

Changes to the Taxation of UK Resident Non-Domiciled Individuals - April 2017

In the 2015 Summer Budget the government announced that it would be introducing major changes to the taxation of non-UK domiciled individuals in April 2017 and published an initial consultation document on the reforms in September 2015.

After a long period of uncertainty, the government has now published a further consultation document which provides much more detail on the nature of these reforms and confirms that they will indeed take effect from April 2017.

There are both positive and negative aspects of the new regime and we have set out below our summary of the main changes.

Deemed domiciled

The government has confirmed that individuals who have been UK resident for 15 of the previous 20 tax years will become deemed UK domiciled for all tax purposes with effect from the 16th year of residence, regardless of their domicile status under general law.

A split tax year will count towards to the 15/20 year test and so deemed domiciled status may arrive after little more than 13 calendar years in some cases. Year spent in the UK while a minor will count towards the 15 year threshold.

Individuals with UK deemed domiciled status will not be able to access the remittance basis of taxation and will be subject to UK tax on their worldwide income and gains on an arising basis.

An individual who has acquired deemed domiciled status can only lose it by becoming non-UK resident for at least 6 tax years.

Born in the UK with a UK domicile of origin

Individuals with a UK domicile of origin who return to live in the UK will be treated as deemed UK domiciled for income and capital gains tax purposes for any year in which they are UK resident.

They will be treated as deemed UK domiciled for IHT purposes after being resident for at least one of the previous two tax years. This will provide a short grace period to those returning to the UK for a brief time only.

Trusts settled by such individuals while non-UK domiciled will be treated as a relevant property trusts in any year of UK residence. In other words, a trust's IHT status will follow the settlor's residence status which could change from year to year.

CGT rebasing

Individuals who become deemed UK domiciled in April 2017

and who have paid the remittance basis charge in any year prior to April 2017 will be able to rebase personally owned foreign assets to their 5 April 2017 market value. This concession will not apply to assets held in a company or trust structure.

Rebasing will apply on an asset by asset basis and will be limited to foreign assets in personal ownership at the date of the summer 2015 budget, 8 July 2015.

Under rebasing, only the increase in value between 5 April 2017 and the date of sale will be subject to tax on the arising basis. Gains accruing pre 6 April will not be taxed.

The remittance of the proceeds of sale of an asset which has been rebased to its 5 April 2017 market value will require separate consideration, however. If the asset was purchased with foreign income and gains there may be a tax charge on the remittance of foreign income and/or foreign gains comprised in the proceeds. If, on the other hand, the original funds used to acquire the asset were clean capital, it will be possible to remit the full gain to the UK tax-free.

Foreign capital losses

Individuals who become deemed domiciled will be able to offset foreign capital losses arising after they have become deemed domicile against capital gains arising in the UK.

Mixed Funds Cleansing Concession

Currently offshore bank accounts containing a mixture of capital, income and/or gains cannot be split into their component parts or "unmixed" and remittances from such mixed funds are deemed to consist of income first, then gains and finally capital.

The government has announced that during a transitional period applying from 6 April 2017 to 5 April 2018 it will be possible to separate mixed fund accounts (but not assets bought with mixed funds) into their constituent parts and rearranged into separate accounts, provided the source of the funds can be identified. Overseas assets with the form of a mixed fund can be sold within the transitional period and the sale proceeds separated into their separate components in the same way as money in a bank account.

There will be no requirement to remit from newly segregated accounts in any particular order or within any particular time limit. Funds can be remitted from each separated fund, even if the remittance occurs in a year after the transitional period has ended.

The one year opportunity is open to all non-UK domiciled individuals (not just those who become deemed domiciled on 6 April 2017) except those who were born in the UK or who have never claimed the remittance basis.

Protected Trust Provisions

The government originally proposed to tax UK resident deemed domiciled beneficiaries on benefits they receive from an offshore trust within or outside of the UK (on a "flat rate" basis), regardless of income and gains arising within the trust. Income and gains retained in the trust would not be taxable.

This "benefits tax" idea has now been scrapped on the basis that this would unfairly affect "dry trusts" with no income or gains.

In its place the government has announced a "protected trust" status for trusts set up before the onset of deemed domicile, albeit with some stringent conditions.

Currently, the anti-avoidance rules tax UK resident and domiciled settlors of offshore trusts on income and gains arising in it where the settlor, his spouse or minor children can benefit from the trust. What will constitute "benefits" under the new provisions has not yet been defined.

Trust Gains

Where the settlor becomes deemed domiciled from April 2017 and either assets are subsequently added to the trust or the settlor, his spouse or minor children actually benefit from the trust, trust gains will be treated as made by the settlor and taxed on the arising basis.

It has not been explicitly confirmed whether this arising basis treatment will apply merely for the year in which benefits are received or whether all future trust gains will be attributed to and taxed on the settlor, regardless of further benefits from the trust.

Most advisers take the view that the latter treatment will apply.

Trust Income

Where the settlor becomes deemed domiciled from April 2017 and the settlor, his spouse or minor children actually benefit from the trust, non-UK trust income will be taxed by reference to worldwide benefits received and matched to the structure's non-UK income.

In contrast to trust gains, the trust will not permanently lose its "protected trust" status for income tax purposes once benefits are actually received from the trust. Instead, income tax will apply on a year by year basis according to benefits received and matched to non-UK income.

These provisions will not apply to non-resident trusts with settlors and beneficiaries who are non-UK domiciled and are not deemed domiciled in the UK. The favourable treatment of these trusts will continue.

IHT on residential property

As expected, from 6 April 2017 UK residential property owned indirectly through offshore entities will no longer count as "excluded property" for IHT purposes.

The definition of residential property is wide ranging and will include any building in the process of being constructed or adapted for use as a dwelling or mixed use properties which have been a dwelling at any time in the previous two years. There will be no exclusions for principal private residences or property such as let property which currently benefits from ATED reliefs.

Only debts that relate exclusively to the property in question will be deductible for IHT purposes. The deduction of debt will be pro-rated where there are other assets in the same corporate "envelope" and any debt between connected parties will be disregarded.

De-enveloping

Despite previous hints to the contrary, the government has confirmed that it will not be introducing any form of relief from the SDLT and CGT charges that often follow the removal of residential property from a holding structure.

In some instances, paying ATED charges indefinitely (and without IHT protection) will be preferable to the tax consequences of de-enveloping.

Temporary non-residence CGT rules

These rules will not be applied on an arising basis to a deemed domiciled individual who would have expected to have access to the remittance basis in respect of disposals taking place before the original announcement of the proposals in July 2015.

Summary of services

Jeffcote Donnison are specialists in the field of non-UK domiciled taxation and act for many non-UK domiciled individuals.

Some of the ways in which we can provide assistance with the new rules are as follows:

- Reviewing UK residency to establish the onset of deemed domiciled status and advise on appropriate restructuring
- Reviewing offshore assets and assisting with capital gains tax assets rebasing elections
- Analysing mixed funds and identifying clean capital
- Reviewing UK residential property holding structures and advising on the tax consequences of de-enveloping

For more information, please contact your normal member of the Jeffcote Donnison LLP team or:

Matthew Gandy CTA

email: mgandy@jeffcote.co.uk • tel: +44 (0) 20 7399 3100

James Clerkin CTA

email: jclerkin@jeffcote.co.uk • tel: +44 (0) 20 7399 3100



Jeffcote Donnison LLP
Lumley Street,
Mayfair,
London W1K 6JE

tel: +44 (0)20 7399 3100
fax: +44 (0)20 7408 2435
e-mail: info@jeffcote.co.uk
jeffcotedonnison.co.uk

- ◆ UK and International tax advice
- ◆ Corporate services
- ◆ Business advisory
- ◆ Accounting services