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Comments on draft Finance Bill Clauses 37 – 46 & Schedules 8 - 13

Introduction

This note deals only with the draft Finance Bill provisions that relate to the removal of the concept of domicile as a connecting factor for taxation, the introduction of a new 4-year FIG (foreign income and gains) exemption regime for qualifying new residents, changes to the inheritance tax (IHT) treatment of individuals and trusts and the proposed changes to the remittance basis of taxation.

We are concerned about the speed at which the legislation is being pushed through Parliament; there is in our view insufficient time for the highly technical legislation to be properly scrutinised. This gives rise to the risk of future legislative amendments being required to fix 'unintended consequences'.

We remain concerned that the proposed reforms will not raise the additional tax revenue estimated and may in fact cost the Exchequer. This is substantially as a result of non-UK domiciled individuals ("non-doms"), internationally mobile entrepreneurs, wealth creators and high-net-worth individuals (HNWIs) choosing to move to and invest in other jurisdictions that offer greater incentives than the UK. The proposed IHT changes and, in particular, the lack of complete grandfathering for existing trusts (those set up before any announcement of changes to the tax regime were made) are of most concern to non-doms and are driving significant numbers of non-doms to leave the UK.

We have seen the comments made by the Chartered Institute of Taxation on 23 December 2024, which include many points on drafting/technical issues in connection with the draft legislation. We are in broad agreement with many of the issues highlighted in that note as well as the proposed solutions.

Remittance basis

We do not support the proposed amendments to what constitutes a taxable remittance (Sch 9 para 5). It is not, in our view, appropriate to make significant changes to the remittance rules that substantially widen the scope of what constitutes a remittance in circumstances where the remittance basis is being abolished. The proposals suggest that the non-dom regime remains an unstable regime and is further encouragement for people to leave, particularly combined with the shorter IHT tail for those who leave by April 2025.

The Technical Note[1] indicates (at para 144) that these amendments are in response to the Upper Tribunal decision in Sehgal [2024] UK UT 74. The proposed changes go much wider than that. We consider that Sch 9 para 5 should be withdrawn. The following comments are relevant only if the government nonetheless decides to go ahead with the proposed amendments.

Schedule 9 paragraph 5(7): Specific provision is being inserted into s 809L(9) ITA 2007 (Sch 9 para 5(7)) to make it clear that the use of FIG as security is a remittance. It should be made clear that any remittance is limited to the amount of the loan.

Schedule 9 paragraph 5(8)(a): We do not understand why sending property from outside the UK to a non-relevant person in the UK should be a taxable remittance where the taxpayer receives no benefit from the funds; for example, a gift to a UK charity. HMRC has always maintained that sending money to the UK (even to a non-relevant person) is a remittance. However, we can see no policy reason why this should be the case. It is just a trap for the unwary that can easily be avoided by the well advised who will make the transfer to the non-UK account of the recipient. Rather than enshrining this in the legislation, it should be made clear that money is not brought to the UK if it is sent to a non-relevant person in the UK in circumstances where no relevant person receives a benefit.

[1] Reforming_the_taxation_of_non-UK_individuals.pdf

Schedule 9 paragraph 5(8)(a): For capital gains tax (CGT) purposes a debt is generally situate where the creditor is resident (s 275(1)(c) TCGA 1992). As a result, the effect of para 5(8)(b) appears to be that a UK resident remittance basis user will make a remittance wherever he makes a loan of FIG even if the individual borrower is wholly foreign, the loan is made and repaid wholly abroad, and the money lent never comes to the UK. The same result may follow if someone simply becomes indebted to the remittance basis user. It could also be interpreted to mean that wherever the remittance basis user deposits FIG in a non-UK bank there is a remittance of that FIG, as such a deposit is a debt owned by the depositor and para (I) of s 275(1) is being repealed (para 17). The problem would be cured if general situs rules apply and it is urged this course be taken.

Schedule 9 paragraph 5(11): The proposed change to s 809P(12) ITA 2007 (Sch 9 para 5(11)) appears capable of operating so as to tax funds that have previously been remitted to the UK by a non-resident, which may now be brought into charge because of the new qualification that they need to have been charged to tax. Suppose FIG were remitted but no charge arose because the remittance basis user had become non-UK resident and remitted the overseas FIGs in that period of non-residence. If the funds are taken back outside the UK and then subsequently the individual becomes UK resident again and remits the funds for a second time. it appears that para 5(11) would stop s 809P(12) preventing a charge. We do not think this is the intended policy. It should not matter to HMRC that people remit FIG in a period of non-residence if they have been non-resident for six years. It is not clear when this section is intended to have effect – for example, suppose the remittance occurred prior to April 2025 in a period of absence to buy a house and the individual returned after April 2025. The commencement provisions are unclear. In our view para 5(11) should be deleted.

4-year foreign income and gains (FIG) exemption regime ("4-year FIG regime")

We strongly support the abolition of the remittance basis but do not consider that the 4-year FIG regime is an appropriate replacement given the objective of generating economic activity and raising tax revenue. In our view the 4-year FIG regime is too short to be meaningful or to encourage internationally mobile entrepreneurs, wealth creators and HNWIs to move to and invest in the UK. We encourage the government to consider the introduction of a lump sum regime which would last for a longer period (10-15 years) but require any individual who wished to take advantage of the regime to pay a significant annual levy.

In our view the FIG exemption should operate automatically by default rather than requiring a claim on a source by source (or gain by gain) basis. A requirement to identify (and quantify) all FIG in respect of which exemption is claimed will be off-putting and will make the UK less attractive given that many other jurisdictions which have similar regimes do not require detailed, or even any, disclosure of overseas income and gains. It will be completely impractical in some cases – for example, individuals who own overseas trading groups or other significant overseas structures. It also puts people in a difficult position if they think that the transfer of assets abroad (TOAA) or CGT motive defences may apply but do not know if HMRC will agree. Do they need to make a protective claim? If they do make such a claim, does this prejudice their motive defence in later years? These uncertainties are demotivating in encouraging people to move here. The argument that such people will have to disclose all their FIG after four years anyway or that UK persons already have to declare worldwide income and gains is no answer to this objection as the aim is to attract people to the UK in the first place.

It is suggested that the FIG relief should apply by default except where the individual specifically elects out of it on items of income or gains. This would also help low or medium earners coming to work here who will otherwise have to declare all specific small items of foreign investment income and gains (e.g. foreign rental income) which were previously automatically exempt. Some of these workers may not always realise they are UK resident; they will incur professional fees to access an exemption.

Loss of reliefs: It seems wrong that overseas losses are denied where a claim for relief against foreign income is made even if there is no claim for relief in respect of foreign gains. Surely overseas losses should be available if gains are taxable. It also seems odd that making a claim for relief against foreign income leads to a loss of the CGT annual exempt amount. If a default basis operated, there is more logic to restricting all reliefs and personal allowances.

Trust distributions: It should be specifically provided that any benefit/capital distribution to a beneficiary from a trust during the four year period is ignored for all tax purposes - i.e. it is not matched to capital gains or relevant income arising in those four years or arising in future and so will not affect or reduce the pool of capital gains or relevant income. It is simply ignored. At present the Technical Note (at para 48) and legislation suggest that although a capital distribution from a trust during the four year period is not matched to capital gains (at para 50 Technical Note and new para 4(2) Schedule D1 TCGA 1992) and is not matched to future gains, it is nevertheless matched to relevant income albeit it does not reduce the pool of available relevant income and if not so matched can be subject to tax after the four year period if matched to relevant income arising later. This will effectively nullify the advantages of the 4-year FIG regime for those with trusts.

Partnerships: The definition of 'qualifying foreign income' in the new s 845F ITTOIA 2005 (as inserted by clause 37) is narrower than the definition of 'relevant foreign income' in respect of trading/professional partnerships that are controlled and managed abroad. Under the current rules, s 857 ITTOIA 2005 treats all foreign profits of such firms as 'relevant foreign income', which in turn allows them to be taxed on the remittance basis. The categories in s 845F include profits and adjustment income only where the firm's trade is carried on wholly abroad. If the firm has a UK branch, the foreign profits therefore do not appear to qualify for relief under the new regime. Is this intentional? If so, this does not seem consistent with the policy intention of making the UK an attractive destination for foreign individuals.

Limit to what FIG can benefit from relief: The proposed s 845F ITTOIA 2005 lists what items constitute FIG for the purposes of the relief. It omits life assurance products, most notably offshore investment bonds and personal portfolio bonds. These are important investment vehicles for Europeans in particular and have tax favoured treatment there. There is no need to link the new exemptions to the current remittance regime. The purpose of this regime is to be internationally competitive. We recommend that new residents are exempted from tax in respect of chargeable event gains arising in respect of non-UK situated policies and from the charges levelled on personal portfolio bonds during the four year period.

Temporary Repatriation Facility ("TRF")

In our view there is no reason to limit the TRF to UK residents. Non-residents who have previously been UK resident and are intending to return to the UK may wish to use the TRF; if they subsequently do not in fact return to the UK, any designation will simply result in extra tax revenue for HMRC.

Inheritance tax (IHT)

We welcome the grandfathering of trusts where the settlor died before 6 April 2025 in that in such cases excluded property status will in all cases be governed by existing law.

The partial grandfathering of trusts in existence on 30 October 2024 (effectively mitigating the possibility of a tax charge on the death of the settlor where the trust assets are currently excluded property) is presumably intended to encourage individuals to remain in the UK. However, we are seeing examples where the fact that the relevant property regime will continue to apply is causing settlors to leave the UK sooner rather than later. This means that the trust can be collapsed as soon as the individual is non-resident, to stop the relevant property charges continuing to accumulate. If the government wishes to encourage more people to stay, extending the grandfathering for trusts existing on budget day to include not only charges under the reservation of benefit rules but also ongoing relevant property charges would go a long way towards achieving this. Many individuals are prepared to accept the loss of the trust protections for income tax and CGT purposes. However, the prospect of a trust being permanently within the scope of UK IHT if the settlor dies while still a long-term resident when family members may well not be living in the UK is very unattractive.

It should be made clear in the legislation that s 48ZA(4) IHTA 1984 reads across to s 52 IHTA 1984 such that the life tenant's status will not be taken into account where the settlor dies before April 2025.

Where a deemed domiciliary leaves the UK before 6 April 2025, the underlying principle seems to be that they should be in the same position as under the current rules (i.e. Sch 13 para 45). This is reflected in the fact that they cease to be a long-term resident after three tax years, even if they have lived in the UK for more than 20 tax years. It is therefore odd that their excluded property trusts will come within the relevant property regime for that three-year period. In our view, it would be consistent with the existing policy for the excluded property status of such trusts to be governed by the existing rules.

There is a similar point where a spouse election (to be treated as deemed-domiciled) has been made in the past (pre-30 October 2024). It is difficult to see why, for example, this should impact the excluded property status of trusts previously established by the spouse where they have left the UK and would not otherwise be a long-term resident. It also seems wrong that, where spouses leave the UK before 6 April 2025 but one dies within three tax years of leaving, a ten-tax-year tail should apply to the survivor if they make an election to be treated as a long-term resident (Sch 13 para 27). Again, the policy would, in our view, suggest that the existing rules should apply. This would mean that that the IHT tail should only be four tax years both in these circumstances and where a spousal election is made in respect of a chargeable event prior to April 2025 such as death.

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