

Domicile – A UK Perspective

It is important to ascertain your domicile status, as this will help determine if there are any UK Inheritance Tax implications relating to any lifetime gifts you may have made and also your estate on death.

Domicile – The concept

This is a general law concept. Broadly speaking an individual is domiciled in the country in which he has his permanent home.

Domicile is distinct from nationality or residence. An individual may be resident in more than one country but at any given time he can be domiciled in one only. Generally speaking an individual is domiciled in the country or state in which he has his permanent home.

There are three forms of domicile for UK purposes:

Domicile of Origin – an individual acquires his/her father's domicile at birth. This is not necessarily the domicile of the country where the individual or his father was born. This domicile is retained until the individual acquires a different domicile – of choice or of dependency.

Domicile of Dependency – Until one attains legal capacity to change one's domicile, which in England and the Isle of Man is 16 years of age, domicile will follow that of the person on whom one is legally dependent, i.e. one's father. If one's father's domicile changes during the individual's minority the individual automatically acquires the same domicile, in place of the domicile of origin.

Domicile – A UK Perspective (continued)

On marriage, if before 1 January 1974, a woman automatically acquired the domicile of her husband – a domicile of dependency - and retained this not only whilst her husband was alive and she was legally married to him but also during widowhood or following divorce unless she herself acquired a new domicile of choice. Following a change in the law the domicile of a married woman is no longer necessarily the same as her husband's; it is decided by reference to the same factors as apply in the case of any other individual capable of having an independent domicile. However where immediately before 1.1.74 a woman had her husband's domicile of dependency, she retains that domicile until it is changed by the acquisition or revival of another domicile.

Domicile of Choice – A domicile of choice replaces a domicile of origin or dependency. In order to acquire a domicile of choice an individual must sever ties with his country of domicile of origin or dependency and settle in another country with the clear intention of making his permanent home there. Living in a country for a long time, although important, is not enough in itself to prove one has acquired a new domicile.

A person who is UK domiciled is liable to UK Inheritance Tax on his worldwide estate, subject to the statutory exemptions. A person who is not UK domiciled is liable to UK Inheritance Tax (IHT) only on UK estate; all non-UK estate is "excluded property" and is outside a charge to IHT. However, from 6 April 2017 the ownership by a non-domiciled individual of a UK residential property indirectly through an offshore structure such as an offshore company or trust will no longer benefit from excluded property status. Instead the UK residential property will be subject to IHT.

Deemed UK Domicile

Up until 5 April 2017 an individual who has been resident for 17 out of the previous 20 years will automatically become deemed UK domiciled from the 18th year of assessment, for UK Inheritance Tax only.

Deemed UK Domicile - (continued)

However from 6 April 2017 onwards an individual who has been UK resident for 15 out of the previous 20 years will automatically become deemed UK domiciled from the beginning of the 16th year for Inheritance Tax, Capital Gains Tax and for Income Tax purposes. Years spent in the UK while a person is under the age of 18 will count as years of residence for these purposes. The 15/20 test will also apply to children born in the UK to non-domiciled parents. If they are continuously UK resident as they grow up, they will become deemed UK domiciled by the time they reach 16 years old. Split years of residence under the statutory residence test will count as a full year's residence for the 15/20 test.

Under the new rules, individuals who have become deemed domiciled in the UK who then leave the UK will remain deemed domiciled in the UK for Inheritance Tax purposes for a further 3 consecutive years after leaving and for 6 years for Income Tax and Capital Gains Tax purposes.

Capital Gains Tax

A deemed UK domiciled individual's offshore assets may be rebased at 5 April 2017, in some circumstances. These are that the individual had previously paid the remittance basis charge in any year before 6 April 2017. Those who become deemed domiciled after April 2017 or are born in the UK with a UK domicile of origin will not be able to rebase their assets or take advantage of the segregation of mixed funds mentioned below.

For those who can rebase their assets, foreign gains made after 6 April 2017 will become taxable only insofar as the gain has arisen in respect of the period after 6 April 2017; gains arising in respect of the period up to 5 April 2017 will be able to be remitted without a CGT charge but only if the asset was originally purchased with "clean" capital. Otherwise the foreign gain and/or foreign income element used to purchase those assets will be taxed on a remittance basis. This protection is limited to those foreign situs assets owned at the date of the Budget 2016, on 16 March 2016.

Capital Gains Tax – (continued)

An individual born in the UK with a domicile of origin in the UK will no longer be able to claim non-UK domiciliary status for Income Tax or Capital Gains Tax purposes whilst living in the UK, even if he/she had previously left the UK and acquired a domicile of choice in another country. On return to the UK such an individual's domicile of origin will immediately revive. For Inheritance Tax, however, he/she will be treated as deemed UK domiciled in the tax year only if resident in one of the two previous tax years as well. In such circumstances rebasing of assets for Capital Gains Tax purposes will not be available.

Mixed Funds

Where a non-domiciled individual owns offshore assets or accounts funded partly by untaxed foreign income and/or foreign gains and taxed foreign income &/or gains and clean capital, currently the untaxed funds are considered to be remitted first.

A concession will apply under which the deemed-domiciled individual will be able to rearrange his/her mixed funds overseas to separate them into their constituent parts. This can be done only during the two years from April 2017 to April 2019 but the option to cleanse a mixed fund will not be available to an individual who is unable to determine the component parts of the mixed fund.

Spouse Exemption

Where both spouses are either domiciled in the UK or not domiciled in the UK then transfers of assets between them will be exempt from IHT.

Where one spouse is UK domiciled and the other is not, transfers from the UK domiciled spouse to the non-UK domiciled spouse benefit only from a £325,000 lifetime exemption, with no drop out from accumulation after seven years. From 6 April 2013 it is possible for a non-UK domiciled individual who is married to or in a civil partnership with a UK domiciled person to elect to become UK domiciled person for IHT purposes. However, the downside of such an election would be to bring all the joint assets on a worldwide basis into a charge to IHT on the second death. See our note entitled "Gifts Between Spouses" for further information on this topic.



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