



Future changes to the taxation
of non-UK domiciled individuals

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Further to the announcements made at the UK Summer Budget 2015, the UK Government issued its consultation on the proposed changes to the taxation of non-UK domiciled individuals on 30 September 2015, and has also released additional detail within the 2016 Budget, announced on 16th March 2016.

The Government intends that these changes will take effect from April 2017 and legislation will be introduced in the Finance Bill 2017.

A further consultation will follow in 2016 on the proposed changes to the Inheritance Tax rules on UK residential properties held by non-UK domiciled individuals, which is not covered in this consultation document.

Current rules for taxing non-domiciles

The current UK domicile rules aim to distinguish between those who are permanently resident in the UK and those who do not consider the UK to be their permanent home.

Under these domicile rules, individuals who are resident but not domiciled in the UK:

- Are subject to UK tax on all UK source income and capital gains; but,
- Can choose to use the remittance basis of taxation where they only pay UK tax on their foreign source income and capital gains if or when these are remitted to the UK.

Long-term UK resident remittance basis users have to pay a charge if they wish to use the remittance basis of tax. For those resident for at least 7 of the previous 9 tax years the charge is £30,000, rising to £60,000 for those resident in the UK for at least 12 of the past 14 tax years. In April 2015 a new charge of £90,000 was also introduced for those resident for at least 17 of the past 20 tax years.

Those who have less than £2,000 of unremitted foreign income and gains in a tax year do not need to make a claim to use the remittance basis, and so do not pay the remittance basis charge.

The proposed changes

The proposed changes to the UK non-domicile rules are split into two areas:

- Deemed UK domicile for long-term residents
- Those born in the UK with a UK domicile of origin

Deemed UK domicile for long-term residents

At the Summer Budget 2015, the government announced that it will treat any individual who has been resident in the UK for at least 15 of the past 20 tax years as deemed UK domiciled for tax purposes.

This means that from their 16th year, a foreign domiciliary will become deemed UK domiciled and will no longer be able to use the remittance basis of tax.



At this point they will also be subject to UK inheritance tax (IHT) on their worldwide assets.

An individual who has lived in the UK for 15 consecutive tax years and then leaves the UK for 6 or more consecutive tax years could return here and could claim non-dom status again for another 15 years.

Under these rules, the £90,000 remittance basis charge will no longer be applicable. Please note that an individual may need to pay the £90,000 remittance basis charge for two years; 5th April 2016 and 5th April 2017, then would become deemed UK domicile from 6 April 2017 under the proposed rules.

The government intends to include any year of tax residence when counting the 15 tax years, including split-years.

There will be no grandfathering of the rules. From April 2017, individuals will have to assess their residence for the previous 15 tax years. Where some of these years fall before the UK statutory Residence Test, they will need to assess their residence in those years based on the rules in place at the time.

In the 2016 Budget, the Government confirmed that non-doms who become deemed domiciled in April 2017 can treat the cost base of their non-UK based assets as being the market value of that asset on 6th April 2017. Individuals who are expected to become deemed UK domicile under the 18 out of 20 year rule will be subject to transitional provision with regards to offshore funds to provide certainty on how amounts remitted to the UK will be taxed.

The government is seeking views on whether or not to retain the £2,000 de-minimis threshold for non-domiciled individuals who become deemed domiciled.

The treatment of offshore trusts

To provide some protection to individuals who had set up an offshore trust before becoming deemed domiciled, the government has proposed to treat offshore trusts as follows:

- An individual who becomes deemed-domiciled in the UK will pay tax on benefits that they receive from any offshore trust and any underlying entities. This is irrespective of where the benefit is received.
- This will be based on the taxable value of benefits received by the individual without reference to the income and gains arising in the offshore trust structure.
- As it stands at the moment it would appear that distributions of initial capital would also be taxed. This is potentially punitive and it is hoped that this point will be clarified in due course.
- The individual will be protected from UK tax while neither they nor their spouse or children receive any benefit from the trust (i.e. they will not be taxed on the underlying income and gains of the trust structure).
- However, UK source income will be taxable on the arising basis, as it would be under the existing rules, if either the settlements legislation or the transfer of assets legislation applies.

The government is considering whether to introduce these rules for all UK resident non-domiciles.

This will involve substantial changes to the current UK anti-avoidance rules relating to the transfer of assets abroad.

The government is still looking into these issues and has not yet published draft legislation on these reforms.



Excluded property trusts

Offshore trusts that are set up by an individual who is not domiciled in the UK will remain outside the scope of UK Inheritance Tax (IHT), even after that individual becomes deemed-UK domiciled under the 15 year rule.

UK domiciled or deemed-domiciled individuals leaving the UK

Under the current IHT rules an individual who ceases to be domiciled in the UK will only continue to be treated as domiciled in the UK if they have been domiciled in the 3 years immediately preceding the chargeable event.

Under the proposed deemed-domicile rules, an individual would be treated as domiciled until they have been non-resident for at least 6 years.

The government intends to align these rules by treating a UK domiciled individual as non-domiciled on the later of the date that they acquire a domicile of choice in another country, or the point when they have not been resident in the UK for 6 years.

Born in the UK with a UK domicile of origin

The government proposes to treat an individual who was born in the UK with a UK domicile of origin, but who has acquired a domicile of choice elsewhere, as having a UK domicile of origin for tax purposes while they are resident in the UK.

The individual will continue to be treated as not domiciled in the UK while they are not UK resident (provided that they have not breached the 15 out of 20 deemed UK domicile rule while living in the UK).

This group of individuals will be treated as having a UK domicile for tax purposes. This means there will be no special rules for protection of offshore trusts, either in terms of the tax on income or gains in the trusts, or for IHT purposes.

The excluded property trust rules for IHT will be changed so that they do not apply in these circumstances. This will be the case even for trusts that are set up offshore while the individual was not domiciled or resident in the UK. Once that individual becomes UK resident the assets in that trust will cease to qualify as excluded property and would be liable to inheritance tax charges.

The government is currently proposing a grace period for individuals who only return to the UK for a short period, whereby the individual would also need to have been resident in the UK for at least one of the previous two tax years to fall within then the deemed domicile rule.

Budget 2016 also confirmed that non-doms who become deemed domiciled in April 2017 can treat the cost base of their non-UK based assets as being the market value of that asset on 6th April 2017.



Summary

It should be noted that the changes discussed above are still undergoing consultation and may change from the current proposals during this process. However we anticipate that the proposals will not alter significantly from those outlined above.

These proposals involve substantial changes to the taxation of non-UK domiciled individuals that may have an impact both on future tax planning and also historic tax planning and structures that have previously been put in place.

Clients will need to be aware of the tax considerations on moving to the UK, particularly those who were born in the UK with a UK domicile of origin, and long term UK resident non domiciled clients, will need to be mindful of the new deemed UK domicile rules.

If you or your clients would like to discuss these proposals further, and how these may impact on your situation, please speak to your usual SMP adviser or one of the contacts below:

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