

GIBSON BOOTH

Changes to the taxation of Non-Domiciliaries

Significant changes are being made to the taxation of non-UK domiciliaries. This note is a brief outline of the major changes.

Income tax and capital gains tax

In summary, from 6 April 2017 non-domiciliaries who have been UK resident for at least 15 out of the previous 20 tax years will no longer be able to benefit from the remittance basis of taxation as they will be “deemed” to be domiciled in the UK for income tax and capital gains tax purposes. They will therefore be taxable on their worldwide income and gains instead of just UK source income and gains and remittances of overseas income and gains.

There will however be two valuable relieving provisions:

Rebasing

It is intended that non-domiciliaries will be able to rebase the capital gains tax cost of an asset to its market value at 5 April 2017, thereby effectively wiping out the gain that has accrued from purchase up to 5 April 2017. It follows that proceeds of an asset sold shortly after 5 April 2017 may be able to be remitted to the UK with minimal tax consequences. (However care should be taken to consider what the asset was purchased with initially because if acquired with, say, overseas income then care needs to be taken that there is no remittance of that income).

Rebasing will also be available for gains on offshore funds charged to income tax.

Rebasing will only be available to individuals who become deemed domiciled on 6 April 2017 who have paid the remittance basis charge in at least one year since 6 April 2008. It will not be available for assets that have been in the UK at any time since 16 March 2016 which have been moved abroad.

It is intended that rebasing will apply automatically to qualifying assets. It will however be possible to elect on an asset by asset basis that rebasing should not apply.

Account Cleansing

In the period 6 April 2017 to 5 April 2019 it will be possible to identify clean capital, income and/or gains in a mixed fund account (an account containing a mixture of income, gains and clean capital) and pay identified amounts to one or more separate accounts. This should enable clean capital to be segregated and remitted to the UK tax free. Hitherto clean capital has effectively been “locked” in a mixed account because of strict ordering rules.

Cleansing will be available to all non-domiciliaries who have been taxed on the remittance basis, not just those who become deemed domiciled on 6 April 2017 and it is not necessary that they have paid the remittance basis charge.

Neither rebasing nor cleansing will be available to individuals who have previously had a UK domicile of origin (so called returning non-dom or formerly domiciled resident). Such individuals will be deemed domiciled for tax purposes from 6 April 2017 (with limited exceptions).

Inheritance tax

The previous rule whereby a non-domiciled individual was deemed to be domiciled for IHT purposes after 17 out of 20 years of residence is being aligned with the new 15 out of 20 years rule for income

tax and capital gains tax as above. Additionally, after leaving the UK a deemed domiciled individual will continue to be domiciled for IHT purposes until after 4 years of non-residence, meaning that their worldwide estate continues to be within the scope of UK IHT for this period after leaving.

The scope of inheritance tax is also being extended to UK residential property held through offshore companies from 6 April 2017. To the extent that the value of shares in a foreign close company is attributable to UK residential property those shares will not be excluded from exposure to UK IHT. Such structures should be reviewed.

There will also be provisions which will restrict the deductibility of loans taken out by an offshore company to acquire UK residential property. Overseas assets used as collateral for a loan to acquire UK residential property and loans made to acquire UK residential property will also potentially within the scope of IHT.

Trusts

There are significant changes proposed to the taxation of trusts with a non-domiciled settlor. In outline, income and gains from such trusts can be charged on the settlor on an arising basis when they become deemed domiciled unless they have "protected" status. Protected status can be lost if additions are made to the settlement at a time when the settlor is deemed domiciled.

Additionally, from 6 April 2017 it will not be possible to wash out gains in an offshore trust by making payments to a non-resident beneficiary (except in the year of winding up). Such gains will remain to be matched with future payments to UK resident beneficiaries.

PLANNING

The foregoing is an outline of the major changes which will apply to the taxation of non-domiciliaries from 6 April 2017 and the following are some of the planning points arise:

- Non domiciliaries should consider whether to set up an offshore trust, or add further funds to an existing trust, prior to becoming deemed domiciled so as to take advantage of the IHT benefits. Offshore structures in place prior to becoming deemed domiciled potentially still qualify to be excluded from IHT thereafter.
- Current offshore structures should be reviewed, particularly those owning UK residential property to consider if there is any ongoing benefit from retaining the structure. However potential tax charges on collapsing structures need to be considered.
- Trusts settled by a non-domiciliary who has retained an interest in the trust should seek detailed advice on their position.
- Non domiciliaries should look to "cleanse" their overseas accounts to identify clean capital that can be remitted to the UK tax free.
- Consideration should be given to opening new overseas accounts to receive income and/or gains taxable on the arising basis and so which can be remitted tax free. (Care is still need to ensure historic income/gains are not inadvertently remitted as noted above).
- Consider potential benefits of extracting funds from existing trusts before 6 April and/or before becoming deemed domiciled.

And finally.....

These notes are intended to give an overview of the forthcoming rules to help identify areas where action may be needed. They are not intended to be a detailed analysis and, at the time of writing, final legislation is awaited. Accordingly, advice specific to an individual's circumstances should be sought and no action should be taken with firstly taking specialist advice.