Non Dom and Offshore Trust Changes

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Non-Dom And Offshore Trust Changes

Following substantial changes to the UK's 'non-dom' regime, effective from 6 April 2017, individuals who are living in the UK but are domiciled abroad should review their tax affairs to make sure they are up-to-date, compliant with current UK tax law, and making the most of any appropriate planning opportunities.

Deemed Domicile

- From 6 April 2017, individuals with a non-UK domicile of origin who have been UK resident in at least 15 of the prior 20 tax years will be 'deemed' domiciled in the UK for income tax, capital gains tax ('CGT') and inheritance tax ('IHT') purposes.
- This means they will no longer be able to access the remittance basis of taxation and will instead be subject to UK tax on their worldwide income and gains as they arise. In addition, their worldwide estate will be within the scope of UK IHT.
- Non-UK income and gains arising in earlier years that were subject to the remittance basis will continue to be subject to tax to the extent they are remitted to the UK.
- It is possible to 'reset' the deemed domicile clock by being non-UK resident for six full tax years. They will fall outside the UK IHT net from the fourth year of non-residence.
- Individuals who were born in the UK and have a non-UK domicile of choice (but with a UK domicile of origin) will be deemed domiciled for any year in which they are UK resident. In the case of IHT only, the deemed domicile provisions will apply only if they have been resident in one of the two prior tax years.

Transitional provisions

- Non-UK situs assets qualify for automatic CGT rebasing to their market value at 5 April 2017, provided that:
    - The assets were held directly by the individual (i.e. not through a trust or other structure);
    - The assets were not UK situs assets at any time between 16 March 2016 (or the date of acquisition, if later) and 5 April 2017;
    - The individual became deemed domiciled on 6 April 2017, but remains non-UK domiciled under general law; and
        - They paid the remittance basis charge in at least one year since 2008.
- Rebasing applies automatically if the conditions are met, but it is possible to disapply rebasing (by election) in respect of specific assets, if beneficial to do so – for example, if the original cost was higher than the asset's 5 April 2017 market value.
- Despite some original uncertainty, HMRC subsequently confirmed that offshore non-reporting funds also qualify for rebasing, notwithstanding gains on such funds are ordinarily subject to income tax.
- There was an opportunity for non-doms to 'cleanse' mix funds – in other words, to separate 'clean capital' from other non-UK income and gains in the same bank accounts. This window of opportunity ended on 5 April 2019. Mixed funds should therefore be kept outside the UK to avoid a tax charge on remittances to the UK.

Offshore trusts

- Many non-UK domiciled individuals are settlors (and often also beneficiaries) of non-UK resident trusts holding non-UK situs assets. Provided such trusts were settled by individuals with a non-UK domicile of origin (and they had not acquired a UK domicile of choice, nor become deemed domiciled) the trust's assets should remain outside the scope of UK IHT even once the settlor becomes deemed domiciled.
- In addition, non-UK income and gains of the trust should not be taxable on the settlor (whose circumstances meet the conditions above). They will instead be taxed if and when the settlor (or another beneficiary) receives a capital distribution or benefit, such as the use of trust property.
- These 'protections' will be lost if any further additions are made to the trust when the settlor is deemed domiciled, or after the settlor acquires a UK domicile of choice. What constitutes an addition is very broad, and may include the provision of loans; advice provided by the settlor to the trustees (such as on investment policy); and other 'indirect' additions.

- UK sourced income will continue to be taxed on settlors who are also beneficiaries, as is currently the case.
- Wider anti-avoidance provisions have also been introduced to extend the reach of taxation of offshore trusts, including:
  - Removing the ability to 'wash out' trust gains by making distributions to non-UK resident beneficiaries;
  - Taxing the settlor on distributions made to 'close family members' who are not subject to UK tax on the distribution themselves (such as if they are non-UK resident or claim the remittance basis);
  - Taxing recipients of 'onward gifts', where the original beneficiary was not subject to UK tax on the distribution and subsequently made gifts to UK taxable individuals.
- Special rules apply to carried interest paid to trusts in respect of investment management services performed by settlors. In principle, such carried interest returns will be taxable on the individual directly and should not therefore also be taxed when distributions are made from the trust. Credit may be available where carry is distributed to allow the individual to pay the tax arising thereon. Specialist advice must be sought.

Business Investment Relief

- Business Investment Relief ('BIR') allows non-doms to remit otherwise taxable income and gains to the UK without a charge, provided they are invested into a qualifying business.
- Previously, a qualifying investment would have involved a subscription for new shares in, or making a loan to, a trading, stakeholder or holding company. The BIR provisions have been extended such that an investment can also be made by acquiring existing shares.
- A new category of 'eligible hybrid company' ('EHC') has also been introduced into which a qualifying investment can be made. An EHC is defined as a company that:
  - Is not an eligible trading company or an eligible stakeholder company
  - Carries on one or more commercial trades, or is preparing to do so within the next 5 years
  - Holds one or more investments in eligible trading companies or is preparing to do so within the next 5 years, and
  - Carrying on commercial trades and making investments in eligible trading companies are all, or substantially all, of what it does (or of what it is reasonably expected to do once it begins operating)
- If an investment ceases to qualify (such as on disposal, cessation of company qualifying status or the investor being in receipt or certain extractions of value), mitigating steps must be taken within a grace period. This can be as few as 45 days.
- Please contact us for more detailed information on BIR and how it can be used to facilitate tax-efficient remittances to the UK.

UK residential property

- Non-doms have historically held UK residential property ('UKRP') through non-UK incorporated companies to keep the value outside their IHT net. However, with effect from 6 April 2017, assets (such as shares) deriving their value from UKRP are now within the scope of UK IHT. This applies to both individuals and to trusts.
- Trusts holding UKRP interests directly or indirectly are therefore exposed to an IHT charge of up to 6% on each 10-year anniversary of the trust's creation, and additional charges if the UKRP interest is distributed to a beneficiary. An IHT charge may also arise on the settlor's death if they have not been expressly excluded from benefitting from the trust.
- In addition, loans made to acquire, maintain or enhance UKRP are also within the scope of IHT. For example, if a trust makes a loan to a beneficiary to purchase a property in the UK, that loan may be subject to IHT.
- These changes form part of sweeping reforms to the taxation of UK residential and commercial property. Please contact us for more information and a more detailed flyer on the changes to the taxation of UK real estate.

How Pure Tax can help

- The UK non-dom regime remains an attractive proposition for individuals coming to the UK from overseas. However, ensuring your affairs are appropriately structured is vital to ensure your non-dom status works appropriately for you and your family.

- For deemed domiciled individuals, falling within the scope of worldwide taxation in the UK can seem daunting. Pure Tax can guide you through your changing circumstances and help you get up to speed with your UK tax obligations. For those who are dual-resident, or are otherwise subject to tax in another jurisdiction, we can also help you to understand how to mitigate your exposure to double taxation and claim any appropriate credits.

- Our comprehensive 'Health Check' is a great starting point for reviewing your current position, highlighting pressure points and identifying opportunities. Please contact us to find out more.

This article is intended to provide only an overview of a limited number of areas for possible consideration, and does not constitute advice under any circumstances. No reliance may be placed on the contents of this article and Pure Tax accepts no liability whatsoever towards any person who does so.

Contact Us

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