

## Deemed UK Domicile Changes – Action Required Now!

The principal changes that are effective from 6 April 2017 are as follows:

- Anyone born in the UK with a UK domicile of origin (known as a Formerly Domiciled Resident or “**FDR**”) who is UK resident in a tax year will be deemed domiciled in the UK for all tax purposes (subject to a period of grace for IHT if the individual was not UK resident in either of the preceding two tax years).
- A long-term resident, i.e. one who has been UK resident in at least 15 of the immediately preceding 20 tax years will be deemed domiciled for all tax purposes. Provided they are not also FDRs such individuals may be able to benefit from reliefs/transitional provisions and offshore trust protections. The existing Remittance Basis charges for those who have been resident in the UK for 7 of the previous 9 tax years (£30,000) and 12 of the previous 14 tax years (£60,000) will remain in place. The £90,000 Remittance Basis Charge (which took effect from 6 April 2015 for individuals who have been resident for 17 of the previous 20 years) has become obsolete from 6 April 2017 since all the individuals who have been resident for that length of time will be deemed domiciled.
- An individual could be deemed domiciled both as a FDR and as a long-term resident. Where the conditions for both are satisfied, the less favourable provisions for FDRs will apply (which offer no transitional relief and no protection for trusts as outlined in paragraphs 1 and 2 below).

The scope of IHT has been extended in order for it to have application to:

- UK residential property owned by foreign domiciliaries (or trusts settled by foreign domiciliaries) through a foreign company or partnership on death or on gifts (and periodic/exit charges in relation to trusts).
- Relevant loans (broadly a loan where the funds are used for the acquisition, maintenance or enhancement of an interest in the UK residential property); and
- Security, collateral or guarantees in connection with a relevant loan
- The charges apply to all Non-Domiciliaries, even those who are non-UK resident.

## 1. What Reliefs are Available?

The principal reliefs available to long-term residents are as follows:

- Individuals who became deemed domiciled on 6 April 2017 and who have previously paid the remittance basis charge will not be taxed on gains arising on personally held non-UK assets which relate to the period prior to 6 April 2017. This relief is not available to FDRs. The relief is not available either for assets within trusts or for those held within companies.

**Action: Review all existing arrangements to determine whether relief is available.**

- A special mixed fund cleansing relief applies for the period from 6 April 2017 to 5 April 2019 for non-domiciliaries with cash accounts consisting of a mixture of income, capital and/or capital gains who can separate out those funds into their constituent parts at any time before 6 April 2019. Again, to be eligible the non-domiciliary cannot be a FDR and should have been a remittance basis user for any tax year before 2017-2018. A mixed fund can only be a bank account (or similar cash account). It is a fund which contains more than one category of income, capital or capital gain. Broadly speaking those who can meet the conditions and wish to take advantage of the relief will need to establish new accounts for the different categories of income, capital and gains and transfer the different types of fund across to each account prior to 6 April 2019. It should be noted that the rules are complex.

**Action: Review all banking arrangements to determine eligibility for relief and where relevant take action to meet the deadline of 6 April 2019**

## 2. What Trust Protections are available for Deemed Domiciliaries?

Offering some protection and encouraging long-term residents to remain in the UK after becoming deemed domiciled, the Government has protected deemed domiciled settlors from an immediate tax charge on income and gains of a trust established before becoming deemed domiciled.

- Provided the relevant individual is not a FDR, the deemed domiciliary has protection from certain elements of the Income Tax and CGT anti-avoidance regimes for Offshore Trusts if established before the Settlor becomes deemed domiciled.

- Broadly speaking the protections for such deemed domiciled settlors or settlor-interested trusts prevent the settlor from being subject to tax on foreign income or any trust gains unless an income distribution or a benefit/capital payment is received by the deemed domiciled Settlor or a close family member of the Settlor which can be matched against the overseas income or trust gains. A close family member is defined as (a) the Settlor's spouse, civil partner or cohabitee; or (b) a minor child of the Settlor or of someone within (a).
- Similarly, such trusts will continue to enjoy IHT protection where the assets held within the trust are foreign situs for UK IHT purposes.
- The protections will be entirely lost if the Trust is tainted, i.e. there are non-qualifying additions to the Trust after the foreign domiciliary becomes deemed domiciled.
- The revisions to the Income Tax and Capital Gains Tax anti-avoidance regimes are complex but the protection afforded is welcome and potentially more favourable for a long-term UK resident than under the old rules.

**Action: Check the status of all Settlers to determine any liability issues as above or whether reliefs are available.**

### 3. What are the New Rules with respect to IHT on UK Residential Property held through Offshore Structures?

With effect from 6 April 2017, an IHT charge is imposed on three categories of UK property as follows:

- Interests (i.e. loans or shares) in closely held companies which directly or indirectly derive their value from UK residential property. The interest in the head company will still be caught even if there is a chain of companies underneath before the residential property. Any widely held company (for example a real estate fund) will not be caught.
- An interest in a partnership the value of which is directly or indirectly attributable to UK residential property. Unlike companies, it is immaterial how many partners there are and whether or not they are connected. A real estate fund which is structured as a partnership will therefore fall within the new rules.

- The benefit of loans made to enable an individual, trustees or a partnership to acquire, maintain or improve a UK residential property or to invest in a close company or a partnership which uses the money to acquire, maintain or improve UK residential property. To avoid back to back lending arrangements, assets used as collateral for such a loan will also be subject to IHT under the new rules. An interest in a close company or a partnership which holds the benefit of the debt or the assets used as collateral are also caught.

In addition, where property to which the new rules apply has been disposed of (for example, shares in a company which holds UK residential property are sold), or a loan caught by the rules is repaid, the proceeds of sale of that disposal or repayment will remain relevant property for IHT purposes for two years from the date of disposal or repayment.

The effect of these changes on UK residential property owned in a trust/company structure will mean that the trust will be subject to the relevant property regime and IHT 10-yearly charges and exit charges at a rate of up to 6% will apply to the value of the residential property. Trustees of settlor-interested trusts which were previously excluded property for IHT purposes will also need to consider whether the gift with reservation of benefit rules apply to the value of the residential property within the trust.

**Action: Review all UK residential property structures as above to determine what UK tax liabilities arise (if any) and take the appropriate action whether in terms of restructuring or de-enveloping.**

#### 4. Summary and Next Steps - Where do we go from here?

The changes to the Rules affecting non-UK Domiciliaries mean that non-domicile status is no longer possible for individuals who have been long-term resident in the UK. Nevertheless, there is an opportunity for those who have been in the UK for a short term or who are coming to the UK to have certainty on these issues. In terms of residential property structures those affected by the new rules should consider whether to maintain the existing arrangements or whether some form of restructuring should take place. For those structures where the properties are commercially let and the Annual Tax and Enveloped Dwelling (“ATED”) Relief can be claimed there may be some merit in maintaining the structure in its current form. If not and ATED is payable, the additional IHT implications would suggest that alternative structuring arrangements should be considered, such as direct personal ownership.

If you have any concerns or queries, please contact a member of the Rooks Rider Solicitors' Wealth Planning Team.



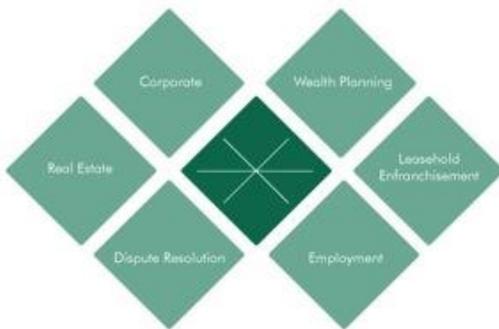
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