Introduction

Welcome to a special edition of our non-dom newsletter.
Here we share our thoughts and practical tips on what clients and advisers may wish to start considering now, following the release of the consultation document.
If you would like to discuss any of the issues raised in this Newsletter, please get in touch – for contacts, click here.

Question time

Clients and their advisers have now had the opportunity to digest the consultation document issued by HMRC on 19 August. Very helpful and constructive meetings have been held with HMRC as part of the consultation process which closes on 20 October.

The landscape is much clearer. It seems certain that 6 April 2017 will indeed be D Day. While the final form of the changes remains uncertain and we still await a lot of detail, the clock is ticking and if one waits, D Day will be here and there may be no time to act.

The most common question being fielded by EY at the moment is, ‘What do we do?’ Clients, trustees and bankers are all seeking guidance on what to do and when to do it.

This is not an easy question (are there any easy questions anymore?). By acting now, one has the risk of moving too early. By delaying, there may not be time to restructure.

In this edition of the non-dom newsletter, we try to answer this question. We share some thoughts in each of the main areas. We would be pleased to hear your thoughts too as HMRC, tax payers and advisers all move forward together cautiously.
Act now: Press go in January

This edition of the non-dom newsletter must carry a health warning! The landscape is much clearer than it was at the start of the summer, but it may change again. However, we believe that the August consultation document represents a firm signpost and that action is, in many cases, now appropriate and necessary. Therefore, in the articles in this edition, we share our thoughts on the type of issues and actions which must be on the agenda.

The health warning is that there could be more twists in the plot. Individuals and trustees taking action need to be aware of the risk of moving too early and balance this against the risk of delay. For example, at the time of writing, there is a suggestion that the CGT tainting rules (whereby you need to deep freeze the trust or lose its protected status forever) will be modified. It will almost certainly (in the normal case) be wrong to do nothing. Structures and assets must be reviewed. Questions like ‘What do I do with my UK residential property?’, ‘What do I do with the Spanish villa?’, ‘Have I got a ‘taint or take’ problem?’ must now all be asked and draft answers prepared. In most cases, the sensible course will be to write the answer to the exam questions now, but not to hand in your answers until the syllabus has finally been settled. But don’t daydream and only pick up your pen in January!

Based on the articles in this special edition of the non-dom newsletter, click here for a list.

Useful links

► Further consultation document published 19 August 2016
► Joint CIOT, ICAEW, STEP and the Law Society discussion paper - click here
► Policy document and draft income tax and capital gains tax legislation published 2 February – click here
► Policy document and draft IHT legislation published 9 December – click here
► Consultation document published 30 September – click here
► Previous versions of this newsletter are available - click here
► HMRC’s Technical Briefing on the main changes to non-dom regime – click here
► HMRC’s Technical Briefing on changes to IHT for UK property - click here
► HMRC’s 15 October 2015 announcement on loan collateral - click here
► Questions – for contacts click here
Expected timetable of main provisions

- Policy announced: 8 July 2015
  - Consultation document published (including some draft legislation): 30 September 2015
  - Consultation closed: 11 November 2015
  - Further draft legislation published: 25 November/9 December 2015
  - Finance Bill Consultation closed: 2 March 2016
  - Further draft legislation published for consultation: February 2016
  - Consultation responses due: 20 October 2016
  - New consultation published with some draft legislation: 19 August 2016
  - Autumn Statement: 23 November 2016
  - Further draft legislation: 5 December 2016
  - Draft Finance Bill published: March 2017
  - New rules come into force: 6 April 2017
  - Bill makes its way through Parliament/Committee stages: April/July 2017
  - Bill receives Royal Assent: July 2017
Act now: Press go in January

Rebasing and mixed funds

► Review existing assets and investments in detail in the context of future needs.
► Determine which assets are likely to qualify for rebasing. Are they comprised of clean capital?
► Analyse accounts to see if cleansing is appropriate. Are sufficient records to hand to achieve this or must records be sought out?
► Consider how future lifestyles are to be funded.
► If remittance basis charge was not previously paid, consider paying the charge for 2016/17 or amending previous year’s tax return to pay the charge.
► Will there be sufficient clean capital from rebasing and cleansing? Can funds be borrowed against clean capital? This can be particularly attractive if linked with a purchase of UK property.
► Consider obtaining valuations of assets.

Non-resident trusts

► It is difficult to think of a trust scenario which will not have to be reviewed.
► If a trust owns UK residential property, the impact of the new IHT rules must be assessed. Is there a Gift with reservation of benefit (GROB)? How should this be addressed? The exclusion of the settlor may be undesirable so life assurance may be an easier solution. Will there be liquid funds to pay 10 year charges?
► The tainting provisions require all trustees to look at existing benefits. Should overseas assets be extracted from trusts now (balancing the IHT position against the future CGT charges)? Should rent be charged for the use of UK residential property? Trustees need to review all actual and future charges in light of any 2008 rebasing etc.
► Trustees should also think about new solutions, eg, if the CGT tainting rules are to be introduced, would it be preferable to hold capital assets via an offshore bond so as to access income tax rather than CGT charges?
How are assets to be held once the deemed domicile rules bite? Are we set to see an even bigger growth in family investment companies?

IHT changes

- If an individual is not yet deemed domiciled, consider establishing a pre-2017 trust.
- Review the IHT and succession strategy.
- Trustees will need detailed record-keeping to track their settlor’s residence status and movements. Should Settlors take a holiday every 10 years?

De-enveloping

- Consider the detailed checklist in our article.
- No de-enveloping relief so balance the pros and cons before April 2017.
Rebasing and mixed funds: much to do

For personally owned assets the key provisions in the trust consultation document were those around rebasing of assets and the cleansing of mixed funds. For both ‘reliefs’, we are still awaiting the draft legislation. As a result, we only have a few short paragraphs in the consultation document to help us understand how they will work. Much remains unclear.

Rebasing

This relief will allow individuals who become deemed domiciled in 2017/18 (under the 15 out of 20 rule) and who have paid the remittance basis charge in at least one tax year to rebase their non UK assets to April 2017 values. This means that when the asset is subsequently sold, only the increase in value will be subject to UK tax. The recent consultation document confirms that the uplift from base cost to April 2017 values will be free of UK tax on a subsequent remittance of the sale proceeds to the UK once the asset is sold. Nevertheless individuals must take care if the asset was originally acquired with non UK income or gains. Here the mixed fund relief (see below) may assist.

The relief is not available for those who become deemed domiciled in a year after 2017/18. In addition, we are informed that this relief will not be available to those individuals with a UK domicile of origin who have a non UK domicile of choice and who become deemed domiciled in 2017/18. Such individuals, who are married (or in a civil partnership) to someone with a non UK domicile of origin may wish to see if the new legislation allows a transfer to their partner to give the uplift (but see below).

The consultation document makes clear that the relief is only available for assets held personally (and not, for example in non UK structures such as trusts or companies). However, where the company is held direct, the relief should be available for the company shares and this may facilitate breaking such structures on 6 April 2017 if they are no longer required (although section 13 TCGA must always be kept in mind).

It seems that the assets must have been held at the time of the summer budget 2015 (i.e., 8 July 2015). This is not entirely clear, as the consultation document simply requires the asset to be non UK situs at that date. So it is not certain if the exchange of one asset for another between 8 July 2015 and 6 April 2017 (eg, the exchange of non UK shares for other non UK securities where CGT deferral is available) will qualify. Or whether the exercise of a non UK share option to obtain non UK shares in the same company will qualify. However, it seems that it will not be possible to move an asset such as a painting, which was in the UK in July 2015, outside the UK in order to rebase.

Individuals who can avail of this relief may now wish to consider obtaining market valuations of their non UK assets. This will assist with future tax-free remittances to the UK once the asset is sold. In addition, the rebasing relief may make it attractive to set up new holding structures for investments on 6 April 2017 rather than in the current year. Rebased assets may, in some circumstances, also be used as collateral for UK loans in a tax efficient way.

While there are still some uncertainties regarding this relief (and we would advise waiting for the legislation before taking any steps), the relief is to be welcomed for those who become deemed domiciled in 2017/18.

Mixed funds – cleansing

This new relief was announced in the most recent consultation document. Unlike the rebasing relief, it will be available to any non-domiciled individual (not only those who become deemed domiciled in 2017/18). However, it will not be available to those who were born in the UK with a UK domicile of origin. It is not clear, but seems unlikely, that the legislation will allow such individuals who have a non-dom spouse to transfer funds to their spouse for segregation.

The relief will allow non-doms to separate out their mixed non UK bank accounts (i.e., bank accounts containing a mixture of non UK income, gains and capital, from one or more years) into different bank accounts outside the UK. This will enable the non-dom to select particular funds for remittances to the UK, rather than have to use the current mixed fund legislation, which latter may be more unfavourable from a UK tax perspective. It appears that the relief will be available throughout 2017/18.
and, while the relief is only available for cash in bank accounts, the consultation document states that it will be possible to sell non UK assets during this year and segregate the proceeds.

This relief, combined with the rebasing relief, should allow individuals to sell a rebased asset on 6 April 2017 and separate the proceeds into its constituent elements for future tax efficient remittances to the UK. This may include setting up new investment structures, either outside or in the UK, in a tax efficient manner.

At present, it seems that the relief is only available for cash held personally and not, for example, for cash held in personal structures such as trusts or investment companies. It may be appropriate to combine distributions from these structures, either this tax year, or next year, with the mixed fund relief as a way of preparing for future remittances to the UK.

Taxpayers should now be identifying mixed funds which may be analysed for this relief (there is no reason why this analysis could not be started now) and also assets which may be sold in 2017/18 for separation of proceeds. The consultation document stresses that the relief will only be available where taxpayers can identify the constituent elements of a mixed fund. It remains to be seen whether an ability to identify elements for the most recent years will be enough to allow these to be separated, leaving a rump mixed fund behind, although we understand this may be possible. Should this be the case, this will open up the relief to more taxpayers.

The 2017 regime brings new tax charges to long-term UK resident non-doms. These two reliefs, where available, may help soften the tax burden and provide a more gentle introduction into the new era.
Non-resident trusts: changes and consequences

Pre-change trusts
The UK personal tax system as it applied to non-domiciled individuals very much encouraged the holding of personal wealth via overseas trusts. Specifically it offered a regime of capital gains only being taxed if matched with a trust benefit remitted to the UK and foreign assets being outside of the inheritance tax charge.

For UK domiciled individuals, trusts which they can benefit from have largely become tax transparent in terms of income, gains and ownership of assets. There is no real tax incentive for such individuals to set up a family trust.

Post-change trusts
Accordingly where individuals, after becoming deemed domiciled under the proposed changes, set up trusts, they may well find that overseas trusts and any underlying companies are UK tax transparent. This raises two immediate issues:

► UK tax charges on the newly deemed domiciled individual on income, gains and assets in the structure without necessarily there being any cash distributed or available to the individual; and

► Gathering information by 31 January after a tax year end in order to complete a UK self-assessment tax return.

The approach of the consultation is that trusts set up after becoming deemed domiciled should not enjoy any special tax privileges and thus will be taxed in a similar way to those set up by UK domiciled individuals. As such there may be specific types of trusts that still have merit but trusts will not generally appeal for tax purposes. It is likely that deemed domiciled individuals will therefore consider the same opportunities as UK domiciled individuals such as family investment companies and tax privileged investments. Trusts will remain important for non-tax reasons such as asset protection.

Pre-change trusts – protections
However the consultation does propose certain tax protections for trusts set up before becoming deemed domiciled. It is therefore important that before 6 April 2017 individuals who will be caught by the deemed domicile proposals carefully consider setting up trusts to benefit from the protections, otherwise the opportunity will be lost. It is also important that existing trusts and underlying companies are reviewed before 6 April 2017 as the protections can be easily be lost or diminished if certain events happen after deemed domicile status is achieved.

There are certain trusts where the changes have less effect eg, if the settlor died not UK domiciled before 6 April 2017 or the settlor and close family members cannot benefit from the trust. The most impacted trust is where the settlor, spouse, civil partner or minor children can benefit from the trust. The following comments concentrate on that type of overseas trust. We shall look at the income tax, capital gains tax and inheritance tax protections proposed.

Income tax:
It is proposed that a trust’s UK income will be immediately taxable on the settlor, as is generally the case now. Non-UK source income of the trust will be taxed on the settlor if benefits are received by the settlor or close family members. The charge will involve matching the benefit with such income. Benefits received by others will be taxed on them based on their tax status. The protection is therefore that foreign income is only taxed as and when a benefit is received.

Settlements and income tax
If the trust has an investment or interest in an overseas company then protection will only be available if the company dividends its foreign income to the trust. If the company retains foreign income that income will be taxed on the settlor unless they can show certain existing safe harbours apply. These are the exclusions from the transfer of assets abroad charge, which are claimed in self-assessment tax returns.
Therefore, as currently proposed, no protection is being given for foreign income retained in overseas companies, although we understand this position may be being reviewed. UK income of the company will be immediately taxed on the settlor. Income of UK companies would not generally be subject to attribution to the settlor.

Post 2017 (for protected settlements)

► UK source income arising to a non-resident trust will continue (as at present) to be taxed on a deemed dom settlor.

► Section 624 etc. will not apply to a deemed dom settlor on foreign income in a trust set up before he was deemed dom - if the income is retained within the trust.

► However – if the settlor, spouse, minor children or other relevant person receives a distribution of relevant foreign income arising in a year when the settlor was non-dom and the trust was protected that distribution will be taxed on the settlor under s. 624 if matched against relevant foreign income.

► Remember this only applies to income at trust level and when the settlement legislation is applicable.

The tax protection afforded to foreign source income of trusts is lost if any property is added to the trust after 5 April 2017 and once deemed domiciled. Property added for trustees expenses in certain circumstances is permissible.

Capital gains tax

It is proposed that trust gains (including gains attributed to the trust from underlying close companies) will not be taxed on the settlor once deemed domiciled provided:

1. The settlor and close family do not receive any benefit from the trust or underlying company and
2. No property is added to the trust other than in certain limited circumstances.

The protection is therefore that trust gains (whether from UK or non-UK assets) are not immediately taxed on the settlor so long as 1. and 2. above are observed. If either of these requirements are breached the settlor becomes immediately taxable on trust gains from that tax year onwards.

Section 86

► Section 86 will be extended to apply to all those who are deemed dom.

► Settlement will be protected (so s.86 does not apply) where the trust was set up before the settlor became deemed domiciled and no additions of property have been made since that date. Note additions for expenses of administration are permissible.

► However – if funds are added to the settlement or the settlor, their spouse or their minor children receive any actual benefits from the trust then the protection will not apply.

► Thus, lose privileged status if you take or taint.

As currently proposed these requirements place considerable pressure on trustees to ensure they are not breached and CGT protection lost. If they are breached, even as to £1, the protection goes- it makes no difference that the benefit is taxable. This is why it is of paramount importance for trustees to review trusts and their companies before 6 April 2017 to ensure there are no ongoing benefits eg, use of a house that after midnight on 5 April 2017 causes the loss of protection.

Section 87

► Settlors who become deemed dom will not be taxed under s.87. - they will either be taxed under s.86 or the trust will remain protected.

► For beneficiaries who receive capital payments and who are deemed dom they will be subject to CGT under s.87, regardless of where the benefits are received.
Inheritance tax

The current situation is that trusts funded before becoming UK domiciled retain their status of being excluded from inheritance tax so long as the trust comprises non-UK assets. Therefore the trust itself does not suffer a charge nor are trust assets deemed to be in the settlor’s personal estate. If property is added to a trust after becoming UK domiciled (either in law or by deeming) then that property is not excluded from charge but it does not taint the earlier settled property. It is clear that non-UK property settled before becoming deemed domicile under the proposals will enjoy the exclusion from a charge to inheritance tax. It is less clear whether this is a new protection which will be lost if property is added to the trust after 5 April 2017 when deemed domiciled.

Next steps

Existing trusts and any related companies should be reviewed to see whether they are impacted by the changes and whether any pre 6 April 2017 remedial work is required. Particularly whether any benefits are currently being provided that might cause a loss of protection.

Individuals who will become deemed domiciled on 6 April 2017 should carefully consider whether a pre change trust is appropriate in order to benefit from the protections vis-à-vis retaining assets personally. This article relates to individuals who become deemed domiciled due to meeting the 15 out of 20 year test of becoming deemed domicile and not those born in the UK who are deemed UK domicile whatever their residence history.
IHT changes for non-doms: Pitfalls and opportunities

The proposed changes to the taxation of non-domiciled individuals (non-doms) in the UK bring forward the point at which a resident non-dom becomes deemed-domiciled for IHT. The effect of these reforms is that an individual will become deemed-domiciled for IHT at the start of their 16th consecutive year of UK residence, rather than at the start of their 17th year of residence. For most non-doms, this means that they need to start planning their succession strategy sooner than they would have done in the past.

Individuals who have left the UK to re-set their deemed domicile clock under the existing IHT rules will also have to change their plans to ensure that the clock is also re-set under these new proposals: there will not be a transitional relief for people whose planned absences under the existing 17/20 rules will not satisfy the requirements of the new 15/20 rules. However, for IHT purposes, an individual will only retain an exposure to UK IHT on their worldwide assets for five consecutive UK tax years after they leave (although based on the comments in the consultation document, this may be intended to be four years). However, they will need to remain non-UK resident for six consecutive years to avoid being caught within the IHT net again if they return to the UK. The spousal election for non-domiciled spouses is now proposed to be unchanged.

On becoming deemed-UK domiciled, an individual’s worldwide estate becomes liable to UK IHT. However the rules which apply to excluded property trusts where a person has become deemed domiciled will not change. Consequently offshore trusts that are set up by an individual who is not deemed domiciled in the UK under either the existing 17/20 or the new 15/20 rule will remain outside the scope of UK IHT, even after that individual becomes deemed-UK domiciled.

It is not currently clear whether or to what extent this protection will be lost, if any property is added to the trust or if a benefit is received by the settlor, his spouse, or a minor child. Setting up such a trust before becoming deemed domiciled may therefore form an essential tool in planning the IHT strategy for many non-doms and these trusts could form a useful mechanism to freeze assets including any growth in value where the settlor and his family do not intend to access the trust funds while resident in the UK. Given the value of these trusts going forward, trustees will need to monitor their terms and activity very carefully in order to preserve their protected status.

The position for individuals born in the UK with a UK domicile of origin (returning doms) is far less favourable; although the consultation confirms a short grace period for IHT only. This means that a returning dom will be subject to IHT on his worldwide estate if he is resident that tax year and has been UK resident for at least one of the two tax years.

The protected status of excluded property trusts that applies to non-doms does not apply to returning doms. Trusts settled by a returning dom while non-domiciled will be within the relevant property regime while the returning dom is UK resident. The trust’s inheritance tax status will follow the residence status of the settlor, and could change from one year to the next if the individual moves in and out of the UK.

Returning doms and their trustees will therefore need to keep careful records of any periods of UK residence so that they can reconstruct the value and transactions in the trust over a 10 year period. Many will need to monitor when the 10 yearly inheritance tax charge falls and some may even consider leaving the UK to avoid a charge in the relevant year. The good news is that if the settlor is resident in the year of the 10 year charge, the charge is apportioned to reflect any periods during which he was non-resident or before he was deemed domiciled.

Individuals who believe they are affected by this rule will need to take advice early, including a complete review of their family background, to avoid the significant risk that they come back to the UK without appreciating the adverse tax consequences until it is too late.

Whilst a great deal in the consultation remains unclear, three golden rules are emerging for non-doms for IHT purposes:

- Plan early
- Act before you arrive or before you become deemed domiciled
- Keep excellent records
Residential property - pushing the envelope?

Go back five years or more and it was standard UK tax planning for non-UK domiciliaries to hold their UK residential property in an overseas company, the shares of which were held by the trustees of an offshore trust. This gave inheritance tax protection; the UK property is held by a company and so not directly within the inheritance tax regime and the trustees would only be within the inheritance tax regime if they held UK situs assets – they wouldn’t as the only assets they hold are non-UK shares. As long as certain conditions were satisfied at the outset, these structures were effective for protecting UK property from inheritance tax charges.

The government’s proposals which were initially announced in the Summer Budget 2015 mean that this planning will no longer offer the protections that it used to. And to highlight the impact of this, we must first go back to the UK residential property taxation changes which were introduced in April 2013.

The Finance Act 2013 introduced the Annual Tax on Enveloped Dwellings (ATED). This imposes an annual charge on UK residential property owned by non-natural persons (generally corporates) where the value is at least £500,000. Relief is available in certain circumstances, such as when the property is rented out to an unconnected person on a commercial basis, but generally it imposes an annual charge at a minimum of £3,500 and a maximum of £218,500 (based on current rates and dependent on which valuation bracket the property falls into).

When ATED came into force, many people considered unwinding their structures to remove the annual charge imposed; however in many cases, this was not the best answer from a tax perspective in the long run.

For example, if we consider a UK residential property valued at £7mn. The potential inheritance tax charge on this property if held directly by an individual at the time of their death would be £2.8mn. The ATED charge for a property in the valuation bracket between £5mn and £10mn is £3,500 and £218,500.

IHT changes – residential property checklist

- From 6 April 2017 the changes bring residential properties in the UK within the charge to IHT where they are held within an overseas structure.
- This is achieved by removing UK residential properties owned indirectly through offshore structures from the definition of excluded property in section 48 IHTA 1984.
- From April 2017 not excluded to the extent the value of any interest in the entity is derived, directly or indirectly, from residential property in the UK.
- Similar position if member of any overseas partnerships which holds a residential property.
- Applies to all IHT chargeable events.
- Will apply to a property even if it is a main residence or let on commercial terms.
- IHT charge will apply where the property has been a dwelling at any time in the two years preceding a transfer.
- Tax will be charged on the open market value of the property at the time of the IHT event. The IHT liability will be determined to the extent the property has a residential use.
- Responsibility for tax on the trustees.
- New liability for legal owners of the property including directors.
- HMRC can impose a charge on the property.
- No de-enveloping relief.
£54,450 per annum. Say the property remains in the corporate and trust structure, the potential ATED charges over a 20 year period are £1,089,000 (although admittedly the charges do generally increase with inflation but, so do property prices and thus inheritance tax charges). Using these figures the ultimate owner would still benefit from the structure from a tax perspective even if they were to survive 50 years.

Because of this, and of course the many additional considerations and tax charges on winding up and distributing from a trust, many chose not to unwind their structures.

Current developments mean that the inheritance tax benefit of these structures will disappear. The government has announced that from April 2017, property held through companies by non-UK domiciliaries will no longer be out of the scope of inheritance tax. We are therefore back in the position where de-enveloping needs to be seriously considered, which comes with a lot of tax considerations. And, it has been confirmed that there will be no transitional provisions to allow individuals to unwind property holding structures without a tax charge.

If changes are to be made to the structures, such as extracting the property so that it is held direct, it is important that this is considered in detail well in advance of 6 April 2017, as the other changes for non-UK domiciliaries that will commence at the same time could make extraction even more difficult.

Property held by corporate in trust

There is potential inheritance tax for the trustees to pay at each 10 year anniversary of the date of settlement under the relevant property regime. In addition, exit charges will come into play if the shares/property are distributed out of the trust post April 2017. The trustees will have responsibility for paying and reporting for these charges.

Further, if the trust is settlor interested (which is often the case for offshore trusts) then because it now holds property subject to the relevant property regime, the gift with reservation of benefit rules will apply. This means that the value of the shares attributable to the property will be regarded as forming part of the settlor’s estate for inheritance tax. The charge will be at 40% on death, although normal double charge relief rules mean that any lifetime inheritance tax paid by the settlor or trustees (eg, the 10 yearly charges) will be deductible from the amount due in respect of the same asset.

ATED continues to be payable annually, unless relief applies.

Removing the property from the structure requires consideration of the tax impact firstly of getting the property out of the company and into the trust, and next extracting the property from the trust. Additional complications are brought in from the changes announced in relation to the taxation of offshore trusts settled by non-UK domiciliaries.

Shares held direct

The value of the shares attributable to the property will from April 2017 form part of the shareholders estate for inheritance tax purposes. The charge will be at 40% on death.

ATED continues to be payable annually, unless relief applies.

Removing the property from the structure requires consideration of the tax impact of getting the property out of the company, which can be costly.

Valuing the shares attributable to the UK residential property

The value of any shares which represent UK residential property will once the changes arrive be within the scope of UK inheritance tax. There may be potential discounts to valuations where the shares are not as valuable as the property itself. Debt will be deductible, but only to the extent that the debt relates exclusively to the property, for example, a mortgage taken out to purchase the property.

The proposals note that debts to related parties will be disregarded. This means that loans from a trust to a company or between trusts, for example, are likely to be disregarded.

Where the company owns other assets in addition to the UK residential property, it will be necessary to value all of these assets to determine the extent to which the shares are subject to UK IHT.
Debts

Debts reduce value -

► has to be a relevant debt – i.e. one which relates exclusively to the property such as a fee used to purchase the property;
► any debts not related to the property will not be taken into account;
► pro-rata approach will be adopted;
► loans between connected parties will be disregarded.

De-enveloping

When considering de-enveloping a structured practical approach is needed and ultimately a cost benefit analysis of retention versus ‘de-envelop’ is required. Stage one will be to collate data and review precise structure and for example the following questions will need to be assessed.

► What structure do we actually have? Identify legal status from a UK tax perspective, eg, Trust, Company partnership, foundation, etc. but acknowledging UK tax rules have different definitions for different taxes (so if settlor excluded for income tax may not be settlor excluded for capital gains tax).

► Why was structure established? Revisit objectives and see if they are still valid and what has changed (Tax law, residence and domicile status of settler, beneficiaries). The overarching purpose may still exist, eg, asset protection or avoid forced heirship rules. Check overseas tax position (eg, relatively recent changes of law or practice – US, France, Israel – that may seek to adversely tax all potential beneficiaries in that jurisdiction).

► Precisely what assets does structure own – directly and indirectly? A simple question but not always one that can be easily answered.

► What is the tax history of the assets and the structure – date of purchase, transaction costs, and any rebasing elections.

► What is market value of assets and are they transferable and/or costs of transfer, eg, local transfer taxes or additional SDLT may be too high (and require real cash now) to even contemplate de-enveloping.

► What would the ideal structure be now to take into account revised non tax objectives, current position of settlor and beneficiaries and current tax rules and proposed rules?

► What alternative structures may achieve similar or majority of objectives. Is there a need to de-envelop everything?

► What is cost (CGT, IT, transfer taxes, transfer costs) of achieving new structure. Is that a real cash cost?

► What are annual and ongoing cost savings of proposed structures?

► What is cost of doing nothing? Could double tax arise in the future?

Once the above information is collated (and do not under estimate the time taken to gather such information and answer these questions) the question of whether to de envelope could potentially be answered.

Unfortunately without a complete or almost complete set of answers one runs the risk of shooting completely in the dark and ending up with a nasty surprise.
Contact details

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