

Amendments 2 to 32 to Clause 35 and Schedule 10: Settlements: anti-avoidance etc

Summary

1. Clause 35 and Schedule 10 introduce anti-avoidance provisions in relation to payments and benefits made from offshore trusts. These technical amendments ensure that the anti-avoidance provisions inserted in the Income Tax (Trading and Other Income) Act (ITTOIA) 2005 operate as intended by clarifying that they apply to both capital and income benefits and ensuring that they will not result in income tax charges on non UK resident beneficiaries and that no double charges arise.

Details of the amendments

2. Amendments 2 to 32 amend paragraph 11 of Schedule 10, which introduces new sections 643A to 643N into ITTOIA 2005.
3. Amendments 2 to 5 amend new section 643A of ITTOIA 2005 (deemed income because of benefits for settlor or close family member). The amendments ensure that there is no income tax charge on the recipient where a benefit paid to a settlor or close family member is matched to protected foreign-source income at a time when he or she is non UK resident.
4. Amendment 6 amends new section 643B of ITTOIA 2005 (meaning of 'untaxed benefits total' in section 643A). The amendment clarifies that the new benefits charge can apply to benefits provided out of both capital and income of the trust and how it will apply in cases where the settlor or close family member is entitled to the income as it arises.
5. Amendments 7 to 11 amend new section 643C of ITTOIA 2005 (meaning of 'available protected income' in section 643A). The amendments amend the definition of 'protected foreign-source income' to ensure that there is no double charging in cases where the trustees have distributed income or made payments out in relation to trust expenses, or where the recipient is already liable to income tax on that income.
6. Amendments 12 to 14 amend section 643F of ITTOIA 2005 (income attributed by section 643A to user of remittance basis). They replace the definition of 'available protected income' with a definition for 'protected income' and define 'the relevant individual'. These definitions apply for the purposes of new sections 643F and 643G.
7. Amendments 15 to 26 amend new section 643G of ITTOIA 2005 (section 643F(4): benefits and income 'relating' to deemed income). The amendments amend the ordering rules to ensure that they work as intended in a case where income is treated as arising to the settlor under new section 643A; and to clarify how items will be

deducted in the calculations in respect of earlier charges under either the settlements benefits code or the transfer of assets code.

8. Amendments 27 and 28 amend new section 643I of ITTOIA 2005 (recipients of onward gifts). The amendments ensure that where there is a chain of gifts to which the onward payment rule applies, the original beneficiary will be absolved from tax liability on the original benefit to the extent it is taxed on a subsequent recipient.
9. Amendment 29 makes a consequential amendment to new section 643K of ITTOIA 2005 (cases where deemed income attributed to recipient of onward gift) as a result of the amendment to section 643A(1) made by Amendment 1.
10. Amendments 30 to 32 amend new section 643M of ITTOIA 2005 (onward gift to settlor or close family member by other recipient). The amendments ensure that no tax charge arises under section 643M where the original recipient was taxed on the original benefit.

Background note

11. Chapter 5 of Part 5 of ITTOIA 2005 (Chapter 5) treats income arising to the trustees of a settlor-interested offshore trust as arising to the settlor (irrespective of whether the settlor enjoys the income). Where income is not treated as arising to the settlor it is treated as income of the settlor if it is distributed or otherwise payable to his minor child. Capital sums (such as loans) paid to such settlors in excess of the trustees' undistributed income is also treated as income arising to the settlor. Where the remittance basis applies to the settlor, foreign-source income is taxed in the year in which it is remitted.
12. However, the Chapter 5 provisions no longer apply to the foreign-source income of certain trusts created when the settlor was not domiciled in the UK (protected foreign-source income) following changes provided by Schedule 8, Part 2 to the Finance (No. 2) Act 2017.
13. As the settlor charges have been disapplied, and to prevent avoidance, paragraph 11 of Schedule 10 to the Finance (No. 2) Bill introduces a new benefits charge into Chapter 5 where benefits paid to the settlor or a close member of his family can be matched against protected foreign-source income. Where the benefit is provided to a close family member of the settlor who is not taxable, a charge can be imposed on the settlor if he is UK resident.
14. In addition, it is possible for an offshore trust to route payments to a UK beneficiary via other beneficiaries who are either not UK resident or who are remittance basis users without the UK resident beneficiary paying UK tax. Paragraph 11 of Schedule 10 tackles this form of avoidance by introducing an onwards payment rule. This ensures that payments made from a trust to a beneficiary who is not UK resident or is a remittance basis user who gives or lends it back to a UK beneficiary within 3 years will be taxed on the UK resident beneficiary.
15. These amendments are needed in order to clarify that the anti-avoidance provisions

inserted by paragraph 11 of Schedule 10 apply to both capital and income benefits and to ensure that they will not result in income tax charges on non UK resident beneficiaries and that no double charges arise.

16. The changes provided by Schedule 10 were announced in December 2016 at paragraphs 2.3.3 (taxation of foreign income in overseas trusts) and 2.3.5 (recycling benefits from protected settlements) of the government's response to further consultation on reforms to the taxation of non-domiciles. The consultation response can be found at: <https://www.gov.uk/government/consultations/reforms-to-the-taxation-of-non-domiciles-further-consultation>