PAYNE HICKS BEACH

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Autumn budget 2024 - The abolition of the non-dom tax regime.

After nearly eight months of uncertainty following the March 2024 Spring Budget, the Autumn Budget has at last delivered a fully formed plan (and 103 pages of draft legislation) to abolish the current tax regime for non-domiciled UK resident individuals from 6 April 2025 and to replace it with a generous but much shorter term regime for new arrivers to the UK based solely on residence.

It will take some time to analyse and digest the draft legislation in detail. In the meantime, this note is intended to give a high level summary of the many facets of the new regime.

The current non-dom regime

Before we analyse the new rules, it is helpful to summarise the current non-dom regime.

The normal tax regime for UK resident individuals is the "arising basis": the individual's worldwide income and gains are taxed in the UK as they arise. However, UK resident individuals who are domiciled outside the UK can elect to be taxed on the "remittance basis": UK source income and gains are taxed in the UK as they arise but foreign income and gains (**FIG**) are only taxed if and when they are brought into the UK.

The regime has undergone a series of changes in recent years, with the biggest change taking effect from April 2017, when the existing concept of "deemed domicile" was extended to include not only inheritance tax but also income tax and capital gains tax. Since then, non-doms who have been resident in the UK for 15 of the past 20 tax years are treated as being UK domiciled for tax purposes and so cannot elect to be taxed on the remittance basis.

To soften the blow of the new deemed domicile rule, the "protected settlement" regime was also introduced in April 2017. The UK has complex anti-avoidance rules which tax a UK resident settlor of an offshore trust structure personally on income and gains arising in the structure if the settlor retains an interest in the trust. However, since April 2017, UK resident non-dom settlors are not taxed on FIG arising in offshore trust structures (unless or until they receive a benefit from the structure); this applies even after the settlor has become deemed domiciled, provided that the settlor does not "taint" the trust by adding value after becoming deemed domiciled. Put simply, since April 2017 it has in effect been possible for a non-dom who has become deemed domiciled in the UK to continue to benefit from a form of the remittance basis for assets held in trust.

The new FIG regime for new arrivers

From 6 April 2025, an individual who becomes tax resident in the UK for the first time (or after a period of at least 10 continuous years of non-UK residence) will pay no UK tax on FIG arising in the first four tax years from becoming UK resident (even if those funds are brought into the UK) regardless of their domicile status or nationality – this regime will therefore apply equally to returning UK nationals who have spent at least 10 years abroad. Unlike similar regimes in other jurisdictions (such as Italy and Switzerland), there will be no charge to benefit from the new regime. However, from the fifth year of tax residence onwards, the special regime will fall away and the individual's worldwide income and gains will be taxable in the UK as they arise in the normal way.

The new FIG regime for recent arrivers

An individual who became tax resident in the UK in 2022/2023 or a later tax year (and who had been non-UK resident for at least 10 continuous years before the current period of residence began) will be eligible for the new FIG regime from 6 April 2025 for the remainder of the four year period (counted from their first year of UK tax residence).

Non-doms who have been UK resident for four or more years on 6 April 2025 but have not become deemed domiciled before that date

The new FIG regime will not apply to these individuals and from 6 April 2025 they will no longer be eligible for the remittance basis of taxation. Their worldwide income and gains will therefore be taxable in the UK as they arise from 6 April 2025.

However, if they dispose of a foreign asset after that date which they held personally at 5 April 2017, they will be able to elect to rebase that asset to its April 2017 value for CGT purposes, provided that:

- they were a remittance basis user in at least one of the tax years from 2017/2018 to 2024/2025; and
- the asset was situated outside the UK between 6 March 2024 and 5 April 2025.

In addition, these individuals will no longer benefit from the protected settlement regime from 6 April 2025 – this is covered in more detail below.

Non-doms who have become deemed domiciled in the UK before 6 April 2025

These individuals will already be taxed on their worldwide income and gains under the arising basis, so this will not change.

In addition, these individuals will no longer benefit from the protected settlement regime from 6 April 2025 – this is covered in more detail below.

Historic unremitted FIG – the Temporary Repatriation Facility

From 6 April 2025 until 5 April 2028, UK resident individuals who have previously been taxed on the remittance basis under the current non-dom regime will be able to designate unremitted pre-6 April 2025 foreign income and gains to be taxed at a special reduced rate under a new "Temporary Repatriation Facility" (the **TRF**) – those funds can then be remitted to the UK without any further tax charge. The TRF rate will be 12% in the 2025/2026 and 2026/2027 tax years but will increase to 15% for the final 2027/2028 tax year.

The TRF will be available not only for unremitted FIG which arose to the individual personally before 6 April 2025 but also to unremitted FIG in an offshore trust or corporate structure that was attributed or matched to them before 6 April 2025. FIG which arose in offshore structures before 6 April 2025 but which has not been matched or attributed before that date will also be eligible for the TRF to the extent that it is matched to benefits received by a qualifying individual during the 3 year TRF period.

FIG that arose to a remittance basis user prior to 6 April 2025 will continue to be taxed at full rates if it is remitted to the UK and has not been designated and taxed under the TRF.

Abolition of Trust Protections

The current "protected settlement" regime, under which FIG arising within settlor-interested offshore trust structures are not taxed on UK resident non-dom settlors (or on deemed domiciled settlors, provided that the trust has not been "tainted") unless and to the extent that they receive a benefit from the structure, will no longer apply from 6 April 2025.

From that date, FIG from such settlements will therefore be taxed on UK resident settlors as they arise (but unmatched pre-6 April 2025 FIG will continue to be matched to benefits under the existing regime), unless the settlor is a new or recent arriver within the new four year FIG regime.

Settlors and beneficiaries who are new or recent arrivers within the new four year FIG regime will also be able to receive benefits from offshore trust structures from 6 April 2025 free of UK tax (at least initially), whether or not the benefits are received in or brought to the UK. However, the value of those benefits will not reduce the pools of relevant income or stockpiled gains available for matching to benefits received by arising basis UK taxpayers.

The Inheritance Tax regime

Individuals

IHT is a currently a domicile-based regime. The worldwide assets of UK domiciled (or deemed domiciled) individuals are within the scope of IHT but for non-doms this is limited to assets which are situated in the UK only. In broad terms, non-UK assets held in a trust settled by a non-dom are also "excluded property" and outside the scope of IHT under the current rules, even if the settlor subsequently becomes UK dom or deemed dom.

From 6 April 2025, IHT will become a residence based regime.

An individual's worldwide assets will fall within the scope of IHT if the individual has been resident in the UK for 10 or more of the previous 20 tax years (a long-term resident). One of the consequences of this rule is the extension of the so-called IHT "tail" – for example, if an individual has been continuously resident in the UK for 20 tax years and then leaves the UK, they will remain a "long-term resident" for IHT purposes for the next 10 tax years even though they are no longer UK tax resident for other tax purposes. Their worldwide assets will therefore be within the scope of IHT throughout this tail period.

To mitigate the harsh effect of the tail for individuals who leave the UK having been UK resident for between 10 and 19 of the last 20 tax years, the tail will be tapered so that:-

- individuals who have been resident for between 10 and 13 of the last 20 years will remain within the scope of IHT on their worldwide assets for 3 tax years; and
- for each additional year of UK residence, the tail will increase by one tax year – so if an individual had been resident for 14 out of the past 20 tax years before leaving, the IHT tail will be 4 years and so on.

A transitional rule will apply to non-dom individuals who are non-resident in the 2025/2026 tax year and would otherwise be long-term residents on 6 April 2025. In effect, the current rules will continue to apply from that date, so that the individual will be treated as being a long-term resident only if and for as long as they would have been deemed domiciled in the UK under the current rules (so if the individual had become deemed domiciled before leaving the UK, they will lose their deemed domicile after three continuous tax years of non-UK residence).

Trusts

For trusts, chargeability of non-UK assets will depend primarily on the settlor's status from time to time (rather than just at the time that the trust was created or assets were added).

If a settlor is or becomes a long-term resident, this means that the worldwide assets of the trust will be subject to IHT unless or until the settlor ceases to be a long term resident (so that the 'tail' described above will also apply to trusts). If the settlor dies, the status of the trust will depend on the settlor's status at the time of their death.

Most trusts, except where there is a "qualifying interest in possession" (a QIIP – more on that below) will be subject to the IHT "relevant property regime", where there is an IHT charge of up to 6% on every 10th anniversary of the trust and a proportionate charge if assets leave the trust between 10 year anniversaries. A proportionate charge will also apply if assets which were within

the scope of IHT become excluded property because the settlor ceases to be a long-term resident. This 'exit tax' is a new feature which could extend to catch trusts whose settlors became non-UK resident as far back as the 2022/2023 tax year.

In addition, if the settlor of the trust is a long-term resident and can benefit from the trust, the trust will also be caught by the "gift with reservation of benefit" rules, so that the worldwide assets of the trust will be exposed to a 40% IHT charge in the event of the settlor's death (in addition to any charges under the relevant property regime). However, in a welcome concession to the non-dom community, the reservation of benefit rules will not apply to non-UK assets held by trusts settled by non-doms before 30 October 2024, even if the settlor continues to benefit.

If a beneficiary has a QIIP in a trust (in broad terms, where the beneficiary - the life tenant - has the right to receive the income from the trust and certain other conditions are met), the life tenant is deemed to be the owner of the trust assets for IHT purposes. The relevant property regime of 10 yearly and exit charges does not therefore apply and instead the trust assets are subject to a 40% IHT charge on the death of the life tenant. Under the current IHT regime, non-UK assets held in a QIIP trust settled by a non-dom are outside the scope of IHT even if the life tenant is UK domiciled or deemed domiciled.

Under the new regime, concessionary treatment will apply to existing QIIP trusts settled by non-doms that held assets outside the scope of IHT immediately before 30 October 2024. Those trusts will be not be subject to IHT when the QIIP comes to an end or on the death of the life tenant. However, after the existing QIIP ends, the IHT status of the trust will then depend on the settlor's status from time to time (or at the time of the settlor's death).

For new QIIP trusts made after 30 October 2024, the trust assets will still be deemed to belong to the life tenant for IHT purposes and will be subject to a 40% IHT charge in the event of the life tenant's death unless neither the settlor nor the life tenant are long-term residents at the relevant time. In practice, the impact of this is likely to be relatively limited because new QIIP Trusts can only be created on death (or in some other very narrow circumstances).

A footnote on domicile

The concept of domicile itself is not being abolished – the proposed changes simply mean that it will no longer be a relevant factor for UK tax purposes.

Domicile remains a connecting factor in many other contexts, such as succession and family law.

AUTHORS

WRITTEN BY OUR TAX SPECIALISTS AT PAYNE HICKS BEACH

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