to Russia's invasion of Ukraine, its application to overseas entities poses several challenges, particularly for trustees. The dazzling speed (in legislative terms) of its introduction may have garnered awards in the corporate register world, but left those actually required to use it with the sense that the makers ran out of time to draft the instruction manual and forgot to insert the final few screws before shipping.

In practical terms, the legislation requires qualifying overseas entities which either own, or wish to buy, sell, or transfer property or land in the UK to register with Companies House and declare the registrable persons connected with the transaction. Notably it also applies to transactions which took place as early as 1999 in England and Wales (2014 for Scotland).

This retrospective nature of the enforcement left no opportunity for those affected to plan for or mitigate the administrative burden and financial cost associated with submitting a filing.

A stipulation of the Act is that overseas trustees must engage a UK agent for submissions. Conveniently, any professional that is supervised under the Money Laundering, Terrorist Financing and Transfer of Funds Regulations 2017 will suffice, although this results in a broad spectrum of qualifying agents with wide-ranging costs, as well as interpretations, of the requirements.

Practical anomalies also exist, notably in reporting for ownership structures. For example, in cases where a company holds property as a nominee for a beneficial owner, the current legislation focuses solely on the legal owner of shares. Consequently, the actual beneficial owner remains undisclosed.

Perhaps more bizarrely, where a trust is involved in the property-holding structure, its details will normally need to be provided (except for the example in the next paragraph), and this is despite the existence of the Trust Register.

Whilst the Trust Register is non-public and has a slightly different purpose, seeking to capture any foreign trustees with existing or potential UK tax liabilities, it also applies to trustees that own properties directly in a trust, and the information captured on the trust is almost identical. Therefore, a trust may end up being registered on two separate, yet almost identical registers (one public, and one not) by owning UK property, which seems a little redundant.

Furthermore, in cases where a property is held directly by a trust, a strange application of the reporting requirement focuses solely on the corporate trustee as the property-owning overseas entity and asks reporting trustees to ignore the key beneficial actors, i.e. the settlor and beneficiaries of the trust, and to simply report the corporate trustee and its owners. This has led some to scratch their heads over whether the Register achieves its original AML objective, as it somewhat clouds the water on beneficial ownership.

A sensible application that we have observed, is where a property is held by a company underlying a trust. In this case the requirement is to disclose all relevant actors, these being the trustee, settlor, beneficiaries, and protector(s).

However, only the trustee and the protector(s) are shown publicly, the rest are made known to Companies House and HMRC but cannot be seen on the Register. From a common privacy perspective this seems to make sense.

A final, and pertinent, concern is the absence of a procedure to deregister companies from the Register upon their liquidation. The original 'A' team responsible for the lightening quick implementation of the Register seem

to have been replaced by a somewhat slower substitute team, as efforts to rectify some of the original problems have encountered significant delays.

When approached, Companies House advised us that they are currently working on the process that will allow an entity to update its information and to submit an application for removal, however this is not yet available.

With no resolution to this issue in sight, trustees should beware of sustained annual costs and additional reporting post-liquidation.

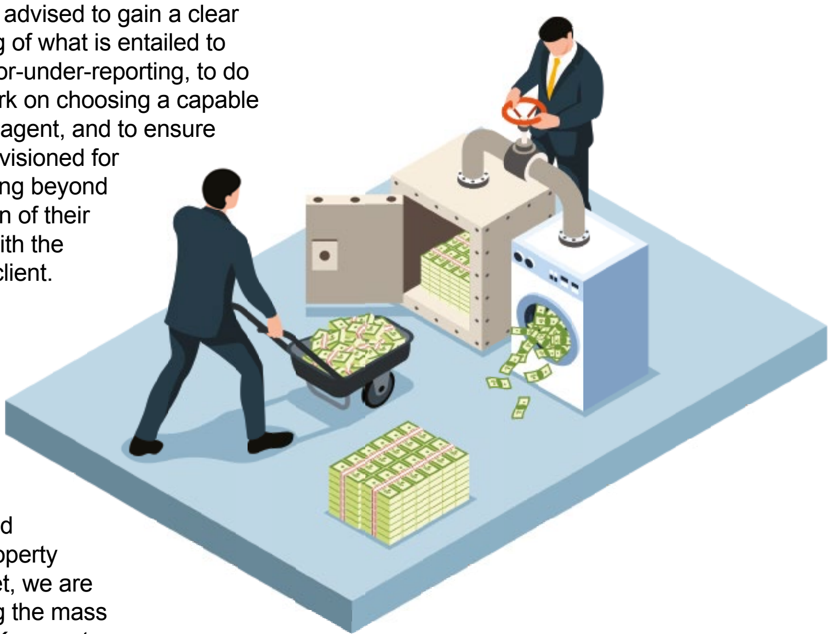
Despite strict financial and ultimately, criminal, penalties applying to those who do not comply with the reporting, a general lack of compliance with it, and of ensuing penalties being issued, has been widely reported in the press.

As of May 2023, it was suggested that over 50,000 foreign property owners had yet to comply. Whether such lack of compliance is intentional, a result of ill-informed overseas owners, or the result of a general lack of clarity on how to apply the rules remains to be seen. However, given the factors outlined above, an overseas trustee would be well advised to gain a clear understanding of what is entailed to prevent over-or-under-reporting, to do their homework on choosing a capable and informed agent, and to ensure they have provisioned for trailing reporting beyond the termination of their relationship with the entity and/or client.

The ever-changing UK regulatory landscape has, undoubtedly, amplified the complexity and cost of UK property ownership. Yet, we are not witnessing the mass disposal of UK property across our clients' structures that might be expected. In fact in December, premium realters Knight Frank reported that in the 12 months from December 2022 175 homes in London were sold at over £10m – the highest figure for 8 years.

This appetite for continued investment in the UK property market may be a reflection that the related, and increasing, administrative burdens can be shouldered by experienced trustees, rather than by the owner themselves.

This shift in the balance of responsibility allows property owners to focus on their core activities, while relying on the expertise of service providers to navigate processes and ensure compliance with evolving regulations.



TAX TRAPS FOR OFFSHORE TRUSTEES

Authored by: Thomas Barker (Associate Director) – Charter Tax

The UK tax system is full of traps for the unwary, and this is perhaps no more so than for trustees of non-UK trusts.

We hope in this summary to highlight some of the main traps which could be around the corner – and how to avoid them.

UK property and the ten-year charge

Most trustees understand the principles of the ten-year charge on trust assets. Where the trust was settled by a non-UK dom, the charge is only on UK assets and it may be that the trustees have a system to flag ten year anniversaries so relevant IHT compliance can be completed in a timely manner.

The rules on what constitutes an asset which is subject to this ten-yearly charge of up to 6% changed in 2017, and these rules may be less well understood. It would be easy to imagine that the systems in place do not flag ten-year charges coming up since 2017 which are now within the new rules but weren't caught before.

Assets within the IHT charge since 2017 include:

1. UK residential properties held within a non-UK company
2. Loans to companies where the loan is used to buy, maintain or enhance UK residential property
3. Loans to beneficiaries (whether from the trust or company) where the beneficiary uses the funds on UK residential property
4. The proceeds from property related loans repaid in two years before a ten-year charge.

As can be seen, the trustees may need to gather more information about loans so that they can record whether these loans are potentially chargeable to IHT at the ten year anniversary.

One further aspect to be aware of is that where the settlor can benefit from the trust, the above property interests are in their estate for IHT purposes and would be charged to tax at 40% should they die at a time when the trust owns the interests. This is true even for non-dom settlors.

Deemed dom settlors and trust tainting

A non-UK domiciled but UK resident settlor of a non-UK trust is taxable on UK income of the trust under anti-avoidance provisions.

Non-UK income of the trust structure is protected from the settlor charge provided that the trust is not "tainted".

Tainting occurs when a settlor who is deemed dom in the UK (has been UK tax resident for 15 out of the prior 20 tax years) adds value to the trust – so where the settlor has not yet been resident in the UK for 15 years, these rules are not relevant.

Adding value to the trust could be as straightforward as adding property to a trust after the deemed dom date, but this is unlikely to happen in this way because it would be detrimental from an IHT perspective. More often than not, adding value will occur inadvertently in one of the following ways:

1. The settlor providing services to the trustees and not charging a market rate
2. The settlor paying trust expenses not on the exemption list
3. Loans from the settlor to the trust / underlying company at less than HMRC's official rate of interest
4. Loans from the trust / underlying company to the settlor at higher than HMRC's official rate of interest.

Note that for loans to meet the criteria, the interest needs to be physically paid each tax year rather than accruing.

These rules are draconian in that they affect the whole trust from the point it is tainted and there is no way to "un-taint" it once tainted. If the trust is tainted by just £1, all income and gains of the trust will then be chargeable on the UK resident settlor from that point on.Where there are loans to or from a settlor who is deemed dom, or approaching the deemed dom date, it will therefore be worth reviewing these to see if the settlor is deemed UK dom, and whether there could be an issue with tainting the settlement.

Trustee borrowing and Schedule 4B

Beneficiaries receiving benefits or distributions from an offshore trust are potentially liable to UK tax on the accumulated income and realised gains of the trust. The rules for matching trust income and gains to distributions is an entire topic of itself and we don't go into the detail here.

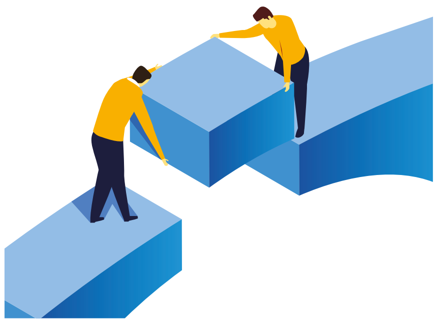
There is a little-known rule where a distribution is made to a UK beneficiary at a time when the trustees have borrowed either from the underlying company, or indeed from another trust or third party lender. This rule means that even unrealised gains of the trust can be charged to tax on a UK beneficiary who receives a benefit / distribution.

While this is not a tax issue which affects trustees directly, it is worth being aware of the potential risks to UK beneficiaries who could be subject to a higher-than-expected tax.

Other property related matters

UK land and buildings create other potential tax and administrative matters for trustees to be aware of, and acronyms to learn:

1. NRCGT. The disposal of land or buildings needs to be reported to HMRC, and there may be a corporation / capital gains tax liability on this. In addition, the disposal of shares in a company which holds UK land and buildings could also generate a tax liability if at least 75% of the company's assets relate to UK property.
2. SDLT. When there is debt on UK property, care needs to be taken if the property is to be moved within the structure because without the correct approach, there could be an SDLT charge.
3. ROE. Non-UK companies and professional trust companies need to file an annual declaration with the Register of Overseas Entities in relation to their ownership of UK property.
4. ATED. This is perhaps the best understood and UK residential property worth over £500k which is not rented out is subject to an annual charge if held in a company.



Summary

UK tax is an important aspect of managing an overseas trust and staying up to date with the principles will enable trustees to keep their trusts compliant, and not fall foul of traps created by successive anti-avoidance rules.

Regular review of trusts in light of changing rules is highly recommended.

Authored by: David Kilshaw (Head of Private Client Wealth Solutions) - Rothschild & Co

Introduction

Many individuals choose to hold their investments in a 'wrapper'. There are several reasons to use a wrapper and it is important that an individual selects the most appropriate one. It is the theme of this article that this requires an individual's advisers to work as one to guide the individual in the selection process.

Why use a wrapper?

There are many reasons to wrap investments. The most obvious is tax efficiency—a wrapper grows investments in a lower tax (often tax free) environment until the individual disposes of an interest in the wrapper.

Perhaps the second most common reason is succession planning, particularly where (for example) a parent wishes to vest wealth in their offspring, while not giving the next generation unfettered access to the wealth.

Other reasons include the ability to build structures around the wrapper such as family constitutions or other governance structures or to start the process of involving junior family members in investment decisions.

It is the wide variety of reasons for using a wrapper that generates the need for advisers to work as one. The tax adviser will need to fit the wrapper to the tax profile of the client; the trust or corporate lawyer will need to tailor it to a client's specific needs (eg drafting the articles for a FIC (see below)) and an investment adviser can ensure the wrapper compliments the investment profile.

It is when a wrapper is selected by one adviser, without a team approach, when things go wrong. If advisers come together as part of the selection process, they can challenge each other and the client benefits.

Family Investment Companies (FICs)

Perhaps the most discussed wrapper in recent times is the FIC. The formation of a FIC illustrates how advisers can work together for an optimal outcome but also how things can go less well when they don't.

FICs are popular because of their simplicity and because many individuals are familiar with companies. At their simplest, FICs involve the creation of a UK company of which the individual is a shareholder and to which the individual lends money which is then invested by the FIC.

The FIC benefits from corporation tax rates and the individual can extract funds without a personal tax charge via repayment of the loan. The FIC can be tailored to an individuals' wider needs by the creation of (say) growth shares for family members or regulating when and how dividends are paid.

A properly thought through FIC is a robust solution. But FICs are in danger of becoming an ''off the shelf '' solution and short cuts cause problems. Unless the advisers come together at the outset there are risks of problems surfacing later. To take two examples. A FIC may be created by a father for his 2 sons, with the articles of the FIC determining when they benefit. But what happens if (say) ten years later the 2 sons cannot agree on the purpose of the FIC or if one son wants to take his share for a new business venture. If the advisers liaise at the outset, there may be a family constitution or clear strategy to deal with such eventualities. If there has not been collective thinking, the FIC may overtime become a trap and a tax inefficient one at that. Similarly, the design of the FIC and the proposed investment strategy for its funds should be aligned at the outset (not least because while dividends received by the FIC will normally be tax free its gains will be taxed at 25% instead of the personal rate of 20%). Certain assets (eg gilts) are better owned outside a FIC due to the loan relationship rules.

Offshore bonds

Offshore bonds are also popular as a wrapper. They enable funds to grow tax free and have the advantage that if an individual later wishes to make a gift of a part of the bond this can (with care) be achieved tax free, whereas the transfer of an interest in a FIC would trigger a CGT charge. As is widely known, an individual can take out of the bond a sum equal to 5% of his initial premium each year. This is often seen as attractive by investors, although, of course, the client is only getting his original investment back tax free.

The main downside with a bond is that when the client does seek to extract monies from the wrapper there is an income tax liability. The given answer to this in many cases is for the individual to persuade him or herself that they will go offshore to encash the bond tax free. This is an example of where the individual should consult his full circle of advisers before committing to a bond.

It may be the correct solution, but the potential investor needs to understand in advance not only the tax rules of going offshore but the practicalities. The individual may welcome experience of how many bondholders do actually go offshore.

Trusts

Trusts are perhaps the most flexible wrappers, and a strong trustee and protector can aid families with a wide range of governance issues. For non-doms, they should always be on the agenda and can provide a tax-free environment even when the settlor has become deemed domiciled in the UK. Regrettably, they can seldom be used for UK domiciled individuals due to the inheritance tax charge which (in the absence of a relief) arises on creation.

OEICS and PUTS

These provide a tax -free environment and a CGT charge on unwinding the wrapper. They can be combined favourably with other wrappers –eg a SICAV can be held within a FIC to provide a tax deferral on gains otherwise taxed at 25%.

Conclusion

The choice of wrappers can be overwhelming. To achieve the optimal outcome, in both the short term and the longer term, tax, legal and investment advisers must all come together.

David is head of wealth solutions at Rothschild & Co, where his role is not to provide tax advice but to work with clients and their legal and tax advisers.

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USING LIFE INSURANCE AS A TAX PLANNING TOOL

Authored by: Holly Hill (Senior Associate) – John Lamb Hill Oldridge

Death and taxes are two guarantees for clients. Given the nature of private client work, it's highly likely that inheritance tax (IHT) will be one of the taxes considered as part of an estates holistic planning strategy. Life insurance is one solution that advisers should be considering: both in terms of value for money but also, and more importantly, because insurance provides the liquid cash required to pay the tax bill.

Insurance can be highly effective when used as part of the client's cash flow management profiling on death. In this article, we demonstrate how life insurance can be used in three tax planning scenarios.

Estate planning for IHT

Despite the varied reliefs available many individuals still face a large liability when passing their assets to the next generation. But as house prices continue to rise, impacting significantly on the value of personal estates, HMRC are collecting record numbers of IHT receipts. The Office for Budget Responsibility has forecast that in 2026-27 they will be taking £8.1 billion in IHT revenue, up from £5.4 billion in 2021. As a result, more of us need to start taking the 40 per cent tax seriously.

Life insurance can offer an affordable solution to inheritance tax planning. Not only does it protect illiquid assets, but, if the policy is placed into trust, the proceeds will be accessible pre-probate and can therefore be used to pay both the probate costs as well as providing a cash lump sum to pay off the IHT due immediately on death. This allows surviving family members to proceed swiftly with an application for probate without having the stress of searching for the cash themselves.

One of the most common policies used for IHT planning is a joint-life second-death, term to age 90 contract.

These structures are ideal for married couples because they are cheaper than single life contracts and take into account the inter-spousal exemption, where unlimited assets can pass to the surviving spouse free of IHT and insure against the liability that will arise on the death of the surviving partner.

'Term to age 90' means that the policy will pay out on the death of the second life assured providing that both deaths occur before the older life reaches, or would have reached, age 90. In the UK market, the longest term to age that can be purchased is to age 90. However, for clients seeking more comprehensive term cover, a term to age 99 contract can be sourced in the offshore market. The extra 9 years of cover works well for couples with a large age gap, or who have a family history of longevity beyond age 90.

For permanent protection, the alternative to a term to 90 policy is a Whole of Life contract. These policies guarantee to pay out whenever the life assured dies, irrelevant of age or circumstance. They are the most thorough form of cover but, as a result of the increased risk to the life office, tend to be significantly more expensive.

Current indicative costs for £1million of cover:

Single Death			
Age	10 years	Term to 90	Term to 99
30	£235	£1,470	£2,465
50	£1,130	£4,370	£8,230
70	£7,365	£14,655	

Joint Life Second Death			
Age	10 years	Term to 90	Term to 99
30	£200	£1,525	£1,835
50	£570	£3,390	£4,585
70	£3,430	£10,725	

Gifts and the 7-year tail

Gifts from one generation to the next are always categorised as Potentially Exempt Transfers PETs) or Chargeable Lifetime Transfers (CLTs) and trigger a liability to IHT that tails off over a 7-year period. During this time, a sufficient quantity of liquid assets must be maintained to cover the IHT liability should it arise. This can cause problems if the donee of the gifted assets wants to utilise them immediately, for example by buying a house.

One way to free up the gift is to purchase life insurance, to cover the potential liability. This provides both the donor and the donee with peace of mind that the gifted assets will never need to be reclaimed for tax purposes.

Gift protection is a very cost-effective option. For a £1,000,000 gift which, excluding nil rate bands, comes with a potential liability of £400,000, the cost of insurance represents just 0.20% of the gifted amount for a 50-year-old donor, and just 0.48% for a donor aged 60. We find it is often helpful for clients to view insurance as a definite c.0.5% cost versus a potential 40% charge.

Current indicative protection costs for a £1million gift:

Year	Sum Assured	Donor age 50	Donor age 60	Donor age 70
1 to 3	£400,0000	£393	£948	£2,799
4	£320,000	£318	£767	£2,276
5	£240,000	£242	£585	£1,750
6	£160,000	£165	£404	£1,223
7	£80,000	£85	£209	£642
Total Cost:		**£1,989**	**£4,809**	**£14,228**
Cost as % of £1m Gift		**0.20%**	**0.48%**	**1.43%**

IHT generated by the sale of a business

In all the furore of the sale of a business and the inevitable 'deal fatigue' that hits shortly afterwards, the long-term impact of having cash rather than BPR relievable shares on the IHT liability is often overlooked. For cash assets now with the client, there will be an immediate liability created. Similarly, there is often a series of gifts made shortly afterwards which will kick start the 7-year gift tail.

For those assets that are gifted straight on, gift cover is available and is comparatively far cheaper than the potential tax liability that would arise on death. From a long-term planning perspective, 'deal fatigue' is likely to mean that clients would understandably like to take a break from long term planning. To protect them while they do this, it is sensible to put up an umbrella of cover up for 5 or 10 years just to provide some breathing space while you work out how to arrange the client's assets for the future.

THE TARTAN TARIFF ON SCOTTISH PROPERTY OWNERSHIP

Authored by: Sarah-Jane Macdonald (Partner) - Wright, Johnston & Mackenzie

With its rich history and picturesque landscapes, Scotland can be the ideal location to invest in additional property, whether it is a holiday home or a little fixer-upper. As alluring as that seems, clients often overlook the tax implications and other compliance burdens.

The “tartan tariff”, as it were, consists of the Additional Dwelling Supplement (ADS), the Register of Controlled Interests in Land (RCI), and Landlord Registration.

What is ADS?

ADS is effectively a second-home tax payable in addition to any Land & Building Transaction Tax (LBTT). Whilst similar in some ways to the SDLT higher rates for additional dwellings, ADS does have certain unique attributes.

One of the key differences is the tax itself, with ADS being charged at 6% of the total purchase price (for purchases of £40,000 or mote). For a holiday home of £250,000 this is an extra £15,000.

Much like the SDLT position, Revenue Scotland takes a hard-line on what is considered to be a residential property, and if it is capable of being used as a dwelling, it is likely to incur that ADS charge.

Mixed-use properties will get the benefit of non-residential rates for LBTT purchases, but ADS is applicable on each of the dwellings being purchased. Multiple Dwellings Relief could assist in that scenario to reduce the tax due, and full relief is available from the ADS if six or more residential properties are being acquired in one transaction.

What is RCI?

Scotland introduced the RCI as a means of creating transparency of property ownership in Scotland. The register is designed to show who owns land (the Recorded Persons, i.e. those named on the titles) as well as who has underlying control of that land (the Associates).

Certain owners, such as companies registered with Companies House who are already subject to transparency regimes won’t have these obligations. However, it will require various individuals, trusts and partnerships that own land in Scotland to make entries on the RCI to show who significant influence or control over land.

The RCI became operational in April 2022 and has a grace period until 31 March 2023, after which non-compliance can result in criminal penalties and fines of up to £5,000.

What about Landlord Registration?

It is also a requirement to register as a landlord before letting residential property, or, if short-term letting, to obtain a short-term let license.

There are certain exemptions from landlord registration, for example if letting to family. Otherwise, a landlord must register with each Local Authority where they will be letting residential property. Failure to do so can result in fines of up to £50,000, and being banned from registration.

Holidays lets ought to be exempt, albeit there is ongoing debate on the specific requirements to qualify. Regardless from 1 October 2023, it is necessary to obtain a Short-Term Let License before taking bookings or receiving guests (there are some transitional rules for those who did so prior to October 2023).

Should clients still invest in Scottish property?

Whilst the Tartan Tariff may seem daunting, it shouldn't put clients off making that investment. If expectations are managed and advice sought as to how best to structure that ownership it will ensure clients understand the tax implications and what compliance is required. A summary of some of the key options are set out below.

Owning Outright

The most straightforward route is to own property outright.

LBTT is charged at either residential on non-residential rates. ADS is then charged at 6% if any one of the individual purchasers owns another property anywhere in the world, at the date of purchase.

It is unlikely an entry in the RCI would be needed unless there is someone with a contractual right to make decisions over that land (care should be taken with powers of attorney).

If it is residential property being let out, the owner(s) will need to register as Landlords in the relevant Local Authority. Joint owners must separately register, but nominate a "lead".

A company could purchase on behalf of an individual(s), holding title as bare trustee. As it currently stands, this would not require to register in the RCI, and would be treated for all other purposes in the same way as if it was a purchase by an individual(s).

Purchase by a Company

Where a company purchases a property, it too will face LBTT at the same rates as an individual. However, companies suffer ADS regardless of whether it owns any residential property. Companies will therefore always have the 6% charge for purchases of dwellings over £40,000.

As a company registered with Companies House, it shouldn't need to make an entry in the RCI, but would need to register as a Landlord (albeit individual directors would not need to register).

Whilst having less property compliance requirements, it would have requirements as a company. There are also broader tax implications to consider particularly as to how income could be extracted as well as, potentially, the Annual Tax on Enveloped Dwellings.

Purchase by a Trust

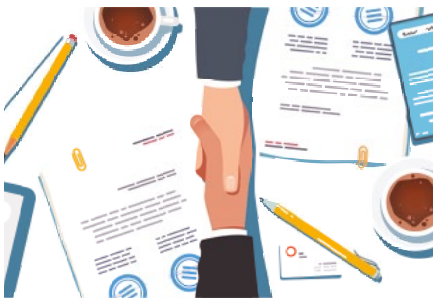
Trusts perhaps have the most compliance. Each trustee must register as a Landlord in the same way as joint owners would, and RCI is required to show any changes of trustee, or any party with influence of control (e.g. a Protector). This is in addition to any requirement to register with HMRC's Trust Registration Service.

Whilst discretionary trusts always suffer the ADS charge, an interest in possession can be granted to avoid ADS and manage the payment of income. If the income beneficiary does not own other property at the date of purchase, no ADS would be payable. Assuming there are flexible trust terms, it can also allow for alteration of the payment of income later.

That said full advice should be sought as to the broader (inheritance tax) position.

Early Advice to Avoid Issues

The key with all of these options is to seek advice early when considering investing in Scottish property. Otherwise, clients may face an unwanted tax sting, or worse a criminal penalty and hefty fine.



THE MERRY-GO ROUND OF HMRC GUIDANCE....

Authored by: Rosie Todd (Partner) – Stevens & Bolton

Given that one of the key pillars of a working tax system is certainty, HMRC seem to have a nasty habit of changing their guidance without warning. Those who regularly advise non-dom clients will be aware that this is particularly notable in HMRC's ever-changing guidance since the sweeping changes in 2017, where the latest twist in the saga is HMRC's announcement in October 2023 that they were, once again, reviewing their position on remittance rules and collateral debts.

What's the background?

Under the main remittance provisions, bringing foreign income and gains into the UK for the benefit of a relevant person can trigger a tax charge. This core provision clearly encompasses amounts being brought to the UK to repay a debt or pay interest on a debt where the repayment takes place in the UK.

The "relevant debt rule" (ss.809L(3)(c) and (d) and 809L(7) Income Tax Act 2007) extends the position in a more indirect way. It applies where clean capital has been brought to, or received or used in, the UK and a debt relating to that capital has been repaid, or interest on the debt has been paid, outside the UK using the taxpayer's foreign income or gain.

Put another way, the relevant debt rule shuts down what would otherwise be an easy loophole (in which a remittance basis user borrows to fund UK expenditure and repays the debt or pays interest out of foreign income/gains, without generating a remittance which would then incur a UK tax charge).

Things get more complex when you start looking at what this might catch. The legislation includes the phrase "used… in respect of a debt" as a criterion for a remittance charge to arise. This is particularly hard to analyse in the context of security for debts. HMRC's view pre-2014 was that a security was not "used in respect of a debt" if the debt is serviced and repaid on commercial terms. In August 2014 they changed their stance and have since then maintained that there are two possible circumstances in this context which can generate remittances:

1. If foreign income/gains are used as collateral; and
2. If foreign income/gains are used to pay interest/repay capital in relation to other collateral.

Collateral – what is caught?

HMRC's currently published view is that if an asset is provided as collateral for a relevant debt, this is "use" in respect of the debt. Any foreign income or gains which the asset represents are therefore deemed to be remitted under the relevant debt rule (see RDRM33170).

This issue is exacerbated by HMRC's position in relation to the amount treated as remitted. Again, this is an area where HMRC have changed their view. Pre-2020, HMRC stated that the amount remitted when security was given would be restricted to the amount of capital loaned together with accrued interest. In December 2020 HMRC changed their guidance and stated that "remittance is not capped at the amount of the loan. The amount of the remittance will be the full amount of the foreign income or gains that are used as collateral for the loan" (RDRM37050).

So HMRC's current position (as stated in their more recent guidance) is that the remittance is of all foreign income or gains that are represented by the asset provided as collateral. This is the case even where the value of the income/gains exceeds the value of the relevant debt (RDRM35270). Counterintuitively, this could lead to a ridiculous position where a remittance basis user takes out a loan in the UK worth £1m but the facility is secured by a pledge over an offshore account with a value of many multiples of the loan value and, under their current guidance, HMRC would treat all the foreign income and gains within those accounts as having been remitted.

What has changed?

Professionals and advisers working in this area have long campaigned for HMRC to change their position on the treatment of collateral. The Chartered Institute of Taxation (CIOT) have expressed their view that the charge should be capped at the level of monies actually remitted. This would seem to be a more logical and intuitive position. Following a meeting in October 2023 between HMRC and CIOT, HMRC have agreed to review its position.

It is not yet clear whether they agree entirely with the CIOT view or, if not, how they may change their own.

Where does this leave us?

Whilst the promise to review their position on collateral seems like a positive step forward from HMRC, we still haven't been provided with their amended guidance and there is no indication of when we might expect anything. The lack of clarity continues in an area where HMRC have flip-flopped over time, changing their view and amending their guidance with no consultation. This isn't the only area of uncertainty within these rules - at the same meeting, HMRC and CIOT also discussed an unrelated point regarding remittance on divorce. This was triggered by HMRC's submissions in the First Tier Tribunal case of Sehgal which suggested that, contrary to the general understanding of the position, HMRC's view is that remittances made to the UK pursuant to a divorce settlement are chargeable. On this point, HMRC have suggested that further discussions will be needed and so advisers are still left in the dark.

Perhaps if we have a Labour government and the remittance rules are entirely removed, such issues will be academic but the fundamental point remains – we will only have a clear, fair tax system when taxpayers (and their advisers) are able to have clarity about what the law says and how it will be applied by HMRC.

WORKS OF ART AND THE CONDITIONAL EXEMPTION TAX INCENTIVE SCHEME

Authored by: Sophie Carr (Senior Associate) – Withers

Art collections are usually amassed with no small degree of emotional connection by their owners. Collectors are therefore inclined to think carefully about how best to pass on works of art to the next generation, either during lifetime or on death. Tax considerations usually come into play at this stage. One tax incentive which applies to heritage assets generally, including works of art, is the Conditional Exemption Tax Incentive Scheme (the 'Scheme'). The aim of the Scheme is to encourage collectors to keep pre-eminent heritage property in the UK and to make that property available to everyone. Critically, the Scheme allows the deferral of the payment of both UK inheritance tax ('IHT') and UK capital gains tax ('CGT') which would otherwise arise on such a disposal. This article sets out the main features and benefits of the Scheme as it applies to works of art.

Tax issues

A collector will usually have views on future of their art collection once they are no longer around. If the owner wishes for their art collection to remain in their family following their death, they will need to consider the tax implications of doing this.

If a collector is domiciled in the UK or 'deemed domiciled' in the UK on the basis of having been UK resident for 15 out of the previous 20 tax years, they will be subject to IHT on their worldwide assets. This will include any personally-held works of art. Broadly speaking, IHT is currently charged at 40% on any assets owned above the value of the 'nil-rate band' which is currently £325,000, subject to any available reliefs and exemptions.

If an art collection comprises a large part of an individual's estate then that individual could have a significant IHT exposure on death.

In that situation, an individual may consider making one or more lifetime gifts of their works of art to younger family members so as to reduce the potential IHT liability.

A gift from one individual to another is treated as a 'potentially exempt transfer' for IHT purposes, meaning that the gift will be free from IHT provided that the donor (a) survives for seven years from the date of the gift and (b) does not 'reserve a benefit' in the work of art once the gift is made. If the donor dies within the seven year period, this will result in an IHT charge of up to 40% of the value of the work of art. The rate of IHT charged on the gift will reduce if the donor survives for three or more years from the date of the gift.

For UK resident individuals, CGT will be due on a gift of a work of art if the value of the item has increased during the individual's period of ownership (unless the individual can claim the remittance basis of taxation and the asset is kept outside the UK). The current rates of CGT are 10% (basic rate) and 20% (higher rate). Each individual has an annual CGT-free allowance, which is £6,000 in the 2023/24 tax year. This allowance will reduce to £3,000 for any disposal made after 6 April 2024. Any CGT charge arising on the disposal of a work of art will be what is known as a 'dry' tax charge, as it will not result in the realisation of any cash which can be used to pay the tax.

Care therefore needs to be taken to ensure that a CGT liability on a disposal can be met from other funds.

The Scheme

Both IHT and CGT can be delayed if a work of art qualifies for conditional exemption under the Scheme. For a work of art to be eligible for conditional exemption, it has to be 'pre-eminent'. In practice, this means that HMRC must consider it to be 'pre-eminent' for its national, scientific, historic or artistic interest. Works of art as well as objects, land and buildings all fall within the potential scope of the Scheme. The item in question can be a single item or part of a group of items, which, when, taken together, are 'pre-eminent'.

For the Scheme to apply, the new owner of the work of art (the recipient of the gift or inheritance) must undertake to:

1. Keep the object permanently in the UK and not remove it temporarily, except for an approved purpose and period;
2. Take agreed steps to preserve it; and
3. Secure reasonable public access to it.

In this context, 'public access' does not mean access only with a prior appointment. It requires the owner of the work of art to open up their home to the public for a certain number of days per year. In practice, this means that access usually has to be given for at least 28 days of the year and outside of those days, the item must be available for visits by appointment. Conditionally exempt works of art which are on display to the public are listed on HMRC's database of tax-exempt heritage assets, which is publicly available. If an owner does not wish to, or cannot, open their home up to the public in this way, an alternative is to loan the object to a museum or gallery that may wish to display it. This may come with its own challenges, which are outside the scope of this article.

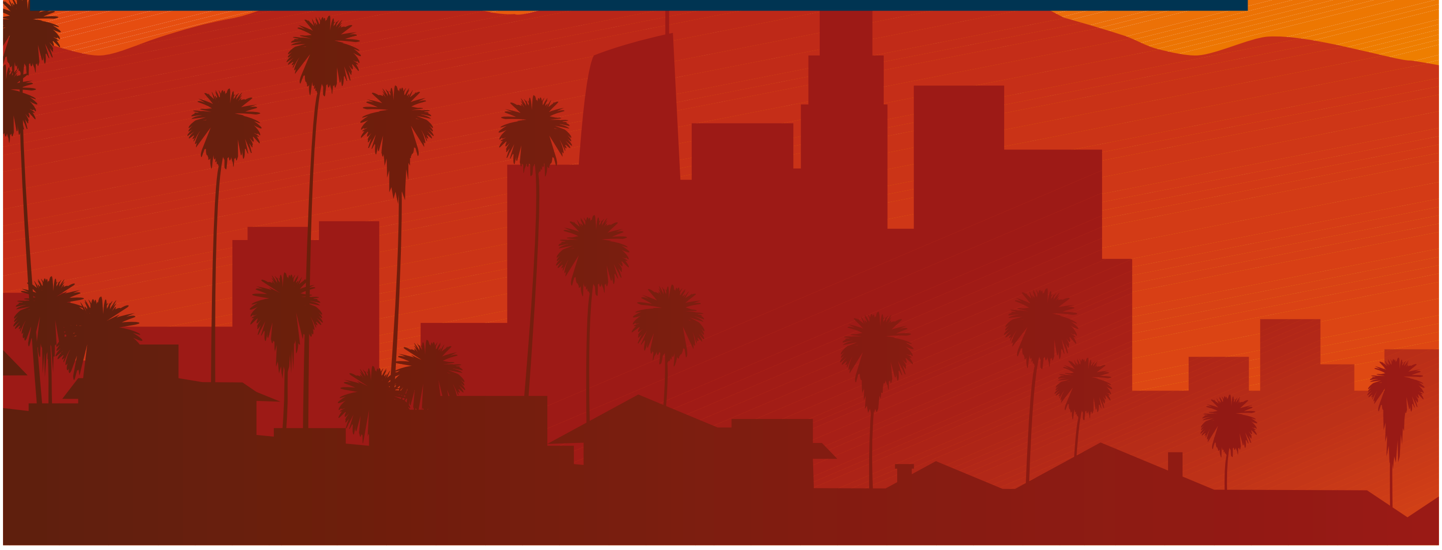
As the name suggests, the exemption under the Scheme is conditional. If the exemption ceases to apply then any IHT or CGT deferred will become due at that stage. The exemption will cease to apply on the occurrence of any of the following events:

1. A material breach of an undertaking, eg careless damage to the item, removal from the UK or a failure of the public access requirements.
2. A sale or other disposal of the item. It is possible for the disposal to be a conditionally exempt transfer, if the new recipient gives new undertakings in respect of the item.
3. The death of the owner. Any passing of a conditionally exempt item will be a chargeable event which could result in IHT or CGT being due, unless the recipient reapplies for conditional exemption and fulfils the requirements for conditional exemption to apply at that time.

Practical considerations

Despite the available tax deferral, owning a work of art which is conditionally exempt is practically difficult, not least because of the requirement for securing public access to the item, which will be unpalatable to some. Collectors will therefore need to decide whether the potential tax deferral merits taking the steps required to benefit under the Scheme.

CHINESE INCOME FIGURES IN CASE AGAINST CALIFORNIAN



Authored by: Alicia Castellanos (CEO and Founder) – Global Tax

Social: A man who worked simultaneously for employers on the West Coast and in the People's Republic of China may be on the hook for failure to file FBARs, among other tax charges.

A federal grand jury in San Jose, California, has indicted local resident Chunsheng "Jay" Huang, 67, on charges of filing a false U.S. tax return and failing to file a Financial Crimes Enforcement Network (FinCEN) Form 114, "Report of Foreign Bank and Financial Accounts" (FBAR).

In a case pursued by the Internal Revenue Service and the Federal Bureau of Investigation, Huang is alleged to have been an employee of a company based in Milpitas, California, for more than 15 years while also working for companies based in the People's Republic of China for at least six of those years.

The indictment alleges that Huang used an account with Industrial and Commercial Bank of China (ICBC) in his sister-in-law's name to receive payments from two companies in China. The indictment also alleges that he failed to report that income on his federal tax returns for 2016 through 2020.

In addition to the obligation to report foreign income for tax purposes, the indictment alleges that Huang did not file a FBAR for 2019 and 2020, the form that U.S. citizens and residents must file if they have a financial interest in or

signature or other authority over a bank account in a foreign country with an aggregate value of more than $10,000 at any time during a particular calendar year.

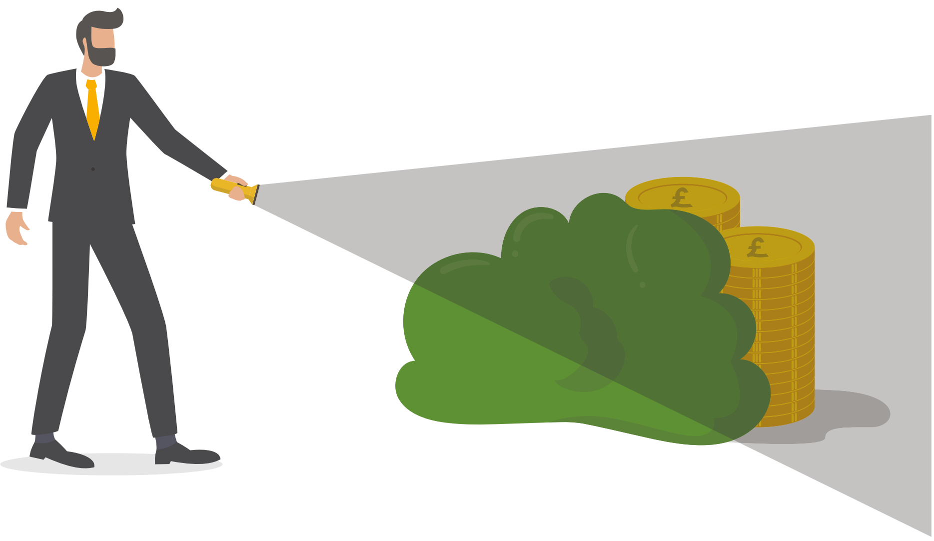
Huang has not made an appearance in the case; an arrest warrant has been issued.

If convicted, he faces a maximum sentence of three years of imprisonment, a $250,000 fine, a year of supervised release and a $100 special assessment for each count of violating 26 U.S.C. § 7206(1) (Making and Subscribing a False Tax Return); and 10 years of imprisonment, a $500,000 fine, three years of supervised release and a $100 special assessment for each count of violating 31 U.S.C. §§ 5314 and 5322(b) (Failure to File Report of Foreign Bank and Financial Accounts).

The case promises to be one of several lately that will test the definition of “willful” non-filing of a FBAR, the penalty for which is much more severe than for that of non-willful failure to file. Recent cases have hinged on factors as varied as to simple mistranslations to infamous historical circumstances surrounding the overseas accounts.

No matter the eventual decision, the U.S. government seems to be making good on its pledge to turn up the heat on failure to file FBARs.

Your tax specialist needs to stay on top of this and many other issues of wealth, foreign income and tax enforcement. If we can help, please let us know.



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