The Offshore Taxation Review

NON-DOMICILED CHARITIES

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In *OTPR* Volume 6, 1996, Issue 3 at pp.213-8, Robert Venables QC challenged the Inland Revenue view that distributions from a non-resident trust to a charity produced a charge under section 87(4) TCGA 1992 despite the capital gains exemption for charities in section 256(1) thereof.

The point was also made that for such a charge to arise the distribution would need to be to a corporate charity which received the payment beneficially from the non-resident trustees, because any receiving charity that was established as a trust would simply obtain a corresponding pool of gains under section 90 TCGA 1992. Subsequent distributions by that charitable trust to any persons who were UK resident and domiciled would cause them to have imputed chargeable gains under section 87(4) TCGA 1992.

Despite the persuasive reasoning in the article, parties contemplating pursuing such arrangements may still feel reluctant to proceed in the light of the Inland Revenue view of the matter, at least unless a further line of defence can be built in.

Gasque

One approach appears to be to make the corporate charity which beneficially receives the capital payment from the non-resident trustees be a company which is resident in the UK but incorporated overseas and so domiciled abroad (*Gasque v IRC* (1940) 23 TC 210). Suitable entities might be a guarantee company established in the Isle of Man, Gibraltar or Ireland with objects which are charitable under UK law. In these circumstances section 87(7) TCGA 1992 gives the corporate charity the additional defence of being itself a beneficiary not domiciled in the UK.

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Dreyfus

First reactions to this suggestion may be to think that the case of *Camille and Henry Dreyfus Foundation v CIR* (1955) 36 TC 126 would preclude the foreign incorporated company from being a charity under UK law. However, the judgment of Sir Raymond Evershed MR in the Court of Appeal specifically indicates that a foreign incorporated company could qualify as a charity in UK tax law if all of its activities occurred in England and all its income-producing capital was invested here. The comments in the Court of Appeal were adopted wholesale by the leading judgment in the House of Lords. Observations of Jenkins LJ at p.152 suggest that the Memorandum & Articles of Association of any such overseas company should preferably direct that it was to conduct its operations exclusively in the UK. It would also seem advisable that they should confine powers to hold or occupy premises, have bank accounts, etc to those which are situated here, should prescribe that the officers be British citizens who are resident in the UK, and should expressly require that the application of funds for charitable purposes is to be as defined in English law, with any issue concerning the proper application of the funds to be dealt with primarily in the UK Courts.

UK Established

By its presence here and UK residence such a company would as a practical matter be "established" in the UK and subject to various UK laws such as Part XXIII Companies Act 1985 and the Taxes Acts. There would also seem no bar to an application for registration with the Charity Commissioners in view of the definition of "charity" in section 96(1) Charities Act 1993 as being any institution, corporate or not, which is established for charitable purposes and subject to the UK High Court in the exercise of that court's jurisdiction with respect to charities. This seems particularly so for an Irish company as Articles 6 & 52 of the EU Treaty guarantee nationals of any Member State, including all legal persons such as companies, the freedom to establish themselves in any member state without discrimination on grounds of nationality.

"Connected Party" Rules

One would need to keep the ownership and shareholder control of the foreign incorporated but UK resident charitable company away from the offshore trustees and from the settlor of the offshore trust plus any person connected with him. Otherwise section 96(1) and (7) TCGA 1992 would treat its onward distributions of funds as if they had been made by the offshore trust rather than by the charity itself. Furthermore, even if the offshore trust already had power to appoint funds

to any charity, a distribution to a settlor controlled company that did not exist at 19th March 1991 might taint the trust under paragraph 9(6) Schedule 5 TCGA 1992 despite SP5/1992 indicating at paragraph 37 that this provision is only aimed at ultra vires distributions.

There would seem to be no problem in genuine independent ownership by any other party, as the company itself would not be of value to such an owner in view of its obligation to apply all its funds for charitable purposes. Furthermore, there seems nothing objectionable in any UK resident settlor or beneficiary of the offshore trust being a director of the company in due course.

Avoiding Settlor Benefits

In *Re Clore's Settlement Trusts* [1966] 2 All ER 272 following the House of Lords decision a few years earlier in *Pilkington v IRC* [1966] 40 TC 416 it was held that a distribution from a trust to a charity was a payment for the benefit of one of the beneficiaries of the trust if the charitable appointment recognised a moral obligation felt by that beneficiary. Therefore if the settlor is a beneficiary of the offshore trust it could be advisable for him to make it clear to the non-resident trustees that he feels under no moral obligation whatsoever to see them appoint funds to any charity which had been established, but that if they were minded to do so then any consent required from him (e.g. as protector to allow the appointment of the charity as an additional beneficiary) would not meet with resistance.

Close involvement of the UK resident settlor at the time the charity is being established and funded (e.g. by him being a director at the outset) should be avoided in case this gives ammunition to the Inland Revenue to contend under section 97(2) and (5) TCGA 1992 that by satisfying the settlor's wish to see the charity funded and/or personally administer the distribution of those funds, the offshore trust is conferring a benefit on him or applying funds for his benefit or is making the initial payment at his direction.

Altruism's Limits

Whether as a practical matter clients would still feel minded to proceed with such charitable arrangements after having all these points explained to them is, of course, another issue. Approval up front from FICO could well be found a pre-requisite to get matters under way. This is unless one finds a client who believes it is for the advancement of education and beneficial (to at least a section of the community) to establish arrangements likely to provoke a response from the Inland

Revenue that extends the knowledge of UK tax professionals as to whether charities can be established tax free from funds trapped in golden offshore trusts and potentially liable to tax up to 64% if extracted by other means.