

August 2008 International Private Client Services Newsletter

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Welcome to the latest edition of the BDO International Private Client Services (IPCS) Centre of Excellence Newsletter, which we hope will be of interest to you. The articles contained in this newsletter have been prepared for your general information only and should not be acted or relied upon without first seeking appropriate professional advice for your circumstances. If you would like any further information on any of the topics discussed in this newsletter, please contact the person named at the end of each article. We would welcome contributions to future editions of this newsletter and, if you would like to submit an article or have any comments or suggestions with regard to this publication, please contact Effie Karamani by email at effie.karamani@bdo.co.uk or by telephone on +44 207 893 2384.



Peter Burnside
Tax Partner

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Spain

Abolition of Wealth Tax

On 13 June 2008 the Spanish government announced that wealth tax will be abolished with effect from 1 January 2008.

The rates of Spanish wealth tax ranged from 0.2% to 2.5%, one of the highest in the EU. Austria, Denmark, Finland, Luxembourg, The Netherlands and Sweden have all abolished wealth tax in recent years, leaving Spain and France as the only EU countries to continue imposing a wealth tax. The Spanish government is now following suit.

The abolition of wealth tax also benefits non-resident individuals, which will undoubtedly make Spain more attractive for investment purposes.

Capital Gains Tax Discrimination under EU Legislation

In 2005 Spain was reported to the European Commission for the different tax treatment of capital gains derived from the sale of Spanish property depending on whether or not the transferor was resident in Spain for tax purposes.

Under former Spanish income tax law, capital gains made by non-residents in Spain were taxed at 35% while residents were taxed at a much lower rate of 15%.

Under these circumstances, the Commission found that Spanish law was not compatible with the capital movement guaranteed by Article 56 of the European Community Treaty, as well as the principle of non-discrimination, and therefore decided to refer the case to the European Court of Justice (ECJ). As a result, Spain modified its domestic tax law by applying a uniform capital gains tax rate of 18% for both residents and non-residents, with effect from 1 January 2007.

However, although the Commission considers that the modification of the tax rates removes the discrimination, it is continuing with the ECJ proceedings. Importantly, Spanish law does not provide any mechanism for addressing this type of situation.



In view of the above, non-Spanish resident individuals who sold assets prior to 1 January 2007 are entitled to register a claim with the Spanish tax authorities and request a tax rebate equal to the difference between the 35% and 15% tax rates. The time limit for registering these claims is four years from the date of payment of the capital gains tax.

The assumption within professional circles is that the Spanish tax administration will deny the claims and it will therefore be necessary to take the case to the Spanish courts. If the claims are rejected by the Spanish courts, the ECJ will need to be consulted and the Spanish Government will then be obliged to act in accordance with the decision of the ECJ.

If the case is successful, the claimants should expect a refund of the excess tax from the Spanish tax administration, together with interest from the date of overpayment. For the time being, however, it is necessary to await the decision of the ECJ and a judgment that Spain's conduct is unlawful.

Finally, individuals resident in countries where tax is levied on a worldwide basis should take into account that, if this claim is successful, some or all of the Spanish tax refunded may have to be paid over to the tax authorities in their country of residence.

For further information and advice on Spanish tax matters, please contact Daniel Aroca of BDO Audiberia via e-mail at daniel.aroca@bdo.es or by telephone on + 34 93 209 8802.

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Switzerland

Diamonds, Toothpaste, and Tax Evasion

The attack

The legendary veil of secrecy covering Swiss financial institutions is facing its greatest ever threat from the US Department of Justice and Internal Revenue Service (IRS), following the plea bargain by Bradley Birkenfeld, formerly of UBS. Bradley Birkenfeld was recently indicted for assisting US citizen, Igor Olenicoff, to hide assets in low-tax jurisdictions such as Switzerland, Panama, Hong Kong, and Liechtenstein.

In addition, Bradley Birkenfeld has admitted to helping file misleading and false tax returns in the United States, placing cash and valuables in safe-deposit boxes, and buying jewellery and artwork for his customers. The extent to which he was prepared to assist clients was revealed when he confirmed that on one occasion, at the behest of a US client, he purchased diamonds using the client's Swiss bank account and smuggled the diamonds into the United States in a toothpaste tube.

As a consequence of the evidence given by Bradley Birkenfeld, a Miami federal judge has ruled that UBS must provide details of all offshore accounts held by

US citizens that might not have been declared to the IRS. UBS allegedly holds assets worth an estimated USD 20,000million, and it has been suggested that it may have assisted with the evasion of USD 300million in US taxes.

It is clear that the veil of secrecy promised by Swiss banks is now under significant threat. So much so that the Swiss Federal Banking Commission has turned its attention to UBS, concerned by the prospect that, together with other banks, it has brought the good name of Switzerland and its banking laws into disrepute.

In the latest twist, UBS has already succumbed to increasing pressure from the United States to disclose confidential information about its customers. On 17 July 2008, Mark Branson, the chief financial officer of UBS's global wealth-management unit announced to a US Senate hearing that UBS plans to close the Swiss bank accounts of all of its American customers and will no longer provide offshore banking or securities services to US residents through its banks. Further, UBS will now agree to handing over to the IRS the names of an undisclosed number of its customers.



Other interested parties

The question now is whether this ground-breaking development will tear open the veil of secrecy covering Swiss banks and, if so, whether this will result in the exposure of Swiss banks to further requests to exchange information with other proactive jurisdictions aligned with the United States, such as the United Kingdom, Germany and France. Certainly, the OECD (covering 35 jurisdictions) and European Union have already exerted pressure on the Swiss authorities to be more transparent and exchange information.

The Swiss banking model is perceived to have an unfair advantage due to its privacy laws and up until now foreign officials tracing the movements of funds have been forced to end their quests at the Swiss border. There have therefore been calls for low-tax jurisdictions to be more transparent and disclose not only the tax withheld in respect of foreign customers but also to exchange this information with the jurisdiction in which the customer resides. It would seem that the actions of Bradley Birkenfeld and UBS may have handed the IRS and other jurisdictions a perfect opportunity to challenge these laws as it has been alleged that not only did the customers submit false returns, but that they were knowingly assisted by the bank. Tax fraud is an offence under Swiss law and therefore the Swiss authorities have already acknowledged that they will be working with the IRS and Department of Justice.

These calls follow the recent press coverage concerning the Liechtenstein bank scandal and the high-profile criminal investigations in Germany for alleged tax fraud. It has also been announced in the last few weeks that Germany has reached an agreement with Jersey to exchange information.

What does the future hold?

Going forward, it is anticipated that Switzerland will agree to a treaty with the European Union by the end of the year to combat fraud, which will also include administrative and legal assistance in cases of tax evasion involving value added tax.

The European Union has suggested Switzerland and other low-tax jurisdictions should review the current agreement allowing these countries to deduct a

withholding tax on the interest earned on the accounts of foreign customers. At present, the withholding tax is easily circumvented with special financial products and 'letterbox companies'. The Savings Directive is scheduled for renewal in 2013 and at recent meetings in Brussels the representatives of low-tax jurisdictions and 'tax havens' were not prepared to discuss banking secrecy. Further, they resisted attempts to accelerate the timetable for reviewing the Directive.

It is believed that the United States will also continue to pursue greater transparency from countries it perceives to be tax havens. In 2007 the 'Stop Tax Haven Abuse Act' was introduced in the United States, which provided for tough measures against 34 jurisdictions including Switzerland, Panama, British Virgin Islands, Luxembourg and Liechtenstein. Interestingly, one of the bill's sponsors is Senator Barack Obama, the Democratic candidate for the US Presidency.

How can we help?

Individuals concerned with the impact of the request for information from UBS and the calls for transparency from low-tax jurisdictions and tax havens should seek specialist professional advice. It is anticipated that other tax jurisdictions will also benefit from the exchange of information with UBS so this should be seen as an early warning. By taking appropriate advice now, the potential damage may be mitigated.

In serious cases, it is essential that proactive steps are taken to secure immunity from prosecution and negotiate a civil settlement of any tax arrears, where possible.

For information and advice on Swiss tax matters please contact Thomas Kaufmann of BDO Visura via e-mail at Thomas.kaufmann@bdo.ch or on +41 (0)44 444 37 15.

BDO Stoy Hayward LLP has a specialist Tax Investigations department dealing solely with voluntary disclosures to the UK tax authorities and managing enquiries and investigations. For further information and advice please contact John Hood via e-mail at john.hood@bdo.co.uk or by telephone on +44208 893 3484 or Dawn Register via e-mail at dawn.register@bdo.co.uk or by telephone on +44208 893 2653, at the London office.

For information and advice on US tax matters please contact Jack Nuckolls via e-mail at jnuckolls@bdo.com or by telephone on +1 415 490 3393 or Stephanie Hunt via e-mail at shunt@bdo.com or by telephone on +1 212 885 7401.

3 Europe

Update on the European Savings Directive

Further to Article 18 of the European Directive 2003/48/EC of 3 June 2003 (taxation of savings income in the form of interest payments), the European Commission was recently required to prepare a report on the operation of the European Union Savings Directive (EUSD). An initial interim report ("Working Document", reference.: SEC/2008/559) has been prepared, presented and discussed at the Economic and Financial Affairs Council (ECOFIN) meeting of 14 May 2008.

This document highlighted the areas that need to be targeted in the future, including the coverage of intermediate vehicles (companies resident in tax havens, partnerships and trust structures) and a review of the scope of financial products covered by the EUSD, both of which are currently being used to avoid its application.

As the EUSD does not apply to interest paid to companies, this means that both the disclosure requirements and withholding tax (depending on the country in which the interest is paid) may be avoided. Also, a series of financial products (mainly 'structured' or 'derivative' financial products and

certain investment funds) do not currently fall within the scope of the EUSD. Some Member States have even expressed their wish to extend the application of the Savings Directive to dividends, capital gains and life insurance payments.

The European Commission is trying to coordinate the work on these areas with internal working groups of the Member States' representatives as well as involving the market operators in the review process. One of the issues to consider is the potentially excessive administrative charges that the EUSD may impose on market operators.

The full report of the European Commission, expected at the end of the year, will contain a quantitative analysis of the EUSD and proposals on how to improve it.

It should be noted that any amendment of the current EUSD may require the approval of a new Directive, which in turn would require the consent of the 27 Member States, the associated and dependent territories and third countries that are currently applying measures comparable to the EUSD on a contractual basis with each EU Member State.



For further information and advice in respect of European tax matters, please contact any of the European members of the IPCS Centre of Excellence listed on page 14.

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Israel

Significant Benefits Announced for New Immigrants and Returning Residents

The Israeli authorities are proposing significant improvements to the tax benefits granted to new immigrants and returning residents.

The benefits proposed include an exemption from tax and from reporting requirements on all non-Israeli source assets held and income derived by the new immigrant and certain returning residents (former Israeli-resident individuals who have resided abroad for at least 10 years before returning to Israel – this may be reduced to five years for individuals returning to Israel in the tax years 2008 and 2009) for a 10-year period commencing from the individual's arrival.

The tax exemptions will apply to all types of income, including, inter alia, interest and dividends from abroad, rental income from property located outside Israel, employment income, business income and capital gains upon the sale of non-Israeli assets, including securities portfolios.

At present, tax exemptions are granted to both a new immigrant and returning resident for a five year period on passive income derived from non-Israeli assets acquired prior to immigration (interest,

dividends, annuities, royalties, and rent). Similar exemptions are granted solely to a new immigrant for four years on business income, should the business have been held by the new immigrant for at least five years prior to immigration. It should be pointed out that at present the new immigrant is required to report all income, whether or not ultimately exempt from tax.

A further tax mitigation to be offered is with regard to foreign companies managed and controlled by new immigrants and returning residents. These companies are not to be deemed Israeli-resident, under certain conditions, merely as a result of their being managed and controlled by the new immigrant or returning resident. This is for a period of 10 years after the immigration.

The benefits package will undoubtedly enhance Israel's status as a jurisdiction attractive to high net worth individuals wishing to enjoy a low-tax regime.

For further information or advice on Israeli tax issues please contact Eli Alice of BDO Ziv Haft via e-mail at elial@bdo.co.il or by telephone on +972 3 638 6868.



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The Netherlands

Proposed Reform of Inheritance and Gift Tax

In April 2008 the Netherlands State Secretary for Finance outlined his plans for an inheritance tax reform. A bill will be proposed in 2009 with the intention that the new inheritance tax regime comes into force on 1 July 2010. The proposed changes will potentially have a significant impact on individuals who are not resident in the Netherlands but have Netherlands connections.

Current Position

Currently, Netherlands inheritance tax (*successierecht*) is imposed on worldwide assets if the deceased is tax resident in the Netherlands, regardless of the residence status of the heirs to his/her estate. If the deceased is not resident in the Netherlands, the heirs will be liable to inheritance tax on Netherlands sited assets only. The residence position of the deceased therefore determines the scope of the inheritance tax charge, although the heirs are liable for the tax.

An individual who has previously been resident in the Netherlands will continue to be treated as tax resident in the Netherlands for inheritance tax purposes up to and including 10 years after his/her migration.

New Proposal

Under the proposal, the tax residence of the heirs will determine the scope of the liability to inheritance tax. If the heirs are resident in the Netherlands they will be liable to inheritance tax on their share of the worldwide estate, irrespective of the country of residence of the deceased at his or her death. Heirs resident in a country other than the Netherlands will only be liable to inheritance tax on Netherlands sited assets.

Further, at present the tax is levied on children on the death of the first parent even if no actual inheritance is received because all of the assets pass to the surviving parent. The new proposal includes provision for postponing the tax charge in these circumstances until the death of the second parent.

Taxpayers, Rates and Exemptions

The current inheritance tax law contains four tariff groups each with seven tax brackets. The State Secretary has proposed reducing the tariff groups to two:

- Category 1, applicable to children and partners, and
- Category 2, applicable to all other heirs.

The State Secretary proposes to reduce the number of tax brackets in each category to two. For Category 1 the maximum tax rate will be 20% and for Category 2, less than 50%. The Government believes that by widening the tax base this will reduce the amount of tax payable per person.

Abolition of Tax Planning Methods

The State Secretary also proposes to introduce measures to bring an end to the following tax planning methods/structures:

- **Combination will:** This type of will entitles heirs to choose the most advantageous way of inheriting the estate.
- **Trust structures:** Discretionary trusts shelter funds from tax because assets held by a trust no longer belong to the settlor and are not yet in the ownership of the beneficiary.
- **Avoiding the 10-year term:** If an individual leaves the Netherlands and takes up the nationality of his/her new country of residence before the end of the 10-year period, the Netherlands no longer has a claim on his/her estate.
- **Revocable gifts.**

International Aspects

Property inherited from foreign trusts or foundations by a Netherlands-resident individual will be subject to inheritance tax in the Netherlands. Double taxation relief will be available for tax paid in the other country.

A potential tax charge may also be introduced on the 'deemed income' of a Netherlands resident beneficiary in respect of assets held in the trust.

Business Succession

The new proposal also addresses the need to simplify the current business succession procedures. An investigation is being conducted to determine whether more business-friendly conditions can be applied when granting exemption from inheritance tax on the transfer of business assets. A review is also being undertaken to determine whether protective tax assessments issued by the tax authorities in such cases may be abolished.

In applying the exemption from inheritance tax on business succession, valuations of a business at arm's-length market rates need to be taken into account. The means that unrealised goodwill and hidden reserves are included.

Conclusion

If the proposed changes become effective from 1 July 2010 they will have a major impact on former Netherlands-residents with children in the Netherlands who are their heirs, as well as for individuals who have set up a trust and wish to return to the Netherlands or where the beneficiaries of the trust are Netherlands-resident.

Once there is more clarity and certainty regarding the new proposals, careful planning will be essential in the next couple of years for individuals affected by the changes.

For further information and advice on Netherlands tax issues, please contact Toine van Beers of BDO CampsObers via e-mail at toine.van.beers@bdo.nl or by telephone on +31 40 269 82 88.

6 Russia

Investment in Residential Real Estate in Moscow

In the past, the Land Code of the Russian Federation restricted the rights of foreign nationals to acquire and let land in border districts. The revision of this Code has now made it possible for non-Russian citizens to acquire land in the Russian Federation. It is therefore a good time for investors to consider the booming residential real estate market in Moscow.

Why invest in Moscow?

In 2007, the apartment sales market was one of the most rapidly developing real estate sectors in Moscow. Average prices for new prime residential properties increased by 22.9% in the course of last year. It was thought after the unprecedented 90% rise in 2006 that further uplift was unlikely. However, this did not prove to be the case. The sustained price growth can be explained by the limited supply and by the growing unsatisfied demand.

For those wishing to invest in property for letting, the high rates of inflation need to be taken into account. In 2007 alone the official average rate of inflation amounted to almost 12% (source: «Rosstat»). In accordance with Russian law all rental payments need to be effected in Russian roubles. However, as most apartments are let for a term of less than 12 months, this provides an opportunity to renegotiate subsequent rental prices. Demand for quality living accommodation will either be high or low depending on whether rentals are fixed in currency units (e.g. equal to US\$ or Euro) and payments are effected in Russian roubles (RUR) at the applicable rate on the date of payment.

Tax Implications

The Russian Federation has double tax treaties in place with more than 60 countries, including most



European states, the US, Canada and Australia. As a general rule these treaties give Russia the taxing rights over income derived from the lease and/or sale of immovable property situated in Russia.

Rental income received by individuals who are not resident in Russia is subject to Russian income tax at 30%. Individuals who are considered to be tax-resident in Russia (e.g. by spending more than 183 days within a 12-month period in Russia) are taxable on their rental income at only 13%.

A tax deduction of up to RUR 1 million (approximately USD 42,000) of the purchase price of an apartment or residential house is granted once in a lifetime. The costs of acquiring financing from Russian banks are also deductible. However, amortisation or other expenses are not deductible for tax purposes. Upon the sale of a residential property an individual is granted a tax deduction of RUR 1 million if he or she has been the owner of the property for up to 3 years. A tax deduction equal to the disposal proceeds will be granted in respect of residential property that has been owned for more than three years.

An individual who acquires residential property for letting purposes is entitled to register as an 'individual entrepreneur' with the Russian tax authorities and use the simplified taxation system.

This means that the individual may elect either to have all of his/her income taxed at 6% or to have his/her net income (i.e. taxable revenue minus tax-deductible expenses) taxed at 15%. In the former case, all revenue from the future sale of the property will be subject to income tax. In the latter, only the difference between the purchase and sales price will be taxable.

Of course, individuals who are not resident in Russia may be taxable in their home countries on income arising from a Russian property. Depending on the country of residence, relief for the Russian tax paid may be granted either by deduction from or credit against the domestic tax liability.

Despite the rapidly increasing property prices, investment in Moscow's real estate market may still provide good returns as demand is usually always high for centrally located residences. Saint Petersburg and other big cities in the so-called 'regions' are also developing and the lower residential property prices in these cities offer an attractive alternative to Moscow for middle to long-term investment in Russia.

For further information and advice in connection with Russian real estate matters, please contact Richard Wellmann via e-mail at r.wellmann@bdo.ru or Dmitry Streinikov via e-mail at d.streinikov@bdo.ru or by telephone on + 7 495 797 5665, of BDO Unicon.

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Denmark

Termination of Tax Treaties

As forecast in the October 2007 edition of this newsletter, the Danish Tax Minister announced the termination of the tax treaties with France and Spain on 10 June 2008. This means that the tax treaties will no longer apply with effect from 1 January 2009. The abrogation of the treaties will have particular impact on:

- Pensioners moving from Denmark to France or Spain with their Danish pensions, and
- Danish-resident individuals owning real estate in France.

From 1 January 2009, Denmark will tax payments made from Danish pension schemes to individuals resident in France or Spain. Further, Danish-resident individuals owning French real estate for private use will be liable to Danish real property tax.

Special transitional rules will apply to individuals who were already tax-resident in France or Spain as

at 29 November 2007 and who received payments from their Danish pension schemes before 1 February 2008. Although there will be no Danish tax in respect of the pension income, a liability to tax may still arise in France or Spain, as appropriate.

Also, individuals who are tax-resident in Denmark who acquired their French real estate prior to 29 November 2007 will also avoid the Danish real property tax in respect of their French property.

Finally, it is important to note that all structures currently in place, comprising Danish companies owning valuable real estate in France and/or Spain (either directly or via a local company), will need to be reviewed.

For further information and advice on Danish tax issues, please contact Hans-Henrik Nilausen of BDO ScanRevision via e-mail at HHN@bdo.dk or by telephone on +45 39 15 52 00.

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Sweden

Changes to the Tax Treaty between the Nordic Countries

On 4 April 2008 the governments of the Nordic countries (Denmark, Faeroe Islands, Finland, Iceland, Norway and Sweden) signed a protocol regarding changes in the double tax treaty. The main change effects the taxation of capital gains on the disposal of shares.

In its current version the double tax treaty states that if a person moves from country A to country B, and disposes of shares in a company that is resident in country A, the capital gain may be taxed in country A if the disposal takes place within a five-year period from the relocation. (Note that under some circumstances gains arising on the sale of shares in

companies in other contracting states are also taxed in country A). However, gains arising on shares in companies in non-contracting states are only taxed in the individual's country of residence.

The result of this is that if an individual moves from Sweden to Denmark, for instance, and disposes of shares in a non-Swedish company only Denmark will have the right to tax the capital gain. Further, in conjunction with favourable domestic Danish tax legislation, the taxable gain may be restricted.

However, as of 1 January 2009 the double tax treaty will be changed to state that an individual moving

from one contracting state to another and disposing of shares will be taxed in the first contracting state if the disposal of shares takes place within a 10-year period from the date of the relocation. It is the increase in value that took place before the relocation that may be taxed. There is no restriction as regards the shares, i.e. shares in companies in any country (not only the contracting states) are included.

From a Swedish/Danish perspective the changes have major consequences. Denmark has been regarded as a very attractive country to relocate to

for Swedish individuals with substantial holdings in foreign companies. The changes to the treaty, together with the recent changes of Swedish domestic tax law, will mean that an individual moving to Denmark and disposing of shares (irrespective of the company's residence) will be taxed in Sweden if the sale takes place within a 10-year period from the relocation.

For further information or advice on Swedish tax issues please contact Maria Frostberger of BDO Nordic AB via e-mail at maria.frostberger@bdo.se or by telephone on + 46 31 704 1334.

9 United Kingdom

The UK – Still a Tax Haven..? Update on New Tax Regime from 6 April 2008

Following our article in January, we set out below a summary of the new rules introduced from 6 April 2008 for the taxation of UK-resident non-domiciled individuals.

The Chancellor's Budget announcements on 12 March 2008 significantly modified some of the original proposals, which appeared in the draft legislation released in January. The Finance Bill 2008 was issued on 27 March 2008 and received Royal Assent on 21 July 2008.

Remittance basis

A non-UK domiciled individual who is resident in the United Kingdom will have to claim the remittance basis annually on a self-assessment tax return, unless his/her total offshore unremitted income and gains are within the de minimis limit of GBP2,000 (which has increased from the GBP1,000 originally proposed).

Unless the de minimis limit applies, an individual who elects to be taxed under the remittance basis, will lose his/her personal allowance (currently GBP6,035) and capital gains tax annual exemption (currently GBP9,600).

Individuals who are over 18 years of age and have been resident in the United Kingdom for seven out of the previous nine tax years (running from 6 April to 5 April

each year) will also have to pay an annual remittance basic charge of GBP30,000. This charge is payable even if no remittances are made during the year. The UK tax authorities have confirmed that they will not treat the GBP30,000 as a taxable remittance to the United Kingdom even if paid out of offshore income or gains if paid direct to them by cheque/bank transfer from an overseas bank account.

Following the intensive consultation process, the GBP30,000 charge will now be treated as a tax payment in respect of unremitted income and gains (nominated by the tax payer), rather than as a stand-alone 'fee'. Specific ordering rules will apply, such that the income/gains matched with the charge will be treated as the last offshore income/gains to be remitted to the UK by the taxpayer. This effectively means that all foreign income and gains would need to be remitted to the United Kingdom by the individual (and be subject to tax in the United Kingdom) before the individual can obtain the benefit of paying the GBP30,000 charge.

Although the position is not entirely clear at present, the GBP30,000 charge will most probably be creditable against overseas tax under appropriate double tax treaties. This will be especially important for US citizens. The downside is that detailed record keeping will be essential.

Another significant change relates to capital losses. Prior to 5 April 2008, capital losses realised on overseas assets were not available for relief against the UK-resident non-domiciled individual's UK/foreign remitted gains.

From 6 April 2008, an election may be made at the same time as the first claim for the remittance basis, to allow all capital losses. If the election is not made at this time then it cannot be made at any time thereafter. A requirement of this election is that all unremitted foreign gains must be reported going forward which, for confidentiality reasons, will not be desirable for most individuals.

Anti- avoidance measures

The Finance Act contains new anti-avoidance rules to prevent individuals leaving the United Kingdom for short periods of non-UK residence, during which remittances could be made to the United Kingdom. This follows the existing treatment for offshore capital gains.

From 6 April 2008, if an individual is non-UK resident for less than five complete tax years, all foreign income and gains remitted to the United Kingdom during that period will be taxable in the year in which the taxpayer resumes UK residence. The treatment of income arising during the period of non-UK residence is not clear at this stage.

The government's draft legislation in January brought an end to the long-established principle of 'source ceasing', which facilitated the remittance of overseas income and gains to the United Kingdom free of tax. This measure remains unchanged in the Finance Act, although some of the other anti-avoidance proposals have been relaxed.

Remittance in kind

The new legislation basically treats assets acquired overseas and brought to the United Kingdom as a remittance of the overseas income used to acquire the asset. However, there are a number of exceptions to this rule.

Personal effects, such as clothes and jewellery, and assets costing less than GBP1,000 will be exempt from a charge. Similarly, assets brought to the United Kingdom for repair or restoration will be exempt, as will assets brought to the United Kingdom for less than a total of nine months. This goes some way



towards eliminating the absurdity of the original wide-sweeping proposals. In addition, works of art brought to the United Kingdom for the purpose of public display will be exempt under the remittance-in-kind provisions.

Significantly, any asset purchased out of untaxed foreign income and held at 11 March 2008 will be exempt from a charge under the remittance basis for as long as the asset is owned, even if the asset was kept outside the UK and is later imported.

Any assets acquired out of overseas income or capital gains, which are exempt from charge under the remittance in kind provisions but sold in the United Kingdom, will give rise to a tax charge at the point of sale.

Alienation of Income and Gains

The draft legislation imposed tax charges on the donor on all gifts of overseas income or gains made to a close relative overseas and subsequently brought by that relative to the UK.

The revised proposals have narrowed the charge to apply to gifts made to spouses, civil partners, cohabitees and to children/grandchildren under the age of 18. Appropriately structured gifts to parents, siblings and adult children or grandchildren can therefore still be made after 6 April 2008 without giving rise to a liability on the donor.

The charge will also catch gifts to certain trusts and companies if the trust/company subsequently remits funds to the UK.

It appears that the new alienation provisions will only apply to foreign income and gains realised after 5 April 2008.

Offshore Mortgages

Under the previous rules, non-UK domiciled individuals could repay the interest on monies borrowed from overseas and secured against a UK property with untaxed foreign income, without incurring a tax charge under the remittance basis.

These types of arrangements have been targeted in the new legislation and, from 6 April 2008, interest payments made out of untaxed foreign income will be treated as a taxable remittance. Grandfathering provisions will apply to loans already in existence at 12 March 2008 until the earlier of the loan repayment or 5 April 2028. This favourable treatment will be withdrawn in the event that there are any changes to the terms of the loan.

Mixed accounts

In the past, there has been no statutory guidance on how remittances from overseas 'mixed accounts' (comprising a mixture of income, gains and 'pure' capital), should be taxed. As a matter of practice, remittances have generally been treated by the UK tax authorities as having been made first from income, then gains (pro-rated to the sale proceeds) and only then out of the pure capital.

Under the new legislation from 6 April 2008, remittances from a mixed account will be matched with funds in a prescribed order, ensuring that taxed income/gains and pure capital are matched last.

This order of matching will not be applied in the case of overseas payments, to the detriment of the taxpayer. Payments made from a mixed account outside the United Kingdom will be matched pro-rata with all categories of funds in the account. This means that taxable income/gains cannot be 'washed out' overseas, prior to making a tax-free remittance to the United Kingdom.

Non-Resident Trusts

The draft legislation imposed a tax charge, where none previously existed, on all UK-resident non-domiciled settlors of offshore trusts in respect of all capital gains realised by the trustees (subject to an election for the remittance basis to apply).

This proposal was significantly modified in the amended legislation. From 6 April 2008 any non-UK-domiciled individual (including the settlor) who receives a capital

payment from an offshore trust will be taxable if the payment is matched with 'stockpiled' (i.e. pooled, undistributed) gains within the trust, whether those gains were realised in respect of UK or non-UK sited assets. If the individual elects for the remittance basis, the tax charge will only apply to the extent that the funds are remitted to the United Kingdom.

Complex computational provisions will be adopted to calculate the timing and level of the tax charge (which will range from 18% to 28.8%, depending on the time that has elapsed between the date that the relevant trust gain(s) arose and the date on which the capital payment was made). This inevitably imposes a more onerous burden on trustees (and their advisors) to keep clear and detailed records.

The trustees are, however, entitled to make a one-time election to treat all assets held by the trust (and/or by any underlying company held by the trust) as if they had been sold and reacquired at market value on 6 April 2008. This effectively rebases the assets and washes out gains accrued prior to 5 April 2008. The election is, however, coupled with a reporting requirement to provide detailed information about the trust/companies to the UK tax authorities.

Non-resident Companies

From 6 April 2008, gains realised by certain non-UK resident companies will be attributed to UK resident, non-domiciled shareholders and taxable on the remittance or arising basis, depending on whether an election for the remittance basis has been made. There have been no major amendments to these provisions since the draft legislation

What next?

Although the Finance Act has managed to address some of the practical problems and queries raised by the draft legislation, it is still difficult to predict how these changes will impact upon real-life scenarios.

The above is only a summary of the main changes. Appropriate professional advice is therefore essential in order to mitigate any adverse implications arising as a result of the new legislation.

For further information and advice on UK tax matters, please contact Effie Karamani via e-mail at effie.karamani@bdo.co.uk, or by telephone on +44 207 893 2384 or Paul Ayres via e-mail at paul.ayres@bdo.co.uk or by telephone on +44 207 893 2247 of BDO Stoy Hayward LLP.



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