Inheritance tax and foreign doms: a welcome simplification?

Inheritance tax and trusts | Personal tax | International Tax



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We consider the fundamental shift from domicile to residence as the key inheritance tax test, and the mechanics of the long-term residency rules.

Key Points

What is the issue?

Significant reforms to UK inheritance tax rules were introduced by the Finance Act 2025, primarily affecting long-term UK residents, replacing domicile with residence as the key connecting factor.

What does it mean to me?

These changes introduce a long-term resident test, establish a ten-year residence rule with a transitional tail period, and simplify the treatment of foreign domiciles

and trusts.

What can I take away?

Transitional provisions provide relief for those leaving on or before April 2025, and special rules apply to younger individuals.

The 2024 Budget announced several major changes for inheritance tax, marking a radical reform of this tax akin to the 2006 changes for trusts. Although the seven-year potentially exempt transfers rule and normal expenditure out of income exemption remain intact, Finance Act 2025 made fundamental changes to the taxation of both non-doms living in the UK long term and those who have been non-UK resident for many years. These changes extended to income tax and capital gains tax (outside the scope of this article), as well as inheritance tax, and came into effect from 6 April 2025.

This article focuses on the inheritance tax position after April 2025. Practitioners will still have to deal with estates where the death took place before April 2025 or excluded property trusts where the settlor died before April 2025. Trustees will therefore need to remain familiar with the old rules, especially the complex rules on resettlements in Inheritance Tax Act 1984 ss 82/82A which were repealed with effect from April 2025 where the settlor is still alive but are still relevant to earlier settlements.

Inheritance tax position from 6 April 2025

The new inheritance tax regime applies to all chargeable events from 6 April 2025 except that trusts where settlors died before April 2025 are generally governed by the old regime (see tinyurl.com/yc6tvrtb).

Overview

The difficulty that the government faced when considering inheritance tax is that if, as proposed in March 2024, domicile is no longer a connecting factor for any tax purpose, then a residence test alone is insufficient. After all, it would be odd to tax someone on their worldwide estate if they died when they had only just become UK resident for the first time. It would be equally odd not to tax them at all if they died

just after leaving the UK having lived here all their lives.

Some sort of transitional period was therefore required. In the end, the government settled on a ten-year period of inheritance tax exemption for people newly arrived in the UK, and a tail of between three to ten years depending on how long they had stayed in the UK before they left.

Despite some criticism that this is a cliff edge forcing people to leave in their ninth year of UK residence, in the author's view these proposals represent a reasonable compromise. Moreover, a residence test is much more certain than a domicile test, particularly for those who had left the UK with a UK domicile of origin many years ago but had not finally settled anywhere else. In these circumstances, if the person had not established a domicile of choice in a particular country, their UK domicile of origin continued even if they never intended to return here.

Another welcome simplification is the abolition of the concept of a formerly domiciled resident. This applied to some born here with a UK domicile of origin, who later acquired a foreign domicile of choice and then resumed residence in the UK.

Long-term residence status

The meaning of long-term residence status is defined in Inheritance Act 1984 s 6A (as inserted by Finance Act 2025 s 44(1)(3)).

An individual is deemed to be a long-term resident in a tax year and therefore subject to inheritance tax on worldwide assets if they were tax resident in the UK for at least ten of the previous 20 tax years.

Therefore, from 6 April 2025 any foreign property (and UK open-ended investment companies and authorised unit trusts) owned outright by an individual is free of inheritance tax, provided the person (wherever domiciled) has:

- not been UK resident for any ten consecutive tax years during the 19 tax years before the tax year of the chargeable event (whether death or gift); or
- not been UK resident for at least 'the required number' of consecutive tax years ending with the tax year **before** the current tax year. The 'required number' is discussed further below.

UK residence is determined according to the statutory residence test in Finance Act 2013 Sch 45 (or under common law prior to 2013). It will never be necessary to consider years before 2004-05. Treaty non-residence does not count towards years of non-residence for the purposes of this test.

Someone who fails to satisfy the above residence criteria is a long-term resident, even if they have subsequently left the UK. Their common law domicile or deemed domicile status is irrelevant.

Therefore, a UK domiciliary who has left the UK after spending 20 years or more in the UK and is then non-UK resident for ten consecutive tax years will only then cease to be a long-term resident. They will therefore not be subject to inheritance tax on non-UK assets at the start of the 11th tax year, even if they intend to return to the UK or in fact do so. After ten consecutive years of non-residence, only the year of return and future years of residence count towards UK residence for the purposes of the inheritance tax test. The ten years of non-residence provide a complete break.

Overall, this means that a person will be a long-term resident in 2025-26 if they have been UK tax resident in ten or more of the tax years between 2005-06 and 2024-25 unless they have been non-UK resident for ten consecutive years since 2015-16 or are within the transitional provisions below.

A person who lived in the UK for, say, 20 years before leaving and was then non-resident but not for ten consecutive years, will need to be non-resident for 11 years out of the last 20 to cease to be a long-term resident.

Assets

UK assets and Sch A1 property (enveloped residential property) remain in scope of inheritance tax on the same basis as before April 2025, regardless of residence.

Also, the same exemption for Free of Tax to Residents Abroad (FOTRA) gilts applies as before April 2025; i.e. it is based solely on an individual’s non-residence in any particular year when an inheritance tax charge arises. Such gilts can be free of inheritance tax on the death of the non-resident individual even if they are still a long-term resident. Gilts can be a useful insurance policy against early death for the person who has just left.

The ‘required number’ of years

To determine the ‘required number’ of non-resident years, take the 20 tax years ending with the last tax year for which the individual was UK resident. Find the number of those tax years for which the individual was UK resident. Broadly, the time an individual remains in scope after leaving the UK is shortened when they have been resident in the UK for between ten and 19 years. The intention is to avoid a hard cliff edge for those who may want to stay, say, 13 or 14 years in the UK but do not want to have a ten-year inheritance tax tail after they leave (see Inheritance Tax Act 1984 s 6A(3)).

- Those who are resident for between ten and 13 years will remain a long-term resident for three tax years.
- This will then increase by one tax year for each additional year of UK residence. If a person was resident for 15 out of 20 tax years on leaving, they would remain a long-term resident for five years after leaving. If they were resident for 17 out of 20 tax years on leaving, they would remain in scope for seven tax years.
- Once they have been UK resident for 20 tax years, it will require ten tax years of consecutive non-residence or 11 years of non-consecutive tax years out of the previous 20 to lose their status of long-term resident. This is referred to (colloquially) as the ‘ten-year inheritance tax tail’.

Inheritance tax tail

There have been objections to the length of the inheritance tax tail, and it is certainly longer than the pre-2025 position for foreign doms.

Under the previous rules, an individual could effectively lose their deemed domicile after only three tax years of non-residence, even if they had been UK resident for many years, provided they did not return within six years of leaving (see Inheritance Tax Act 1984 s 267). However, the inheritance tax tail could be very much longer than ten years if the individual had a UK domicile of origin and was unable to prove that they had settled in a particular place.

The new legislation clarifies their position from April 2025 by setting a bright line test.

Some non-doms argue that they should not be subject to a ten-year tail under the new rules if they are poor when they leave and only make their fortune after they

leave. This seems a poor point. The UK has no exit tax and so does not tax on the basis of what people own before or after they leave.

For an individual who is 20 years old or younger immediately before the tax year of charge, the test from April 2025 is whether they have been UK resident for at least 50% of the tax years since their birth (see Inheritance Tax Act 1984 s 6B). If they were under the age of one immediately before the relevant tax year, they are not a long-term UK resident.

Lifetime gifts of excluded property by an individual who is not a long-term resident at the time of the gift remain outside the scope of inheritance tax, even if the individual dies within seven years and is then a long-term resident.

Transitional inheritance tax relief

Transitional inheritance tax relief for leavers is defined under Finance Act 2025 Sch 13 para 46. There is a transitional rule for non-domiciled or deemed domiciled individuals who are non-resident in or before the tax year 2025-26. Those individuals who are not domiciled in the UK under common law on 30 October 2024 (whether or not deemed domiciled) can effectively lose their inheritance tax tail after only three years of non-residence, provided they are not resident in 2025-26 and do not return to the UK.

If they return to the UK within ten years of leaving, the new rules will apply. In effect, then they can take advantage of the position under the old law stated above.

Although this transitional provision will not apply to individuals who are UK domiciled under common law on 30 October 2024, it does apply to formerly domiciled residents. If the individual was not a formerly domiciled resident and not deemed domiciled under s 267 (because they had been here less than 15 years by April 2025 or had lost their deemed domicile by then), they are not within the scope of inheritance tax at all provided they are non-resident in 2025-26.

This transitional provision gave a clear incentive for non-doms to leave by April 2025. For example, a non-dom who had been here for 40 years and leaves on 6 April 2026 will have an inheritance tax tail for 10 years after leaving. If that same non-dom is non-UK resident as at 6 April 2025, they will only be within scope of inheritance tax on foreign assets until 6 April 2028, provided they do not become UK

resident within 10 years of leaving.

For younger non-doms, inheritance tax may not be a practical concern; however, for the older non-dom having a shorter inheritance tax tail may well be crucial.

The foreign domiciliary: transitional provision

Amit is non-domiciled and was UK resident for 11 years, becoming non-resident for the whole of 2025–26. As he never became deemed domiciled before 6 April 2025, under the transitional provision in Sch 13 para 46 he does not come into scope for inheritance tax on his non-UK assets from 6 April 2025. If Amit returned to the UK, the new rules would apply to him. He would be subject to the ten out of 20 years residence test, which includes the years of residence in the UK up to 2025. If Amit had been UK resident for, say, 40 years in 2023-24, he would be deemed domiciled under the pre-April 2025 rules.

Assume that he became non-resident for the whole of 2024-25 and does not return to the UK. From April 2025, Amit will be a long-term resident, but the transitional provision will apply. Therefore, he will be a long-term resident but only until the start of his fourth tax year of non-residence. Amit will remain in scope for inheritance tax on non-UK assets as a long-term resident until 6 April 2027.

If Amit was deemed domiciled under pre-April 2025 law and then became non-UK resident from 6 April 2025, then he would be a long-term resident for three tax years after leaving. He would cease to be a long-term UK resident on 6 April 2028, provided that he did not return within ten years of leaving.

This gives some scope for tax planning even for those who have only left the UK temporarily. For example, Amit could settle trusts once he ceased to be a long-term resident in the period of non-residence even if he returned within ten years. This would avoid an entry charge even though the trusts would come within the inheritance tax net subsequently. (Watch out for capital gains tax, though, as the temporary non-residence rule would apply if Amit returned within six tax years of leaving).

The returning non-resident UK domiciled person

The new rules also provide some opportunities for UK doms.

Assume that Ruth has been non-resident for ten consecutive tax years and has always been UK domiciled. She returns in 2024-25 and decides to make a gift to her son. This is a potentially exempt transfer and she will need to survive for seven years.

However, on 6 April 2025 Ruth is not a long-term resident and domicile is irrelevant. If she makes a gift of foreign assets to her son, this is not a potentially exempt transfer but a gift of excluded property and she does not need to survive seven years.

Ruth could also settle assets on trust without an entry charge. She will be eligible for the four-year capital gains tax and income tax exemption.

In upcoming issues, Emma will cover the targeted areas of spouses, deemed domicile and treaties, and the complex world of trusts and settlements.

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