PRIVATE FOUNDATIONS - AN ASPECT OF THE REMITTANCE BASIS

by Felicity Cullen

A foreign private foundation ("Foundation") might be described as a corporate vehicle which exhibits many of the characteristics of, and in some ways resembles a settlement or trust.[1] It has no exact equivalent in the law of England.

The UK tax treatment of a Foundation, its Founder and its beneficiaries is (because of its uncertain status for UK tax purposes) to a considerable extent a matter of speculation and, as Robert Venables QC has said[2], "anyone who prefers to become a Founder of a Foundation ... must appreciate that he is entering upon unchartered waters." There are many tax issues to be considered when establishing a Foundation and during the life of that Foundation. In this note I propose to consider only one of those many issues. This issue has evolved as a result of the amendments to the remittance basis of taxation in FA 2008. It concerns the capital gains tax ("CGT") treatment of gains accruing to the Foundation (as distinct from gains which may accrue to the Founder on creation of the Foundation).

For the purposes of considering this point, a number of assumptions are made as follows:-

- it is assumed that one of the fundamental tax issues concerning a Foundation, namely whether it should be treated as a company or a trust for tax purposes, can be neither conclusively nor exclusively resolved one way or another

- it is assumed that the trustees of the trust (if the Foundation is that) are resident, for tax purposes, outside the United Kingdom

- it is assumed the company (if the Foundation is that) is resident, for tax purposes, outside the United Kingdom

- it is assumed that the Founder of the Foundation will be an individual who is resident and ordinarily resident in but domiciled outside the United Kingdom for tax purposes

- it is assumed that the Founder will effectively control the Foundation for the benefit of himself and his family. As many Foundations will be created for asset protection purposes, this is indeed likely to be the case

- it is assumed that the Founder will be able to direct that all of the assets in the Foundation can be transferred to him or applied for his

benefit.

Analysis

Though it will depend upon the type and terms of the particular Foundation created, as well as the law of the jurisdiction under which it is formed and by which it is regulated, the property in (to use a neutral term) the Foundation will probably not be "held in trust" so that the Foundation should not be treated as a settlement[3] for general CGT purposes. For the purposes of ss.86A – 96 TCGA 1992, however, the definition of "settlement" is the wide income tax definition, which is now found in s.620 IT(TOI)A 2005. Under this definition, "Settlement" includes any disposition, trust, covenant, agreement, arrangement or transfer of assets ...". It is considered that a Foundation will fall within this definition of settlement (in s.620 IT(TOI)A 2005) so that gains accruing to those persons who are regarded as the trustees of the Foundation[4] will be attributable to and chargeable on persons (beneficiaries) who receive capital payments (as widely defined) from the Private Foundation which (if those persons are taxable on the remittance basis in its new form) they remit (as defined by FA 2008) to the United Kingdom.

On the basis that the Foundation may also be a company for UK tax purposes, the provisions of s.13 TCGA 1992 will also apply to attribute capital gains accruing to the Foundation to the participators in it according to their respective interests. On the assumption that the Founder is able to direct that the whole of the assets "in" the Foundation are transferred to him (or otherwise provided for his benefit), all of the gains accruing to the Foundation will be attributable to the Founder in accordance with s.13 TCGA 1992 and the new remittance rules which are (effectively) made applicable to s.13 TCGA 1992 by s.14A TCGA 1992. Before the introduction of the new rules in FA 2008, non-domiciled individuals were wholly excluded from liability under ss.13 and 87 TCGA 1992 even if they were resident in the UK for tax purposes. So the potential for liability to CGT to arise under these rules is a recent development.

Significantly, it will be apparent that there are two possible charges on the same gain. In practice, one would expect there to be a charge to CGT on the single gain accruing to the Foundation under one provision only. The question of priority of charge is, however, quite a difficult one. Under the new remittance basis, s.13 TCGA 1992 will apply to charge gains accruing on the disposal of assets situated in the United Kingdom on an arising (rather than a remittance) basis. In these circumstances (i.e. where gains accrue on the disposal of assets situated in the United Kingdom), it seems likely that HMRC will seek to apply s.13 TCGA 1992 in priority to s.87 TCGA 1992. Where, however, assets situated outside the United Kingdom are disposed of by the Foundation, it seems more logical for the charge under s.87 TCGA 1992 to apply so as to cause tax to be suffered by the (more direct) beneficiary of the gain.

It may be that there is some experience of the potential conflict between these two potential heads of charge in matters involving UK domiciled founders of Foundations. Historically, however, it seems likely that there will have been relatively few such founders. The lack of a decisive conclusion on this point is typical of many tax points concerning Foundations so it is not wholly surprising; it is, nevertheless, not satisfactory. What might be more surprising – indeed alarming - is the potential extent and impact of the new unchartered waters of the remittance basis. Mapping has only just begun.

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[1] For a general summary of jurisdictions in which Foundations may be established, reference should be made to the Private Foundations Handbook 2007, published by the ITPA in March 2007, editor Milton Grundy.

[2] The Liechtenstein Foundation and UK Tax Avoidance – Robert Venables QC, The Offshore Tax Planning Review, Volume 4, 1993/94 Issue 3.

[3] As defined in s.68 TCGA 1992. Strictly, s.68 TCGA 1992 defines settled property as "any property held in trust other than property to which section 60 applies (and reference, however expressed, to property comprised in a settlement are references to settled property". It is considered that the property in a Foundation is not held "in trust" and so is not settled property. Accordingly, the property in the Foundation is not comprised in a settlement for the purposes of s.68 TCGA 1992.

[4] Determining the identity of the trustees of the Foundation can, itself, be a difficult exercise.