

**DOMICILE– UK
UK INHERITANCE TAX ISSUES
CHANGES TO BE EFFECTIVE FROM 6 APRIL 2017**

1. UK Domicile of Origin – Settlor Interested Trust

HMRC have confirmed that certain changes to the domicile rules will apply **from 6 April 2017**.

For example, let us assume:-

- an individual **has a UK domicile of origin** due to having been born in the UK with a UK domiciled father;
- he/she has become domiciled elsewhere, under a domicile of choice;
- he/she has created an offshore discretionary trust **in which he/she can benefit**, funded with non-UK assets;
- subsequently he/she decides to return to live in the UK.

Up to 5 April 2017, in these circumstances, the individual's UK domicile of origin would usually revive but the excluded property status of the trust would continue for the lifetime of the trust provided it was invested in non-UK property. Therefore no Inheritance Taxes would apply to the trust assets.

However, the following consequences will apply from 6 April 2017, in circumstances when the settlor is or becomes UK resident.

- **The Excluded Property status** of the trust will no longer apply because, instead of considering the domicile of the settlor at the date the trust assets were settled, it will be relevant to look at the domicile of the settlor at the date of each capital distribution and at each 10 year anniversary date. Therefore the trustees will be liable to Inheritance Tax (IHT) at each 10 year anniversary of the trust's creation and IHT exit charges will apply when capital is paid out.
- The 10 year anniversary charge will be based on the full market value of the trust fund at that anniversary date, with a maximum tax charge of 6%, subject to any relevant reliefs, but the charge will be apportioned based on the period of UK residence of the settlor during the previous 10 years. No exit charge would apply at the point when/if the settlor becomes non-resident again. However, IHT exit charges will apply when capital is distributed from the trust after the property has become 'relevant' property as well as after any 10 year anniversary.

- If the settlor dies whilst resident in the UK he will cease to be resident in the UK by virtue of his death. It would appear that the settlement will only return to its excluded property status if the settlor had retained his foreign domicile of choice at the date of death. This may be difficult to establish if he/she dies while resident in the UK. If he dies when UK domiciled, then we believe that the trust will continue to be liable to 10 year Inheritance Tax anniversary charges and Inheritance Tax exit charges.
- In addition to this, while the settlor remains UK resident and domiciled and can benefit from the trust, the whole value of the trust fund will form part of his/her estate on his/her death under the Gift with Reservation of Benefit rules, and liable to UK Inheritance Tax at a maximum of 40%. Therefore double taxation will apply.

2. UK Domicile of Origin – Trust in which the Settlor cannot benefit

Again let us assume that the circumstances are the same as the first example except that the settlor cannot benefit from the trust. In this case, from 6 April 2017, for as long as the settlor is resident in the UK, the trust will be within a charge to IHT on each 10 Year Anniversary, pro-rated for the period the settlor is UK domiciled in the 10 year period. If the settlor becomes non-resident again, then once his deemed UK domicile period has come to an end, the trust will no longer be liable to these 10 year anniversary charges.

It would seem that the 10 year anniversary charges on the trustees will continue to apply after the death of the settlor if the settlor was UK domiciled at the date of his death, but not if at that date he/she had retained his foreign domicile.

As the settlor cannot benefit from the trust there will be no Gift with Reservation of Benefit charge in respect of the value of the trust and therefore no Inheritance Tax liability thereon on his estate on his death.

3. Non- UK Domicile of Origin

The above changes will not apply to trusts established by non-doms before they become deemed-domiciled under the 15/20 test, i.e. where the settlor of the trust had a domicile of origin **outside** the UK when the settlement was made and funded, even though the settlor has become deemed UK domiciled due to having been resident in the UK for 15 out of 20 years. In such circumstances the Excluded Property status of the trust will continue to apply if the trust is invested wholly in non-UK assets at the relevant date. The value of the trust will not form part of the settlor's estate on death for UK Inheritance Tax purposes, even if it is a settlor interested trust. It is important that no funds are added since the settlor has become deemed UK domiciled.



Crowe Clark Whitehill LLC™

Trust Income & Gains – Income Tax & Capital Gains Tax (CGT)

Trust income & gains will not automatically become taxable on the settlor, even if he can benefit from the trust.

From 6 April 2017 we understand that **all benefits** from an offshore trust will be liable to Income Tax on the beneficiaries to the extent that they can be matched with untaxed trust income or unmatched gains.

Any payment made to a close family member of the settlor from 6 April 2017 that is matched to existing trust income or gains will be taxed on the settlor unless the recipient is taxed personally.

Capital payments made to a non-UK resident beneficiary will no longer reduce the pool of trust gains, regardless of the domicile of the settlor. This ensures gains cannot be 'washed out' by making distributions to non-resident beneficiaries, except in the year the trust is wound up.

Rules will be introduced to prevent a non-UK resident beneficiary, who is not a close family member, from receiving a benefit from the trust and then giving or lending it to a UK resident beneficiary within the following three years.

If you would like to know more then please contact

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