

Guide to the new rules for non-doms: IHT (Lecture P1074 – 6.19 minutes)

Exposure to IHT is largely dependent on domicile. UK-doms are liable to IHT on their worldwide assets. Non-doms are only subject to IHT on assets situated in the UK. Foreign assets of non-doms are “excluded property” and are outside the scope of IHT.

Deemed domicile

The deemed-dom rules also apply for IHT. Individuals becoming deemed-dom will no longer have excluded property protection and their foreign assets will be exposed to IHT from the date deemed-dom is triggered.

Deemed-dom status has existed for IHT for decades. Individuals have historically been deemed-dom for IHT and thereafter fully within the UK IHT net once they had been UK resident for 17 or more of the 20 years ending with the transfer. This meant that individuals became deemed-dom for IHT from the start of their 17th consecutive year of residence. This has now been superseded by the 15/20 rule so individuals now become deemed-dom for IHT from the start of their 16th consecutive year of residence (thereby accelerating domicile status by 12 months).

Deemed-dom for IHT is lost once the taxpayer has 4 consecutive tax years of non-residence. This 4-year break is exclusive to IHT only. Strictly speaking 6 tax years of non-residence are required for deemed-dom to be lost for income tax and CGT although this point is largely of theoretical interest only as domicile status has no bearing on the income tax and CGT tax liability of non-residents.

FDRs are also deemed-dom for IHT although they have a one year “grace period”. This means that FDRs will be deemed-dom for income tax and CGT from the tax year in which they trigger UK residence but for IHT purposes deemed-dom is not triggered until the following 6 April.

Therefore a FDR who comes back to the UK for a very short period will be treated as UK dom for income tax and CGT but non-dom for IHT. I suspect that there won't be too many in this position.

[PS: It is a little irritating that this seems to have been sold to us as a one-year grace period. It isn't. The grace period could be a matter of weeks depending on when the taxpayer arrives in the UK. For example, if a FDR becomes UK resident in March 2018, he is deemed-dom for IHT from 6 April 2018. By my counting, that is not one year...]

Excluded property trusts

One bit of welcome news is that it is “business as usual” for excluded property trusts.

Before April 2017, individuals who were likely to trigger deemed-dom for IHT under the 17/20 rule could transfer their foreign assets to a trust (typically an offshore one although this wasn't essential). No IHT would be due on the transfer being one of excluded property. Any CGT could be avoided by making a remittance basis claim (the gains could never then be remitted as no proceeds existed).

The trust would be non-UK dom by virtue of being established by a non-dom settlor. The trust assets would accordingly be outside the scope of IHT being foreign assets owned by a non-dom trust. The non-dom status of the trust would not change even if the settlor became UK dom, thereby offering ongoing IHT protection for foreign assets within the trust.

This planning continues to be available under the new regime (albeit that the arrangements now need to be put in place 12 months earlier). A deemed-dom can therefore continue to have access to his foreign assets via the trust whilst keeping those assets outside the scope of UK IHT. [There is no question of any reservation of benefit issues here as the original transfer was of excluded property.]

Perhaps not surprisingly the same courtesy has not been extended to poor old FDRs. Any foreign assets settled into trust by a FDR while they were domiciled outside the UK will cease to be treated as excluded property for any tax year in which the FDR is resident in the UK. So if the FDR dies while UK resident, the trust assets will fall into his estate.

UK residential property

From April 2017 UK residential property owned by a non-dom through a non-UK envelope - such as an overseas company or offshore trust - is no longer regarded as excluded property. Therefore if a non-dom individual dies owning shares in a non-UK company which in turn holds UK residential property, the value of the shares which is represented by that UK residential property will be chargeable to IHT. The residence status of the taxpayer is irrelevant.

This measure is intended to block historical planning by non-doms who protected their UK property interests from IHT by holding them via an overseas envelope. [The ATED, ATED-related gains and higher SDLT rates were intended to dissuade non-doms from using offshore structures to acquire UK residential property but many non-doms seem to have accepted these charges in order to secure IHT protection. This will no longer be the case.]

UK residential property held through an overseas company will be chargeable to IHT if:

- The company would be a “close” company were it UK resident (being one controlled by 5 or fewer shareholders or by its directors); and
- The individual has at least a 5% interest in the company.

Shareholders in large non-UK multi-national companies with UK property investments will therefore not be affected.

The rules apply to all UK residential dwellings regardless of whether the property is occupied, empty or let. There are exceptions for dwellings used as residential accommodation for schools, colleges, universities or the armed forces, or as children’s homes, hotels, hospitals, hospices or prisons. Unlike the ATED, the IHT rules apply irrespective of the value of the property.

The residential property will include any land which is occupied or enjoyed with the dwelling (such as a garden or grounds). There is no relief if the property is the only or main residence of the individual.

The rules do not currently apply to commercial property. Where a property has mixed residential / commercial use - for example, a shop with a flat above it - only the value of the residential part will be subject to IHT.

To ensure compliance by non-UK Executors, HMRC has powers to prevent the sale of the UK property by imposing a legal charge on the property until any outstanding IHT liability has been paid.

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