**MIXED FUNDS CLEANSING RULES FOR NON-UK DOMICILIARIES**

The latest reforms to the taxation of UK resident but foreign domiciled individuals (“RND”) came into effect as expected from 6 April 2017.

The matching rules for remittances to the UK from unremitted foreign income and capital gains has long been a challenge for both taxpayers and their advisers. Having to operate segregated capital, income and capital gains accounts always proved to be cumbersome and invariably clean capital would get tainted with foreign income or capital gains.

It is therefore a welcome feature of the new rules that there is an opportunity for individuals to cleanse their mixed funds which will enable RNDs to potentially unlock clean capital and also by segregating they can determine the source of any remittance to the UK. Even where the RND does not need to remit funds to the UK at present, it is important to take up this opportunity if there is the prospect of wishing to remit funds to the UK in the future.

This opportunity is available to all RNDs who have used the remittance basis prior to 6 April 2017 unless they are returning RNDs who had a domicile of origin in the UK. There is no requirement to have paid the remittance basis charge in any given year as is the case with the relief for rebasing of assets to 5 April 2017 market value for capital gains tax purposes.

This opportunity is only available for cleansing taking place between now and 5 April 2019.

**Mixed Fund – What does it actually mean?**

A mixed fund is simply an account which has a mixture of clean capital, foreign income and foreign capital gains.

Where a remittance is made from that account to the UK, the income is treated as the first source, then capital gain, then finally the capital. This is clearly to the disadvantage of a RND from a UK tax point of view.

A RND who invested his clean capital would receive sale proceeds which would be a mixture of clean capital and capital gain. These sale proceeds generally could not be split between capital and capital gain and therefore segregated. In time all of the clean capital would become mixed and when a remittance is made it would be of the capital gain first and then the capital.

**How do I cleanse my mixed fund account?**

The new rules not only allow the opportunity to segregate income from capital in a mixed fund but also potentially allow a RND to segregate the capital from capital gains.

There are three important considerations that have to be observed:

1. You have to be able to identify each source within the mixed fund to be able to cleanse it.
2. You can only cleanse a non-UK bank account which is in cash
3. You only have one opportunity to cleanse on each bank account

If a RND has an asset which represents a mixed fund this cannot be cleansed unless it is sold first and then the cash can be segregated. Where investments are held it is important to consider the timing of any realisation of the investment for the cleansing process.

If you are unable to identify the source within the mixed fund account then this cannot be cleansed.

A RND will have to nominate all transfers out of the mixed fund that the RND wants to cleanse. Some care needs to be taken in the analysis of the mixed fund account as over nominating a source will mean that the cleansing will not have been done and the normal mixed funds rules and offshore transfer rules will apply. It is however still possible to cleanse the new account as it has not been cleansed previously provided it is done before 6 April 2019.

**Example**

Roger came to the UK in 2012/13 and has claimed the remittance basis of taxation. Roger has a foreign mixed fund account of £80,000 which contains the following having made an investment of £10,000 and received sale proceeds of £20,000:

Clean capital £50,000
Foreign investment sale proceeds £20,000 of which £10,000 is capital gains
Foreign income £10,000

If Roger were to remit £15,000 to the UK it would comprise of £10,000 income (taxed at up to 45%) and £5,000 capital gain (taxed at up to 20%) under the normal matching rules.

However, Roger decides to cleanse his mixed account before remitting funds to the UK. He transfers £10,000 to a new capital gains account and £10,000 to a new foreign income bank account leaving £60,000 capital remaining in his account.

Roger can now make a payment from his cleansed mixed fund account to the UK of £15,000 with no tax due as it all relates to capital. The new income and capital gains accounts can be used outside the UK with no tax consequences provided those funds are not remitted to the UK.

As a reminder, this opportunity is only available until 5 April 2019 so it is important to establish the source within the account in good time to be able to make the transfers and ensure the new bank accounts are opened in time.

Where you do have a mixed fund account and you wish to consider cleansing it, please contact our Private Client Director Rakesh Dabasia rakesh.dabasia@rayneressex.com or your usual Partner contact at Rayner Essex.

***Disclaimer: Please note that this document is not intended to give specific technical advice and should not be construed as doing so. It is designed to alert clients to some of the issues and not intended to give exhaustive coverage of the topic. Professional advice should always be sought before action is either taken or refrained from as a result of information contained herein.***

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