Offshore Bond Trust – Long Term UK Residency

The Finance Act 2008 introduced new rules for the taxation treatment of those resident but non-domiciled in the UK. This arrangement allows funds, up to a certain level, to be remitted to the UK annually without tax charge provided that it is created and managed properly. It is a solution for those who will be long-term resident and non-domiciled in the UK.

Features

An offshore trust is created and cash is settled. It is important that the cash settled does not contain unremitted foreign capital gains or foreign income which arose during a period in which the settlor was UK resident.

An offshore company is also created by the trustees and the trustees lend the settled funds interest free to the company. The funds are invested by the company in an offshore bond from an offshore insurance company. The gains within the bond are not realised until the bond is encashed, or it matures, but the company can make an annual withdrawal from the bond of up to 5% of the amount originally invested. The withdrawal from the bond within this limit is treated as a partial encashment and is not deemed to be income or a chargeable gain for the purposes of UK taxation.

The company makes annual loan repayments to the trust of an amount equivalent to the bond withdrawal. The trustees can then make distributions from the trust up to the same amount as the loan repayment and thus provide tax free funds in the UK.

If the settlor leaves the UK permanently the bond can be allowed to mature or be encashed as soon as he is no longer deemed to be UK resident for tax purposes. The gain on encashment or maturity will not then be subject to UK taxes.

However, if the settlor remains in the UK beyond the maturity or encashment of the bond, the gain arising on encashment, whilst arising within the company, will still be attributed to the settlor. Such gains are subject to income tax on an arising basis at the appropriate rate. This can be avoided.

If it becomes clear that the settlor is likely to remain UK resident beyond the encashment or maturity of the bond the trustees can make arrangements to sell the company shares to a third party, usually an offshore bank. The sale will be negotiated based upon the value of the company assets (the bond). The company sale will be treated as a chargeable disposal for capital gains tax purposes. Only gains then remitted to the UK would be subject to capital gains tax, in the hands of the recipient. If gains are retained by the trustees offshore and later remitted a supplementary charge to tax is incurred.

Advantages

- Provides a tax free source of funds in the UK for resident non-domiciled individuals
- The investment growth remains offshore and is not subject to UK taxation until encashed
- Bond can be encashed or allowed to mature once the settlor has left the UK and is not resident for UK tax purposes
- The company can be sold prior to bond encashment creating a chargeable gain subject to capital gains tax, if remitted to the UK, at a rate significantly less than the rate of income tax payable if no action is taken
- Can avoid payment of £30,000 "remittance basis charge", if circumstances allow

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