HM Revenue & Customs

Reform of an anti-avoidance provision: Transfer of Assets Abroad

Summary of responses and further consultation

18 July 2013

Subject of this consultation:	At Budget 2012 the Government announced a consultation on the transfer of assets abroad legislation. The consultation sought views on whether proposed amendments would ensure that the legislation remained compatible with European Union law, on certain clarification changes, and on whether any other changes were required. A new exemption and other changes were legislated for in Finance Act 2013. This document summarises responses received to the wider questions in the 2012 consultation, and seeks views on the matching rules for the benefits charge and on draft guidance.
Scope of this consultation:	The Government is seeking views on possible amendments to the legislation which sets out the operation of the matching rules and on the draft guidance which is being published alongside this document.
Who should read this:	The Government is interested in the views of professional bodies, tax advisers and other interested parties.
Duration:	The consultation period runs from 18 July 2013 to 10 October 2013
Lead official:	Paul Jefferies and Julie De Brito, HM Revenue and Customs
How to respond or enquire about this consultation:	Responses can be sent to: mailto:PTIconsultation.specialistpersonaltax@hmrc.gsi.gov.uk or by post to: Paul Jefferies or Julie De Brito G45 100 Parliament Street London SW1A 2BQ
Additional ways to be involved:	HMRC intends to meet with interested parties during the consultation period.
After the consultation:	The Government will publish its response to the matching rules consultation after responses have been considered. The responses received will assist in the design of any reform of the current rules with a view, if appropriate, to legislating in Finance Bill 2014. In this case, draft legislation would be published in the Autumn for consultation.
Getting to this stage:	Finance Act 2013 introduced amendments ensured at clarifying the operation of the rules and ensuring that the legislation is compatible with European Union law. As part of the initial consultation in 2012 respondents were asked to consider any other changes which could be made to the rules.
Previous engagement:	As well as the 2012 consultation and response documents, meetings have been held with a number of interested parties.

Contents

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1. Introduction and background

The transfer of assets abroad (ToA) legislation provides for a charge to income tax on an individual who is resident in the UK where there has been a transfer of assets and, as a result of the transfer (and/or any associated operations), income becomes payable to a person abroad, but an individual can still enjoy income, or receive or have entitlement to receive a capital sum or other benefits from the arrangements.

A consultation document, *"Reform of two anti-avoidance provisions (i) the attribution of gains to members of closely controlled non-resident companies, and (ii) the transfer of assets abroad"*, was published on 30 July 2012. The document dealt with the Government's proposals to respond to the European Commission's infraction notices against these two anti-avoidance provisions. It also proposed other changes to clarify certain aspects of the provisions, including three for the ToA rules. At the same time the Government said that it would welcome suggestions for further improvements to the two anti-avoidance provisions as part of a wider review. The consultation closed on 22 October 2012 and 35 responses were received, 28 of which related to the ToA rules. Of these, 22 contained suggestions for further reform.

This document deals with the ToA rules only.

The Government is grateful to all of those who took the time to attend meetings and respond to the consultation.

The Government responded to the comments made on the proposals to deal with the infraction, and the other proposed changes, in its response document issued on 11 December 2012. Draft legislation was published at the same time. That response document did not summarise the suggestions received for further improvements, but said the Government would conduct a more detailed review of those suggestions and consider whether changes could be made without further cost to the Exchequer which are fair and do not weaken these important anti-avoidance provisions.

Finance Act 2013 contains provisions that amend the ToA rules with the aim of ensuring compatibility of the rules with EU law, and to implement two of the three other improvements proposed in the July 2012 consultation: double charging and double taxation relief. The third clarification proposal, to change the rules for matching the benefit received by a UK resident individual to the income of a person abroad under the benefits charge, has not yet been implemented because those who commented on the draft legislation raised a number of concerns and the Government wanted to take further time to consider this issue.

This document:

- summarises and responds to the suggestions for further improvements to the ToA rules made in response to the July 2012 consultation document;
- seeks further views on the rules for matching the benefit received by a UK resident individual to the income of a person abroad under the benefits charge; and
- introduces draft revised guidance on the ToA rules and seeks views on it.

Overview of current legislation

The existing legislation is in sections 714 to 751 of Income Tax Act 2007 which may be found at
http://www.legislation.gov.uk/ukpga/2007/3/part/13/chapter/2.

In summary, the legislation imposes a charge to income tax on an individual who is resident[1] in the UK where:

- assets,[2] (including property or rights of any kind) are transferred[3] and
- as a result of the transfer, and/or an operation associated with the transfer,
- income becomes payable to a person abroad, and the individual (who will be charged to income tax)
    - has power to enjoy income of the person abroad as a result of a relevant transaction, and the income would have been chargeable to income tax had it been the individual's income received in the UK (sections 720-6); or
    - receives, or is entitled to receive, a capital sum the payment of, or entitlement to, which is in any way connected with a relevant transaction (sections 727-30); or
    - receives a benefit, provided out of assets which are available for the purpose, as a result of a relevant transaction and the individual is not liable to income tax under the previous alternatives nor otherwise liable to income tax on the benefit (sections 731-735A). These sections apply only where the individual receiving the benefit is not the person who transferred the asset.

For the purposes of this legislation a 'relevant transaction' can either be the transfer itself or an 'associated operation'. An 'associated operation' means an operation of any kind effected by any person at the time of the transfer or before or after it.

The operation must be in relation to:

(i) any of the assets transferred,
(ii) any assets representing the assets transferred,
(iii) any income arising from the assets in (i) or (ii), or
(iv) any assets representing income that has accumulated from the assets in (i) or (ii) (section 719(2)).

'A person abroad' is a person who is resident, or an individual who is domiciled outside the UK (section 718). This can include trustees and personal representatives.

There are exemptions from the 'transfer of assets' income tax charge where the individual satisfies an officer of HMRC that specific conditions are met. There will be no charge if[4]:

- it would be unreasonable to draw the conclusion, from all the circumstances

[1] The concepts of 'ordinarily resident' and 'ordinary residence' were withdrawn by the 2013 Finance Act
[2] Section 717 ITA explains the meaning of 'assets'
[3] Section 716 ITA defines the term 'transfer'
[4] The conditions for exemption are slightly different if the transaction took place before 5 December 2005. The legislation is in sections 737 to 738 for post- 5 December 2005 transactions and in section 739 for pre- 5 December 2005 transactions. Section 740 provides rules if relevant transactions include both pre- and post- 5 December 2005 transactions.

of the case, that avoiding liability to taxation was the purpose, or one of the purposes, for which the relevant transactions or any of them were effected; or (if that is not the case)

- all the relevant transactions were genuine commercial transactions and it would not be reasonable to draw the conclusion, again from all the circumstances of the case, that any one or more of those transactions was more than incidentally designed for the purposes of avoiding liability to taxation; and/or,
- income attributable to transactions on or after 6 April 2012 that are genuine (considering all the relevant circumstances) is exempt from charge where to charge tax on the income would be a restriction of EU treaty freedoms.

A 'commercial' transaction (section 738) is one that:

- is effected in the course of a trade or business, or with a view to setting up and commencing a trade or business, for the purposes of that business, and
- is on terms that would have been agreed between unconnected persons acting at arm's length, and is not one that would not have been entered into between unconnected persons.

2. Responses to the July 2012 consultation

This chapter summarises the responses received to the consultation document *"Reform of two anti-avoidance provisions (i) the attribution of gains to members of closely controlled non-resident companies, and (ii) the transfer of assets abroad*" in respect of the ToA legislation, and should be read in conjunction with that document. As explained in Chapter 1, it supplements the summary of responses published on 11 December 2012.

The Government is grateful for the detailed consideration that stakeholders have given this consultation. It has not been possible to include all the detail of the responses here although all the comments have been analysed and considered fully.

Twenty two responses were received with regard to the ToA legislation.

Radical reform

Most respondents stated that the rules were out-dated and needed to be reviewed in their entirety. Two respondents offered to be part of a working group to carry out this review, suggesting that by doing this a solution could be found that would improve the legislation to make it clear, certain and workable for both taxpayer compliance and HMRC enforcement.

Government response

The Government has already taken steps to make the operation of the transfer of assets provisions more certain by introducing a new exemption and two new clarification rules (on double charging and double taxation treaties) in Finance Act 2013.

After further consideration, and after having reflected fully on comments made, the Government is not minded to carry out a wider reform of the ToA rules at present; this is effective anti-avoidance legislation that protects the UK Exchequer from abusive transactions to move income offshore. It is committed to implementing the Finance Act 2013 reforms, and to taking forward consultation on the matching rules for the benefits charge with a view, if appropriate, to legislating in Finance Bill 2014. In addition, HMRC is publishing and consulting on detailed guidance on the ToA rules.

Definitions

Many respondents stated that there was a lack of clarity around definitions in the legislation, particularly in respect of 'associated operations' and 'transfers'. Three respondents noted that the definition of 'associated operations' in particular caused problems as the current definition was, as one commented, 'far too wide to apply in practice'.

Spouses

Three respondents asked for clarity around whether section 714(4) of the Income Taxes Act 2007 meant that a spouse could be assessed in the place of a transferor or whether they were correct in thinking that it meant that the transferor charge was engaged where the spouse receives a capital sum or has the power to enjoy. One respondent asked for confirmation that only the transferor and not their spouse could be taxed on the income arising to the overseas person, and that the reference to a spouse is only relevant when considering whether a transferor is able to benefit from a transfer.

Transfers and transferors

One respondent suggested that legislation should explicitly state that a transfer must cause income to arise overseas from which the transferor can benefit. The respondent also said that a transferor should only be taxable to the extent that they provided funds which give rise to the income receivable by the offshore person. Another respondent said that transfers in respect of a UK business should be allowed.

Government response

The Government recognises concerns about some of the terms used in the legislation. HMRC has, therefore, developed comprehensive guidance, which it is publishing in draft alongside this document, on the transfer of assets legislation. The draft guidance sets out how HMRC interprets and applies terms such as “associated operation” and “transfer”.

The guidance provides clarification of HMRC’s view of the way the legislation works, although as the rules cover a wide range of circumstances it is not possible for the guidance to specifically mention every possible permutation. The Government considers that the publication of this guidance should alleviate many of the concerns brought out during the consultation process. This is discussed further in Chapter 4.

The concerns around spouses are specifically addressed in the draft guidance.

De minimis

Some respondents suggested that it would be sensible to introduce a *de minimis* level so that transfers below a particular threshold would be outside the scope of the ToA rules, although opinions varied as to what level this should be set (one suggestion was £10,000). Some respondents said that the rules for ToA should mirror those for section 13 Taxation of Chargeable Gains Act (TCGA) 1992 where there is a participation threshold or *de minimis* (prior to Finance Act 2013 there was a 10 per cent *de minimis*, which has now increased to 25 per cent). One respondent noted that someone with a small interest may not have the power to obtain the necessary information to report the income arising to them to HMRC, and that a minority holding is a good indicator that a transfer is genuine and not for tax avoidance purposes.

Government response

The Government has no plans to introduce a *de minimis* level into the transfer of assets rules. This is because this is anti-avoidance legislation and genuine transactions are outside its scope. A *de minimis* could also provide opportunities to sidestep the rules by fragmenting transactions to ensure they fell below any threshold set. Rules to protect against such behaviour would be complex. Similarly, as the rules cover a wide variety of circumstances involving entities from corporates to trusts, it would make the rules far more complex to introduce a *de minimis* participation level which could cover all circumstances.

Remittance basis

Some respondents raised various issues around the interaction of the ToA rules and those for users of the remittance basis. One respondent thought that the ToA rules and the capital gains tax rules in section 87 TCGA 1992 should be aligned for remittance basis users.

Government response

The draft guidance covers the effect of the ToA rules on users of the remittance basis of taxation. Generally these rules work as they stand so the Government has no plans to make any changes at this stage, although the interaction with the remittance basis will be factored in to any eventual changes to the matching rules for the benefits charge under section 731.

Ordinary residence

In view of the withdrawal of the concept of ordinary residence, one respondent wanted a special exemption to be introduced for individuals who are resident in the UK for less than three years. Another respondent asked for an exemption for people in receipt of Overseas Workday Relief as in theory, now that the concept of ordinary residence has been withdrawn, income from overseas companies could be taxable.

Government response

The Government does not think that it is necessary to legislate for a special exemption. The withdrawal of ordinary residence is a simplification measure introduced alongside the new Statutory Residence Test and to introduce new rules to exempt particular groups would mean that the rules become overly complex. In practice, individuals who are in the UK for only a short time will be unlikely to be subject to a ToA charge as they will likely be able to demonstrate their offshore arrangements were set up before they came to the UK and either were not motivated by the avoidance of UK tax or have genuine commercial substance.

In addition, anyone who is non-domiciled and claims the remittance basis is only taxed on relevant income that is remitted to the UK. This applies to the ToA rules and the withdrawal of ordinary residence has not changed this.

Tax relief

Several respondents questioned why the legislation did not provide relief for tax paid locally by the person abroad when the ToA charge is on a person other than the transferor under section 731 (that is, when there is a benefits charge). One commented that any local taxation by the offshore vehicle should be fully offset against the UK individual's tax liability on the same income. Another respondent observed that where non-resident trustees are taxed in the UK on UK source income, Extra Statutory Concession B18 enabled UK beneficiaries in receipt of trust income distributions to claim credit against their own tax liability. They said there should be a similar provision for ToA income.

Government response

The draft guidance mentioned in Chapter 4 of this document covers this point, particularly at paragraph INTM602680. The Government is currently reviewing the rules for matching the benefit received by a UK resident individual to the income of a person abroad under the benefits charge under section 731. This point is discussed further in Chapter 3 of this consultation document.

General Anti-Abuse Rule

Three respondents thought that the introduction of a general anti-abuse rule meant that the ToA provisions were no longer required.

Government response

The Government considers that the ToA provisions are still needed. The General Anti-Abuse Rule (GAAR) is intended as an additional tool alongside other anti-avoidance rules to challenge and counteract abusive tax avoidance schemes. It is not designed to replace targeted anti-avoidance provisions such as the ToA rules which are effective in themselves. Consequently the ToA rules are needed to tackle arrangements that may not be tackled by the GAAR.

Clearance procedure

A number of respondents said that there should be a clearance procedure, where individuals could seek advice prior to making a transfer as to whether it would be caught by the ToA rules or not.

Government response

The Government does not think that a clearance procedure is appropriate for this particular legislation. The ToA provisions are anti-avoidance legislation and, as such, it would not be appropriate to provide a mechanism by which those who wish to avoid UK tax can test the boundaries of the legislation.

Charge where a capital sum is received

One respondent asked for the capital sum charge (in section 727 Income Tax Act 2007) to be abolished as they felt that it added little to the protection provided by the ToA charge made when the transferor has the power to enjoy income arising to a person abroad. They suggested that if it were not abolished then it should only apply for a minimum specified period and not, as they read the rules, in perpetuity. One other respondent suggested that this provision should be limited so that the charge to tax is on the capital sum rather on an amount calculated by reference to the income arising to the person abroad.

Government response

There are no plans at present to abolish or amend the capital sum charge. It performs a vital function; without it it would be easy to circumvent the anti-avoidance rules and income could potentially remain untaxed. Draft guidance on the operation of the rules can be found at paragraph INTM601020.

Exclusions

Respondents argued for the introduction of various different exclusions from the rules. One suggested that a sale for full market value should not be a relevant transaction. Another commented that there should be a similar exemption in the ToA rules to that in the Controlled Foreign Companies (CFC) legislation so that, subject to an economic test, a person resident or established in an EU state would not be counted as a 'person abroad' for the purposes of ToA. The same respondent argued that income which has already been subject to UK corporation tax should be specifically excluded from being taken into account for a ToA charge.

A further respondent suggested that there should be an exemption for people in receipt of overseas workday relief as, in theory, income from overseas companies could be taxable under the ToA rules. Another respondent said that there should be an exemption similar to the 'excluded countries' exemption in the CFC legislation.

Government response

The Government does not think it necessary to add specific exclusions mentioned by respondents to the legislation because, particularly following the new exemption and clarification introduced in Finance Act 2013, the legislation operates in an equitable way. The new guidance published alongside this document aims to provide a comprehensive and clear guide to the way that the rules operate. For example, further clarity around transfers is provided in the new draft guidance being published today.

The ToA legislation is broadly drawn to prevent avoidance of tax by the transfer of an asset in a diffuse range of circumstances. The effect of the exemptions provided in the regime is that, broadly, genuine or commercial transactions are not caught without the need for precise detailed exclusions which would add to the complexity of the legislation very considerably.

Offshore funds

Potential issues with the interaction between the offshore funds rules in The Offshore Funds (Tax) Regulations 2009 (SI 2009/3001) and the ToA rules were pointed out by one respondent who commented that it was not clear which should take priority. The respondent noted that where offshore funds are disposed of by non-UK resident settlements, the regulations treat the resulting offshore income gain as both income for the ToA rules and a capital gain. The respondent suggested that offshore income gains should either be treated as income or as gains, and that it would be most sensible to remove them from the scope of the ToA rules.

Government response

Although the new draft guidance does not specifically mention the interaction between the Offshore Funds (Tax) Regulations 2009 (SI 2009/3001) and the ToA rules, there is detailed guidance available on the Offshore Funds Regulations. Changes made to the legislation in Finance Act 2013 ensure that where an individual has paid tax on income under another part of the Tax Code then there will not be a ToA charge on that income.

Motive defences and tainting

Several respondents requested greater clarity on the operation of the exemptions in sections 736 – 742 (the motive defences). One respondent asked for more clarity around what actions are relevant when considering if a structure has been tainted. They suggested that the loss of exemption should not be 'all or nothing', but should instead apply to an appropriate proportion of the income received by the offshore person.

Government response

There is a significant amount of new draft guidance available on the existing exemptions from the ToA legislation and the additional exemption introduced in Finance Act 2013. For example, INTM602800 seeks to clarify the 'tainting' question above. However, the Government welcomes suggestions on whether further clarification is needed in this area.

Companies

One respondent pointed out that a more radical reform would be to introduce rules to allow companies to elect to be fiscally transparent in a similar way to the US system.

Government response

The Government notes the point made but is not minded at present to make such a radical change which would have ramifications beyond the ToA regime.

Interaction with the settlement code

One respondent said that interaction between the settlement code and ToA in IR bulletin April 1999 should be put on statutory basis.

Government response

The double charging provisions introduced in Finance Act 2013 are aimed at resolving this point. Draft guidance is also available at paragraph INTM602460 and elsewhere.

Self Assessment

Another respondent questioned whether the current ToA system was truly compatible with self-assessment.

Government response

The Government believes that there are no compatibility issues with ToA and self-assessment. Individuals indicate that they believe a transfer is exempt under the rules on their self-assessment return and HMRC will only investigate further if, on a risk-based assessment, there are indications of potential issues.

Double charging

Several respondents provided examples of situations where they consider that the way in which ToA rules operate give a result that is tantamount to double taxation. The situations or arrangements which were said to cause most concern involve tiers or layers of 'persons abroad' (such as groups of companies) and distributions being paid either to a parent company or to a trust abroad. Such distributions were said to effectively create a 'pool' of income arising to a person abroad which exceeds the income genuinely created in the structure. Two respondents requested a specific statutory rule to preclude an individual being charged to tax on dividends received in respect of income that had been taken into account in a charge under the ToA provisions. Other respondents wanted the introduction of rules to take into account income tax which had already been paid, to avoid double charging. Another concern was the interaction of the ToA rules with other provisions in the UK tax code such as the Offshore Fund rules. Several respondents considered that the provision in subsection 745(1), which effectively gives credit for basic rate tax already paid on income of the person abroad where there is a ToA charge on the transferor, should also apply to benefits charges under section 731.

Government response

The ToA provisions cover a wide and very varied range of potentially complex situations, arrangements and structures. The legislation contains rules which seek to address any potential for double charging under the regime but by necessity these are broadly drawn. Express provisions to prevent double charging in the diffuse range of specific situations would greatly increase the length and complexity of the statute and could never remain comprehensive.

The Government introduced amendments to the statute in Finance Act 2013 to make it clear that where an individual has paid income tax under another part of the Taxes Acts then they will not also be charged under the ToA provisions in respect of that income.

These amendments supplement provisions already in the legislation that ensure:

- no amount of income may be taken into account more than once in charging income tax under this chapter (subsection 743(1))
- if an individual receives income that has been taken into account in a ToA charge on the transferor then the income is not taxed again on receipt (subsections 743(2A) & (2B))
- credit is given for basic rate tax borne on income taken into account in relation to a ToA charge (subsection 745(1))

In addition the guidance at INTM601680 explains how credit is currently given for income tax borne by the person abroad where the ToA charge is a benefits charge under section 731. Together these rules aim to limit the scope for 'double charging' under the ToA provisions. The Government is not currently minded to introduce additional specific rules to clarify the operation of these rules in particular circumstances but will continue to consider stakeholder representations on this complex issue. HMRC would welcome comments on the guidance in this area, as explained in Chapter 4 of this document.

3. Consultation on matching rules for the benefits charge

Background

Section 731 ITA 2007 provides for income tax to be charged on a UK resident individual who receives a benefit arising out of a transfer of assets abroad. The tax charge is linked to the income arising to a person abroad resulting from the transfer of assets. The "matching rules" that link the benefit received with the income of the person abroad are in sections 733 to 735A ITA 2007.

For some time commentators have suggested it would be beneficial to have greater certainty on how benefits are matched to relevant income, particularly in circumstances where there is more than one beneficiary within the scope of a section 731 charge. The July 2012 consultation asked whether further rules were necessary to provide more certainty and made a comparison with the capital gains matching rules in section 87 and 87A TCGA 1992.

The July 2012 consultation established that more certain rules would be welcome, and draft legislation published for consultation in December 2012 included proposals for new matching rules. The proposed rules were based on the approach taken by the capital gains matching rules, and were designed with the aim of providing more certainty for taxpayers while not providing an opportunity for manipulation of ordering or timing so that benefits received by UK resident individuals fall out of charge.

Although commentators were broadly in favour of the clearer, more certain rules there were concerns that the rules did not give an equitable outcome in some circumstances. As a result, the Government announced that the changes to the rules to determine the amount of the section 731 benefit charge would be deferred to allow for further consideration and consultation with interested parties. The Government is grateful for continued stakeholder engagement with this issue.

The current legislation

Section 731 ITA 2007 imposes a charge on an amount of income treated as arising for the tax year if:

- a relevant transfer occurs,
- an individual who is resident in the United Kingdom receives a benefit,
- the benefit is provided out of assets which are available for the purpose as a result of the transfer or one or more associated operations,
- the individual is not liable to income tax under either section 720 or section 727 by reference to the transfer, and
- the individual is not liable to income tax on the benefit other than under section 731.

In broad terms, section 733 provides a set of "matching rules" linking the benefit received by a UK resident individual to the income of a person abroad. As the benefit and linked income may arise at different times, the matching rules look back over previous years comparing the accumulated untaxed benefits with the accumulated unmatched income and charge the lower of the two amounts.

Section 733, via a number of steps, calculates the income to be charged:

- Steps 1 and 2 identify the amount or value of the benefits received by an individual in the current and earlier years to arrive at the total of untaxed benefits.
- Steps 3 to 5 calculate the income ("relevant income") available for the current year which can be used directly or indirectly to provide a benefit and adds to this amount of relevant income for earlier years to arrive at the figure of available relevant income.
- Step 6 compares the total untaxed benefits and the available relevant income.
- The amount of income treated as arising under section 732(2) for any tax year is the total untaxed benefits unless the available relevant income is lower, in which case it is the amount of available relevant income that is the income treated as arising.

Sections 735 and 735A adapt the section 733 matching rules for income arising under section 732 to individuals not domiciled in the UK who are remittance basis users. From the income treated as arising to the individual under section 732, any relevant foreign income is identified and is treated as the relevant foreign income of the individual. For the purpose of this identification section, 735A orders the income so that relevant income of earlier years is matched before relevant income of later years. Relevant income which is not relevant foreign income is matched before relevant foreign income. Foreign relevant income is only charged to the extent that it is remitted to the UK.

Perceived problems with the current rules

The responses to the July 2012 consultation document and the December 2012 draft legislation brought out the concerns summarised below.

1. **Timing** - To identify relevant income, it is necessary to determine whether the income arising to the person abroad can be used directly or indirectly for providing a benefit to a UK resident individual. Commentators raised the issue of <u>when</u> this question should be determined and suggested several possibilities: the point at which the income arises, the point at which the benefit is received, another defined point, the end of the tax year for each of the above, or a combination of the above.

Government response

HMRC considers the relevant income of the tax year to be the net amount of income arising during that year to the person abroad that can be used directly or indirectly at the end of the year to provide a benefit to a UK resident individual. Income which is genuinely paid away during the year (for example as expenses) does not count towards the relevant income of that year. Once the relevant income for a year is established in relation to UK resident individuals, this will only be reduced by income treated as arising to those individuals under section 732.

Question 1 – The draft guidance at INTM601680 confirms this application of the legislation. Is anything further needed to provide certainty?

2. **Allocation of relevant income** - Commentators raised concerns about the extent to which an amount of relevant income may be considered to be available, or is distributed, to provide benefits to more than one individual. There was particular concern expressed where the person abroad is a non-UK resident trust which has both UK resident and non-UK resident beneficiaries.

   Where the same relevant income can provide benefits to both UK resident and non-UK resident beneficiaries, commentators noted that the current legislation permits the full amount of the relevant income to be matched to benefits received by the UK resident beneficiaries. Some commentators suggested that relevant income should be apportioned according to the beneficiaries to whom it is available, including both UK resident and non-UK resident beneficiaries.

   Commentators were concerned that the December 2012 draft legislation appeared to extend the scope of what is considered relevant income in the current legislation by expanding the requirement for it to be available to provide a benefit to the UK resident individual in section 733(1) to include, in the proposed new section 732(5), providing benefits to individuals. So where, for example, a non-UK resident trust has two sub-funds in which the assets are held separately and one sub-fund is only available to provide benefits to a non-UK resident beneficiary with the other only available to provide benefits to a UK resident beneficiary, the net accumulated income of both sub-funds would at the end of the tax year constitute relevant income for that year in relation to the UK resident beneficiary. Under the current legislation, only income arising to the sub-fund able to provide benefits to the UK resident beneficiary would constitute relevant income in relation to that beneficiary.

   Some commentators suggested that relevant income should be apportioned according to whom it is actually distributed as benefits rather than to whom it is available to be distributed as benefits. So if the trustees of a non-UK resident trust exercise their discretion to distribute half of the fund, accumulated from income over a number of years, to non-UK resident beneficiaries it was suggested that only the half of the fund remaining should be treated as relevant

income available to be matched to any benefits distributed to UK resident beneficiaries in later years. Under current legislation, the full amount of the accumulated fund would remain as relevant income in respect of benefits distributed to UK resident beneficiaries.

Government response

The Government notes the views that have been expressed but is concerned that some of the suggestions made would give scope for 'washing out' relevant income to non-chargeable individuals in order to limit any charge on benefits received by a UK resident beneficiary. The Government is not prepared to dilute the effectiveness of the benefits charge in this way. However, the Government would welcome further views on how more certainty might be provided in relation to allocation of relevant income.

Question 2 – How might more certainty be provided around allocation of relevant income without introducing opportunity for tax avoidance?

Where an amount of relevant income can be taken into account more than once for a charge under the ToA provisions, sections 743 and 744 act to prevent a duplication of charge. So where relevant income that arises in, for example, a non-UK resident discretionary trust constitutes relevant income in respect of benefits received by two or more UK resident beneficiaries, that relevant income can be apportioned between those beneficiaries in a "just and reasonable" manner. Some commentators raised concerns that "just and reasonable" is open to interpretation, and does not sit comfortably within a system of self assessment.

Government response

The provision of "just and reasonable" apportionment of relevant income under sections 743 and 744 accommodates a wide range of circumstances where an unjust result might otherwise arise under the benefits charge. The Government is conscious that ensuring a fair and equitable outcome across all possible circumstances whilst providing certainty of approach is challenging, and would welcome suggestions for how greater certainty might be provided in a practical manner that does not introduce scope for avoidance.

Question 3 - Are there workable alternatives that would provide greater certainty to the current "just and reasonable" apportionment of relevant income under sections 743 and 744 that would not introduce opportunity for tax avoidance?

3. **Other issues**

- Some commentators suggested the rules in sections 735 and 735A for matching relevant income to benefits received by non-domiciled individuals who are remittance basis users were helpful in so much as they provided some degree of certainty in terms of ordering income over and above section 733. However, there was also concern expressed that the rules were complex and difficult to operate.

- There was some concern put forward regarding the extent to which a UK resident beneficiary may be required to know the allocation of income to other beneficiaries, and their domicile status, to be able to calculate their own self assessment. It was suggested that this may give rise to issues of confidentiality and conflicts of interest.

- Commentators expressed concerns that the transitional provisions in the December 2012 draft legislation did not produce equitable results in a number of respects. Commentators noted there was a difficult balance to be struck in achieving a fair and proportionate outcome while minimising complexity.

Government response

The Government notes the views which have been put forward and would welcome ideas to address these issues as part of the next steps in deciding on any reforms to the matching rules.

Question 4 – How can the matching rules be reformed to achieve greater certainty while managing complexity and operational difficulties?

Next steps

The Government accepts that the current rules can give rise to uncertainty and that the December 2012 draft legislation, while providing greater certainty, may not provide an equitable result in some cases. The Government, therefore, proposes to set up a working party comprising of HMRC and external volunteers to discuss the concerns raised and develop detailed options for reform. The Government anticipates that any legislative reforms arising from the working party would be introduced by Parliament within the Finance Bill in 2014, with draft legislation published this Autumn.

While open to options to provide greater clarity and certainty, the Government remains firm in its belief that the ToA rules must remain effective in countering tax avoidance. Any new method of matching benefits with relevant income, therefore, must not introduce scope for manipulation of timing or allocation to permit relevant income to be washed out through matching to non-chargeable benefits.

Possible options for reform

Option 1: Amend the December 2012 draft legislation - It may be possible to amend the December 2012 draft legislation to address the concerns raised that it extends the scope of what is considered relevant income under the current rules, and to address concerns that the transitional provisions may give an inequitable result in some cases.

Question 5 - How might the December 2012 draft legislation be amended to address concerns raised whilst providing greater certainty and maintaining effectiveness against tax avoidance?

Option 2: Provide greater clarity and certainty through guidance - Some commentators suggested that it may not be possible to amend the December 2012 draft legislation to satisfactorily address concerns raised and, therefore, the existing rules should remain. If so, it may be possible to provide greater clarity and certainty through guidance. The draft guidance published alongside this consultation document sets out HMRC's established practice on the operation of the matching rules.

Question 6 – Does the draft guidance provide sufficient clarity and certainty on the operation of the matching rules? If not, how might the guidance be improved to provide this?

Option 3: Amend the current legislation - It may be possible to amend or supplement the current rules set out in sections 731 to 735A to provide greater certainty.

Question 7 - How might the current legislation be amended to provide greater certainty whilst maintaining its effectiveness against tax avoidance?

Option 4: Introduce a new set of matching rules - It may be possible to introduce into the legislation a new regime for matching relevant income to benefits received. Some commentators have suggested it may be possible to introduce a regime that provides a simplified system of pooling.

Question 8 - Could a new regime provide greater certainty whilst maintaining effectiveness against tax avoidance? How would this new regime operate, and could transitional provisions be designed that would be workable and equitable?

4. Consultation on draft guidance

Draft guidance

Many respondents to the July 2012 consultation document stated there was a lack of clarity around terms and concepts in the ToA legislation. The Government recognises that it would be beneficial to provide greater clarity and certainty on how the ToA legislation operates and is applied.

HMRC, in line with the wider policy for Open Government, normally makes its guidance intended for internal use publicly available. The guidance on the ToA rules is currently very limited. HMRC has, therefore, developed comprehensive guidance which it is publishing in draft alongside this consultation document.

The guidance provides clarification of HMRC's view of the operation of the ToA legislation. The Government considers that the publication of this guidance should alleviate many of the concerns brought out during the consultation process.

Feedback would be welcomed on the scope and content of the guidance. In particular, it would be valuable to have views on whether the guidance is comprehensive, clear and provides sufficient certainty. Any concerns regarding the policy underlying the legislation should be fed back separately.

5. Summary of consultation questions

The questions on the consultation on matching rules for the benefits charge in Chapter 3 are:

Question 1 – The draft guidance at INTM601680 confirms this application of the legislation. Is anything further needed to provide certainty?

Question 2 – How might more certainty be provided around allocation of relevant income without introducing opportunity for tax avoidance?

Question 3 - Are there workable alternatives that would provide greater certainty to the current "just and reasonable" apportionment of relevant income under sections 743 and 744 that would not introduce opportunity for tax avoidance?

Question 4 – How can the matching rules be reformed to achieve greater certainty while managing complexity and operational difficulties?

Question 5 - How might the December 2012 draft legislation be amended to address concerns raised whilst providing greater certainty and maintaining effectiveness against tax avoidance?

Question 6 – Does the draft guidance provide sufficient clarity and certainty on the operation of the matching rules? If not, how might the guidance be improved to provide this?

Question 7 - How might the current legislation be amended to provide greater certainty whilst maintaining its effectiveness against tax avoidance?

Question 8 - Could a new regime provide greater certainty whilst maintaining effectiveness against tax avoidance? How would this new regime operate, and could transitional provisions be designed that would be workable and equitable?

6. The consultation process

Consultation on matching rules for the benefits charge

The Government would welcome responses to the questions in Chapter 3 on the matching rules for the benefits charge. A summary of consultation questions is in Chapter 5. Responses should be submitted by 10 October 2013.

The Government would welcome volunteers to participate in a working group with HMRC to discuss the concerns raised in the consultation and develop detailed options for reform. Organisations wishing to take part should send contact details to the address below by 5 August.

Comments on draft guidance

HMRC would welcome feedback on the scope and content of the guidance. Comments should be submitted by 10 October 2013.

Where possible, please submit comments on the matching rules consultation and the draft guidance in separate documents.

Consultation Framework

This consultation is being conducted in line with the Tax Consultation Framework. There are 5 stages to tax policy development:

- Stage 1 - Setting out objectives and identifying options.
- Stage 2 - Determining the best option and developing a framework for implementation including detailed policy design.
- Stage 3 - Drafting legislation to effect the proposed change.
- Stage 4 - Implementing and monitoring the change.
- Stage 5 - Reviewing and evaluating the change.

This consultation is taking place during stage 2 of the process. The purpose of the consultation is to seek views on the detailed policy design and a framework for implementation of the proposals, rather than to seek views on alternative proposals.

How to respond

A summary of the questions in this consultation is included at Chapter 5.

Electronic responses should be sent to:

PTIconsultation.specialistpersonaltax@hmrc.gsi.gov.uk

Written responses should be sent to:

Paul Jefferies / Julie de Brito
HM Revenue and Customs
Specialist Personal Tax
100 Parliament Street
London SW1A 2BQ

Paper copies of this document or copies in Welsh and alternative formats (large print, audio and Braille) may be obtained free of charge from the above address. This document can also be accessed from HMRC Inside Government. All responses will be acknowledged, but it will not be possible to give substantive replies to individual representations.

When responding please say if you are a business, individual or representative body. In the case of representative bodies please provide information on the number and nature of people you represent.

Confidentiality

Information provided in response to this consultation, including personal information, may be published or disclosed in accordance with the access to information regimes. These are primarily the Freedom of Information Act 2000 (FOIA), the Data Protection Act 1998 (DPA) and the Environmental Information Regulations 2004.

If you want the information that you provide to be treated as confidential, please be aware that, under the FOIA, there is a statutory Code of Practice with which public authorities must comply and which deals with, amongst other things, obligations of confidence. In view of this it would be helpful if you could explain to us why you regard the information you have provided as confidential. If we receive a request for

disclosure of the information we will take full account of your explanation, but we cannot give an assurance that confidentially can be maintained in all circumstances.

An automatic confidentiality disclaimer generated by your IT system will not, of itself, be regarded as binding on HM Revenue and Customs (HMRC).

HMRC will process your personal data in accordance with the DPA and in the majority of circumstances this will mean that your personal data will not be disclosed to third parties.

Consultation Principles

This consultation is being run in accordance with the Government's Consultation Principles.

The Consultation Principles are available on the Cabinet Office website: http://www.cabinetoffice.gov.uk/resource-library/consultation-principles-guidance

If you have any comments or complaints about the consultation process please contact:

Amy Burgess, Consultation Coordinator, Budget Team, HM Revenue & Customs, 100 Parliament Street, London, SW1A 2BQ.

Email: mailto:hmrc-consultation.co-ordinator@hmrc.gsi.gov.uk

Please do not send responses to the consultation to this address.

Annex A: List of stakeholders consulted

HMRC received representations for further reform from the following organisations:

The Association of International Accountants
Baker Tilly
BDO
Boodle Hatfield
The Chartered Institute of Taxation
Deloitte
Ernst & Young
Frank Hirth
Grant Thornton
Hunter Rawlinson
The Institute of Chartered Accountants in England and Wales
KPMG
The Law Society
Macfarlanes
Mishcon de Reya
Moore Stephens
OneE Tax Limited
PriceWaterhouseCoopers
Rawlinson and Hunt
Simmons and Simmons
Society of Trust and Estate Practitioners
Taylor Wessing