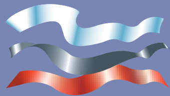

Saffery Champness
CHARTERED ACCOUNTANTS

INTERNATIONAL CLIENT

July 2010

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REGISTERED FIDUCIARIES

Editor's comment

Welcome to the July issue of International Client.

For the international client, the UK's Emergency Budget proved to be far less punitive than many had feared. A Capital Gains Tax (CGT) rise to 28% for higher-rate taxpayers is balanced against a generous extension of the existing Entrepreneur's Relief (charging CGT at just 10%) to a lifetime limit of £5 million of gains.

Perhaps more important though, were some measures at which the Emergency Budget just hinted. General tax avoidance and the taxation of non-domiciled individuals were two areas identified for review and in which future UK legislation can almost certainly be expected. We will publish more details in future issues of International Client as they are announced.

This issue contains a wide range of articles, from recent case rulings concerning foreign workers being 'Ordinarily Resident' in the UK, through to the pitfalls and opportunities of differing UK/India tax legislation.

I hope you find this issue interesting and informative. If you would like to discuss any of the issues raised here, please do not hesitate to contact us.

Clare Cromwell

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THE NEWSLETTER FOR INTERNATIONAL INDIVIDUALS, TRUSTEES AND THEIR ADVISERS

INTERNATIONAL CLIENT

01

THE UK'S EMERGENCY BUDGET: IMPLICATIONS FOR INTERNATIONAL INDIVIDUALS

Following the Emergency Budget on 22 June, in this article we outline the key measures announced by the Chancellor of the Exchequer that may impact upon international individuals living and/or working in the UK.

Capital Gains Tax

Capital Gains Tax (CGT) was the most widely-trailed topic in advance of the Emergency Budget. There was no surprise that an increase was announced, but there had been speculation that this would be 40% or even 50%. Instead, for higher rate taxpayers (paying Income Tax at 40% or 50%), UK resident trusts and non-UK domiciled individuals claiming the remittance basis (and paying the £30,000 "Remittance Basis Charge"), the flat rate of CGT has been increased to 28% for disposals after 22 June 2010. Otherwise, it remains at 18%.

The exemptions simply extend the existing Entrepreneur's Relief (charging CGT on qualifying assets at only 10%) by increasing the lifetime limit of eligible gains from £2 million to £5 million. The extension to a lifetime limit of £5 million of gains will undoubtedly be seen as very generous indeed.

There was also some expectation that the annual (CGT-free) allowance would be substantially reduced. However, it has remained intact, at £10,100.

It was something of a surprise though that the new measures would take effect from midnight on Budget day. There was an opportunity to encourage owners of capital assets to sell over the course of the remainder of this tax year at 18% CGT, and thereby create a one-off boost to tax revenues. This opportunity has been missed, and it is likely that many assets that might otherwise have been sold will now be retained until some future year when owners hope the CGT rate may fall again.

Incidentally, following the increase in the CGT rate from 18% to 28% the maximum effective tax rate on capital payments for UK resident beneficiaries (regardless of domicile) will increase from 28.8% to a mighty 44.8%.

Whilst the Budget was full of decided proposals (eg the increase in VAT to 20% from 4 January 2011), there were also several areas in which further action was sign-posted, with consultations and reviews initiated. These can presumably be seen as the shape of things to come.

Tax avoidance

The Government is to examine whether to bring in a general anti-avoidance rule (GAAR) to form one element of "strengthened defences". If this is brought into effect, we should expect widely drawn catch-all wording.

Many of the UK's international competitors have GAARs in place, so the Government may draw some comfort from the fact that a UK GAAR will not affect its international tax competitiveness.

Also, there are going to be "consultations" over the summer on bringing Inheritance Tax on trusts

within the disclosure of tax avoidance schemes regime.

Similarly, there is to be an examination to establish whether there should be further changes to the present rules governing Stamp Duty Land Tax on high-value property transactions, in order to prevent perceived avoidance in this area.

Non-UK domiciled individuals

The review of the taxation of non-domiciled individuals continues with a promised consideration as to whether there should be changes made to the current rules, which were substantially changed in the 2008 Finance Act, to ensure that such individuals "make a fair contribution to reducing the [Budget] deficit".

In the area of relief for pension premiums, the Government wishes to engage with employers, pension schemes, experts and other interested parties to establish the best design for a new relief regime to replace the proposed complex rules due to take effect from 6 April 2011. It is likely that there will simply be an annual maximum allowance for relievable contributions for everyone in the range of perhaps £30,000 to £45,000.

We will report on the outcomes of the areas being reviewed in future issues of International Client.

REAL ESTATE INVESTMENTS: FIVE REASONS TO USE A PIC

Real estate often features as a preferred asset class for many international clients, being a tangible and traditional investment, but providing diversification from the typical range of financial products offered by private banks. Moreover, owning property is often an emotive issue that goes beyond purely investment considerations.

International clients, particularly those from low or no-tax jurisdictions, may well acquire real estate without considering local taxation implications. But local taxation is not the only consideration. Using a foreign Private Investment Company (PIC) to make estate investments in more sophisticated and highly taxed jurisdictions (the UK being just one example) offers real benefits. We've outlined five very good reasons why a PIC could be a good asset:

1. Privacy

The use of a foreign PIC to purchase and own a property protects the client's identity from public disclosure. It is the PIC's name that appears in the Land Registry and the PIC's directors who represent the PIC in dealings with the vendors and estate/property management agents. This all helps to maintain a client's privacy.

2. Convenience

A PIC's directors and their administration team will co-ordinate the purchase and subsequent use and management of the property, dealing with all the day-to-day issues of managing, insuring and maintaining the property, generally through local professional agents.

3. Flexibility

The use of a PIC provides one point of contact for a client in all matters pertaining to a property. In addition, the interest in a PIC can be transferred at will to other family members or third parties with relative ease, compared to a transfer of shares in the real estate itself.

4. Taxation

A PIC can also be a useful way for non-UK resident and domiciled individuals to mitigate exposure to UK Inheritance Tax.

A word of warning though: professional advice on how to operate and administer a PIC structure must be taken to avoid unnecessary and unwanted UK tax liabilities.

5. Succession Planning

Though a PIC is not a succession planning tool in itself, it can be combined with more sophisticated forms of succession planning, retaining the benefits outlined above, for example through the use of trusts and foundations.

VOLCANIC ASH AN 'EXCEPTIONAL CIRCUMSTANCE'

HM Revenue & Customs (HMRC) has confirmed that any days that a non-UK resident has spent in the UK over and above the days they were actually due to be present in the UK, solely as a result of the volcanic ash cloud, will be treated as "exceptional circumstances" when looking at an individual's residency position and therefore ignored for the relevant test.

FOREIGN EMPLOYEES AND UNEXPECTED UK TAX BILLS

Two recent cases suggest that HM Revenue & Customs (HMRC) might be about to move the goalposts in relation to foreign workers being 'Ordinarily Resident' in the UK.

Where foreign employees are seconded to work in the UK, with the intention of staying for less than three years, it was understood that they would not be classed as Ordinarily Resident. This meant that they would only be taxed on an 'arising basis' on the proportion of their earnings that related to their UK duties. Therefore, provided the proportion relating to their non-UK duties is paid to them offshore it would be taxed only if remitted to the UK.

Fabio Genovese and Dr Andreas Tuczka both came to the UK with the intention of leaving within three years but, for a variety of reasons, they both stayed longer.

In the Genovese case, it was concluded that Mr Genovese should be treated as having become Ordinarily Resident from the beginning of the fiscal year in which he exceeded three years of working in the UK. In Dr Tuczka's case, however, it was concluded that the ruling in the Genovese case was wrong and, because Dr Tuczka was in the UK for employment, he had always been here for 'a settled purpose'. Therefore, he was treated as Ordinarily Resident from the date he originally arrived, regardless of any original intentions to be here for less than three years.

With an Income Tax rate of 50% and the fact that many internationally mobile individuals are highly paid, these recent precedents could cause a significant increase in their UK tax liability.

Advice should be sought well in advance of coming to the UK to take up employment.

OUR INTERNATIONAL REACH

Saffery Champness is a member of Nexia International, a worldwide network of independent accounting and consulting firms that operates from 105 countries, comprising 590 offices and over 20,600 personnel. Nexia is ranked amongst the top ten networks of its type worldwide by fee income. Our membership of the network significantly enhances our worldwide reach and the cross-border capacity available to our clients.

THE LIECHTENSTEIN DISCLOSURE FACILITY

The UK entered into a Tax Information Exchange Agreement with Liechtenstein on 11 August 2009, which is to become effective when both countries have completed the internal procedures required to bring into force the agreement.

On the same date, Liechtenstein announced a five-year "taxpayer assistance and compliance programme" and HM Revenue & Customs (HMRC) announced a five-year "special disclosure facility". This is known as the Liechtenstein Disclosure Facility (LDF) and runs from 1 September 2009 to 31 March 2015.

The LDF is peculiarly generous in comparison with HMRC's previous amnesty for UK residents. Firstly, the window in which to report extends for five years (compared to just a few months) and, more importantly, the period over which the taxpayer needs to review their affairs is restricted to only 10 years, from accounting periods/tax years beginning on or after 1 April 1999.

The penalty is restricted to only 10% of the outstanding tax and there is an assurance against criminal prosecution.

Certain criteria must be met to be able to take advantage of the LDF, but if a taxpayer has assets in Liechtenstein and has undeclared UK tax liabilities in respect of offshore income and gains from previous years, the LDF offers an excellent opportunity to regularise their affairs.

OUR OFFICE IN GUERNSEY

Saffery Champness has had an office in Guernsey for over 30 years and outside London it is the largest office in our network, with over 100 members of staff.

Guernsey is located off the coast of France and forms part of the Channel Islands. It is not part of the United Kingdom nor is it a member of the EU. It has its own Government, legal and taxation systems and, as a result, has grown to become one of the world's top 20 international finance centres. The island plays host to many banks, investment and fund management companies and fiduciaries, together with a supporting infrastructure of law and accountancy firms.

Our Guernsey office provides fund administration services plus the usual accountancy, audit and tax services. However, what distinguishes this office from its mainland siblings is that the vast majority of the staff is employed to provide fiduciary (trust and company) services. Indeed, we are now one of the largest independent providers of such services in the Channel Islands.

Guernsey has become one of the world's leading trust centres, primarily due to its stability (one of the oldest Governments in the world), its benign tax system (most trusts and companies managed in Guernsey suffer no tax on the island) and because of the wealth of experience that the island has developed over the years.

The clients that we look after are typically international individuals or families who want to establish trust and /or company structures to hold and manage their wealth.

They may establish their trusts for tax purposes, for estate planning, for asset protection or for a myriad of other reasons. The one thing that they all have in common is that they want to ensure that their assets will be safe, will be professionally managed and that they will receive a highly personal service from a firm that they trust and in a jurisdiction that they trust.

For more information on how we can assist you, don't hesitate to contact us directly.

HIRE ACT INCREASES COMPLIANCE COSTS

The US "Hiring Incentives to Restore Employment" (HIRE) Act was enacted by President Obama on 18 March 2010 and was effective immediately.

It is likely to have far-reaching and in some cases undesirable consequences for US citizens living outside the USA and for institutions with US clients or interests.

The Act was intended to encourage US firms to hire and employ unemployed individuals by offering tax credits and relief. However, elements of earlier legislation including the Stop Tax Haven Abuse Act are embedded in the HIRE Act.

Under the new rules, unless foreign financial/institutions enter into an agreement with the IRS to report information about its US account holders each year, a 30% withholding tax will be applied to all US investments. This will dramatically increase the compliance and reporting costs of such financial institutions and there is a suggestion that such institutions may choose to refuse US clients rather than have the added compliance burden. Entities such as trusts and family offices, which typically invest through these institutions, will also be affected.

The new legislation will also tax certain US beneficiaries of non-US trusts on their use of the property. Trustees and beneficiaries are therefore strongly recommended to seek professional advice regarding the implications of this as soon as possible.

TAX TREATMENT OF DELAWARE LLCS

Careful planning is required where UK residents operate their business through overseas entities as the UK tax treatment may differ from the overseas treatment.

One example is the Delaware LLC which is treated as a partnership and therefore tax transparent in the US. Consequently, the trading profits are taxed on the individual members.

However, the UK treats a Delaware LLC as a company for tax purposes and therefore regards the business profits as taxable at the company level.

This difference in treatment gives rise to a potential double tax charge in the UK when the distributions from the Delaware LLC are taxed on the individual. This is because the UK will not receive credit for the tax deducted in the US.

In the recent case of a Mr Swift, it was held that a particular Delaware LLC should be taxed in the UK as though it were a partnership and not a company. Therefore, Mr Swift was able to claim relief for the US tax suffered against his UK tax liability.

HM Revenue & Customs has issued a statement saying that, in essence, their position has not changed and they will not allow credit for the US tax deducted. However, they are prepared to look at any claims made for double tax relief in these circumstances.

INDIAN-UK TAXES: PITFALLS AND OPPORTUNITIES

INCOME AND CAPITAL GAINS TAX

Unlike in the UK, the terms Resident and Ordinarily Resident are specifically defined in Indian tax legislation.

An individual is said to be Indian Resident in the previous year if he was either:

a) 'in' India in that year for more than 181 days, OR

b) 'in' India for a total of more than 364 days over the four years preceding AND more than 59 days in the respective year

If you were a citizen of India and you left India in any previous year for employment outside India or have simply made earlier visits, then the last hurdle in (b) is increased from 59 to 181 days.

In addition, a person is not Ordinarily Resident in India in a previous year if he has:

a) been non-resident in nine of the 10 years leading up to the relevant year, or

b) has only been 'in' India in the seven years leading up to the relevant year for less than 730 days (just over 104 days per year)

As India's economy becomes more influential and third generation Indians living in the UK increase their contact with India-based family, it is entirely possible to become Resident and possibly even Ordinarily Resident in India with the consequential duty to report to the tax authorities. The UK/India Double Tax Treaty should prevent any clear miscarriages, but the taxpayer should be aware that it is possible to become Indian resident by spending only three months a year in India.

Inheritance Tax

A very old treaty also exists to cover capital taxes, but appears to have been simply forgotten because in the UK, Inheritance Tax (IHT) is charged on an individual's estate when an individual gives away assets and/or upon their death, but India has not had an equivalent tax since 1985.

The fact remains that the treaty is still in force and in the right circumstances it will ensure that non-UK assets in an Indian domiciled individual's estate are chargeable to Indian estate taxes (ie no taxation at all) as opposed to UK estate taxes of up to 40%.

It is very important to note that the treaty will only protect the estate on death. It will not protect lifetime gifts and therefore a significant mismatch can occur.

When an individual dies who, under general law, is domiciled in some part of India, the UK is restricted by the treaty to charging IHT only on property situated in the UK. Property situated in the rest of the world is therefore not subject to death taxes in the UK or India (watch for local taxes though).

In the UK, for IHT purposes, there is also the concept of 'deemed' domicile. An individual who is not domiciled in the UK for general law purposes will be 'deemed' to be UK domiciled for IHT purposes once he has been resident in the UK for at least 16 out of the previous 20 years.

Therefore, on the face of it, the worldwide assets of an individual who has maintained their general law domicile in India but who has been in the UK for a long time and so is 'deemed' UK domiciled are subject to UK IHT on their death at 40%. However, under the treaty, all of the non-UK situated assets should be excluded from the UK's IHT charge.

Contrast this with the IHT position where an individual gifts their entire estate away the day before they die. This 'inter-vivos' gift would not be covered by the treaty and so the entire value of the gift would suffer UK IHT.

Therefore, where a UK taxpayer is domiciled in India and has significant non-UK assets, they should seek advice on their estate planning options to ensure the optimum use of this treaty.

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