

Guide to the new rules for non-doms: Income Tax & CGT (Lecture P1073 – 9.23 minutes)

In 2015 the Government proposed a number of changes to the taxation regime for individuals who are UK resident but non-UK domiciled (the population commonly called “non-doms”). These measures became effective from 6 April 2017 thereby affecting non-dom clients from the 2017/18 tax year.

These notes will cover the main changes for income tax and CGT. The domicile changes for IHT will be covered in a separate article.

You should note that there have been no changes to the common law of domicile. Therefore the starting point in determining a client’s domicile status continues to be to examine whether he has either a domicile of origin, dependency or choice in the UK.

The new regime only affects those who can establish that they are non-UK domiciled under general law.

Deemed domicile

Two populations of individuals who are non-UK domiciled under general law will be deemed to be domiciled in the UK for taxation purposes from 6 April 2017. These new “deemed-doms” will either be:

- “Long-term residents”; or
- “Formerly Domiciled Residents”.

The effect of being deemed domiciled in the UK is that the individual is thereafter taxed on the same basis as someone domiciled in the UK under general law. For as long as he is UK resident, a deemed-dom will now pay UK income tax and CGT on his worldwide income and gains (with appropriate relief for any non-UK tax suffered). The remittance basis is denied.

Long-term residents

Individuals who are non-UK domiciled but who have been UK resident in at least 15 of the preceding 20 tax years will be deemed-dom.

The process to determine deemed domicile is:

- Identify the 20 year “look-back” period ending in the tax year immediately before that which you are testing. So if you are testing 2017/18, the look-back period always starts in 1997/98 and runs to 2016/17; then
- In that period, count how many of these tax years are years of residence.
- If you have any 15 or more years of residence, your client is deemed-dom. Deemed-dom is triggered at the start of the 16th year. If you don’t have 15 years, test again next year. The process is the same but the “look-back” period will shift forward one year.

When counting your tax years, a “split year” will count as a year of residence as will any years of residence while the individual was a minor.

What this means from a practical perspective is that non-doms who were UK resident before 6 April 2003 and have been UK resident ever since, became deemed-dom on 6 April 2017. Non-doms who didn't become resident until after April 2003 cannot therefore trigger deemed-dom under the 15/20 test until 6 April 2018 at the earliest.

Formerly domiciled residents (FDRs)

FDRs are individuals who are non-UK domiciled under general law but who were born in the UK with a UK domicile of origin and who are resident in the UK. Some call these people “returning UK-doms”.

FDRs will typically be British individuals who previously left the UK and acquired a foreign domicile either by choice or dependency, but who have since returned to live in the UK whilst still preserving their non-dom status under general law.

Anyone born in the UK with a UK domicile of origin will always be a FDR if he resumes residence in the UK irrespective of how many years he has lived abroad or whether he has any connections to the UK.

Deemed domiciled under both rules?

An individual could be deemed-dom both as a long-term resident and a FDR.

This could happen where an individual born in the UK to UK parents left the UK and settled permanently abroad thereby acquiring a non-UK domicile of choice. The individual later returned to live in the UK and has remained UK resident for over 15 years without his UK domicile of origin being resurrected.

In these cases the individual is deemed to be domiciled in the UK as a FDR (as this set of rules offers less by way of transitional tax reliefs!).

Consequential amendments

There are a veritable shed-load of consequential amendments to existing legislation (“knock-on rules”) to consider.

Here are the 4 most important ones:

1) The “£2,000 rule”:

Non-doms with less than £2,000 per annum of unremitted foreign income and gains have always been able to access the remittance basis without a claim (so no loss of personal allowances, no loss of CGT exemption and no exposure to the Remittance Basis Charge).

This will continue to apply even if the individual becomes deemed-dom. This decision is common sense as the tax at stake is thought to be small compared to costs of collection. It is the only time a deemed-dom will be able to access the remittance basis.

2) Effect on the Remittance Basis Charge (RBC):

The RBC continues to apply for those non-doms who claim the remittance basis and have lived in the UK for long enough to trigger the charge. However the £90,000 RBC which applied where a non-dom had been UK resident for 17 or more of the previous 20 tax years has now been rendered obsolete (having been superseded by the 15/20 rule which will treat the taxpayer as deemed-dom and thereby unable to use the remittance basis).

The £30,000 and £60,000 RBCs remain in place.

3) Capital gains tax rebasing:

Non-doms using the remittance basis only pay CGT on foreign capital gains if those gains are remitted to the UK. This benefit is now denied for deemed-doms.

However the Government accepted that it could be unfair to tax deemed-doms on capital gains that accrued before the new regime was implemented. Cue some relief in the form of 5 April 2017 rebasing.

Rebasing allows capital gains on foreign-situs assets held at 5 April 2017 to be calculated using the value of the asset at 5 April 2017 (rather than by reference to historic cost). Rebasing will accordingly have the effect of extinguishing capital gains on non-UK assets which accrued up to 5 April 2017. Valuation exercises may therefore need to be carried out.

However there is a (very large) sting in this seemingly generous tail.

Rebasing is only available to “qualifying individuals”. Qualifying individuals are those who:

- Became deemed-dom under the 15/20 rule on 6 April 2017; and
- Paid the RBC in any tax year (one year is enough) before 2017/18.

Rebasing is not therefore available to those individuals:

- Who will become deemed-dom under the 15/20 rule after 6 April 2017; or
- Who were born in the UK with a UK domicile of origin (ie, FDRs); or
- Who had previously avoided the RBC by not claiming to use the remittance basis.

Care must therefore be taken here as **NOT ALL DEEMED-DOMS WILL BE ELIGIBLE FOR REBASING!**

Rebasing applies on an asset-by-asset basis. Rebasing is automatic where applicable although taxpayers can elect to disapply the relief where it is not beneficial.

4) Mixed-fund “cleansing” relief

Practitioners with non-dom clients using the remittance basis will know what a nuisance the mixed fund ordering rules are. Try as we might to persuade our non-dom clients to keep their foreign income, foreign gains and clean capital in separate offshore accounts so that the source of their remittances can be evidenced, for a multitude of reasons this often doesn't happen.

The consequence is that we often end up with money being held in one big offshore pot leaving the client exposed to the statutory mixed fund rules. Without delving into the complexities, these rules say that income is remitted before gains, and gains are remitted before capital. Basically if remittance basis users want to bring their money in to the UK, the government will do what they can to tax it at the highest possible rate.

But attitudes have softened over in Whitehall as the penny has dropped that we, as a struggling nation in need of any economic help we can get, might actually want to incentivise non-doms to bring their money to the UK for the general wellbeing of UK plc. So a 2-year window has opened during which non-doms can segregate their existing mixed funds (typically by hiving-off clean capital) into new foreign bank accounts such that it can later be remitted to the UK free of tax. The window closes on 5 April 2019.

“Mixed fund cleansing” is available to any non-dom to whom the remittance basis applied in any tax year before 2017/18 (other than FDRs who seem to be persona non grata).

This is a no-brainer. If you have a non-dom client who uses (or has ever used) the remittance basis and they have a bank account containing mixed sources, you should get them to clean it. All they need to do is a) identify how much of that bank account represents clean capital (most of the time this will be money in the account before they became UK resident or it could be money from gifts, inheritances or loans) and then b) get their bank to move this amount into a new account. Do this now as April 2019 will be here before you know it.

There is no restriction in the number of accounts which can be cleansed. There is also no minimum holding period for a new “cleansed” account. For example if a client wishes to access tax-free money from a mixed fund, the clean capital element can be hived-off into a new account on day one, those newly liberated funds can be remitted to the UK on day two and the now empty account can be closed on day three. Just make sure you give clear and unambiguous instructions to the bank as not all the staff in the local branch of Foreign Bank plc will be fully au-fait with the provisions of Schedule 8 Part 4 of FA (No 2) 2017...

Contributed by Steve Sanders