2015

TAX MEMORANDUM

PART I

OPTIMUM STRUCTURES FOR NON-UK DOMICILIARIES TO PURCHASE AND HOLD UK RESIDENTIAL ACCOMODATION (TAKING INTO ACCOUNT THE PROPOSALS IN THE SUMMER BUDGET OF 8 JULY 2015)

AND

PART II

THE PROPOSED NEW NON-DOM RULES

SET OUT IN THE OPEN CONSULTATION DOCUMENT OF 30

SEPTEMBER 2015

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Grays's Inn

22 October 2015

PART I

OPTIMUM STRUCTURES FOR NON-UK DOMICILIARIES TO PURCHASE AND HOLD UK RESIDENTIAL ACCOMODATION

INTRODUCTION

The UK tax regime applicable to residential accommodation has gone through some major changes over the last few years and further changes are in the pipeline.

The law in this area does not seem to be able to stop still for a minute.

The Finance Act 2013 contains provisions imposing an annual tax on the holding of "enveloped dwellings" (dwellings owned by a company or certain other vehicles) and a new 28% charge to capital gains tax on "ATED-related gains." When companies purchase properties which is subject to the ATED a 15% charge to SDLT may be payable.

Those new provisions were originally only concerned with single dwelling houses worth more than £2m (referred to as high value residential property (HVRP)) although changes, made by the Finance Act 2014, lowered that threshold with effect from 20 March 2014 (for SDLT) to £500.000 and for the ATED and ATED-related gains from 1 April 2015 to £1m and from the 1 April 2016 to £500,000.

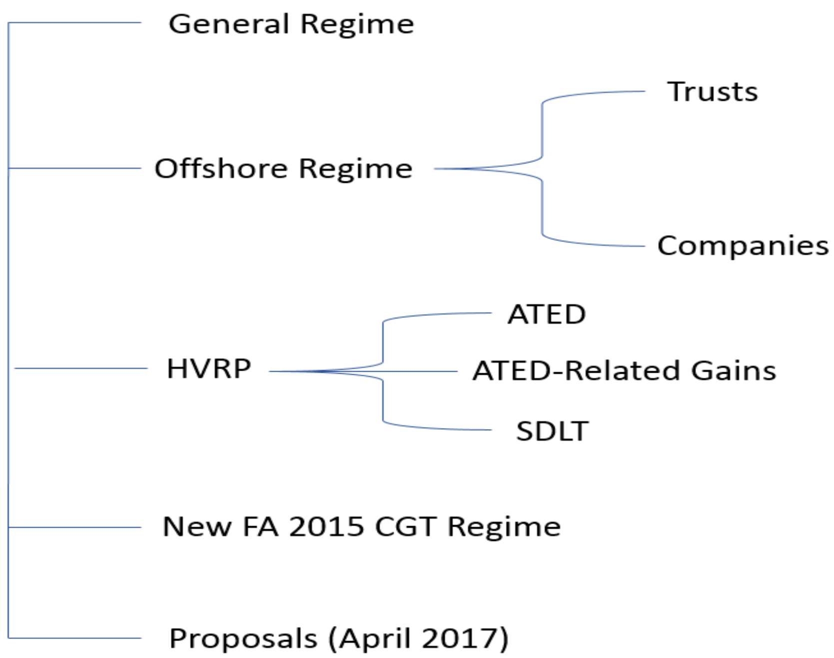
There is also a new regime in the Finance Act 2013 for disallowing loans (as deductions for inheritance tax (IHT) purposes) aimed at people who try to avoid the new provisions by taking properties out of companies. One may be going out of the frying pan (the ATED) into the fire (IHT).

The above provisions are imposed on top of the general CGT regime applicable to non-resident persons (TCGA 1992 s2 and the s10) and the general anti-avoidance CGT rules which apply to overseas trusts (TCGA 1992 ss 86 and 87) and overseas companies (TCGA 1992 s 13) and the codes are intended to meld together in perfect harmony.

When one had grasped how these regimes work together the Autumn Statement 2013 of 19/12/13 provided there would be a general CGT charge "on future gains made by non-residents disposing of UK residential property from April 2015."

The new charging provisions found their way into the Finance Act 2015 s37 and Sch 7.

Just when things seemed to quieten down a little the Chancellor in the Summer Budget of 8 July 2015 set out proposals to fundamentally change the UK domicile rules (making individuals deemed domiciled in the UK for income tax and capital gains tax and IHT from April 2017 if they have been resident in the UK for 15 out of the past 20 years) and apply a "look-through" where foreign companies hold UK residential property for IHT purposes. A consultation paper on the former was published on 30 September 2015 entitled "Reforms to the taxation of non-domiciles."



THE GENERAL CGT REGIME APPLICABLE TO NON-RESIDENTS

Residence Condition

The general rule is a person must be resident in the UK for the year the gain is made if CGT is to be payable (TCGA 1992 s2).

Exceptions

Spit Year

There is an exemption for the non-resident part of a split year (TCGA 1992 s2 (1B). Thus if the taxpayer comes to live in the UK for the first time in the middle of a tax year gains made prior to his arrival will be CGT free. Note Concession D2 is no longer relevant.

Temporary Non-residence

There is an anti-avoidance rule which covers individuals who become temporarily non-resident and make gains and then return to the UK (TCGA 1992 s10A and FA 2013 Schedule 45 Part 4).

Section 10 Trap and s 25(3)

Also a non-resident can be liable for CGT if the non-resident carries on a trade e.g. runs a hotel or car park (not just a business e.g. a letting of land to a hotelier or car park operator) in the UK through a branch or agency and disposes of an asset used in the UK for the purposes of the same (TCGA 1992 s10). It is not possible to avoid this charge by ceasing the trade and then selling the asset whilst non-resident-see TCGA 1992 s25 (3).

NON-RESIDENT TRUSTS AND CGT

The key offshore settlement section is normally TCGA 1992 s87 which taxes gains (called "s2(2) amounts") made by non-resident trustees on UK resident beneficiaries on a receipts (capital payments) basis (s87 (3) and 87A). The remittance basis may also be available; see s87B.

The s2(2) amount would not include a gain taxable on the trustees under TCGA 1992 s10 (UK branch or agency) as it would be subject to tax under general principles (see s87(4)(a)).

Note these rules may be recast from April 2017 following the changes referred to in Part II of this Tax Memorandum.

UK RESIDENT INDIVIDUALS AND NON-RESIDENT TRUSTS OWNING SHARES IN NON-RESIDENT COMPANIES

TCGA 1992 s13 apportions gains made by non-resident "close" companies to a UK resident shareholder (participator) provided he/she and connected persons would have over 25% of the gains apportioned to their holdings (s13(4)).

Note it is provided in s13 (1A) that s13 does not apply if the gain is an ATED-related gain.

If a non-resident trust owns the shares any apportioned gain is added to the s2 (2) amount of a TCGA 1992 s87 settlement-see s13 (10).

A big inroad into the effectiveness of this provision was made by FA 2013 with respect to disposals after 5/4/12. Section 13(5) provides the section shall not apply to:

> "(c b) a chargeable gain accruing to the company on a disposal of an asset where it is shown that neither—
>
> (i) the disposal of the asset by the company, nor
>
> (ii) the acquisition or holding of the asset by the company,
>
> formed part of a scheme or arrangements of which the main purpose, or one of the main purposes, was avoidance of liability to **capital gains tax** or corporation tax,"

HIGH VALUE RESIDENTIAL PROPERTIES AND THE THREE SPECIAL LEVIES WHICH APPLY TO THEM

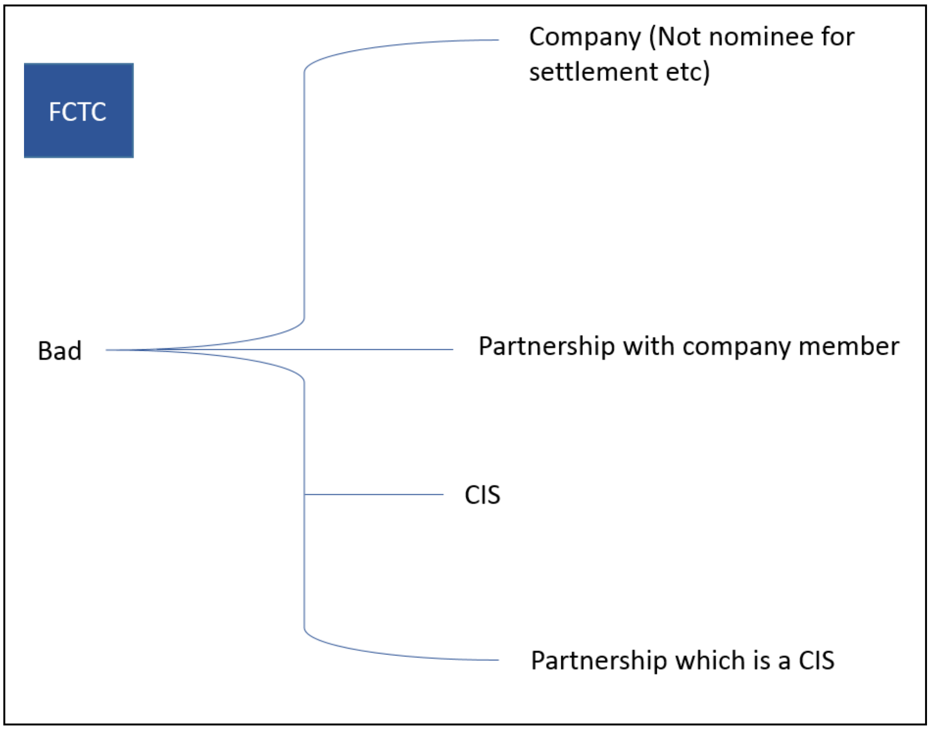
FIRST SPECIAL LEVY: THE ANNUAL TAX ON ENVELOPED DWELLINGS (THE ATED)

Scope

This new charge, which came into force on 1st April 2013, is imposed on "Chargeable Persons". See s 96(1).

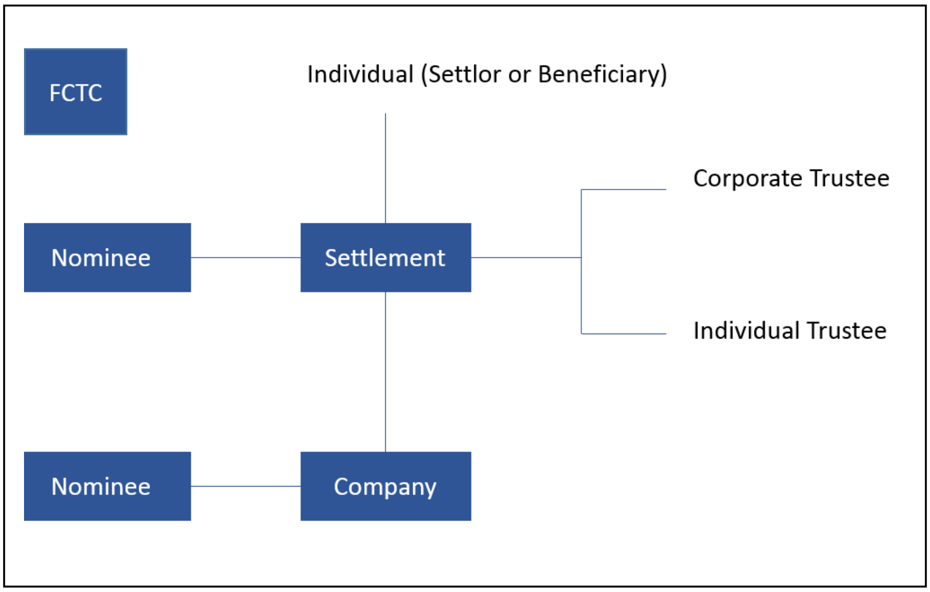
Chargeable Persons comprise:

1. companies,
2. collective investment schemes (even though all the participants may be individuals)
3. partnerships which have a company as a partner.



Settlements, whether onshore or offshore and whether or not they have corporate or personal trustees, will not be liable for the ATED and nor will companies acting as nominees for the same and nor will a partnership of individuals or an individual and the settlement (s95) (unless it amounts to a collective investment scheme: see below).

Stiftungs and foundations which the writer has had cause to look at in the context of this legislation have amounted to settlements and not companies for all relevant purposes.



If a company is put into liquidation it ceases to beneficially own the property (from the commencement of the liquidation) so the ATED is not chargeable thenceforth (Ayerst v C & K [1975] 2 ALL E R 537 at 559).

"Partnership" means UK partnerships created under PA 1890, LPA 1907 or the LLPA 2007 or the LLPA (Northern Ireland) 2002 and "firms and entities of a similar character to any of [those 4 types of partnerships] formed under the law of a country or territory outside the United Kingdom." See s 167(1) (d).

Note that if the partnership also falls within the definition of a collective investment scheme (CIS), the CIS provisions take priority (s 167(4)).

Thus if an overseas partnership comprising only individual members amounts to a CIS the ATED charges are exigible (this may have importance, for example, if there is a commercial letting by the partnership to a non-qualifying individual).

If the overseas partnership law creates a separate body-as in the case of a UK LLP- there is still a complete see-through (see s167 (2)).

Example

> It is arguable that one can create a Mauritius partnership which results in the creation of a separate legal person. The partners are a family settlement and an individual. The Partnership owns an interest in a single dwelling in the UK

worth over £2 (or otherwise within the HVRP threshold for the time being). The structure does not fall within the ambit of the ATED even though on the proper construction of Mauritius law the property is owned by a separate legal person and is not held for the partners. These structures may have IHT advantages where a business – property letting – is being carried on but the occupier is a "non-qualifying individual." For there to be a partnership properly so-called a business must be carried on (see SDLT33110). Note HMRC warned in para. 4.8 of their paper *Ensuring the Fair Taxation of Residential Property* December 2012 that they will monitor this area "in case of any manipulation." Also see the April 2017 see-through proposals which if implemented will take away the IHT attractions of the Mauritius LP.

"Non-qualifying individual" is widely defined in s136 and will include an individual connected with the company which owns the property and the settlor of a settlement if the shares are owned by a settlement and persons connected with the settlor.

Reliefs

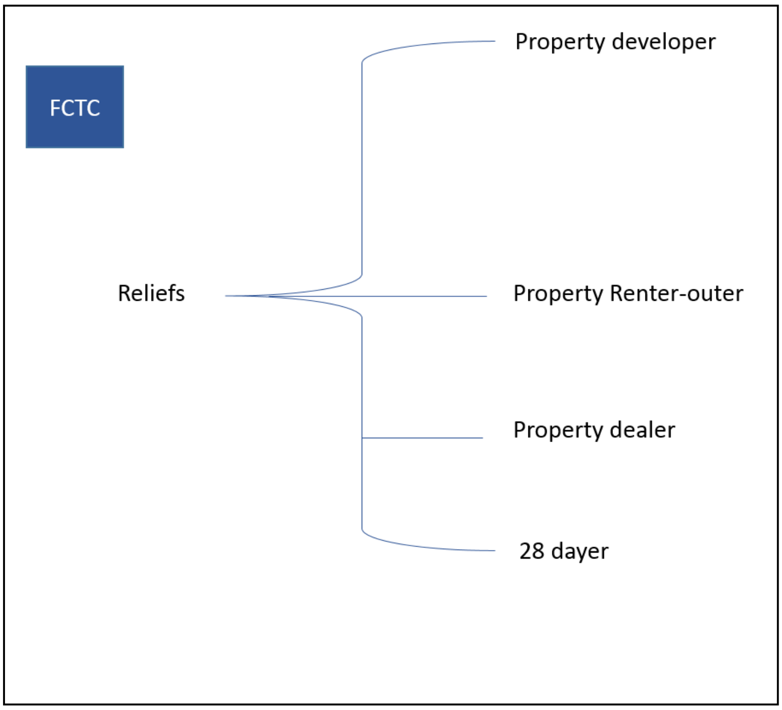
If one is within the ambit of the ATED there are a number of reliefs and exemptions available and these include (the list is not exhaustive):-

1. *a property development business*: dwellings held for the purpose of the property development trade of the company and not permitted to be occupied by a non-qualifying individual (ss 138-140);

2. *a property rental business*: dwellings held for the purpose of letting on a commercial basis and not permitted to be occupied by a non-qualifying individual (ss 133-136); note this relief applies to overseas landlords who pay income tax on their rent as well as UK companies which pay corporation tax on the rent;

3. *a property trading business*: dwellings held for the purpose of a trade of buying and selling property and not permitted to be occupied by a non-qualifying individual (s 141);

4. *properties which are run as a business*: properties open to the public with access to a significant part of the interior for at least 28 days per year; the business must be run on a commercial basis and with a view to profit (s 137); the taxpayer may have a house with special features and open it to the public for at least 28 days as a business and so avoid the ATED.



The Original Rates of ATED

The rates of the ATED for **2013/14** were as follows:-

Taxable Value of Property	Annual Chargeable Amount
£2m - £5m	£15,000
£5m - £10m	£35,000
£10m - £20m	£70,000
Greater than £20m	£140,000

Points on the ATED

Some consider the rates to be modest and taxpayers who own properties in other jurisdictions may be use to such charges.

The chargeable period for the imposition of the ATED is from 1st April to 30th March of each year (rather than following the tax year).

Where the ATED is applicable to part only of the chargeable period, the chargeable amount will be apportioned accordingly. Thus if the property is owned by a company from 1/3/13 to 30/9/13 when the property is transferred to Mr X the ATED charge on a £15m house (the 3rd band) is £35,000.

This is important because some taxpayers may have wanted to liquidate companies to mitigate the ATED and they may have postponed the liquidations until after 5.4.13 when they could break their UK residence status under the new statutory residence rules (Finance Act 2013 s218) with a high degree of certainty. They will have had to have paid a small amount of the ATED only: if, for example, the property is transferred out on the liquidation on 30/4/13 one twelfth of the annual ATED is payable.

The ATED is index linked (annually to the CPI) (s101).

Residential properties will need to be valued every five years and the first ATED valuation date will have been 1st April 2012 to see which level of charge applies (s102).

Later rates of ATED

For **2014/15** the rates are respectively:

£15,400 (property values £2m-£5m),

£35,900 (£5m-£10m),

£71,850 (£10-20m) and

£143,750 (over £20m).

In the Autumn Statement of 3/12/14 it was announced for **2015/16** there would be a special increase in the ATED rates by 50% above inflation so the rates are thus:

£23,350 (property values £2m-£5m),

£54,450 (£5-£10m),

£109,050 (£10-£20m) and

£218,200 (over £20m).

<u>Example of the ATED</u>

> A settlement based in Jersey owns Jersey Ltd which owns beneficially a property worth between £2m-£5m. The company will be liable for the ATED of £15,000 per annum for 2013/14. If the property were owned by the settlement direct the ATED will not apply; this however will have IHT disadvantages if the settlement would otherwise be an excluded property settlement within IHTA 1984 s48 (non-UK domiciled settlor with settlement holding non-UK located assets).Note however the proposed changes (dealt with below) from April 2017 where the corporate veil is to be lifted for IHT purposes where a foreign company owns UK residential property.

<u>SECOND SPECIAL LEVY: THE NEW CAPITAL GAINS TAX CHARGE ON ATED-RELATED GAINS IN TCGA 1992 SS2B-2F AND SCHEDULE 4ZZA</u>

<u>Scope and Reliefs</u>

A new 28% CGT charge applies to disposals made by persons after 5 April 2013 if the following conditions are satisfied:-

1. there is a relevant high value disposal

2. an ATED-related gain accrues on that disposal and

3. the gain accrues to a person who is not an excluded person.

Condition 1: Relevant high value disposal (TCGA 1992 s2C)

To amount to a relevant high value disposal four conditions must be satisfied.

There must be a disposal of a chargeable interest (broadly an interest in land e.g. a freehold or a leasehold) (Condition A).

That chargeable interest must be an interest (e.g. leasehold or freehold) in a single-dwelling (e.g. a house or flat); the legislation refers to this as “a single-dwelling interest” (TCGA 1992 s2C (6) and FA 2013 s108) (Condition B).

The vendor must have been within the charge to the ATED on one or more days whilst it owned the single-dwelling interest (Condition C).

Finally the sale consideration must exceed the threshold amount (Condition D).

The general threshold amount was originally £2m. This was reduced to £1m for disposals in the tax year 2015/16. It will be reduced to £500,000 for disposals on or after 6 April 2016. If the sale consideration falls below the ATED threshold for the time being there will be no ATED-related gain.

There are provisions however in TCGA 1992 s2D which ensure that if the vendor only disposes of part of its interest in the dwelling the threshold amount is proportionately reduced.

Condition 2: ATED-related gain (TCGA 1992 Schedule 4ZZA)

The ATED-related gain is the gain on the dwelling which has accrued since 5 April 2013: there is deemed to be a market value acquisition on that date. Indexation is not available. That gain is then reduced for the days the dwelling was not within ATED (e.g. the dwelling would not be within ATED if it was let to strangers, or was below the ATED threshold or was not a dwelling) between 6 April 2013 and the date of disposal.

Example

> The dwelling owned by Jersey Limited had a market value of £5m on 5 April 2013. It is sold in 2016 for £6m and during the period from 5 April 2013 to the disposal date in 2016 it had been within the ATED for ¾ of the days in that period. £.75m of gain is chargeable to the new CGT charge at 28%. Had it been within the ATED throughout that period (e.g. a non-qualifying individual was permitted to occupy the dwelling throughout that period) the full £1m would be within the new charge.

Note the non-ATED-related gain is any gain which accrued pre 6 April 2013 and any post 5 April 2013 gain which is not ATED related (see the new Schedule 4ZZA para 4(1) of TCGA 1992 inserted by Finance Act 2013 Schedule 26 paragraph 16). This non-ATED-related gain may amount to a trust gain within TCGA 1992 s87 for example. If the gains are not caught by that section or TCGA 1992 s86 or s10 they are wholly free of CGT. Note non-ATED-related gains do not benefit from a new 5April 2013 market value base cost and they can be subject to an apportionment to company participators under TCGA 1992 s13. If the non-ATED related gain accrues to a company within the scope of corporation tax it is subject to corporation tax in the same way as other chargeable gains.

Note a taxpayer may elect not to apply the 2013 rebasing which would be an unusual thing to do.

There are special rules for losses (these are ring-fenced for use only against ATED-related gains: see 2E) and there is a special tapering relief in s2F.

Condition 3: Excluded Persons (TCGA1992 s2B (2))

An individual or trustee of a settlement or a personal representative may be a member of a partnership or a collective investment scheme and thus not excluded from the ATED. TCGA 1992 s2B (2) excludes them from the new CGT charge.

<u>Share Sales</u>

The charge will not apply to indirect disposals such as sales of shares in companies which own high value residential property.

<u>Example</u>

X settlement sells Jersey Limited which owns a dwelling worth £10m which the settlor lives in. No ATED-related gain can arise on the share sale; however the ATED charge must be paid each year by the company and there may be an ATED-related gain realised if the company sells the property in the future.

Tie-in with the ATED

This new CGT charge is intimately tied-in with the ATED (s2C(4)) so only where property which has been or is within the ATED is disposed of at a gain can the new charge be imposed. Thus if the seller of the property – a company or a partnership with a company member or a collective investment scheme – qualifies throughout for any of the above mentioned reliefs- property development business, property letting business etc. – it will not be subject to the ATED-related capital gains tax charge.

Consistency

The above ensures consistency between the two charges and also the stamp duty land tax provisions charging 15% are applicable to purchases of properties within the ATED.

The 3 levies are thus intimately related.

More consistency

For more consistency the government decided the new CGT charge will apply to companies etc. which are resident in the UK (there had been the hope the charge would be restricted to non-resident companies etc. but that is not to be) in respect of gains built up on or after the 6th April 2013. Corporation tax will apply to the part of any gain built up before 6/4/13 and to any non-ATED gain which accrues thereafter (with the benefit of indexation).

THIRD SPECIAL LEVY: STAMP DUTY LAND TAX (15%)

It should be noted that the original 15% SDLT charge (found in FA 2003 sch4A) was amended by the Finance Act 2013 Schedule 40 to include a series of reliefs to mirror those in the ATED legislation e.g. relief for property dealers and lettings to strangers.

Thus if a company purchases residential property and any of the above relief are applicable (property development business, property letting business etc.), as well as the ATED not being applicable the 15% SDLT charge will also not be applicable.

If one falls outside the 15% rate the normal stamp duty rates applicable to the purchase of residential property apply (these rates have effect from 4/12/14 (unless contracts were exchanged prior to 4/12/14):

> the portion of sale consideration up to £125,000 is charged at 0%,
>
> the portion between £125,001 and £250,000 at 2%,
>
> the portion between £250,001and £925,000 at 5%,
>
> the portion between £925,001 and £1,500,000 at 10% and
>
> the portion over £1,500,000 is charged at the rate of 12%.

Thus if a property is purchased for £185,000 the duty is £1,200 i.e. 0% on £125,000 and 2% on £60,000.

At the higher value end, the 12% rate is not far off the 15% rate applicable to companies which buy properties which are subject to the ATED.

The payment of the normal residential rates (0%-12%) on the purchase by a company will be conditional on the appropriate relief (e.g. a property letting business being carried on) applying for 3 years (which may be considered a short period) following the purchase of the property and the property not being occupied by a non-qualifying person in that time. See Schedule 40 paragraph 4 of Finance Act 2013 and the new paragraphs 5G-5K inserted into Finance Act 2003 Schedule 4.

Note the 15% rate applies to purchases after 20 March 2014 (subject to transitional provisions) where the consideration is over £0.5m (instead of the original figure of £2m). This greatly expands the application of the 15% rate.

DON'T OVERLOOK THESE THREE SPECIAL LEVIES

These charges have been likened to the three headed hound from Hell – Cerberus.

> Example
>
> A company buys high value residential property for use by a non-qualifying individual. It pays 15% SDLT and an annual charge of up to £140,000 (2013/14) or £143,750 (2014/15) or £218,200 (2015/16) and if it cannot bear that any longer and sells the property, it will pay CGT of 28% on any gain.

NEW DISSALOWABLE DEBT PROVISIONS AIMED AT PEOPLE TRYING TO AVOID THE ATED CHARGE

The Finance Act 2013 contains provisions which:-

> (1) disallow certain debts as deductions from the estate of deceased persons for inheritance tax purposes and
>
> (2) require certain debts to be allowed as deductions only if they are repaid on death.

These provisions are in Finance Act 2013 Schedule 36 and that Schedule inserts new provisions (ss. 162A, 162B, 162C and s.175A) into IHTA 1984.

General rule on debts

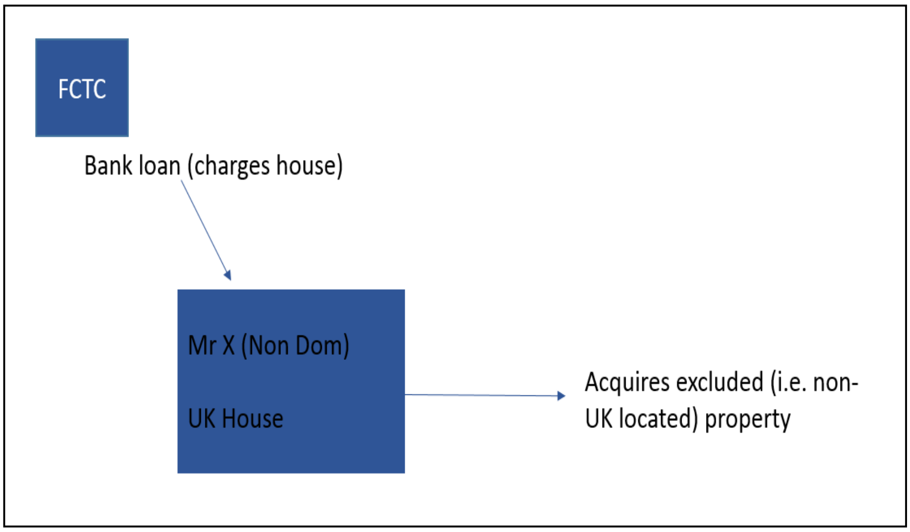
The general rule is all debts are deductible for IHT purposes if incurred for full consideration (IHAT 1984 s5(5)).

> Example
>
> D agrees to owe L £1m. That is not deductible as the debt is not incurred for full consideration. L advances £1m to D by way of loan. That debt is incurred for full consideration.

Non-Domiciliaries borrowing to buy excluded property: disallowed debts

There are provisions in the new section 162A IHTA 1984 which provide that if a taxpayer who is not domiciled in the United Kingdom charges a UK house in order to acquire excluded property the debt is only deductible from the excluded property and not from the UK house.

The debt effectively therefore goes unrelieved.



There are exceptions to this rule (IHTA 1984 s.162A (2)-(4)) but the rule does mean that in general it is not possible for non-UK domiciled persons to charge a UK house and buy excluded property and mitigate the inheritance charge on the house.

Example (Disallowed Debts)

> Mr. X is not domiciled in the UK. He owns a UK house. On his death IHT at up to 40% is payable on the house as it is located in the UK. He borrows an amount equal to the house and charges the house and invests the borrowed monies in non-UK located assets. On the face of it no IHT is payable as the debt reduces to nil the value of the UK located house and non-UK assets do not bear IHT. The new s162A however prevents the debt against the house from being deductible for IHT purposes.

Note that if a non-domiciliary borrows monies to purchase the property in the United Kingdom in the first place and charges the property then there will be no difficulty in the debt being allowable. The problem only arises if the individual already owns a property and takes a charge against it with a view to buying excluded property (including putting his money in an overseas bank account which will be the purchase of excluded property for these purposes).

Note it may also be possible for the non-dom to borrow to buy shares in an overseas company which owns the UK property and then liquidate the company with the loan attaching to the UK property without the legislation being offended. See IHTM28015 example 2 which reads thus:

Example 2

> Axel, who is not domiciled in the UK, owns shares in an overseas company, which owns a UK property. Axel acquired the company by borrowing £1m. The company is liquidated and the UK property is transferred to Axel.

IHTA84/S162A(2) refers to the disposal of excluded property for consideration in money or money's worth. You may accept that liquidating the company and transferring the property to Axel meets that requirement so the liability may be allowed as a deduction against the UK property, although the allowable liability cannot exceed the value of the UK property that was transferred to the Axel.

<u>The general limited consequences of the new provisions</u>

If one borrows to buy UK land full relief for the borrowing is available.

If you borrow against UK land which you already own and deposit the proceeds overseas in a bank or use it to buy foreign property no IHT relief is available for that borrowing (IHTA 1984 s162B and s162A).

The key provisions in IHTA 1984 read thus.

162A Liabilities attributable to financing excluded property

(1) To the extent that a liability is attributable to financing (directly or indirectly)—

(a) the acquisition of any excluded property, or

(b) the maintenance, or an enhancement, of the value of any such property,

it may only be taken into account so far as permitted by subsections (2) to (4).

162AA Liabilities attributable to financing non-residents' foreign currency accounts]

(1) This section applies if—

(a) in determining the value of a person's estate immediately before death, a balance on any qualifying foreign currency account ("the relevant balance") is to be left out of account under section 157 (non-residents' bank accounts), and

(b) the person has a liability which is attributable, in whole or in part, to financing (directly or indirectly) the relevant balance.

These provisions are narrowly drafted.

"Excluded property" means property situated outside the UK – IHTA 1984 ss 272 and s6

<u>Example</u>

B borrows further monies under legal charge (charged on the UK property) to enhance the UK house. This additional borrowing is fully deductible for IHT purposes because it does not relate to property outside the UK.

<u>Example</u>

B adds to the loan in order to raise monies to pay school fees at a UK school under a contract governed by UK law. This additional borrowing is fully deductible for IHT purposes.

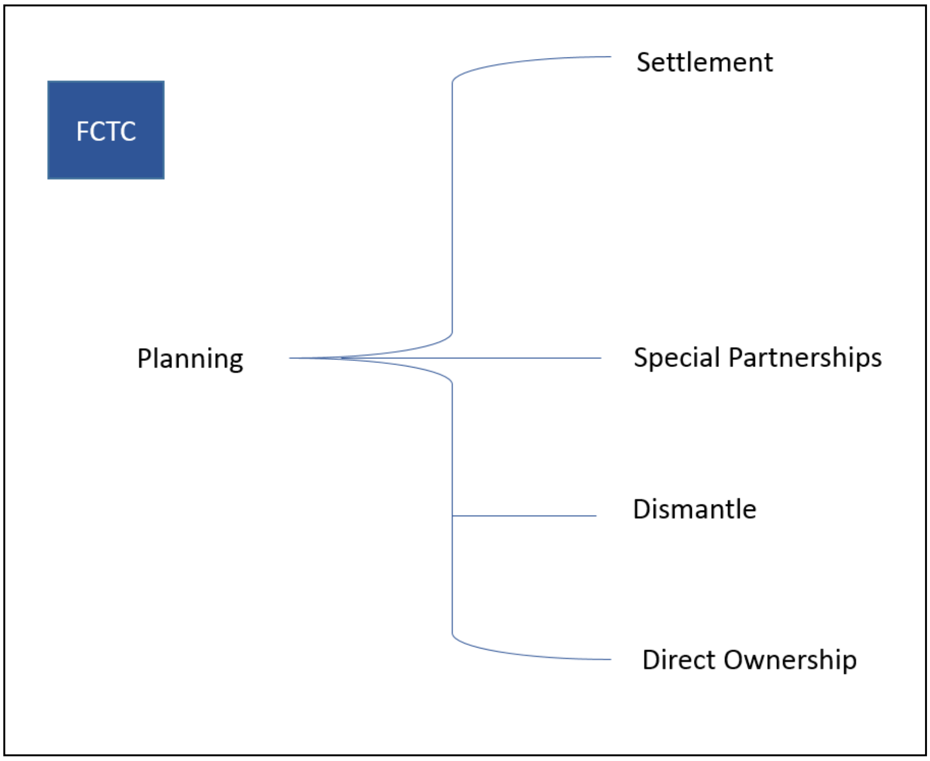
New rule requiring loans to be repaid on death

As well as the above provisions there is a new provision in IHTA 104 s.175A which states that a liability can only be taken into account on the death of an individual to the extent that it is discharged on or after the death out of the estate or out of excluded property owned by the deceased immediately before the death.

This is a major provision which will affect all estates and not just estates of non-UK domiciliaries.

If the liability is not discharged there is a relieving provision which states that it could be taken into account if there is "a real commercial reason" for the liability not being discharged and the securing of a tax advantage is not the main purpose or one of the main purposes of leaving the liability undischarged. This is unlikely to help if the loan was from a connected party. See HMRC Manual IHTM28027. Note however if the personal representatives of the deceased non-domiciliary borrow from a family member to discharge the debt no problems should arise. See HMRC Manual IHTM28028.

OPTIMUM STRUCTURES AND THE 3 LEVIES



Overseas Settlements are Safe

With the alignment of the three levies, this will mean none of the 3 charges (the ATED, the new CGT charge and the 15% SDLT charge) will apply to an overseas settlement which buys, owns or sells high value residential property even if the trustees are corporate trustees. This is welcome news. However, the inheritance tax position will have to be considered by taxpayers as it is difficult to create deductible charges against the property.

Dismantling present Structures to avoid the ATED

If taxpayers need to liquidate offshore companies owned by settlements to avoid the ATED, they may need to wash gains under the matching rules in TCGA 1992 s87A by making offshore distributions from the settlements so the gains cannot be carried back to earlier years where UK resident beneficiaries have lived in the accommodation and so received "capital payments" (TCGA 1992 s87 (2)).

In the normal case SDLT is not payable on the liquidation of a company but SDLT may be in point if there are loans outstanding at the time of liquidation. See the HMRC statement of 20 December 2003 "SDLT on de-enveloping transactions."

Some taxpayers are leaving there structures in tact to preserve the IHT advantages of the same but this is to be changed from April 2017 (see below).

Direct ownership: the simple route

If an individual owns the dwelling direct none of these three provisions will have relevance but IHT is a major consideration. The spouse exemption may give a temporary respite. Note that if the taxpayer buys the UK property at inception in his own name and borrows to do the same even from a connected party SDLT will be payable but the loan will be deductible on his death under general principles (IHTA 1984 s162A will not apply): the loan still has to be paid-off on death in the usual case (IHTA 1984 s175A) but a connected party loan taken out for the purpose should be acceptable to HMRC.

THE NEW CHARGE IMPOSED GENERALLY ON NON-RESIDENTS WHO DISPOSE OF UK RESIDENTIAL PROPERTY ON AND AFTER 6 APRIL 2015

Introduction

The legislation is found in FA 2015 s37 and Sch7 and this inserts new provisions into TCGA 1992.

When the new provisions apply

The new charge applies to disposals made on and from 6 April 2015 *and* to gains accruing from that date (FA 2015 Sch 7 para 60).

There is to be rebasing as at 6 April 2015 and that will be the default position: a time apportionment option is available: see the new Sch 4ZZB paras 1-10. In addition taxpayers can opt for neither of the above 2 routes to apply and thus compute the gains (or loss) over the entire period of ownership.

Restricted to residential property

The new charge does not cover offices and industrial properties and is restricted to a disposal of property which is dwelling which is defined in Sch B1 para 4(1) thus:

> "4 (1) …..a building counts as a dwelling at any time when
>
> (a) it is used or suitable for use as a dwelling, or

(b) it is in the process of being constructed or adapted for such use."

The charge will apply to a dwelling even though it is let on commercial terms to an unconnected person.

Property used primarily for communal use – such as boarding schools and nursing homes – will avoid the new charge and so will communal care homes and nursing homes and purpose built student accommodation (see Sch B1 para 4(3)).

Non-residents

The charge will apply to gains realised by non-resident persons of all kinds and is not restricted to disposals by individuals.

The rate payable by **individuals** will normally be 28% on any gains. The annual exempt amount will be available in line with UK residents (this is £11,100 for 2015/16).

The new charge will apply to non-resident **settlements** at 28% with an exemption half of that available to individuals. There are interaction provisions with the present non-resident settlement code in TCGA 1992 s87.

Example

> X overseas settlement makes a gain on the disposal of let residential UK property after 5 April 2015. The ATED is not relevant (as it does not apply to settlements even if there is a corporate trustee) but a trust gain (strictly a "s2(2) amount") is realised under TCGA 1992 s87 and this can be matched with capital payments received by beneficiaries of the settlement. However, if the gain is chargeable under the new CGT regime that gain is disregarded in calculating the s 2(2) amount. Note part of the gain may fall outside of the new regime because of the rebasing as at 6 April 2015: such gain remains within the TCGA 1992 s87 code as rebasing as at 6 April 2015 will only apply to gains made under the new regime.

Non-resident companies will in general be within the scope of the new CGT charge.

They will bear the new charge at the corporation tax rates. This is presently 20%. For the financial years 2017, 2018 and 2019 it will be 19%. For the financial year thereafter it will be 18%. These are stunningly low rates for the UK.

If the company makes an ATED-related gain it pays 28% tax on the same: if the gain escapes the ATED-related gains regime it pay corporation tax at 20% (and going down).

Example

> Cayman Inc makes a gain which is outside the ATED e.g. it is residential property let to strangers. It pay 20% corporation tax (at present). That is a better result than if the property was held by an individual or settlement who were non-UK resident (they will have borne tax at 28%). If the gain were within the ATED the better result would be to have the property in a settlement or the individual's name. If the company were outside the ATED and the new CGT regime (because it is not "close") the decision is easy: have the property in the company but note the SDLT charge on purchase.

However not all foreign companies will fall within the new charge.

If the company is not closely-held for example – i.e. not under the control of 5 or fewer participators – the provisions may not be applicable (see s 14F TCGA 1992 and Sch C1 para 2).

Share disposals not caught

The Government does not propose to tax the disposals of shares by non-residents in companies which hold the residential properties.

The Annual Tax on Enveloped Dwellings (the ATED) and the new regime

As mentioned above. the ATED code is to remain intact. If a gain made by a company avoids the ATED-related gains charge found in TCGA 1992 Sch 4ZZA (for example, the dwelling is let to a stranger) it may nevertheless be assessed under this new CGT regime found in the next Schedule-Sch 4ZZB.

Example

> Jersey Limited owns residential property let to strangers. The ATED and the ATED-related gains regime are not in issue but any gain will be taxed under the new CGT regime.

Interaction-taxes clambering over each other for attention

If a non-resident company sells UK residential property it may be a land dealer in which case none of the above provisions are relevant.

If the company holds the land as an investment or for non-dealing purposes there are three regimes to consider. The 3 regimes are the ATED-related gains regime and the proposed new CGT regime; the third regime is in TCGA 1992 s10 and that applies if the non-resident company owns an asset in the UK from which it trades e.g. it owns a hotel in the UK or a car park in the UK from which it or its agents or employees carry on a trade. For good measure TCGA 1992 s13 must be considered if for example the shareholders in the company are resident in the UK and the above 3 charges are avoided.

One will also need to consider TCGA 1992 ss86 and 87 and even Schedules 4B and 4C if settlements are involved.

One may feel the tax code is getting congested

> Example
>
> Panama Inc disposes of UK residential property at a gain in 2017. The ATED charge may apply. Failing the ATED (e.g. the property is let to strangers), the new CGT charge can apply. Failing that (e.g. the company is not close) there will be no UK tax charge. This assumes the property is not stock and the artificial land transactions provisions (ITA 2007 s752) and s720 ITA 2007 do not apply. Not also s13 of TCGA 1992 must be taken into account if there are UK resident shareholders in Panama Inc. TCGA 1992 s10 (UK branch which trades) may also be relevant. There are trap for the unwary and the wary.

Principal Private Residence Exemption (PPRE)

The Government has struggled over the PPRE.

The provisions are in FA 2015 Schedule 9 and this inserts new ss 222A, 222B and 223A into TCGA 1992.

If the individual is not tax resident in the UK he can only get the CGT private residence exemption if he spends a minimum of 90 midnights in the property over the year.

Taxpayers wanting to keep their non-UK residence status will need to consider this as stays of *more* than 90 midnights result in a further tie to the UK when determining an individual's place of residence (see FA 2013 Sch 45 para 37 (90-day tie)) and that additional tie may make the individual resident in the UK for all income tax and capital gains tax purposes.

One redeeming clause in the new legislation is TCGA 1992 s222C(7) which treats time spent in the dwelling by the spouse or civil partner of the non-resident as time spent by the non-resident.

> <u>Example</u>
>
> Mr A is not resident in the UK. He spends 70 midnights in the UK in his UK house. His wife accompanies him for 40 of those midnights but in addition spends 25 midnight alone in the mansion. Mr A passes the 90 midnights test and the house can be nominated as his principal private residence.

<u>No Withholding Tax</u>

The Government had considered introducing a form of withholding tax to ensure the levy is "robust and sustainable" but that approach is not to be pursued.

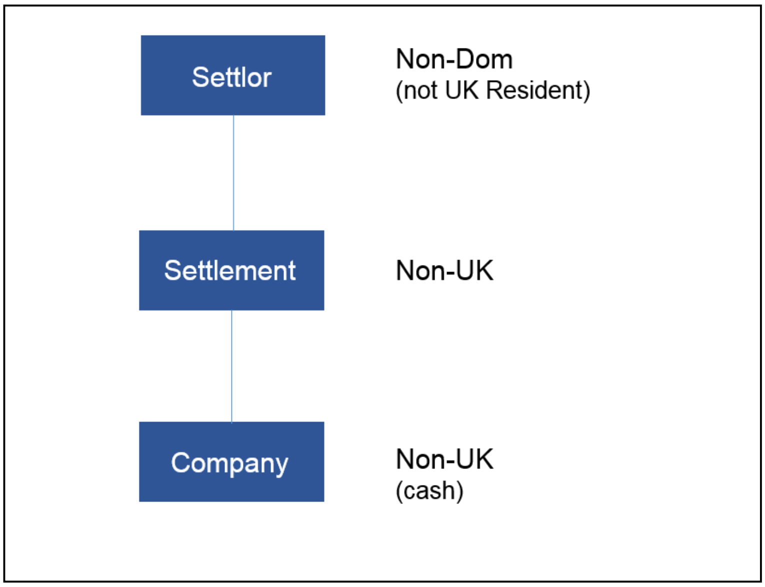
<u>A new population of taxpayers</u>

The Government realise the new levy "will bring in a new population to the UK tax system."

<u>HOW SHOULD RESIDENTIAL PROPERTY IN WHICH THE TAXPAYER IS TO LIVE BE PURCHASED NOW?</u>

A standard structure is an offshore settlement owning an offshore company. Who should buy the new residential property in which the settlor (who is not resident and not domiciled in the UK) is to live: –

> *the settlement,*
>
> *the company owned by the settlement and which has the necessary funds or*
>
> *the settlor?*



If there are to be sufficient borrowings deductible for IHT purposes (which can be on commercial terms or a commercial deeply discounted bond could be issued to raise the monies) Proposal I below may be the most attractive.

PROPOSAL I

The settlement buys the property using a nominee with loans (interest free repayable on demand) from the company.

PROPOSAL II

The settlor buys the property using a nominee with loans (interest free repayable on demand) from the company.

PROPOSAL III

The underlying company buys the property using its own monies.

TAXATION

PROPOSAL I (PURCHASE BY SETTLEMENT THROUGH NOMINEE COMPANY)

The ATED is avoided and there are deductible IHT loans subject to FA 1986 s103 but note GAAR Guidance Part D Part VI D31D. The reservation of benefit provisions in FA 1986 s102 will be offended if the settlor is a beneficiary under the settlement (but little turns on this if there is an appropriate debt shelter). The new loan provisions in IHTA 1984 s175A will need to be considered. The SDLT will be 0%-12%. There are no deemed directorship issues (ITEPA 2003 ss67 and 97).

The trust bears the 10 year anniversary charge on UK located property but the loans should be deductible. The new loan provisions in IHTA 1984 ss162A et seq. and 175A are not in issue re the 10 year anniversary charges. If in years to come the property is sold the purchaser will pay SDLT on the purchase price.

The settlement will be within the new CGT regime effective from 6/4/15 but the principal private residence exemption may be available.

PROPOSAL II (PURCHASE BY SETTLOR PERSONALLY VIA NOMINEE COMPANY)

The ATED is avoided and there are deductible IHT loans subject to s103. The SDLT will be 0%-12%. There are no deemed directorship issues.

One will be within the new CGT code for non-UK resident persons effective from 6/4/15 but the taxpayer is in a position to use the PPR CGT exemption if the conditions are satisfied.

The settlor does not bear any 10 year anniversary charge. The loans will be deductible subject to s103 but connected persons loans will need to be discharged at death under the recent IHT changes; however it is possible to satisfy the legislation by borrowing from a connected person to replace the loan after death. If in years to come the property is sold the purchaser will pay SDLT on the purchase price.

PROPOSAL III (PURCHASE BY COMPANY)

The ATED is not avoided. There is a major 15% SDLT charge on acquisition. One must consider the deemed directorship position but they will be wholly irrelevant as the settlor is not resident in the UK.

One will be within the new CGT code for non-UK resident persons which was effective from 6/4/15 but only the corporation tax rates will apply.

The taxpayer is not in a position to use the PPR CGT exemption.

The purchaser company will not bear any 10 year anniversary charges; also the trust is an excluded property settlement and no IHT is payable under the 10 year anniversary or interim charge provisions. Note however the proposed IHT see-through provisions mentioned below which apply from April 2017.

Later on if a purchaser wants to buy the property the shares can be sold instead thus avoiding any SDLT charges.

CONCLUSION ON THE THREE PROPOSALS

Proposal I is likely to prove the most attractive one if there are deductible IHT debts and the gift with reservation provisions in FA 1986 s102 do not apply.

Proposal II has the attraction of simplicity and if an appropriate loan can be taken it is an attractive route: indeed this is better than the settlement alternative if the gift with reservation provisions were to apply to the settlement.

HOW SHOULD A RESIDENTIAL HOUSE TO BE LET TO UNCONNECTED PERSONS BE PURCHASED NOW – COMPANY PURCHASE MAY BE THE BEST OPTION

The SDLT levy on purchase by a company is 0%-12%. The 15% levy is avoided.

One attraction in a company purchase is there is no ATED charge and any new CGT charge is at the corporation tax rate: that charge also is avoided if the company is not close.

IHT is not an issue but one must consider the deemed directorship question and the proposed new see-through IHT rules effective from April 2017.

The PPRE will not be available.

The shares can be sold free of SDLT (and SD in the case of a non-UK company: see Stamp Act 1891 s14(3)).

THE 8th JULY 2015 SUMMER BUDGET – BIG CHANGES FROM APRIL 2017 FOR NON-DOMICILIARIES AND SITUATIONS WHERE UK RESIDENTIAL PROPERTY IS HELD IN FOREIGN COMPANIES

HMRC on 8 July 2015 in the summer budget issued Technical Briefings on:

(1) the radical changes proposed to the non-dom rules and

(2) the treatment of UK residential property held in foreign companies for inheritance tax purposes: a "corporate see-through" is proposed.

An Open Consultation (OC) (www.bit.ly/1OhCZni) was issued on the proposed changes to the non-dom rules on 30 September 2015 and this is dealt with in outline below and more fully in Part II of this Tax Memorandum.

A consultation paper on the IHT corporate see-through is expected in early 2016.

New deemed domicile rules proposed

With effect from April 2017 (so there is no need to immediately panic, yet) an individual who has been resident in the UK for more than 15 out of the past 20 years will be deemed to be UK domiciled for income tax and capital gains tax and inheritance tax purposes from the beginning of the 16th year of residence (OC para 3).

Recycling the deemed domicile

If the individual has become deemed domiciled in the UK he can break that by leaving the UK for 6 years or more consecutive years. If he then comes back to the UK he will not be deemed to be domiciled in the UK until after 15 years of UK residence (out of the prior 20 years).

Settlements

If during the 15 year period the taxpayer sets up a settlement it is possible he will only be taxed after he becomes deemed domiciled in the UK when he receives (and only when he receives) benefits from the trust. The charge will arise whether or not the benefits are remitted to the UK.

Foreign companies holding UK residential property – casting aside the corporate veil for inheritance tax

It is proposed from April 2017 that for inheritance tax purposes UK residential property held by a foreign company will be treated as held direct by the shareholder.

IHT will therefore be imposed on the value of UK residential property owned by the offshore company on the occasion of any chargeable event. This would include:

- the death of the individual wherever resident who owns the company shares

- a gift of the company shares into trust
- the 10 year anniversary of the trust
- distribution of the company shares out of trust
- the death of the donor within 7 years of having given the company that holds the UK property away to an individual
- the death of the donor or settlor where he benefits from the gifted UK property or shares within 7 years prior to his death - the reservation of benefit rules will apply to the shares of a company owning UK property in the same way as the rules currently apply to UK property held by foreign doms and generally to UK doms

Mortgages

It is not known if the new company see-through provisions will apply to a foreign company which has a mortgage against UK land.

The relevant part of the brief states:

> 13. This will require a change in the legislation to provide that shares of offshore companies or similar structures are not excluded property to the extent that they derive their value directly or indirectly from UK residential property (as defined for non-residents CGT) or to the extent that the value of those shares is otherwise attributable to UK residential property.
>
> Example
>
> X in not domiciled in the UK. She owns a UK house worth 5m. She bought it with a borrowing (mortgaged on the property) from a non-resident company owned by a settlement created by her non-UK domiciled father. One must see if the new rules will be extended to treat the loan rights vested in the company as located in the UK for IHT purposes.

What does it all mean?

Non doms have time to consider these new rules.

The ability to put assets into a settlement and be taxed on a benefits basis only is a very important relief if it finds its way to the statute book.

Under the new statutory residence rules many non doms may decide to break their UK residence.

The non dom status can be recycled by becoming non-resident for 5 years.

The new IHT see-through rules will mean the IHT advantage in holding UK residential property whether let or not via a foreign company will no longer be available after April 2017. Creating allowable debts and using the usual IHT reliefs for gifts of house interests in FA 1986 s102B may be the way forward.

CONCLUSIONS ON THE STRUCTURES FOR NON-UK DOMICILIARIES TO PURCHASE AND HOLD UK RESIDENTIAL ACCOMODATION

The CGT regime on UK residential property is becoming complex and full of traps for the unwary (and the wary).

Careful planning is needed as the pitfalls are many – the ATED, the ATED-gains regime, SDLT at up to 15% on corporate purchases (the writer has already come across a number of cases where taxpayers have been inadvertently caught by the 15% charge), the new CGT charge from 6/4/15 and the new IHT debt provisions – and the planning areas are few.

For the future (after April 2017) the new deemed domicile rules for income tax and capital gains tax and IHT must be considered and the see-through of foreign companies holding UK residential property for IHT purposes.

PART II

THE PROPOSED NEW NON-DOM RULES SET OUT IN THE OPEN CONSULTATION DOCUMENT OF 30 SEPTEMBER 2015

Introduction

In the summer budget technical briefing of 8 July 2015 the government set out its proposed changes in skeleton form to the non-dom rules to come into effect in April 2017.

An Open Consultation (OC) (www.bit.ly/1OhCZni) paper was issued on the proposed changes on 30 September 2015 adding flesh to the bones and this is dealt with below.

Stick and Carrot

In essence under the new rules there is a big stick which makes non-doms deemed domiciled in the UK (and thus wanting to flee the UK) and then there is the carrot to stay which is their ability to create settlements, whilst non-deemed domiciled, to take away the full brunt of the arising basis of assessment.

Non-doms should not be daunted by these new rules: the government recognises their contributions to the country and does not want them to flee. It only wants to pluck the goose not cause it to fly away.

Where a person is domiciled under general principles

The fulcrum upon which the remittance basis turns is domicile.

Domicile of Origin

An individual acquires a domicile of origin when born (*Henderson v Henderson*) (1967) p.77).

This will generally have been the same as his father's domicile at the date of birth of the individual.

That domicile of origin will continue until the individual acquires a domicile of dependency or a domicile of choice.

Upon his acquiring a domicile of dependency or a domicile of choice that new domicile will remain his domicile until abandoned.

If the domicile of dependency or choice is abandoned, without another domicile of dependency or choice being acquired, the domicile of origin revives (*Udny v Udny* (1869) 1 L.R. Sc. & Div. 441).

The domicile of origin is adhesive, i.e. difficult to get rid of. This is for two reasons. First, the onus is on whoever alleges a person has acquired a domicile of choice to prove it. Secondly, although the standard of proof is a civil standard, the acquisition of a domicile of choice is regarded as a serious matter, not to be lightly inferred from slight indications or casual words (*Buswell v I.R.R.* (1974) S.T.C. 266).

<u>Domicile of choice</u>

Once a domicile of choice, however, is acquired it is relatively difficult to abandon it.

It is only abandoned if the individual both ceases to reside in the country of choice and ceases to intend to reside there permanently or indefinitely (*I.R.C. v Duchess of Portland* (1982) S.T.C. 149).

Normally loss of one domicile of choice means that another domicile of choice is acquired but that is not necessarily the case; if a new domicile of choice is not acquired the domicile of origin will revive.

To acquire a domicile of choice it is necessary for an individual to have his sole or chief place of residence in that particular country or be an inhabitant of that country and intend to live there permanently or indefinitely (*Plummer v I.R.C.* (1987) S.T.C. 698).

A person only acquires a domicile of choice in a new country if his intention to remain there is firm and settled (Re *Clore (No 2)* (1984) S.T.C. 609).

It is frequently difficult to tell whether a person intends to remain in a country.

In *I.R.C v Bullock* (1976) S.T.C. 409 the Court of Appeal stated that this test is not satisfied if the person would return to the country of his origin on the happening of certain and definite and realistic contingencies; such contingencies include retirement, the attainment of a specified age, inheritance of a title, or the death of an older spouse. Such contingencies would also include a change in Government if there is a realistic possibility of that happening.

<u>Example</u>

> Mr X lives in the United Kingdom but has a domicile of origin outside the UK. He intends to return to an overseas jurisdiction on his retirement, or on attaining a specific age of 60. Mr X would not have a U.K. domicile of choice (unless the facts indicate he would not survive to his retirement age or age 60).

The acquisition of a domicile of choice is not, however, precluded if the person merely says he would return to his country of origin when he has made his fortune, when he has had enough of the new territory or when his health fails (*Re Furse* (1980) S.T.C. 596). This is because those latter contingencies are too remote and doubtful.

Statements a person makes are not conclusive with respect to his domicile (*Wahl v Attorney General* (1932) All E.R. 92).

Domicile of Dependency – Children

There is a type of domicile known as a child's domicile of dependency.

This can be attributed only to a child under 16.

A child's domicile of origin is displaced by a child's domicile of dependency if the domicile of his father changes whilst the child is under the age of 16. If this happens, the domicile of choice which the father thereby acquires becomes the child's domicile of dependency.

On attaining 16 a domicile of dependency is retained by the child as a domicile of choice. However, if a child does not live in the territory and never intends to live there, this acquired child's domicile of dependency (which is really a form of domicile of choice) is forthwith abandoned and the child's domicile of origin (being the place of his father's domicile at the time of the child's birth) revives (unless the child has taken up a new domicile of choice in another country).

Example

> X is born in Cyprus when his father is domiciled in Cyprus. X's domicile of origin is in Cyprus. Whilst X is under the age of 16, X's father changes his domicile to Spain and the father keeps that domicile of choice. X will have acquired a child's domicile of dependency in Spain (where he lives with his father). He will lose that child's domicile of dependency in years to come if he moves to Germany (where he intends to live permanently or indefinitely): in this case he will acquire a domicile of choice in Germany.

Domicile of Dependency – Wife

Until 1974 a married woman did not have a domicile independent from that of her husband. She had a wife's domicile of dependency. This rule was abolished in 1973 (Domicile and Matrimonial Proceedings Act 1973, s.1).

A married woman's domicile is now determined independently of that of her husband's but a woman who on January 1, 1974 had her husband's domicile (i.e. a wife's domicile of dependency) retains that wife's domicile of dependency automatically as a domicile of choice: she must abandon it before she can acquire or reacquire her own domicile.

New deemed domicile rules proposed applicable to income tax, capital gains tax and inheritance tax

With effect from April 2017 (so there is no need to immediately panic, yet) an individual who has been resident in the UK for more than 15 out of the past 20 years will be deemed to be UK domiciled for income tax and capital gains tax and inheritance tax purposes from the beginning of the 16th year of residence (OC para 3).

Example

> Non-dom X has been continuously UK resident in the UK for the tax year 2002/3 and subsequent tax years. X will have been resident for 15 years up to and including 2016/17. X becomes deemed domiciled in the UK under the new rules on 6/4/2017.

Recycling the deemed domicile

If the individual has become deemed domiciled in the UK he can break that by leaving the UK for 6 years or more consecutive years.

If he then comes back to the UK he will not be deemed to be domiciled in the UK until after 15 years of UK residence (out of the prior 20 years).

Example

> Non-dom Z is deemed domiciled in the year 2018/19. Z becomes non-resident in the UK for the years 2019/20 to 2024/25. That is 6 full tax years. If Z become resident in the UK in 2025/26 he will start his 15 out of the last 20 years deemed domicile test again.

Children

Children will have their domicile determined under general domicile principles and this will not change. The children normally take the father's domicile at the date of birth.

The deemed domicile status however will not be passed from parent to children but they may acquire a deemed domicile on their own.

Example

> W is not domiciled in the UK under general principles but is deemed domiciled in the UK (England and Wales). W has a child born in the UK who takes W's non-UK domicile under general principles but not the deemed of W. After 15 years of continuously living in the UK the child will be deemed domiciled in the UK. This is the case even though the child has not reached adulthood.

How is residence determined for these purposes?

Non-doms may have been resident in the UK under the statutory residence tests from 6 April 2013 and (for earlier years) under the former case law rules.

It is likely under the new legislation residence will be determined under those rules but without the split year reliefs under the statutory residence tests being available (OC para3.1).

Example

> W non-dom takes up residence the day before the beginning of tax year 1 and leaves the day after tax year 13. W satisfies the 15 year test.

Settlements

If during the 15 year period the taxpayer sets up a settlement it is possible he will only be taxed after he becomes deemed domiciled in the UK when he receives (and only when he receives) benefits from the trust. The charge will arise whether or not the benefits are remitted to the UK.

HMRC will have to see how that approach fits in with ITA 2007 s720 which can charge tax on the settler (a remittance basis user) as the income arises (if it has a UK source) in the settlement if the settlor has the power to enjoy the income and there was a tax avoidance motive.

It would seem the government will not apply that section but create a new form of "benefits tax" with no regard to whether there are capital gains or income receipts or pure capital amounts in the settlement. At a stroke one cuts through the Gordian knot of the treatment of mixed funds in a settlement.

This is major new thinking.

The relevant part of the OC para 3.2 reads thus and every paragraph is potentially gold dust if it finds its way to the statute book:

> The government intends to base the new rules on the taxable value of benefits received by the deemed domiciled individual without reference to the income and gains arising in the offshore structure. This will be a very significant change to the way that the income and gains arising in offshore trusts and their underlying entities are taxed and it means that there will be no need for trustees to have to recreate the history of the income and gains in the trust for tax purposes once an individual becomes deemed-UK domiciled.
>
> Once a non-dom becomes deemed-UK domiciled, it will no longer be relevant whether a benefit is received in the UK or overseas; the value of that benefit will be treated as taxable regardless. However, UK source income will be taxable on the arising basis, as it would be under the existing rules if either the settlements legislation or the transfer of assets legislation applied.
>
> The government is considering whether the new regime should apply to all non-domiciled individuals who are resident in the UK rather than being limited to those who become deemed-domiciled, though while an individual is not deemed-domiciled, benefits will be taxable only when remitted here. This would give greater consistency and would avoid the complexity of transitioning to new rules when an individual has been resident for 15 years.
>
> The government continues to consider these issues and is not yet in a position to publish draft legislation on this aspect of the reforms.

<u>Example</u>

Y is soon (in 2018/19) to become deemed domiciled in the UK. He is a remittance basis user. He puts assets into a Jersey discretionary settlement (in 2017/18) for the benefit of himself and his family. In 2018/19 he pays income tax and CGT on an arising basis on assets in his own name. He pays no tax on the settlement income and gains. The settlement will pay income tax on UK source income under normal rules. If he receives a benefit from the trust whether or not the benefit is received in the UK he will bear the new benefits tax regardless of whether any gains have accrued in the settlement or there has been a receipt of income by the trustees. The UK government are adept at inventing new taxes. We do not know at present what the rate of this new benefits tax will be.

<u>Example</u>

K non-dom has been resident in the UK for 12 years up to 2017/18. He is a remittance basis user. He created a settlement in 2009/10 and has been battling with HMRC for years over whether ITA 2007 s720 applies to the settlement. He has received no benefits but the settlement has received UK source income.

> The new rules mean HMRC may only assess K to the extent he receives benefits. The rental profits (normally the rent less property running expenses and interest paid to a connected company) will be assessed on the trustees or their underlying company (if the same holds the property) on an arising basis in the normal way. It is unlikely the new rules however will apply to past years (where ITA 2007 s720 was in point). This may mean the demise of ITA 2007 s720 for the non-doms in the future.

<u>Implications for IHT</u>

IHT has a 17 out of 20 years rule for deemed domicile (IHTA 1984 s267).

This is to be changed to 15 years out of 20 from April 2017 so individuals who are not deemed domiciled in the UK for IHT purposes under the present rules (but will be caught by the new rules)(this affects people who became UK resident after 5 April 2000) should create their settlements now.

<u>People born in the UK with a UK domicile of origin</u>

There is to be a new rule that if an individual is born in the UK and has a UK domicile of origin and he obtains a foreign domicile of choice his domicile of origin will revive if he becomes resident in the UK regardless of his intentions to return overseas (OC para 4).

<u>CONCLUSIONS ON THE NON-DOM CHANGES FROM APRIL 2017</u>

The new changes may not have a major impact on non-doms because of the ability to create settlements.

Also they will not have to pay the heafty £90,000 annual remittance basis user charge (which applies to non-doms who have been resident in the UK for at least 17 out of the last 20 years).

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Gray's Inn

22/10/15