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Offshore Family Limited Partnerships - The next generation of Inheritance Tax planning?

Following the enactment of the Finance Act 2006, the UK government introduced an Inheritance Tax (“IHT”) charge of 20% levied upon the value of assets transferred into virtually all trusts by a UK domiciliary or deemed domiciliary, with a further charge every 10 years which equates to 6% of the trust value and further charges on distributions. An Offshore Family Limited Partnership (“OFLP”) can provide a tax effective alternative, subject to the donor surviving for 7 years following the gifting of the interests in the OFLP and retaining no benefit in the gifted interests.

How does it work?

An OFLP has separate legal personality. The OFLP will usually be based in Jersey and the terms of the partnership will be contained within a Partnership Agreement written under the appropriate law.

General Partner - the OFLP will have a General Partner who is responsible for managing the partnership and its assets. The General Partner could be an offshore company thereby limiting their liability. There is usually a restriction that Limited Partners will not be allowed to withdraw capital or transfer interests without the General Partner’s consent, thereby leaving residual control with the General Partner.

Limited Partners - there will be at least one Limited Partner who will have an interest in the capital and income of the OFLP but who will not have control over its management or business. The Limited Partner has limited liability in the partnership up to the sum of his or her interest and there is no limit on the number of Limited Partners. It is common for Limited Partners of the OFLP to be the second or third generation family members.

How will it operate?

The Partnership Agreement can give the Limited Partners either a fixed interest in the income and capital of the assets of the OFLP or a flexible interest in those same assets, without direct ownership. The interest could be determined by the General Partner using various discretionary and commercial criteria as set out within the terms of the Partnership Agreement. The Partnership has legal title to the assets and the Agreement sets out the relationship (in a similar fashion to a trust deed) between the General Partner who has oversight and responsibility for managing the assets on behalf of the Limited Partners. This is similar to the fiduciary relationship between trustees and beneficiaries.

The advantages of a Family Limited Partnership

The key advantages of forming an offshore Family Limited Partnership are:-

- It can reduce the donor's inheritance tax liability on their estate if they are UK resident or hold UK situs assets;
- It can provide a separation of control and ownership of assets;
- It can give the donor a mechanism to control how the assets pass onto the next generation through succession planning;
- It can ring fence certain assets to protect and provide a barrier to commercial or creditor risk against the donor;
- Family assets can be consolidated in an investment structure.

Advantages of structuring offshore

In addition to those advantages already noted, a Family Limited Partnership can offer further benefits if structured offshore, such as:-

- FSA regulation will not be required provided that the OFLP is restricted to a relatively small number of family members. If the Partnership becomes wider, there are different Collective Investment Schemes that operate which can be created capitalising on Jersey's 'lighter touch' regulatory environment;
- Jersey prohibits the enforcement of judgments against Limited Partnership assets unless the

judgment is granted against the General Partner acting in his capacity as General Partner of the partnership;

- A UK registered Limited Partnership will be subject to public disclosure requirements at Companies House in the UK whereas using either Jersey or the British Virgin Islands means no such disclosure requirements exist, offering enhanced confidentiality for the family;
- Multinational (UK resident but non domiciled) clients who may have UK connections but be resident elsewhere, may use the planning to achieve other inheritance tax benefits for other jurisdictions; and
- Multinational clients may be able to generate other opportunities through the use of offshore planning.

Capital Gains Tax ("CGT") and Stamp Duty Land Tax ("SDLT")

It is possible to transfer assets to an OFLP without triggering a CGT liability. This could occur where assets are transferred at a loss, no gain or if the asset is cash and therefore gain neutral.

There may be, subject to careful planning, opportunities to use business asset holdover relief if the assets to be donated are part of a trading business in the UK.

SDLT should not be payable upon the transfer of land into an OFLP provided the partners are connected for the purpose of the legislation. It

should be noted that anti-avoidance provisions may apply if there are arrangements in place to withdraw capital or to replace or modify the partners at some later stage. Generally, the SDLT position will always need to be checked in detail.

Tax advice

Specialist advice should be sought before the structure is created. To assess its suitability, the client should also consider:-

- The objectives of the family, the donor and the Limited Partners;
- Whether the structure is suitable given the value and nature of the assets to be protected;
- Whether there is a business to satisfy the requirement for a partnership;
- Whether the regulatory requirements acceptable.

IHT planning will generally not be effective if the donor who is gifting the OFLP interest reserves a benefit over those same interests. It is therefore important to consider which assets should be placed into the OFLP.

OFLPs are treated as tax transparent which means that the partners are assessed to tax on the income and gains of their partnership interests. This avoids the double layer of taxation that occurs if you place assets into a trust or corporate vehicle.

Costs

The costs to create, manage and provide administration services to an OFLP are comparable to those costs levied for a trust arrangement. These costs will depend upon a variety of factors including the nature of the underlying assets, the volume of transactions and the frequency and detail of reporting.

Conclusion

The OFLP is another wealth planning vehicle which offers flexibility and the option for tax efficient structuring for family wealth. The regulatory requirement in the UK means that the cost of setting up an onshore family limited partnership can be high. These requirements do not exist offshore and therefore the cost of setting up an OFLP should be less than its onshore counterpart.

Jersey Trust Company

Jersey Trust Company is one of Jersey's leading independent providers of private wealth, corporate and fund administration services. Our head office is located in Jersey's financial district of St. Helier and through our continued international expansion we have opened offices in jurisdictions such as London, Glasgow, the British Virgin Islands and Geneva.

Our private wealth clients can expect experience, confidentiality and tailored solutions from us, which we believe are essential to the foundation of a successful long-term partnership. We have a dedicated Private Wealth division with experienced directors and teams led by professionally qualified managers who provide formation and administration services for vehicles such as trusts, companies and partnerships, as well as more recently, private trust companies and foundations. We have extensive experience of structures for individuals and families with a diverse range of asset classes which allows us to provide real added value to new and existing clients alike.

Regulated by the Jersey Financial Services Commission

This publication is intended to provide an overview of the subject matter and is not comprehensive in nature or to be construed as legal or tax advice. We recommend that clients seek professional advice on any particular matter.

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