

Draft Legislation on Residence and Domicile

1. On 18 January 2008, HMRC finally published the draft legislation and explanatory notes in relation to the proposed changes to the UK's residence and domicile tax rules. The draft legislation, the explanatory notes and frequently asked questions (FAQs) can be found on HMRC's website under the following link: <http://www.hmrc.gov.uk/cnr/res-dom-tax-amends.htm>. As the legislation is still in draft form, a number of issues will need to be clarified and changes may also be made as the draft clauses are debated.

The legislation is due to be effective from 6 April 2008 and it is vital that anyone who is affected by the new rules seeks advice prior to that date to ensure their arrangements are as efficient as possible.

2. The following is a summary of some of the most important changes:

Cost of use of the remittance basis

- There will be a £30,000 charge for taxpayers who have been UK resident for seven out of the previous nine tax years if they wish to continue to claim the remittance basis. This charge is in addition to any other tax liability for the tax year in question (for example on any remittances made). Tax years spent in the UK prior to the legislation coming into force will be included in the total number of years spent in the UK so that anyone who arrived in the UK in March 2002 will be subject to the new charge from 6 April 2008. Residence in part of a tax year will count as a full year. The £30,000 charge does not apply if the unremitted income or gains is less than £1,000.
- Those who make a claim to be taxed on the remittance basis will lose their entitlement to various personal tax allowances e.g. the personal income tax allowance and capital gains tax annual exemption. This applies also to those non-domiciled taxpayers who have been UK resident for less than seven years. The loss of allowances will not apply if the unremitted income or gains is less than £1,000.
- Those entitled to claim the remittance basis will be able to choose from one tax year to another whether they wish to be taxed on the remittance basis i.e. can 'opt in and opt out' of the charge. Those who choose not to use the remittance basis one tax year will be taxed on a world-wide basis for that year. Unfortunately, income and gains from previous tax years when a remittance basis claim was made are taxable if remitted in a later year when the remittance basis is not claimed.

The definition of a remittance

- The definition of what constitutes a remittance has been extended in several ways. From 6 April 2008, if non-UK investment income is used to purchase an asset outside the UK (for example a car or art) which is thereafter brought to the UK, this will be considered a taxable remittance of the income which was used to purchase the asset. Any assets already in the UK as at 6 April 2008 may be affected.
- The draft legislation also contains rules to be used in order to identify remittances from mixed funds.

- Under the new legislation, if a UK resident, non-domiciled individual gifts non-UK income to a “relevant person” outside the UK and that person remits that gift to the UK, a tax charge will arise to the donor when the remittance is made. A “relevant person” includes various relatives and a couple living together as if they were married or civil partners. Settlers of trusts are also connected to their trustees as relevant persons.
- From 6 April 2008 overseas investment income remitted will be taxable even if the source of the income has ceased in a previous tax year. Where an individual has used the old style planning (cessation of source rules) and not yet remitted the funds from sources ceased before 6 April 2007 to the UK, advice should be sought to consider remitting those funds before 6 April 2008.
- It seems likely that offshore mortgages will be affected by the extension of the definition of a remittance.

Attribution of trust gains

- The draft legislation contains wide ranging provisions designed to stop trust gains from being able to be remitted to the UK free of tax. This is through the extension of provisions currently within Sections 86 and 87 of TCGA 1992 which operate to tax UK resident and domiciled settlors and beneficiaries on gains of offshore trusts to include non-domiciled settlors and beneficiaries. These rules will have retrospective effect as all gains realised in an offshore trust since 17 March 1998, which have not yet been paid out to the beneficiaries, will be used to match against capital payments after. Capital payments made in previous tax years could potentially also result in a tax liability in certain situations. The draft provisions in this area are extensive, and as a result any UK resident but non-domiciled settlors or beneficiaries of offshore trusts should take advice as a matter of urgency.
- There will also be an obligation to notify HMRC of the existence of new and already existing trusts.

Attribution of gains to members of non-resident companies

- The anti avoidance rules which currently operate to tax UK resident and domiciled individuals on gains in overseas close companies are to be extended to non-domiciled participators of such companies. The remittance basis should be available if appropriate as above provided that the gains are on non-UK situs assets.
3. The consultation period ends on 28 February 2008. It is anticipated that the changes will take effect from 6 April 2008. All existing planning should therefore be reviewed as a matter of urgency.

Please note that this summary is intended for general guidance only and does not constitute legal advice.

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