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PRIVATE CLIENT TAX PLANNING 2009

UK RESIDENT NON-UK DOMICILIARIES – MANAGING THE FA 2008 REGIME TO ADVANTAGE

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Simon McKie

MA (Oxon), Barrister, FCA, CTA (Fellow), APFS TEP

McKie & Co (Advisory Services) LLP
Rudge Hill House
Rudge
Somersetshire
BA11 2QG

Tel: 01373 830956 Fax: 01373 830326
Email: simon@mckieandco.com
Website: www.mckieandco.com

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SECTION I

INTRODUCTION

1.1.1 The Pre-Budget Report 2007 seems an age away. So much has happened since then in the economy that the agitation over the taxation of private equity and the strange political manoeuvrings which led to the introduction of the Remittance Basis Charge seems like a tale of another age.

1.1.2 The new regime is monstrously complex and it is only in its application to concrete examples that one can see its implications. So this lecture considers a series of examples illustrating its operation in detail.

SECTION II

APPLICATION OF THE REMITTANCE BASIS: SECTIONS 809B – 809E[1]

AN EXAMPLE

Example I

Senor Sidoli[2] became resident in the United Kingdom in the fiscal year 2001/02 together with his wife Maria and his youngest son Giovanni, who was born on the 31st May 1991. They have remained resident and ordinarily resident in the UK since that time. His eldest son, Guiseppe, who was born on the 31st August 1985, remained in Italy to complete his schooling until the 30th June 2003 so that he became resident and ordinarily resident in 2003/04 and thereafter.

None of the family made any capital gains in 2008/09 nor had any employment income for that year nor had they remitted any income or capital gains in respect of previous years. Their investment income for the year was as follows:-

NAME	UK INCOME £	OVERSEAS INCOME ARISING IN YEAR £	OVERSEAS INCOME REMITTED IN YEAR £
Paolo	100,000	500,000	300,000
Maria	Nil	4,000	2,500
Giovanni	1,000	30,000	2,500
Guiseppe	0	30,000	2,500

1 All reference in these notes are to ITA 2007 unless otherwise stated

2 All characters in the examples in this lecture are not domiciled in a country of the United Kingdom and are resident and ordinarily resident here unless otherwise stated. They have made an election under s.809B to which s.809C applies for all relevant years unless otherwise stated

Paolo makes a claim for the remittance basis to apply. Section 809B applies to him for 2008/09 because he is UK resident in that year, he is not domiciled in the United Kingdom in that year and he has made a claim under that section. He is also within s.809C so he must nominate the income to which the Remittance Basis Charge is to apply.

Maria falls within s.809D for 2008/09 because she is resident in the UK but not domiciled here in that year and her unremitted foreign income and gains are less than £2,000 (£4,000 – £2,500).

Giovanni does not fall within s.809E because he has UK source income. He therefore makes a claim under s.809B. He does not fall within s.809C because he is not eighteen years of age or over at any time in 2008/09.

Guiseppe also doesn't fall within s.809E because he has remitted income and gains to the United Kingdom. He therefore makes a claim under s.809B. He does not fall within s.809C because he has not been UK resident for at least seven of the nine years immediately preceding 2008/2009.

The result is that the remittance basis applies to every member of the Sidoli family in 2008/09 but the Remittance Basis Charge applies only to Paolo.

SECTION III

THE EFFECT OF THE REMITTANCE BASIS ELECTION: SECTIONS 809F AND 809G

AN EXAMPLE

Example II

This example considers the effects of the remittance basis by comparing the results of making and not making the election. Mr Reinette has the following income and gains.

	INCOME AND GAINS	INCOME AND GAINS ARISING AND RECEIVED IN UK
	£	£
UK Employment Income	250,000	250,000
Gains on UK situated Assets	10,000	10,000
Foreign dividends not from minority holdings	50,000	5,000
Foreign dividends from minority holdings	27,000	5,400
Interest on foreign bank accounts	20,000	0
Capital Gains on assets situated outside the UK	8,000	0
	365,000	270,400

N.B. Unremitted income and gains are £94,600.

Taxation Calculation without Remittance Basis

	£
Income Tax	
UK employment income	250,000
Foreign dividends not from minority holdings	50,000
Foreign dividends from minority holdings	

27,000 x 10/9	30,000	
Interest on foreign bank account	20,000	
Total income	350,000	
Less personal allowance	6,035	
Total income after personal allowance	343,965	
Income Tax thereon:-		
34,800 @ 20%	6,960	
80,000 @ 32.5%	26,000	
229,165 @ 40%	91,666	
	124,626	
Tax credit (£27,000 x 1/9)	<3,000>	
Total Income Tax liability		121,626
Capital Gains Tax		
Capital Gains	18,000	
Less: annual exemption	9,600	
Excess of taxable amount over annual exemption	8,400	
Capital Gains Tax @ 18%		1,512
Combined Income and Capital Gains Tax if no election is made		£123,138

Taxation Calculation with Remittance Basis Election[3]

	£
Income Tax	
UK employment income	250,000
Non-qualifying foreign dividends	5,000
Qualifying foreign dividends 5,400 x 10/9	6,000
	261,000
Income tax thereon:-	
34,800 @ 20%	6,960
226,200 @ 40%	90,480
	97,440

[3] The amounts assessable under s.809H are shown separately below

Tax credit (£6,000 - £5,400)	<600>	
Total Income Tax Liability		96,840

Capital Gains Tax

Capital Gains	10,000	
Capital Gains Tax 18%		1,800
Additional tax assessable under Section 809H		30,000
		128,640
Less tax if no election had been made		123,138
Increase in tax due to election		£5,502

RECONCILIATION

	£	£
Tax saved on unremitted income		
Foreign dividends not from minority holdings ((£50,000 - £5,000) @ 32.5%)	14,625	
Foreign dividends from minority holdings ((£30,000 - £6,000) @ 32.5%) – ((£30,000 - £6,000) ÷ 10)	5,400	
Interest on foreign bank account (£20,000 – 0) @ 40%	8,000	
		<28,025>
Loss of personal allowance £6,035 @ 40%		2,414
Loss of 32.5% rate on foreign dividends (£5,000 + £6,000) @ (40% - 32.5%)		825
Tax saved on unremitted gains £8,000 @ 18%		<1,440>
Loss of CGT annual exemption £9,600 @ 18%		1,728

Remittance Basis charge	30,000
	5,502

SECTION IV

EFFECT ON WHAT IS CHARGEABLE – CAPITAL LOSSES

TCGA 1992 SECTIONS 16ZA – 16ZD

SECTION 16ZA

4.1.1 Section 16ZA provides that an election may be made in "the relevant tax year". The relevant tax year is the first year for which:-

(a) a claim for the Remittance Basis is made; and

(b) the individual is not domiciled in the United Kingdom.

4.1.2 If no election is made in the relevant tax year it cannot be made in respect of subsequent years. There is, however, a long period to decide whether or not the election should be made because the time limit is the standard one in TMA 1970 s.43, being five years after the 31st January next following the year of assessment to which it relates.

4.1.3 If the individual does not make an election, foreign losses accruing to him in:-

(a) the relevant tax year; or

(b) any subsequent tax year except one in which he is domiciled in the United Kingdom

are not allowable losses.

4.1.4 Note that this would disallow losses even in a year in which a taxpayer has not made the Remittance Basis election.

SECTION 16ZB

4.2.1 Where the election is made, s.16ZB has the effect that losses cannot be set off against foreign chargeable gains which have arisen in a previous tax year but which are treated as accruing in a later tax year by reason of their remittance.

4.2.2 This is so whether or not the individual has made a Remittance Basis election for the year concerned.

SECTION 16ZC

4.3.1 Section 16ZC applies to an individual for a tax year if:-

(a) the individual has made an election under s.16ZA;
(b) the Remittance Basis applies to the individual for that tax year; and
(c) the individual is not domiciled in the United Kingdom in the tax year.

4.3.2 Where the section applies, a series of steps are specified for the purpose of calculating the amount on which an individual is to be charged to Capital Gains Tax for the tax year. Under those steps, allowable losses are deducted first from foreign chargeable gains accruing to the individual in the tax year which have been remitted in that year. Secondly, they are deducted from foreign chargeable gains accruing to the individual in that year to the extent that they have not been so remitted. Thirdly, they are deducted from other chargeable gains accruing to the individual in that year. In arriving at a taxpayer's gains chargeable to Capital Gains Tax for the year, however, the losses deducted from foreign chargeable gains accruing to the individual in that year which have not been remitted in the year are ignored.

4.3.3 The result is that losses set against foreign chargeable gains which are not remitted in the year are regarded as having been used and therefore cannot relieve other gains and, in particular, chargeable gains on disposals of UK situated assets.

AN EXAMPLE

Example III

Mr Umaga makes the following gains, losses and remittances. His foreign income is sufficiently large so that it is clear that it will be advantageous for him to make the Remittance Basis election in 2008/2009 and 2009/2010. His income is less in 2010/2011 so he needs to determine his capital gains tax position in order to determine whether or not to make the Remittance Basis election. He makes an election under TCGA 1992 s.16ZA. His capital gains, losses and remittances of gains in the years 2008/2009 – 2010/2011 are as follows.

Year	Gains		Losses		Remittances of Gains realised in:		
	UK	Foreign	UK	Foreign	2008/09	2009/10	2010/11
2008/09	100,000	0	0	200,000	0	N/A	N/A
2009/10	0	500,000	400,000	0	0	0	N/A
2010/11	0	500,000	0	0	0	500,000	200,000

No election under Section 16ZA

2008/2009	**£**	
Capital Gains (UK)	100,000	
Allowable losses	0	(foreign losses are not deductible)
	100,000	

2009/2010	**£**
Capital Gains	0

2010/2011	**£**
Capital gains (500,000 + 200,000)	700,000
Less losses brought forward	<400,000>
	300,000

Election under Section 16ZA

2008/2009

Section 16ZB does not apply because foreign chargeable gains have not accrued on or after the relevant tax year (2008/2009) but before the applicable tax year (2008/2009). Section 16ZC applies.

Capital Gains	100
Foreign losses deducted from non-foreign chargeable gains	<100>
	0

2009/2010

Section 16ZB does not apply because foreign chargeable gains have not accrued on or after the relevant tax year (2008/2009) but before the applicable tax year (2009/2010). Section 16ZC applies.

Apply steps in s.16ZC(2).

	Foreign chargeable gains arising and remitted in year (a)	Other foreign chargeable gains accruing in the year (b)	Other gains accruing in the year (c)
Step I	**£**	**£**	**£**
Gains	0	500,000	0
Losses deducted			
Foreign losses BF (200,000 – 100,000)			
UK losses of the year (400,000)	<0>	<500,000>	0

Step II

The chargeable amount is equal to aggregate chargeable gains (£0) less losses deducted under (a) and (b) above (£0). So the chargeable amount for the year is nil.

2010/2011

Section 16ZB and Section 16ZC apply.

Step I

	Foreign chargeable gains arising and remitted in year £	Other foreign chargeable gains accruing in the year £	Other gains accruing in the year £
Gains	200,000	300,000	0
Losses offset	0	0	0

Unremitted gains carried forward are £300,000 of the gains arising in 2010/2011.

If he does not make the Remittance Basis election he will be taxed on the full £50,000 of foreign gains which arose in the year. By making the election he is taxed on only the £200,000 of those gains which were remitted in the year.

Mr Umaga is taxable on the aggregate of:-

		£
(a)	The adjusted taxable amount	200,000
(b)	The relevant gains (the gains realised in 2009/2010 were reduced by the set off of losses in 2009/2010 under Step I of s.16ZC(2))	0
	Amount on which Capital Gains Tax is chargeable	200,000

	Without Election	**With Election**
	£	**£**
Aggregate gains on which CGT is chargeable in 2008/2009 – 2010/2011	400,000	200,000
Allowable losses carried forward at 6th April 2011	0	0
Realised but unremitted gains at 6th April 2011	300,000	300,000

Making the election allows the foreign losses made in 2008/2009 to be utilised. One might not make the election in circumstances where one wants losses to be set-off against UK gains rather than unremitted gains.

SECTION V

THE REMITTANCE BASIS CHARGE: SECTION 809H

AN EXAMPLE

Example IV

Mr Chabal has the following income and gains in 2008/2009.

	Income and gains arising in year	Remittances of income and gains arising in year[4]	Foreign tax suffered
	£	£	£
UK capital gains	10,000		
Foreign source interest income	20,000		10,000
Foreign source dividend income not on a 'minority holding'	40,000	35,000	
Foreign capital gains	170,000		30,000

Mr Chabal, seeing that he has unremitted income and gains of £195,000 makes the remittance basis election nominating the foreign source interest income and the foreign capital gains.

Under s.809H(2) Income Tax and Capital Gains Tax are calculated as if the nominated income and gains were not subject to the Remittance Basis.

	Arising Basis	Remittance Basis	Total
Income Tax			
Foreign interest (grossed up for foreign tax)	30,000	-	30,000
Foreign dividends	-	35,000	35,000
Total income			£65,000

[4] No income or gains from prior years were remitted in the year

	Arising Basis	Remittance Basis	Total
Less personal allowance[5]			6,035
			58,965
Tax thereon:-			
At 20% on 34,800			6,960
At 40% on 24,165			9,666
			13,626
Less double tax relief			<10,000>
			£3,622
Capital Gains Tax			
Gains in year (£200,000[6] + £10,000)	210,000	-	210,000
Capital Gains Tax thereon at 18%			37,800
Less double tax relief			<30,000>
			7,800

Under s.809H(4) & (5) one then makes a comparison with the tax liability which would have arisen if the nominated income were not included in taxable income.

Income Tax	£
Foreign dividend income	35,000
	35,000
Tax thereon:-	
At 20% on 34,800	6,960
At 40% on 200	80
	7,040
Capital Gains Tax	
Gains in year	10,000

[5] Under s.809H(2) the Income Tax charged on the nominated income and gains is charged as if s.809B did not apply to the individual in the year so it is only from the nominated income that one can deduct the personal allowance. If this personal allowance had exceeded the nominated income, the excess could not have been deducted from the foreign dividend income

[6] Grossed up for foreign tax

Capital Gains Tax thereon at 18%	1,800

Relevant tax increase (s.809H(5))

Liability including nominated income (3,622 + 7,800)	11,422
Liability excluding nominated income (7,040 + 1,800)	8,840
	2,582

Deemed increase to nominated income under s.809H(4)

(£30,000 - £2,582) x 100/40	68,545

Mr A's Liability for the Year

Liability including actually nominated income	11,422
Liability on income deemed to be nominated under s.809H(4) (68,545 @ 40%)	27,418
	38,840

Should Mr A have made an election under s.809B?

Liability without Election

Income Tax	**£**
Foreign source interest	30,000
Foreign source dividends	40,000
	70,000
Less personal allowance	6,035
	63,965
Tax thereon:-	
At 20% on 30,000	6,000
At 10% on foreign dividends of 4,800	480
At 32.5% on 29,165	9,479
	15,959
Less double tax relief	<10,000>
	5,959

Capital Gains Tax

Total gains	210,000
Annual exemption	9,600
	200,400
Capital Gains Tax at 18%	36,072
Less: double tax relief	<30,000>
	6,072

Total tax liability on an arising basis

Income Tax	5,959
Capital Gains Tax	6,072
	12,031

Why has the Remittance Basis claim proved to be unfavourable, in spite of the fact that Mr Chabal has unremitted gains of £195,000? These are four reasons. First, he has lost the personal allowance. Second, he has lost the Capital Gains Tax Annual Allowance. Thirdly, he has lost the dividend rates on foreign dividends. Fourthly, s.809H(4) effectively denies him the benefit of double tax relief on the income he nominates.

Can Mr Chabal withdraw his claim? TMA s.33(2A)(c) prevents an error or mistake claim. But is a bad decision to make a claim an error or mistake within s.33 in any event? He could amend his return within TMA s.9ZA but only within twelve months of the filing date.

What would have happened if the nominated income had borne tax in excess of £30,000? Section 809C(4) would have had the result that the claim was invalid. The Financial Secretary to the Treasury said in the debates on the Finance Bill that taxpayers in these circumstances would be invited by HMRC to amend their return. That assumes that HMRC are capable of reliably identifying such cases.

SECTION VI

SECTIONS 809I AND 809J: ORDER OF REMITTANCES

AN EXAMPLE

Mr A has the following income and capital gains in 2008/2009.

	Income and gains arising in the year £	**Income and gains remitted in the year which have arisen in the current year**[7] £	**Foreign tax suffered** £
UK trading income	50,000		
Foreign rental profits	50,000		
Foreign interest	50,000	10,000	
Foreign earnings	20,000		
Foreign dividends on minority holdings	30,000	30,000	20,000
Foreign dividends not on minority holdings	88,000	26,400	12,000
UK gains	10,000		
Foreign gains	90,000	18,000	10,000

Mr A's claim under s.809B for 2008/2009 nominates the whole of his foreign interest under s.809C(2). He was not aware that £10,000 of his interest had been remitted to the United Kingdom. Because it had been so remitted, s.809I applies and therefore s.809J applies to substitute a deemed order of remittance for the actual remittances.

[7] There are no remittances in respect of prior years' income and gains

If s.809I applies, the following steps are to be taken for the purpose of determining the income or gains treated in a tax year (the "relevant tax year") as remitted to the United Kingdom by the individual.

Step One – find the total amount of:-

(a) *The individual's nominated income and gains; and*

(b) *The individual's remittance basis income and gains*

that have been remitted to the United Kingdom in the relevant tax year. This amount is the "relevant amount".

		£
(a) =		10,000
(b) =	(£50,000[8] + £30,000[9] + £20,000[10])	100,000
		110,000

Step Two – find the amount of foreign income and gains of the individual for the relevant tax year (other than income or chargeable gains nominated under s.809C) that is within each of the categories of income and gains in paragraphs (a) to (h) of subsection (2). If none of ss.809B, 809D and 809E apply to the individual for that year, treat those amounts as nil (and accordingly go to step 6).

(a) =	Relevant foreign earnings (other than those subject to a foreign tax)	20,000	(foreign earnings)
(b) =	Foreign specific employment income (other than income subject to a foreign tax)	0	(none)
(c) =	Relevant foreign income (other than income subject to a foreign tax)	50,000	(rental profits)

[8] Foreign dividends and gains grossed up for foreign tax suffered
[9] Foreign dividends and gains grossed up for foreign tax suffered
[10] Foreign dividends and gains grossed up for foreign tax suffered

(d) =	Foreign chargeable gains (other than gains subject to a foreign tax)	0	(none)
(e) =	Relevant foreign earnings subject to a foreign tax	0	(none)
(f) =	Foreign specific employment income subject to a foreign tax	0	(none)
(g) =	Relevant foreign income subject to a foreign tax	150,000	(foreign dividends)[11]
(h) =	Foreign chargeable gains subject to a foreign tax	100,000	(foreign chargeable gains)[12]

Step Three – find the earliest paragraph for which the amount determined under Step Two is not nil. If that amount does not exceed the relevant amount, treat the individual as having remitted the income or gains within that paragraph (and for that tax year). Otherwise, treat the individual as having remitted the relevant proportion of each kind of income or gains within that paragraph (and for that tax year. The "relevant proportion" is the relevant amount divided by the amount determined under Step Two of that paragraph.

£20,000 of the relevant amount of £110,000 is matched with foreign earnings.

Step Four – reduce the relevant amount by the amount taken into account under Step Three.

The relevant amount is reduced by £20,000 to £90,000.

Step Five – if the relevant amount (as reduced under Step Four) is not nil, start again at Step Three. In Step Three, read the reference to the earliest paragraph of the kind

[11] Foreign dividends and gains grossed up for foreign tax suffered
[12] Foreign dividends and gains grossed up for foreign tax suffered

mentioned there as a reference to the earliest such paragraph which has not previously been taken into account under that step.

Steps Three and Four are repeated so that the relevant amount is matched with the foreign rental profits of £50,000. The remaining £40,000 of the "relevant amount" is matched pro rata with the foreign dividends.

Step Six – if the relevant amount (as reduced) is not nil once Steps Three to Five have been undertaken in relation to all paragraphs of subsection (2) for which the amount determined under Step Two is not nil, start again at Step 2.

The relevant amount is nil.

So Mr A's total remittances of £110,000 are deemed to be remittances of:-

	£
Foreign earnings	20,000
Foreign rental profits	50,000
Foreign dividends on minority holdings (£40,000 x 50/150)	13,333
Foreign dividends not on minority holdings (£40,000 x 100/150)	26,667
	110,000

What are the effects of ss.809I and 809J on Mr A's tax liability?

If ss.809I and 809J had not been enacted.

	£	£
Income Tax		
UK trading income		50,000
Foreign interest:-		
Actually remitted	10,000	
Nominated	40,000	
		50,000

Foreign dividends on minority holdings[13] 50,000 + (50,000 x 1/9)	55,555
Foreign dividends not on minority holdings[14]	30,000
	185,555
Income assessable under s.809H(4) (£30,000 – (£40,000 @ 40%)) x 10/4	35,000
	220,555

Tax thereon:-	**£**
34,800 @ 20%	6,960
185,755 @ 40%	74,302
	81,262
Less tax credit on foreign dividends from minority holdings	<5,555>

Double Tax Relief

Foreign dividends on minority holdings restricted to ((55,555 @ 40%) – 5,555)	<16,667>
Foreign dividends not on minority holdings	<12,000>
Total liability	47,040

	£
Capital Gains Tax	
UK gains	10,000
Remitted foreign gains[15]	20,000
	30,000
Capital Gains Tax @ 18%	5,400
DTR 10,000 x 10/100	<1,000>
	4,400

[13] Foreign dividends and gains grossed up for foreign tax suffered
[14] Foreign dividends and gains grossed up for foreign tax suffered
[15] Foreign dividends and gains grossed up for foreign tax suffered

Total Income Tax and Capital Gains Tax

Income Tax	47,040
Capital Gains Tax	4,400
	51,440

Actual Tax Liability

	£
Income Tax	
UK trading income	50,000
Foreign earnings	20,000
Foreign rental profits	50,000
Foreign dividends on minority holdings	13,333
Foreign dividends not on minority holdings	26,667
Nominated income (foreign interest)	50,000
Income assessable under s.809H(4) (30,000 – (50,000 @ 40%)) x 10/4	25,000
	235,000
Tax thereon:-	
34,800 @ 20%	6,960
200,200 @ 40%	80,080
	87,040
Less tax credit on foreign dividends on minority holdings	<1,333>
Double Tax Relief	
Foreign dividends on minority holdings restricted to ((13,333 @ 40%) – 1,333)	<4,000>
Foreign dividends not on minority holdings 26,667 / 100,000 x 12,000	<3,200>
	78,507
Capital Gains Tax	
UK gains	10,000

Tax thereon @ 18%	1,800

Total Income Tax and Capital Gains Tax

Income Tax	78,507
Capital Gains Tax	1,800
	80,307
Less liability which would have arisen but for ss.809I & 809J	51,440
Increase in liability due to ss.809I & 809J	28,867

SECTION VII

SECTIONS 809Q AND 809R: MIXED FUNDS

MIXED FUNDS

7.1.1 Sections 809Q and 809R contain rules for determining the composition of transfers from mixed funds.

SECTION 809Q

7.2.1 Section 809Q applies only where Condition A in s.809L is met and:-

> *"(a) the property or consideration for the service is (wholly or in part) or derives (wholly or in part, and directly or indirectly) from, a transfer from a mixed fund, or*
>
> *(b) a transfer from a mixed fund, or anything deriving (wholly or in part, and directly or indirectly) from such a transfer, is used as mentioned in section 809L(3)(c)."*

7.2.2 Where the section applies it applies only for the purposes of determining whether Condition B in s.809L is met and if it is met, determining (under s.809P) the amount of income or chargeable gains remitted.

7.2.3 It is important to appreciate, therefore, that the rules in s.809Q only apply for very limited purposes.

7.2.4 Where the section applies subsection (3) provides a five-step process for determining the composition of the transfer from the mixed fund.

SECTION 809R

7.3.1 Section 809R also applies for narrow purposes. It applies only for the purpose of Step One in s.809Q(3), under which, for each of the categories of income and capital set out in subsection (4) of s.809Q, one finds the amount of income or capital of the individual for the relevant tax year which is in the mixed fund immediately before the transfer.

7.3.2 As we have seen, s.809Q only applies where there is a transfer from a mixed fund (subsection (1) ibid). Subsection (6) ibid defines a mixed fund as:-

> *"... money or other property which immediately before the transfer contains or derives from-*
>
> *(a) more than one of the kinds of income and capital mentioned in subsection (4), or*
> *(b) income or capital for more than one tax year."*

7.3.3 Because s.809R applies only for the purposes of Step One of s.809Q(3) it does not apply for the purposes of s.809Q(1) and (6). Therefore, in deciding whether one has a mixed fund at all, on a literal construction, one cannot apply the rules for determining the composition of the fund which are contained in s.809R. Where s.809R applies, the following rules are to be followed under Step One of S.809R (3):-

> *"(2) Treat property which derives wholly or in part (and directly or indirectly) from an individual's income or capital for a tax year as consisting of or containing that income or capital.*
>
> *(3) If a debt relating (wholly or in part, and directly or indirectly) to property is at any time satisfied (wholly or in part) by –*
>
> *(a) an individual's income or capital for a tax year, or*

(b) anything deriving (directly or indirectly) from such income or capital,

from that time treat the property as consisting of or containing the income or capital if and to the extent that it is just and reasonable to do so.

(4) Treat an offshore transfer from a mixed fund as containing the appropriate proportion of each kind of income or capital in the fund immediately before the transfer.

"The appropriate proportion" means the amount (or market value) of the transfer divided by the market value of the mixed fund immediately before the transfer.

(5) A transfer from a mixed fund is an "offshore transfer" for the purposes of subsection (4) if and to the extent that section 809Q does not apply in relation to it.

(6) Treat a transfer from a mixed fund as an "offshore transfer" (and section 809Q as not applying in relation to it, if it otherwise would do) if and to the extent that, at the end of a tax year in which it is made –

(a) section 809Q does not apply in relation to it, and
(b) on the basis of the best estimate that can reasonably be made at that time, section 809Q will not apply in relation to it.

(7) In this section 'mixed fund' means money or other property containing or deriving from –

(a) more than one of the kinds of income and capital mentioned in section 809Q(4), or
(b) income or capital for more than one tax year.

(8) If section 809Q applies in relation to part of a transfer, apply that section in relation to that part before applying subsection (4) in relation to the rest of the transfer.

(9) If section 809Q applies in relation to more than one transfer from a mixed fund, when undertaking step 1 in relation to the second or any subsequent transfer take into account the effect of step 2 of section 809Q(3) (composition of transfer) as it applied in relation to each earlier transfer."

7.3.4 Having provided very detailed computational rules for determining the composition of transfers from mixed funds the draughtsman has then included a mini-general anti-avoidance rule (the "Mini GAAR") in s.809S which provides as follows:-

"(1) This section applies if, by reason of an arrangement the main purpose (or one of the main purposes) of which is to secure an income tax advantage or capital gains tax advantage, a mixed fund would otherwise be regarded as containing income or capital within any of paragraphs (f) to (i) of section 809Q(4).

(2) Treat the mixed fund as containing so much (if any) of the income or capital as is just and reasonable.

(3) "Arrangement" includes any scheme, understanding, transaction or series or transactions (whether or not enforceable).

(4) "Income tax advantage" has the meaning given by section 683.

(5) "Capital gains tax advantage" means –

(a) a relief from capital gains tax or increased relief from capital gains tax,

(b) a repayment of capital gains tax or increased repayment of capital gains tax,

(c) the avoidance or reduction of a charge to capital gains tax or an assessment to capital gains tax, or

(d) the avoidance of a possible assessment to capital gains tax."

AN EXAMPLE OF THE APPLICATION OF SECTIONS 809Q & 809R

Mr Van Heerden set up a Jersey Bank Account (the "A Account") on the 31st March 2005. He transferred all of his money into this account, being £2m. On the same day he also established another account (the "B Account") without placing any money in it at that time. He earmarked the B Account for his foreign source income.

He instructed his bankers that when interest was credited annually to the A account it was to be transferred on the same day to the B Account. The following interest was credited to the A Account in this way and then transferred to the B Account:-

30th April	**£**
2005	10,000
2006	120,000
2007	100,000

This interest was not subject to foreign tax.

Until this time he had not been resident or ordinarily resident in the United Kingdom but he became so on the 6th April 2005.

On the 30th June 2006 Mr Van Heerden made a disposal of foreign situated assets, receiving proceeds of £500,000 which he paid into the A Account and realised a gain of £100,000. This gain was subject to foreign tax.

On the 30th June 2007 he received a dividend of £500,000 from a UK company and paid that dividend into his A Account.

On the 31st March 2008 he closed the A Account transferring the balance of £3,090,000 to a new Jersey Account (the "C Account"). The balance transferred included £90,000 of interest which was credited to the account on its closing.

He instructed the bank that any interest arising in respect of the balance on the C Account should be credited to his B Account.

On the 15th April 2008 he paid a cheque of £1m in respect of a foreign dividend into his C Account. In completing the instruction to his bankers he had inadvertently given the account number of his C Account instead of that of the B Account. This dividend was subject to foreign tax.

On the 30th April 2008 he transferred £500,000 from the A Account to his wife's Isle of Man account.

On the 31st May 2008 he transferred £250,000 to a new account in the Isle of Man which he had established.

On the 30th June 2008 he transferred £1m from the A Account to his UK bank account.

How do ss.809Q and 809R apply to these transactions?

The Transfers on the 30th April 2008 and 31st May 2008

Condition A of s.809L is not satisfied in respect of the moneys transferred to Mr Van Heerden's wife so s.809Q does not apply. Similarly, Condition A is not satisfied in

relation to the moneys transferred to Mr Van Heerden's Isle of Man account on the 31st May 2008 and so again s.809Q does not apply to that transfer.

The Transfer of 30th June 2008 to Mr Van Heerden's UK Bank Account

The transfer on the 30th June 2008 to Mr Van Heerden's UK bank account satisfies Condition A because money was brought to the United Kingdom by a relevant person. We shall assume that the property, the money transferred, is a transfer from a mixed fund within s.809Q(1)(a). Therefore, in determining whether Condition B is met we must apply the five steps set out in s.809Q(3).

Step 1

For each of the categories of income and capital in paragraphs (a) to (i) of subsection (4), find (applying section 809R) the amount of income or capital of the individual for the relevant tax year in the mixed fund immediately before the transfer. "The relevant tax year" is the tax year in which the transfer occurs.

The opening balance of Account C was received from Account A on the 31st March 2008. That was not a transfer to which Section 809Q applied and so under s.809R(5) it was an offshore transfer. Therefore, one must treat the transfer from the A Account to C Account as containing "the appropriate proportion of each kind of income or capital in the fund immediately before the transfer." As the whole fund was transferred the appropriate proportion is one.

So the question is: what kinds of income and/or capital did the A Account hold immediately before the transfer on the 31st March 2008?

Section 809R tells one to treat property which derives wholly or in part (and directly or indirectly) from the individual's income or capital for the tax year as consisting of or containing that income or capital. So if we can say that the balance on the A Account

derived from Mr A's income or capital wholly or in part we must treat the account as consisting of or containing that income or capital.

The account must derive from the money paid into it, except to the extent that those moneys have been paid out of it. How are we to match transfers out of the account with transfers into it? The answer is that if those transfers are not transfers within s.809Q, which they will only be if Condition A of s.809L is met in respect of the transfer concerned, then they are offshore transfers and they consist of the appropriate proportion of each type of income and capital in a mixed fund under subsection (4) ibid.

The only transfers out of the C Account before the closing transfer were the transfers of interest. Because of Mr Van Heerden's instruction to his bankers, that interest was first to be credited to the account and was then to be transferred to the B Account. The result of subsection (4) is that the transfers in respect of that interest did not consist wholly of interest for the purposes of s.809R. We therefore need to work out what was transferred on each occasion on which there was a transfer in respect of interest.

Date	Transaction	Capital	Foreign interest	Foreign capital gains	UK dividend income	Net movement	Balance
31/03/2005	Opening capital	2,000,000				2,000,000	2,000,000
30/04/2005	Interest credited		10,000			10,000	2,010,000
30/04/2005	Transfer to B Account	<9,950>	<50>			<10,000>	2,000,000
		1,990,050	9,950	-	-	2,000,000	2,000,000
30/04/2006	Interest credited		120,000	-	-	120,000	2,120,000
30/04/2006	Transfer to B Account	<112,644>	<7,356>	-	-	<120,000>	2,000,000
		1,877,406	122,594	-	-	2,000,000	2,000,000
30/06/2006	Capital proceeds credited	400,000		100,000	-	500,000	2,500,000

Date	Transaction	Capital	Foreign interest	Foreign capital gains	UK dividend income	Net movement	Balance
30/04/2007	Interest credited		100,000		-	100,000	2,600,000
30/04/2007	Transfer to B Account	<87,593>	<8,561>	<3,846>	-	<100,000>	<2,500,000>
		2,189,813	214,033	96,154	-	2,500,000	2,500,000
30/06/2007	UK dividend receipt				500,000	500,000	3,000,000
31/03/2008	Interest credited		90,000			90,000	3,090,000
31/03/2008	Transfer to C Account	<2,189,813>	<304,033>	<96,154>	<500,000>	<3,090,000>	0
		0	0	0	0	0	0

So we have now determined the composition of the opening balance on the C Account and we can apply the like process to determining the composition of the account immediately before Mr A's transfer to his UK bank account on the 30th June 2008.

Date	Transaction	Capital	Foreign interest without foreign tax	Foreign capital gains with foreign tax	UK dividend	Foreign dividend with foreign tax	Net movement	Balance
31/03/08	Opening balance	2,189,813	304,033	96,154	500,000	0	3,090,000	3,090,000
15/04/08	Foreign dividend rec'd					1,000,000	1,000,000	4,090,000
15/04/08	Transfer to wife	<267,703>	<37,168>	<11,755>	<61,125>	<122,249>	<500,000>	3,590,000
		1,922,110	266,865	84,399	438,875	877,751	3,590,000	3,590,000
31/05/08	Transfer to IOM Account	<133,852>	<18,584>	<5,877>	<30,562>	<61,125>	<250,000>	3,340,000
		1,788,258	248,281	78,522	408,313	816,626	3,340,000	3,340,000

So the amounts of income and capital within each of the categories given in subsection (4) were as follows:-

		£
(a)	employment income (other than income within paragraph (b), (c) or (f))	0
(b)	relevant foreign earnings (other than income within paragraph (f))	0
(c)	foreign specific employment income (other than income within paragraph (f))	0
(d)	relevant foreign income (other than income within paragraph (g))	248,281
(e)	foreign chargeable gains (other than chargeable gains within paragraph (h))	0
(f)	employment income subject to a foreign tax	0
(g)	relevant foreign income subject to a foreign tax	816,626
(h)	foreign chargeable gains subject to a foreign tax	78,522
(i)	income or capital not within another paragraph of this subsection	2,196,571
		3,340,000

Step 2

Find the earliest paragraph for which the amount determined under step 1 is not nil. If that amount does not exceed the amount of the transfer, treat the transfer as containing the income or capital within that paragraph (and for that tax year). Otherwise, treat the transfer as containing the relevant proportion of each kind of income or capital within that paragraph (and for that tax year). "The relevant proportion" is the amount of the transfer divided by the amount determined under step 1 for that paragraph.

The earliest paragraph is Category (d) and so the £1m transferred is treated as containing £248,281 of the foreign interest which had been credited to the A Account.

Step 3

Treat the amount of the transfer as reduced by the amount taken into account under step 2.

The transfer of £1m is reduced by £218,281 to £751,719.

Step 4

If the amount of the transfer (as reduced under step 3) is not nil, start again at step 2. In step 2, read the reference to the earliest paragraph of the kind mentioned there as a reference to the earliest such paragraph which has not previously been taken into account under that step in relation to the transfer.

The amount of the transfer has not been reduced to nil so one starts again at Step 2. This time, the earliest paragraph for which the amount determined under Step 1 is not nil is paragraph (g). That amount exceeds the remaining balance of the transfer and so one treats the transfer as containing the relevant proportion of each kind of income or capital within that paragraph and for that tax year. Thus, the remaining transfer of £751,719 is matched with the foreign dividend. The amount of the transfer is then reduced by the amount matched with the foreign dividend to nil.

Step 5

If the amount of the transfer (as reduced under step 3) is not nil once steps 2 and 3 have been undertaken in relation to all paragraphs of subsection (4) for which the amount determined under step 1 is not nil, start again at step 1.

In step 1, read the reference to the relevant tax year as a reference to the tax year immediately before the last tax year for which step 1 has been undertaken in relation to the transfer.

The amount of the transfer as reduced is nil.

So Mr Van Heerden's transfer on the 30th June 2008 to his UK bank account consisted of foreign interest which had not borne foreign tax of £248,281 and foreign dividends of £751,719 which had borne foreign tax.