

Briefing document

Becoming deemed UK domiciled

Introduction

Legally non-UK domiciled individuals who are not deemed UK domiciled (DD) are able to claim the remittance basis of taxation, under which most types of foreign income and gains are only taxable if they are remitted to (brought into) the UK. Furthermore, non-UK domiciled individuals who are not DD are only within the scope of inheritance tax on UK assets and certain foreign interests that derive value from UK residential property.

Becoming DD for tax purposes significantly changes an individual's tax position. DD individuals are normally ineligible to pay tax under the remittance basis of taxation (subject to one limited exception explained below) and worldwide assets are within the scope of inheritance tax.

This note contains a high-level summary of a number of key points that are relevant to individuals who will soon be or have recently become DD. This is a complicated area of taxation, and it is essential that advice is taken on your specific circumstances.

Deemed UK domicile

Individuals who are legally non-UK domiciled are DD for income tax, capital gains tax and inheritance tax purposes if they meet either or both of the following conditions:

- **Long-term UK residence:** Individuals who were UK resident in at least 15 of the previous 20 tax years. This applies regardless of the individual's residence status in the tax year under consideration. For example, if an individual is UK resident for 15 consecutive tax years, he or she will be DD in tax year 16 whether or not he or she is UK resident in tax year 16.

For inheritance tax purposes only, DD ceases from the beginning of the fourth consecutive tax year of non-UK residence, if this results in DD ceasing sooner than would otherwise be the case.
- **Formerly domiciled residents:** Individuals who are UK resident, were born in the UK and who have a UK domicile of origin (i.e. were UK domiciled at birth). Individuals are only DD for inheritance tax purposes under this rule if they were UK resident in at least one of the previous two tax years.

The above rules were introduced with effect from 6 April 2017. They only apply to individuals who have been UK resident in at least one tax year from 2017/18 onwards.

There are further provisions under which non-UK domiciled individuals may be DD for inheritance tax purposes only. Notably, under the pre-6 April 2017 rules, individuals were DD for inheritance tax purposes if they were UK resident in at least 17 out of 20 tax years, up to and including the current tax year. This rule applies to individuals who satisfy this residency requirement and have been continuously non-UK resident from 2017/18 onwards. The last tax year in which individuals could be DD under this rule was 2019/20.

Income tax and capital gains tax

UK resident, deemed UK domiciled individuals

Set out in this section of the note are some key points that are relevant to the income tax and capital gains tax position of UK resident DD individuals. The below points are relevant to both long-term UK residents and to formerly domiciled residents. There are some points of difference in the tax position of individuals and trusts to which an individual has added property, depending on the rule(s) under which the individual is DD.

The remittance basis

DD individuals cannot claim the remittance basis. As a result, such individuals (on the basis they are UK resident) are normally taxable on worldwide income and gains (the 'arising basis').

There is one exception to this rule: the remittance basis applies automatically to individuals who are legally non-UK domiciled and have less than £2,000 unremitted foreign income and gains in a given tax year.

Paying tax on the arising basis

Income and gains within the scope of UK taxation

Worldwide income and capital gains realised in tax years in which the arising basis applies are fully taxable in the UK. No reliefs are available to reduce the taxable amount of income or capital gains to take account of periods of non-UK residence and/or the remittance basis applying in earlier tax years.

When the DD rules were first enacted, individuals who became DD under the long-term UK residence rule in the 2017/18 tax year, who were not also formerly domiciled residents and who satisfied certain conditions, were eligible for rebasing. Where rebasing applied, the value of the individual's foreign assets were rebased to their value on 5 April 2017 for the purposes of calculating the gain realised on a subsequent disposal of the asset, provided the individual remains DD but legally non-UK domiciled until disposal. Rebasing is not available to individuals who become DD in later years.

Reporting

Consideration should be given to establishing what foreign sources of income and capital gains exist, and to how such income and gains are to be calculated and reported for UK taxation purposes. It may be appropriate to consider rationalising asset holdings and income sources, where this simplifies an individual's affairs. Where relevant, investment advice should be obtained from a suitably qualified person.

Foreign income received and gains made in tax years to which the remittance basis applied

Most foreign income and gains realised in tax years in which the remittance basis applied are chargeable on remittance to the UK, even if the individual is DD at the date of remittance. Care should be taken to ensure that the source of any remittances to the UK can be identified, and the way in which funds are held should be managed to provide an individual with as much certainty of their tax position as possible.

Inheritance tax

From the date DD for inheritance tax commences, the worldwide estate of DD individuals is within the scope of inheritance tax. Inheritance tax can also apply to gifts made in the seven years before death and to most lifetime gifts into trust. DD does not apply to gifts retrospectively, and so gifts of foreign assets made before DD commenced are not revisited and therefore remain outside the scope of inheritance tax.

It may be appropriate for an individual who will soon become DD to consider making lifetime gifts. Consideration may need to be given to the level of resources the individual has in comparison to what they are likely to need during their lifetime, and to how long the individual is likely to be DD.

Settlor-interested trusts

General income tax and capital gains tax position

In general, UK resident individuals who are able to benefit from a trust they created or to which they added property ('settlor-interested trusts') are personally taxable on trust income and gains as they arise. This can apply to income and gains made either by the trustees directly and/or by companies the trustees own.

Settlors are regarded as being able to benefit from a trust if they or (broadly) certain family members can potentially benefit from a trust, regardless of whether or not they actually do so.

There are limited exemptions under which UK resident settlors of settlor-interested trusts are not taxable on trust income as it arises, which principally relate to the reasons the trust was created and property added. The remainder of this note assumes that this point is not relevant.

Non-UK resident settlors of settlor-interested trusts may be chargeable on UK source income of such a trust in some cases, though the comments in this note relating to the income tax and capital gains tax position of settlors of settlor-interested trusts assume that the settlor is UK resident.

Trusts settled by non-UK domiciled individuals who are not formerly domiciled residents

There is an exception from the above outlined position, in that non-UK domiciled settlors of settlor-interested trusts are only subject to income tax and capital gains tax in relation to foreign trust income and both UK and foreign trust capital gains if they receive a benefit from the trust. Various conditions must be met. Notably:

- The trust must have been created and any property added when the settlor was both legally non-UK domiciled and at a time when the individual was not DD for income and capital gains tax purposes;
- If the settlor has since become DD due to long-term UK residence (only), he or she must not have added any property to the trust while DD. Detailed rules apply to determine whether or not property has been added to a trust, and;
- The settlor must not be a formerly domiciled resident.
- The settlor must be legally non-UK domiciled.

UK source income and certain types of foreign income are not eligible for the above system which restricts taxation to occasions on which a benefit is received from the trust: UK resident settlors are chargeable on such income as it arises, even in the absence of benefiting from the trust.

If the settlor settles further property on trust after becoming DD, he or she is taxable on all trust income and gains as they arise (subject to the availability of the exemptions referred to above, which, as noted, principally relate to the reasons the trust was created and property added).

Inheritance tax of trusts which have a settlor who is not a formerly domiciled resident

Most trusts, particularly those created during lifetime, are subject to inheritance tax every ten years and/or on distribution of assets. Where the settlor of the trust was non-UK domiciled for inheritance tax purposes when assets were settled on trust, trustees are only subject to inheritance tax on UK situated assets and, broadly, certain foreign interests that derive value from UK residential property. In order for this position to apply, on the date of settlement, the settlor must have been both legally non-UK domiciled and not DD for inheritance tax purposes.

The inheritance tax position of the trustees does not change if the non-UK domiciled settlor of the trust subsequently becomes DD due to the application of the long-term UK resident rule, provided no further property is added to the trust after DD commences, and provided the individual is not a formerly domiciled resident.

Formerly domiciled resident settlors

With the exception of the remittance basis applying automatically in the limited circumstances outlined above and remaining chargeable on remittances of foreign income and gains received in any earlier tax years to which the remittance basis applied, formerly domiciled residents are essentially taxable as though they are legally UK domiciled.

Formerly domiciled residents who are settlors of settlor-interested trusts are chargeable on all trust income and gains as they arise; taxation is not limited by reference to the extent the individual has benefited from the trust. This applies regardless of whether or not the formerly domiciled resident was DD when the trust was created and/or property settled.

In addition, when a ten year anniversary of the trust occurs and/or the trustees make a distribution of trust assets, if the settlor is DD for inheritance tax due to the application of the formerly domiciled resident rule, the trustees are within the scope of inheritance tax on both UK and foreign assets.

If the settlor is not DD for inheritance tax in the tax year in which the tax point arises, the trustees are only within the scope of inheritance tax on UK situated assets, or certain non-UK situated assets that derive value from UK residential property and so are deemed to be UK situated for inheritance tax purposes.

This means that foreign assets may not be subject to an inheritance tax charge if the settlor is non-UK resident or still within the grace period for inheritance tax DD purposes on the date of charge.

Find out more...

This note reflects the law in force as at 6 April 2020. Please be aware that it does not cover all aspects of this subject. In particular, it should be borne in mind that trust taxation is a particularly complicated area of taxation and this note contains a high-level summary. Various other points should be considered, including the tax position of the trustees and any underlying companies, and rules that can impute a tax charge to an individual other than the individual who actually received a benefit from the trust. Suitable advice should be taken.

To find out more about any aspect of the above, please discuss with your usual Deloitte contact. If you do not have a usual contact, please contact Michelle Robinson (michellerobinson@deloitte.co.uk). For further information visit our website at www.deloitte.co.uk.

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