Resident non-domiciles: the end of the line?

Personal tax



20 March 2024

Following the Spring Budget 2024, we consider the abolition to the non-dom regime, what this means for affected taxpayers, and points to consider in advance of 6 April 2025.

Key Points

What is the issue?

The Chancellor has proposed to replace the taxation of non-doms with a ‘modernised residence-based regime that is simpler, fairer and more competitive’.

What does it mean for me?

As well as the new four-year foreign income and gains regime, the Budget announcements also set out proposals for transitional rules and a wholesale

overhaul of how inheritance tax will apply to non-UK assets.

What can I take away?

Whilst the changes are fundamental for all non-doms and connected structures, there is a lot of uncertainty on the exact operation of the rules, particularly relating to inheritance tax.

Following a series of significant changes to the taxation of non-doms in both 2008 and 2017, the Spring Budget may have effectively signalled the end of the regime entirely from 6 April 2025.

Currently, many UK resident non-domiciled individuals elect to be subject to the ‘remittance basis of taxation’ each tax year, whereby individuals are subject to UK tax on foreign income and gains when remitted to the UK. The use of the remittance basis arguably attracts internationally mobile families and their businesses to the UK, although it has been criticised as outdated and unfair.

The Chancellor has proposed to replace it with a ‘modernised residence-based regime that is simpler, fairer and more competitive’.

As well as the new four-year foreign income and gains regime, the Budget announcements also set out proposals for transitional rules and a wholesale overhaul of how inheritance tax will apply to non-UK assets. A lot of the finer detail is still to be released and the inheritance tax proposals will be subject to consultation; however, it is clear that the transitional rules are intended to facilitate investment in the UK.

The changes announced are far-reaching, but before anyone rushes to do anything, it is worth bearing in mind that nothing will come into force until after the next General Election. While it seems certain that there will be a significant change to the taxation of non-doms, a lot can change before 6 April 2025.

New four-year rule for foreign income and gains

Arriving to the UK

For recent or new arrivals, a four-year rule comes into force:

- From 6 April 2025, the foreign income and gains regime will be available to individuals (regardless of their domicile) for their **first four tax years of tax residence** after a period of at least 10 years of non-UK residence.
- Those claiming to be taxed under the foreign income and gains regime will be fully exempt from UK tax on their foreign income and gains, even if these are remitted to the UK.
- Those arriving to the UK before 6 April 2025 may still be able to benefit from the new foreign income and gains regime if they are within their first four years of tax residency in 2025/26 (and subject to meeting the 10 years of non-UK residency condition).

See ***Bridget: the new four-year rule*** for an example of how this will work in practice.

Whilst tax exemptions are welcome news for many, the four-year period is shorter than many of the inbound tax regimes offered in other European economies; for example, Italy grants a 10 year incentive regime for new residents.

Bridget: the new four-year rule

Bridget moved to the UK after 40 years in Spain. She is non-UK domiciled and has non-UK assets. Bridget is UK tax resident in 2023/24 and plans to sell her Spanish property in 2025/26. How do the new rules affect her?

- **2023/24 and 2024/25:** Bridget is a resident non-domiciled individual, eligible for the remittance basis.
- **2025/26:** Bridget can claim exemption from tax on foreign income and gains this year, which includes the sale of her property.
- **2026/27:** This is the last year Bridget can claim the foreign income and gains regime.
- **2027/28:** Bridget will be subject to worldwide income tax and capital gains tax from this year, for as long as she is resident in the UK.

Resident non-domiciled individuals currently in the UK on or before 5 April 2025

In an attempt to ensure that existing resident non-domiciled individuals remain in the UK, there are helpful transitional rules aiming to minimise the disruption and alleviate fears of a mass exodus:

- Resident non-domiciled individuals are eligible to claim the foreign income and gains regime if they are still within their first four years of UK tax residence.
- For 2025/26 only, resident non-domiciled individuals who are not eligible to claim the foreign income and gains exemption will only be subject to UK tax on 50% of their foreign income (not foreign gains), provided the individual is not yet deemed domiciled as at 5 April 2025.
- Personally held foreign assets can be rebased to their 5 April 2019 value (for capital gains tax), provided the individual is not yet deemed domiciled as at 5 April 2025 and has claimed the remittance basis historically. This will be subject to further conditions.

In addition to the above, the government has also announced an attractive 12% tax rate on certain remittances to the UK, under a Temporary Repatriation Facility, which it estimates will result in £15 billion flowing into the UK.

The Temporary Repatriation Facility

Any individual who has historically claimed the remittance basis (prior to 6 April 2025) can remit their foreign income and gains to the UK between 6 April 2025 and 5 April 2027 and be subject to a flat 12% tax on remittances.

If the Temporary Repatriation Facility is implemented, it could represent a crucial one-off opportunity for non-doms still living in the UK. For many longer-term non-doms, the use of the remittance basis has left them with limited access to funds in the UK due to the potential 45% tax cost of remitting historic funds.

From 6 April 2027, remittances of pre-6 April 2025 foreign income and gains will be taxed at ‘normal tax rates’.

See **Reece: using the Temporary Repatriation Facility** for an example of how this works in practice.

The Temporary Repatriation Facility applies to personal foreign income and gains remitted during the Temporary Repatriation Facility period. Foreign income and gains generated in trusts pre-April 2025 are specifically excluded from the Temporary Repatriation Facility, but further clarity will be needed to understand whether a distribution from a trust pre-2025, which would normally then be considered the beneficiary's foreign income and gains, could then be eligible for the Temporary Repatriation Facility.

Reece: using the Temporary Repatriation Facility

Reece is a resident non-domiciled individual who has been in the UK for the past 20 years (i.e. he is now deemed domiciled). He has claimed the remittance basis historically and has a mixed fund account with the following sources within it:

- Untaxed relevant foreign income (2015/16): £5 million

If Reece remitted the full £5 million to the UK in 2024/25, up to £2.25 million tax would be payable. However, if he can, Reece could defer his remittance to 2025/26, and only be subject to 12% tax under the Temporary Repatriation Facility; i.e. £600k.

Protected trusts: income tax and capital gains tax

One aspect of the proposals that hasn't received as much attention in the media so far are the proposed changes to the taxation of offshore trusts. Although many observers expected that any change to the taxation of non-doms would come with an element of grandfathering for existing 'protected trust' structures, there are in fact significant changes proposed.

Currently, foreign income and gains within a protected trust settled by resident non-domiciled individuals are not subject to UK tax until a distribution is made to a UK resident beneficiary.

From 6 April 2025:

- Foreign income and gains generated whin trusts will be taxable on the settlor(s) if the trust is 'settlor-interested' as defined under current rules in force.

- Beneficiaries of existing protected trusts will continue to be subject to UK tax on distributions received from a trust with reference to pre-2025 foreign income and gains within the trust.

See ***Lucia: protected trusts*** for an example of how this works in practice.

The impact of these changes cannot be understated as they represent a radical change to the taxation of trusts.

Lucia: protected trusts

Lucia has been UK tax resident since 2000. As a resident non-domiciled individual, in January 2017 Lucia settled a protected trust with non-UK assets before becoming deemed domiciled. The beneficiaries include Lucia and her husband.

On or before 5 April 2025:

- Foreign income and gains arising in the trust are not subject to UK tax.
- Distributions are matched to stockpiled trust foreign income and gains and are taxable.

From 6 April 2025:

- Foreign income and gains arising to the trust are immediately taxable on Lucia at up to 45% tax.
- Distributions matched to pre-April 2025 stockpiled trust foreign income and gains are taxable.

Inheritance tax

Among the areas impacted by the change to the non-dom policy is inheritance tax. These wide-ranging changes include a new residence-based system for inheritance tax, the details of which will be subject to further consultation.

It is expected that UK assets will remain subject to inheritance tax obligations, irrespective of one’s tax residency status. However, for non-UK assets, inheritance tax liability will depend on the residence (rather than domicile) of the individual, with a ‘cliff-edge’ after 10 years of residence, whereby worldwide assets will fall into the

scope of inheritance tax (and remain in scope for the first 10 years of non-residence).

Given that non-doms are not currently subject to worldwide inheritance tax from their fourth year of non-UK residence, the increase to 10 years would significantly increase their tax exposure.

These proposals are subject to consultation, and the government has indicated that other ‘connecting factors’ may also determine whether an individual is within the scope of the new rules. This could mean that in some cases individuals may be subject to inheritance tax on worldwide assets, even if they are non-UK resident for more than 10 years.

It will be interesting to see how this develops as we begin to see further detail trickling through following the consultation.

Inheritance tax and trusts

Another part of the change to be aware of is the inheritance tax impact on trusts. Although this will again be subject to consultation, the current proposal is that the treatment of trusts will now follow the inheritance tax status of the settlor at the time of each potential inheritance tax event (such as settlement and 10 yearly charges).

Helpfully, the government has clarified that non-UK assets in trusts settled by non-doms before 6 April 2025 should continue to be excluded from inheritance tax. There is, therefore, still an opportunity for current non-doms to protect their non-UK assets from inheritance tax permanently, by settling onto trust. However, the settlor may then be subject to tax on the trust’s foreign income and gains as it arises after 6 April 2025.

Summary

Whilst the changes are fundamental for all non-doms and connected structures, there is a lot of uncertainty on the exact operation of the rules, particularly relating to inheritance tax. Importantly, the general election, which is due before January 2025, is likely to have a bearing on the final form the non-dom changes take.

It is not quite the ‘end of the line’ for non-doms and their families, but it is certainly a more challenging and uncertain tax landscape.

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