Introduction
Welcome to the latest edition of the non-dom newsletter.
This month we focus on the practical steps that should be considered before the rules change on 6 April 2017, as well as providing the latest developments from HMRC.

If you would like to discuss any of the issues raised in this newsletter, please get in touch – for people to speak to, click here.

All Systems (and Advisors) Go!
Recent activity levels confirm that the countdown to ‘D-Day’ has finally started. Clients and advisers alike have realised that, although the paint is not yet dry, HMRC are still finalising some of the rules, and if action is not taken now, then 6 April 2017 and the new non-dom regime will be upon them and it may be too late. Delay is no longer a viable option.

As well as summarising the latest developments, this newsletter is designed to be a practical edition. And because everybody is so busy, with no time for extraneous reading, we have divided it into sections:

► What to do if you are a trustee
► What to do if you are a banker or investment adviser
► What to do if you are a non-dom tax payer

Our aim is to make life easier at this stressful time. We have a lot of practical experience of these issues so do speak to one of the contributors to this edition listed at the end of this issue, or your usual EY advisor.

We remain convinced that the final outcome for non-doms need not be all negative. Our message to non-doms is simple: Keep calm and carry on as a non-dom.
Tainting trusts: An update

One of the key features of the new rules for non-doms is the protected settlement. An important tenet of the protected settlement is that the valuable capital gains and income tax protections are lost once a trust becomes tainted. This can happen where a settlor or a trust of which the settlor is a beneficiary adds property to a settlement, subject to certain exceptions.

This raises a number of questions about what constitutes an addition of property for these purposes. In a recent announcement, HMRC has clarified its position slightly, at least in respect of interest-free loans. HMRC’s view is that interest-free loans repayable on demand will constitute an additional of property from 6 April 2017, even where the loan was made before that date. There may be some respite for term loans which may not be considered a provision of property until such a time as the term expires if the funds remain outstanding (although the position here is slightly less clear).

The HMRC clarification is both good news and bad news - good news in the sense that the position is now clear, but bad news for the many trusts and settlors with loans of this kind in place. Such loans will now urgently need to be reviewed in the light of the new rules.

To soften the blow, and in recognition of the fact that there is now little time to review these arrangements before the rules are implemented on 6 April, HMRC has announced that there will be some transitional provisions (though whether by means of legislation or concession is not yet clear). So, where loans remain outstanding at 6 April 2017, they will not be treated as additions (and so not taint the trust) so long as they are either repaid or put on a commercial footing by 6 April 2018. There is a catch, however. In order to qualify for this treatment a commercial rate of interest (or an amount in lieu) must be paid not just in respect of 2017/18 but also for 2016/17.

The HMRC announcement still leaves many unanswered questions – what is a commercial interest rate, for example? What is the position if the settlor is guarantor of a commercial loan from a third party? Discussions with HMRC continue, but at least those trusts with interest-free loans in place now know for certain the loans must be reviewed (and likely restructured) – albeit at the eleventh hour.

It’s a wrap

Investment wrappers have always had a role for the high net worth investor and they may become increasingly important in the new regime.

An investment wrapper is a structure which holds investments on behalf of the individual and their family instead of the individuals holding the investments in their personal names. Wrappers may be set up for non-commercial tax reasons, such as estate planning or asset protection. However, the wrapper is usually a separate taxpayer in its own right and, where the wrapper suffers no UK tax, or tax at a lower rate than personal rates, there can also be tax benefits.

Wrappers with which readers may be familiar include insurance products and personal investment companies but there are others.

Why might wrappers take on an increased significance from 6 April 2017?

Consider an individual with an offshore investment portfolio, investing only in non UK situate assets. The individual has always claimed the remittance basis and has never planned to remit from the portfolio. So income and gains have become mixed and reinvested over time. If the individual becomes deemed domiciled on 6 April 2017 they will pay income tax at rates of up to 45% on interest income, 38.1% on dividends and 20% on gains, even though the funds remain
offshore and are reinvested. In addition to an increased tax burden, the individual has increased
tax return complexity and costs and a higher administration burden if they decide to remit some
of the now taxed returns to the UK – bank accounts will need to be carefully organised as it will
still be important to keep the earlier unremitted returns segregated and outside the UK.

By moving the investments to a wrapper, and allowing the investment returns to roll up within
the wrapper the individual may achieve an outcome similar to the remittance basis; a lower or
even nil UK tax rate and a lesser compliance burden, deferring both of these until value is
extracted from the wrapper.

The choice of wrapper will be a personal one, depending, for example, on the investments the
individual wishes to hold, the level of control they wish to exert, and plans for future extraction.
Many taxpayers may set up more than one wrapper.

At EY, we can explain the tax treatment of the various wrappers on offer. We have also
developed a tool to help you evaluate the tax and banking costs of the alternative wrappers.
This can be tailored to your particular circumstances to assist you in your decision making.

STEP publish clarifications

The Society for Trust and Estate Practitioners (STEP) has published a Guidance Note which gives
further clarification of HMRC’s view of various aspects of the draft legislation on the taxation of
non-doms. The Note contains email exchanges with HMRC as well as clarification of certain
points by HMRC speakers at a tax conference.

In brief, some of the points covered by the Note are as follows:

Rebasing

► Rebasing will apply to assets held through partnerships (including LLPs and nominees).

► The remittance basis charge for 2016/17 or an earlier year must be paid to obtain the
benefit of rebasing.

► Rebasing will apply to assets acquired between 16 March 2016 and 6 April 2017 as well
as assets already held on 16 March 2016.

Mixed Fund Cleansing

► Pre-6 April 2008 income/gains cannot be cleansed.

► There are no ordering rules for cleansing so taxpayers can transfer out whatever they
want – income, gains, clean capital.

► There is no limit on the number of accounts into which a transfer can be made.

► Cleansing can apply to any individual non-domiciliary who has been subject to the
remittance basis in the past (other than a formerly domiciled resident, or ‘returning
dom’) even if that individual has subsequently acquired a UK domicile of choice.

Offshore trusts

► Interpretations following the 1991 rule change can be used for considering HMRC’s view
on tainting and trust additions. HMRC will not approach the issue of tainting
sympathetically.
► Capital payments made in earlier years to non-residents and matched prior to April will not be disturbed but pre-April 2017 capital payments to non UK residents cannot be used to match and wash-out future gains arising after April 6 2017.

UK residential property

► The provisions relating to collateral given for loans are recognised as going too far and HMRC will look again at these with a view to a cap.

► The two year rule for individuals is deliberately intended to apply to disposal of company shares but not to disposals of residential property.

For the full Guidance Note, available on the STEP website, see the Useful links section below.

Useful links

► [STEP Guidance Note](#) clarifying HMRC’s view of certain aspects of the legislation.

► [Additional draft clauses](#) published 26 January 2016

► [Response to consultation document](#) published 5 December 2016

► [Draft Finance Bill](#) published 5 December 2016

► Further [consultation document](#) published 9 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 2015 - [click here](#)

► Consultation document published 30 September 2015 - [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](#)
Action stations: what to do if you are a trustee

Trustees do not give tax advice (typically), but it is difficult to think of any offshore trusts that will not need to be reviewed before 6 April 2017. So what should trustees be doing? We make some suggestions below in the hope they will help trustees in this time of pressure.

1. Alert beneficiaries. It would seem prudent to write to beneficiaries and settlors to alert them to the magnitude of the changes and to recommend they consult with their tax advisers. We have helped some trustees draft such communications - let us know if we can assist here.

2. Understand the key technical drivers. Although trustees do not provide tax advice they will need to understand the main tax rules and the consequences that flow from them. For those administering trusts, the key points to focus on are:

   ► Offshore trusts will have a favoured status post-6 April but only if they are not tainted; see below on this critical point.

   ► Under this favoured status, they will be known as 'protected settlements'.

   ► The capital gains and non-UK source income can roll up free of UK tax in the trust.

   ► If a benefit is provided to a beneficiary post-6 April, that beneficiary will be subject to tax if they are dom or a deemed dom even if the benefit is provided outside the UK (subject to special rules for close family members).

   ► The anti-avoidance provisions are to be tightened, so the ability to wash out gains to non-residents and the basis on which benefits are valued are all to be changed. This means that post-6 April, trustees will need to think very carefully - and take tax advice as appropriate - before making any distributions.

3. Avoid tainting. This is probably the key thing for trustees to focus on. Tainting can start from 6 April 2017. Tainting is the provision of property or value to an existing trust by a settlor or a trust of which the settlor is a beneficiary. Tainting can be obvious, e.g., the addition of cash, but it can be less obvious, e.g., an interest-free loan. If a trust is tainted post-5 April it loses its protected status. In effect, it becomes transparent and the income and gains are taxed on the settlor.

So what should trustees do to avoid tainting? The short answer is to alert settlors to the problem, tell them to take advice and proceed with care. Other actions which may help include:

   ► Not accepting any additions to a trust post-6 April unless the person making the addition confirms they have taken tax advice (not only for their own position but on the wider tax consequences of the addition)

   ► Being aware of the position of interest-free loans and review the client portfolio for these. Read the update on HMRC’s views as set out below and consider if loans should be adjusted

   ► Reading SP5/92. This was published by HMRC the last time that tainting haunted offshore trust jurisdictions and is well worth dusting off

   ► Thinking about fees. Is this a chance to agree prepayments with clients? In any event, payment structures must be reviewed and no fee payment accepted post-6 April unless it is ‘fit for purpose’ in the new regime. HMRC has agreed that certain payments can be made to trustees for their services without tainting but that payments to underlying companies cannot. Agreements may thus need adjusting
Thinking ahead. What is likely to happen in the next few months and can preventive action be taken now? For example, a trustee may hold shares in a private company which is to be sold. If, as is common, the trustees do not give warranties on sale, but the settlor does on their behalf, then trustees may wish to consider whether post-April that might taint the trust. Should such an agreement be put in place now?

4. Be alive to the sort of readjustments to offshore structures which may be required before April. Your role may not be to give tax advice but a client may be appreciative if you are aware of planning options such as:

► If a beneficiary is to be a deemed dom on 6 April, would they like any trust distributions to be made pre-6 April while the remittance basis remains available?

► Should overseas assets (e.g., the Spanish villa) be extracted pre-April? From D-Day if the deemed domiciled beneficiary lives in an overseas property owned by the trust there may be a tax charge

► Should the trust be divided into two? Perhaps so that one part can be more closely monitored to avoid tainting

► If the trust is an excluded property trust with UK residential property, should the settlor be excluded to avoid gift with reservation problems. Has the client considered de-enveloping?

5. Be aware of the new anti-avoidance provisions and their potential impact on historic actions, present positions and future events. Trustees should perhaps consider recommending to clients that they have their structures ‘health-checked’ in light of the new rules. For example, have there been any earlier distributions which may now fall foul of the ‘onward gift’ rules or does a practice of distributions to non-residents have to be changed? Is the interest rate being paid on loans which would otherwise be capital payments in line with HMRC’s new valuation rules for benefits?

6. Think out of the box. ‘Rebasing’ (whereby offshore assets can benefit from a tax-free CGT rebasing where owned by individuals who become deemed domiciled on 6 April) and ‘cleansing’ (whereby mixed funds can be broken into their component elements) do not apply to offshore trustees. However, similar concepts should be considered with the trust’s tax advisers. For example:

► Assets within a trust can be rebased via a sub-fund election. This will trigger trust gains but in the right circumstances there would be no immediate tax charge. It there are outstanding capital payments which are yet to be matched, this may be a useful strategy before April. There are legal consequences of such a decision, however, and it should be considered carefully with the help of a relevant professional.

► If funds are distributed to a non-domiciled beneficiary, once they are in their account the beneficiary may be able to cleanse them in the April 2017 – April 2019 window.

7. The final ‘what to do’ point if you are a trustee? Pick up the telephone to EY if you need support. We would be pleased to chat. See the contributors list at the end of the newsletter or speak to your usual EY adviser.

8. Finally, it’s not all bad news for trustees. As explained in the news section, trusts will be very effective wrappers and do not require the beneficiary to pay the remittance basis charge.
Action stations: What to do if you are a banker or an investment adviser

Investment conditions must always be key. We may not have invented the maxim about tax tails wagging the investment dog, but we subscribe to it. Nevertheless, between now and 6 April 2017, investment advisers with non-dom clients cannot operate without a strong eye on the tax changes. So, here we offer some thoughts on what the bankers and wealth advisers helping clients with investments should have in mind.

1. First, know your client. It is no longer enough to classify clients as ‘dom’ or ‘non-dom’. In particular, you must know whether they become deemed domiciled on 6 April 2017 and if so, whether they will be returning doms or 15 out of 20 doms. Clients who will become deemed dom would be well advised to review their portfolios before that date. So speak to clients and recommend they review their status with their tax advisers.

2. Second, this is a great opportunity to discuss future plans with clients (and targets)! The non-dom changes may be tax changes but in truth the key discussions before April are lifestyle ones. Clients need to consider how long they are likely to stay in the UK; when they propose to leave, if ever; how much money they need offshore; how they will fund their UK expenses. The answers to these lifestyle questions will determine what they should do before April.

For example, a client who is in the UK for only a few years may decide to wrap his investments (see “It’s a wrap” in this issue, on that), live off his UK salary and then unwrap the tax shelter once he is offshore. In contrast, the client who is in the UK for the longer term may be much more focused on rebasing and the need to get clean capital in the UK.

3. Be familiar with the concepts of ‘rebasing’ and ‘cleansing’ and how these concepts can help your clients. The concepts were discussed in a prior edition of this newsletter (see link here) but in essence if an individual is deemed dom on 6 April (broadly because he or she has been UK resident for 15 out of the last 20 years) they can uplift the value of their assets tax-free to their 6 April value. This has a number of potential consequences:

   ► They are unlikely to want to sell their assets before 6 April;
   ► They will want to know market value at that date (although it may not be prudent to update tax packs to the 5 April values);

4. There may be possible actions for the client to discuss with their tax advisers – for example, move offshore investments from a UK dom spouse to a non-dom spouse before 6 April as only the latter may qualify for rebasing – but be sure to consider any inheritance tax impact here;

5. As a result of the new mixed fund ‘cleansing’ – the ability to break a mixed fund into its component parts to achieve a tax efficient remittance of funds to the UK – clients may contact you for records and, between April this year and April 2019, want your support with consequential help on bank account movements.

6. Contact your non-dom clients to ask them for any instructions (in conjunction with their tax advisers) on the changes (if any) they wish to make to their bank account structures. For those who do not become deemed dom on 6 April, it may well be the case that they will not request any changes. But be aware that they are likely to want such a discussion in the tax year before they become deemed domiciled.

For those becoming deemed domiciled on 6 April, more immediate change is likely. For example, if they have been participants in the traditional sport of mandating interest on the capital account into a separate income account, they may well choose to cease to play the game on 6 April. They will want
the interest on the capital account (which is from 6 April tax paid and so clean capital) added to the capital account.

7. Check with clients whether they want to take any actions before April – for example, if they do not quality for rebasing they may want to realise investments to take advantage of the remittance basis. If possible, they may want interest to be received before April for the same reason. Remember, if selling capital assets the 30 day bed and breakfast rule will apply;

8. Discuss investment philosophy and investment timelines with clients. As their domicile status changes, so might their investment parameters. Clients who are deemed domiciled may no longer be adverse to UK situs investments, for example.

9. When moving monies, consider asking clients if they need to speak with their tax adviser before confirming instructions. For example, some tax payers seem to believe that once they become deemed domiciled their offshore monies (taxable on the remittance basis) can be moved to the UK without a tax charge. This is not the case. Monies taxable on the remittance basis remain taxable on the remittance basis.

10. Start talking to clients about wrappers. See “It’s a wrap” in this newsletter. As clients start to pay tax on their worldwide income they may become more focused on tax deferral vehicles. Wrappers that are being discussed a lot at present are offshore insurance bonds and family investment companies. The latter provide clients with access to corporation tax rates and the practice of having two such companies is rapidly establishing itself – an offshore incorporated company for offshore investments funded by monies taxable on the remittance basis and a UK incorporated company for UK investments funded by a loan from clean capital.

11. If your client’s investments are held by trustees, speak to the trustees and perhaps read the trustee section in this newsletter.

12. And finally, get close to the client’s tax adviser. Increasingly, all decisions by the client are likely to benefit from consultation with you and their tax people.
Action stations: What to do if you are a non-dom taxpayer

The non-dom changes are fundamental and will recast the landscape. However, we are firmly of the view that for many non-doms the changes, with proper advice, need not be all negative. So what should non-dom taxpayers be doing between now and 5 April?

1. First, do speak to your advisers. While we still do not have all the detail from HMRC we have enough for decisions to be made. Do not defer the call to your trustees, your investment advisers or your tax adviser.

2. Second, it is imperative that you authorise and instruct your advisers to speak to each other. An action taken by one adviser without consultation with your other advisers may not be the best one.

3. Ensure you know your tax status. In particular when do you become a ‘deemed dom’. If you have been resident for 15 out of 20 years in the UK you are likely to become deemed dom on 6 April. This means you may need to take action before 6 April.

4. Make sure you have discussed the concepts of ‘rebasing’ and ‘cleansing’ with your advisers. See the earlier edition of this newsletter for details on these (link here). These ‘reliefs’ could provide a lot of opportunity to save tax and bring monies tax-free to the UK.

5. If you are the settlor and beneficiary of an offshore trust, make sure that you review its status before April. It is difficult to think of a single trust which will not need some form of adjustment at this time.

6. Discuss your future lifestyle intentions with your advisers. While the changes are tax driven, the real consequences are lifestyle. How long will you stay in the UK? How will you fund your UK expenditure? How you answer these questions will determine how you invest, where you invest and how many bank accounts you decide you need.

7. Discuss now the impact of your changing tax status on your investment philosophy. Do you need to change your bank account structures? Do you need to have separate capital and income accounts? Can you now invest in UK situs assets? Should you be using tax deferral ‘wrappers’ such as offshore bonds and family investment companies.

8. Finally, take a wide look at your tax affairs and consider also inheritance tax (IHT) planning. If your IHT strategy is based on relying on a double tax treaty, you may soon need a plan B as we do not expect these treaty benefits to be available in the medium to long term.
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