Introduction

Welcome to the 2016 Budget and Finance Bill edition of our ‘Non-dom newsletter’.

This issue contains a summary of what we know now and what we still need to know, following the publication of Finance Bill 2016.

If you would like to discuss any of the issues raised in this Newsletter, please get in touch - for contacts, [click here].

Finance Bill edition: The Finance Bill is out, but not for non-doms

Finance Bill 2016 (FB 16) was published on 24 March and the main news for non-doms was ‘there is no news’. In fact, all of the changes to the taxation of non-doms have now been postponed until Finance Bill 2017. The postponement of the legislation was actually contained in the Budget announcements the previous week, and, while it is frustrating to have to wait for more details, this is actually good news.

Previously, the intention was to include the main changes to non-dom taxation in FB 16 and postpone the provisions giving special treatment to trusts until Finance Bill 2017. This would have left us in the uncomfortable position of having a law which stated that s.86 (the provision which taxes gains in settlor interested trusts on the settlor) would apply to non-doms with effect from 6 April 2017, with only a promise of further provisions to limit the impact. It is, in our view, much better to introduce all the provisions together to ensure that they fit together and produce the intended result. It is rumoured we may have further news from HMRC in late April/mid May; if that arrives we will update you via this newsletter.

There was one very significant announcement in the Budget. Those who become deemed-dom on 6 April 2017 will be entitled to capital gains tax rebasing of their offshore assets, as well as some sort of transitional provisions for their offshore funds. It is good to see, here, that the Government has listened to the concerns of advisers. However, with no detailed provisions having been published, we are left to speculate precisely what this means. [See below] for more detail on this and what we know so far. For the time being the watchword for non-doms remains ‘patience’.
Response to consultation: Latest update

We understand that the response to the consultation document dated 30 September is still being considered by HM Treasury and that it is hoped that a response document can be published in April or May. If this timetable is not met, publication will have to wait until after the EU referendum on 23 June.

Private Equity rules for non-doms: An update

As mentioned in February’s newsletter, in addition to the main changes to the taxation of non-doms, the Summer Budget in 2015 introduced significant changes to the taxation of carried interest.

Legislation in FB 16 introduces one new measure which will help reduce the impact of these changes for some non-UK domiciled individuals to a limited extent. Where amounts of carry are treated as income under the new disguised investment management fees rules, these amounts will generally be taxable on an arising basis. However, the Bill introduces a provision to allow those arriving in the UK who have been non-UK resident for at least five tax years to be taxable on the remittance basis where carry received is in respect of foreign pre-arrival services and conditions are met. These provisions will apply to such individuals for the first four tax years of UK residence.

Action needed

Although the precise details of the non-dom changes are not yet known, non-UK domiciled individuals should start to review their circumstances and consider the benefits of taking action ahead of 6 April 2017. The delay to the publication of the detail should not deter individuals from considering their position as soon as possible, with a view to action once more is known. Click here for a suggested action list. Indeed, the delay means the window for action will be even smaller and it is imperative that non-doms do their homework now. Non-doms and offshore trustees must ensure that: (i) all information is to hand and properly documented, including inherent gains; (ii) as far as possible, they have a clear understanding of the impact of the new rules on their position.

Across the globe?

In our series of looking at jurisdictions across the globe, we turn to Jersey.

Jersey

Jersey is a 45 square mile island nestled in the Bay of St Malo, a 40 minute flight from London and a 60 - 90 minute flight from most other major UK cities. Although the island is constitutionally separate from the UK, it benefits from close ties to the UK as a Crown Dependency.

Jersey offers its inhabitants a safe and relaxed island lifestyle, typified with beaches, picturesque cliff trails and rolling valleys. This is complemented by an array of Michelin starred restaurants and bars as well as both UK high street and boutique shops. The Island also benefits from very high standards of education and healthcare.

The standard rate of income tax in Jersey is 20%. There is a beneficial regime available to High Net Worth Individuals (HNWI) whereby income in excess of £625,000 is taxed at 1%. It is necessary to apply to the Population Office to benefit from this regime prior to taking up residence in Jersey. Pre-immigration structuring can effectively cap a HNWI’s annual Jersey income tax liability at £125,000.

Business income tax is charged at 0% for most companies, with a 10% rate existing for certain regulated financial services companies and a 20% rate for Jersey utility and property companies.
Goods and Services Tax is charged at 5%. No taxes are levied on capital gains, inheritance or death, other than stamp duty relating to probate.

The island has established itself as a top tier Offshore Financial Centre and many international banks, wealth and asset managers and fiduciary service providers are present in the island. Business in Jersey is run on well-established law and is overseen by high standards of financial regulation.

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Useful links

► Joint CIOT, ICAEW, STEP and the Law Society discussion paper - click here
► Policy document and draft Income Tax and CGT legislation published 2 February - click here
► Policy document and draft inheritance tax (IHT) legislation published 9 December - click here
► Consultation document published 30 September - click here
► Previous versions of this newsletter are available - click here
► HMRC’s Technical Briefing on the main changes to non-dom regime - click here
► HMRC’s Technical Briefing on changes to IHT for UK property - click here
► HMRC’s 15 October 2015 announcement on loan collateral - click here
► Questions - for contacts click here
Expected timetable of main provisions

- Policy announced: 8 July 2015
- Informal consultation meetings with interested parties: July and August 2015
- Consultation document published (including some draft legislation): 30 September 2015
- Consultation closes: 11 November 2015
- Further draft legislation published for consultation: February 2016
- Finance Bill Consultation closes: 2 March 2016
- Budget: 16 March 2016
- Consultation responses published: Spring/Summer 2016
- Updated draft legislation published: Winter 2016
- Draft Finance Bill published: March 2017
- New rules come into force: 6 April 2017
- Bill makes its way through Parliament/Committee stages: April/July 2017
- Bill receives Royal Assent: July 2017
Act now

The changes noted in the consultation document will only come into effect from 6 April 2017. But the clear message to non-doms is ‘act now’. Non-doms should review their position in light of the further details now provided. Potential action points include:

► Consider impact of rebasing rule and how helpful this may be in the circumstances of investment holders.
► Review and confirm domicile status and, in particular, the domicile of origin of family members.
► For those resident and non-domiciled in the UK, consider establishing and funding trusts ahead of 6 April 2017.
► For those with existing trusts, review their terms and assets. For example, consider rebasing and extracting assets which provide a benefit (e.g. homes or luxury assets) outside the trust structure.
► For those holding carry in trusts, consider whether this is now the most appropriate structure.
► If assets are owned in a corporate structure but not via a trust, consider the potential introduction of a trust.
► For those who have left the UK and expect to be non-resident for less than five years, consider timing of return to the UK.
► Capital losses are likely to be increasingly accessible moving forward so investment advisers need to look at investment portfolios on a wider basis.
► Plan now for periods outside the UK – as they will need to be for six years to breach the deemed-dom status.
► Those with ‘mixed marriages’ (i.e. UK dom of origin spouse and non-UK dom origin spouse) may wish to consider allocation of assets, who establishes family trust etc. where the spouse with a UK dom of origin has a non-UK dom of choice. There is premium on having a spouse with a non-UK domicile of origin.
► Those becoming deemed domiciled on 6 April 2017 may wish to consider whether it is appropriate to make PETs ahead of that date.
► Individuals may wish to review their investments in UK trusts, especially where both UK and non-UK income currently arises to the same trustees.
► See also the action list found in issue one of our non-dom newsletter.
The Budget contained two big announcements for non-doms. First, that all the changes to non-dom taxation would be postponed until Finance Bill 2017 and, second, that a form of rebasing would be introduced for those becoming deemed domiciled on 6 April 2017. In addition, we now know there will be some form of transitional rule for offshore funds, also for those becoming deemed dom in 2017.

Where does this leave us? Was FB 16 a non-event for non-doms or a game changer? The truth is somewhere in between. It would be easy to 'wait and see' but as we explain below, this may not always be the right decision. In terms of the main changes to the taxation of non-doms, the legislation published on 2 February is still our most recent, concrete information. The new announcements at the time of the Budget were very significant, but the information is limited. More details on this are needed as soon as possible to allow people to take appropriate action, if necessary.

With the delay to the publication of any further detail, below we consider what, in our view, is unlikely to change and what is still 'up for grabs'.

The story so far

The first message is that delay in detail will not mean delay in implementation. HMRC is committed to 'D Day' being 6 April 2017 and we do not expect this timetable to slip.

‘Deemed domicile’ rule

No changes are expected to the deemed domicile rule, as announced. An individual with a non-UK domicile will be treated as deemed domiciled in the UK once he has been resident in the UK for 15 out of the previous 20 tax years. Split years will count as years of residence for this purpose.

Individuals born in the UK with a UK domicile of origin (returning doms) will be deemed domiciled in the UK when they are resident here.

Deemed domiciled individuals will not be able to access the remittance basis and will be taxable on the arising basis on all the foreign income and gains that arise in their own name. There will be some form of rebasing for foreign assets, but the details of this remain unclear (see below). In addition, we know there will be a special tax treatment for trusts set up by deemed dom individuals at a time before they became deemed dom (see below).

We also know such individuals will be subject to inheritance tax on their worldwide estates. There will also be an extension to the period an individual remains deemed domiciled after leaving the UK – to align the inheritance tax deemed dom provisions new deemed dom provisions for income and capital gains tax.

In addition, for non-doms who are not deemed-dom, UK residential property held by offshore companies and or trusts will come within the UK inheritance tax net from 6 April 2017. The mechanism for this is as yet unknown, as is the extent of the transitional provisions to allow individuals to unwind such structures.

The known unknowns...

Rebasing

We now know that for capital gains there will be some form of rebasing for foreign situs assets, but it is not yet clear how this will operate. One of the biggest outstanding questions must be whether this rebasing to April 2017 will apply only to those who become deemed domiciled on 6 April 2017 (as the wording in the red book implies) or to all becoming deemed domiciled after this date.

It would seem odd, in our view, to extend this concession only to those becoming deemed domiciled immediately while denying it to those becoming domiciled later.
Also unclear at this stage is whether the rebasing will apply for all purposes or just for the purpose of the arising basis, with the rebased portion of the gain remaining taxable on the remittance basis.

Understanding how this will operate will be crucial. To illustrate why, let’s consider a relatively straightforward example. Mr A has shares in Overseas Co, which he acquired for £100 of clean capital back in the year 2000. Assume the shares are worth £1000 on 6 April 2017. If Mr A sells his shares that day then, if rebasing applies to all gains, Mr A can remit the proceeds to the UK with no UK tax consequences. However, if the gain remains taxable on the remittance basis, Mr will need to keep the whole proceeds outside the UK to avoid becoming taxable on the gain.

Assume, instead, that Mr A holds onto the shares for another year until 6 April 2018, by which point the shares are worth £1,100. Now Mr A has a gain of £100 which is subject to UK tax on the arising basis. He may also have a gain of £900 subject to tax on the remittance basis. If this is the case, he would still need to retain all the proceeds overseas, since the mixed fund ordering rules will treat the remittance basis gain as the first funds to leave the account. This could present serious problems for those with a UK tax bill to pay (on the arising gain) leading to a further possible tax bill, should they remit proceeds to pay it. If, instead, the rebasing applies for all purposes, Mr A can remit the whole amount, since the £100 arising basis gain will be taxable regardless of whether the funds are brought to the UK.

To prevent these difficulties with the mixed fund rules, Mr A may choose to sell his shares on or close to the rebasing date. This will of course have associated costs and risks, and any decision will ultimately need to be influenced as much by investment considerations as by tax ones. It is also unclear whether the rebasing will apply to those returning to the UK having been born here with a UK domicile of origin.

Is rebasing to apply only to assets held by an individual personally or also to assets held in trust? If the latter, how will the new provisions interact with the 2008 rebasing provisions? If the latter, will taxpayers wish to remove assets from trust before 6 April 2017? And what price rebasing? Will taxpayers who wish to rebase have to furnish a lot of information to HMRC and will they be prepared to do so?

More details of precisely how the rebasing provision will apply and to who are needed urgently, to allow individuals to begin considering their position.

**Protection for offshore trusts**

We know that the Government intends to give some form of protection to offshore trusts established by non-UK domiciled individuals before they became domiciled. The policy intention (we understand) is to give protection for foreign income and gains, while continuing to tax UK income. The position with regard to UK gains is a little less clear.

The consultation document published last September suggested that this would be achieved by taxing settlors only in respect of benefits received from such trusts. However, under the proposals, settlors would be taxed on such benefits whether or not the trust in question contained any income or capital gains. In addition, UK income in the structure would continue to be taxable.

The proposals met with general disapproval from tax professionals, and professional bodies, STEP, CIOT, ICAEW and the Law Society combined to produce a discussion paper which suggested an alternative method of taxing benefits, based on a modified version of the transfer of assets abroad rules. We understand that the method of taxing benefits out of trust is still under review.

For those likely to become deemed domiciled in April, the lack of information may be frustrating, but now is the time to start considering options with regard to trusts – whether that be existing trusts or new ones. The process to settle a trust and select trustees can be a lengthy one, so the advice might be start thinking now, but act later.

**UK residential property**

After the announcement at the time of the Summer Budget that the Government intended to bring all UK residential property owned by non-UK domiciled individuals directly or indirectly into the inheritance tax net, there has been little further detail.

The technical note published at the time of the announcement set out the intention to amend the existing rules to provide that shares of offshore companies or similar structures will no longer be excluded property to the extent that they derive their value from UK residential property.
UK residential property for this purpose would follow the definition for non-residents capital gains tax. The note also promised amendments to the relevant property regime.

At the time, the Government indicated it would ‘consider the costs associated with de-enveloping’ as part of the consultation. This, together with later discussions with HMRC, has led many to hope that there may be some form of transitional relief for those looking to unwind structures in view of the new rules.

Again, it is very frustrating for those affected that there is still no real detail on these plans. Unwinding offshore holding structures for UK residential property is likely to be a costly and time consuming business. For those who wish to consider this, the advice again would be to start talking to their trustees and advisers now, but to wait for more detail before acting.

The ongoing silence may suggest that the hope of some form of relief is becoming more remote.

**When will we know more?**

A Government response to the consultation on the main changes to the taxation of non-UK domiciled individuals is still outstanding. We understand that HM Treasury hopes to publish this in April or May and that an initial consultation on inheritance tax and UK residential property is expected at around the same time. However, we understand that this timetable may slip, and if it does, the purdah required by the EU referendum may lead to further details not being available until July or even September.

What is clear is that we are unlikely to have a detailed picture of how the rules will operate until draft clauses are published at the time of Autumn Statement 2016 and possibly not even until the publication of the Finance Bill 2017. Non-doms who are likely to be affected by the changes cannot wait until then to begin considering their position.

**A game changer**

The on-going delay is in itself a game changer. Non-doms now know that they will have only a short time to digest really complex legislation, to reach a decision and implement it. This will only be possible if all information has been collected and analysed in advance and key decision thought through. For example, trustees must know what assets (e.g. overseas villas) need to be extracted from trust, how to do it and the tax cost. Trustees must know which beneficiaries will be deemed domiciled on 5 April 2017 and which beneficiaries are non-UK resident. Individuals must know the gains inherent in their portfolio - they shouldn't necessarily wait to take gains where investment advice is to do so and not just mechanically wait on a promise of rebasing which may prove illusory or unattractive. The non-doms who have the most to fear are those who don't do their homework now. Perhaps it is just like school after all!
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