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Knightsbridge Wealth

technical news

For professionals working with international clients

Returning expats 'hardest hit' by non-dom reforms

Thousands of British expats face significant bills if they return to the UK after new non-dom tax rules come into force.

The UK government initially announced in 2015 that it will pare back the tax perks offered to people whose permanent home or domicile is outside the UK, drawing up new limits on their ability to keep offshore income out of Britain's tax net.

Under the new non-doms system, that went live on 6th April, non-UK domiciles who have resided in the country for more than 15 of the past 20 tax years will now automatically be deemed UK-domiciled.

Non-dom status for Britons who return to the UK but claim to have a permanent home abroad will also be removed.

The move is expected to net the UK Treasury an extra £995m, with an extra £245m coming from the removal of inheritance tax (IHT) loopholes on UK residential properties held by non doms through offshore companies.

Martin Rimmer, head of tax for south-east Asia at The Fry Group in Singapore, home to around 50,000 British expats who predominantly work in finance and legal services, said the changes are deterring some wealthy Brits from returning to the UK. He said that "we are seeing clients wanting to discuss different ways of being tax efficient in the UK such as UK tax advantaged investment schemes, (offshore portfolio bonds, enterprise initiative scheme, ISAs, pensions), and thinking differently about the succession of wealth down the generations. In the case of some, we are seeing them simply decide not to become resident in the UK and changing their long-term plans".

Others are more sanguine and accept that if they want to enjoy the benefits of being in the UK, it will come with the tax consequences the law imposes.

Expats affected by the change were usually born in the UK, went overseas and put down roots and probably became non-UK domiciled to keep their wealth outside the scope of the UK tax net even if they subsequently returned to the UK.

Now tens of thousands of British expats returning to the UK, will be taxed on income and gains from any offshore trusts or companies they owned.

In 2014/15, around 83,200 individuals had a foreign domicile, meaning they did not view the UK as their long-term home, according to figures from HM Revenue & Customs (HMRC).

Meanwhile, there are 53,300 users of the remittance basis, a tax break for non-doms which means they are taxed only on foreign income and capital gains when they are remitted to the UK.

They will also fall into the UK inheritance tax net, subject to a 12-month grace period.

The hardest hit group of individuals are returning expats who will now be deemed domiciled for all tax purposes while they are resident in the UK. What this means is that someone who was born in the UK but has lived all their life overseas with no intention of returning to the UK to live can be deemed domiciled simply because they are seconded to the UK by their employer for say six months, or have to return temporarily to look after a sick relative. The fact that these individuals may retain a foreign domicile under general law is irrelevant.

UK delays non-dom tax changes to offshore trusts until 2018

The UK government has delayed changes to the treatment of overseas trusts held by non-UK domiciles, amid concerns the reforms may force out Britain's wealthiest foreigners.

In a technical briefing published by HM Revenue and Customs (HMRC) last week, the tax office said it has decided to hold back introducing proposals regarding the taxation of income and capital gains paid out of offshore trusts for non-UK domiciles who are in the process of becoming deemed domicile.

"Stakeholders were advised that where the legislation was incomplete or incorrect, the necessary amendments would be made no later than the date for the publication of the Finance Bill. However, it has not been possible to make all of these changes in time and consequently, the government has taken the view to defer publication of the provisions affected," said the tax office.

HMRC added that further changes will be announced "in a future Finance Bill" but stopped short of specifying when.

An overhaul of the taxation of overseas trusts was part of the broader non-dom reforms.

The Treasury originally proposed that from 6 April 2017 those newly deemed UK-domiciled would have to pay CGT on all future capital gains of the trust.

In December, HMRC agreed to water down the original proposals for fear of driving out wealth foreigners.

In draft regulation published that month, it announced that capital gains and foreign income will not be subject to UK tax where there are no payments out of certain qualifying trusts – known as 'protected settlements'.

The tax authority also set out circumstances in which additions of property to a settlement by a deemed domiciled individual might taint that settlement such that capital gains and foreign income may be taxable on the settlor as it arises.

Rachael Griffin, personal financial planning expert at Old Mutual Wealth welcomed that postponement, saying "this area of financial planning is extremely complex, and it is encouraging to see HMRC take more time to consider the detail rather than rush it through in this Finance Bill. For non-doms potentially impacted by the proposed income and capital gains tax changes, this delay could leave them in limbo – as it is difficult to predict with any certainty what the final changes will be.

Surprise 25% Qrops charge rocks UK pension transfer market

People seeking to move their pensions out of the UK could face punitive tax charges under rules unveiled in last month's budget, with both Britons living abroad and foreign nationals based in UK potentially affected. New rules on such transfers mean savers have to pay a tax charge of 25% on their funds before moving the money, unless the transaction involves only European Economic Area (EEA countries) or the funds are being moved to a country where the saver now lives.

The rules are focussed on qualifying recognised overseas pension schemes (QROPS). These are pension schemes based in around 40 countries that HMRC recognises as operating under similar rules as those that apply in the UK. While transfers to other overseas pension schemes already attract tax charges, it has been possible to move money into QROPS tax-free. However, while there are legitimate reasons for such a transaction - a Briton retiring abroad, for instance, or a foreign national returning home after a stint in the UK – QROPS have also been associated with aggressive tax avoidance, pension frauds and scams.

On this basis, many have welcomed the chancellor's crackdown, but there is also concern that some savers will be unfairly caught out.

In particular, the new rules might affect Britons retiring abroad to countries such as the US and Canada, which do not have QROPS set-ups with the UK. People seeking to move pensions there have tended to transfer their money through third-party jurisdictions such as Malta, Gibraltar and Singapore. Such moves could now fall victim to the new tax charges. While the Treasury estimated the QROPS measures will raise a relatively modest £65m to £120m a year, the affect could be that savers who don't meet the tighter criteria laid out by the Chancellor will now find it difficult to get their money out of the UK. Some will face the choice of leaving their pension funds in the UK and trying to draw it overseas when they take their retirement benefits, or bring forced to take a sizeable hit on a transfer.

The 25% charge will affect those requesting an overseas pension transfer on or after 9 March 2017. There are generally between 10,000 and 20,000 transfers to Qrops each year.

It is vital that those exploring international pension provision should only take advice from UK regulated IFAs – such as Knightsbridge Wealth – that also work with local advisers in the country of residence.

Italy introduces non-dom tax breaks to lure wealthy foreigners

Italy has introduced a flat rate of tax aimed at attracting wealthy expats to its shores as it looks to compete with similar regimes offered in the UK and Spain.

The new measure was initially announced last December in Italy's 2017 Finance Bill and was approved by parliament a week later before former prime minister Matteo Renzi resigned following an embarrassing defeat in the Italian referendum.

Similar to the UK's non-dom system, the new flat rate tax of €100,000 a year, which went live on 8 March, will give foreigners a special status exempting them from paying Italian tax on any offshore income and gains. This charge can also be extended to family members, at a cost of €25,000 per person.

One of the conditions is that the individual must reveal their tax residency location to the Italian authorities and would have had to have resided abroad for nine of the last ten years. The regime is available for up to 15 years, unless the individual fails to pay the charges.

A peson is considered an Italian resident for tax purposes if they are in the country for more than 183 days, or six months.

International law firm, Withers, suggested that the "timing, which coincides with the changes to the UK's 'res-non-dom' regime, suggests that Italy might be seeking to woo high net worth individuals looking for a new home following Brexit or deterred by the tightening of rules in the UK."

The approved rules also contain recommendations to simplify Italy's immigration law in connection with the new tax system.

The initiative is an attempt to entice UK-based high net-worth individuals (HNWs) to set up residency in Italy as a way to remain in the European Union following Brexit. Italy's local media are speculating the measure could attract at least 1,000 wealthy individuals, adding an additional €100m to state coffers.

London new homes supply to peak in 2017, but fall sharply from next year

The number of new homes built in London will reach record levels in 2017, and while the majority have sold off plan, more homes will complete unsold this year than at any time over the past decade, according to international property adviser, Savills.

Total net completions (including sub-market and intermediate housing provision) are expected to peak at 46,500 this year, ahead of the minimum 42,000 homes a year target set by the London Plan, but still well short of real housing demand, which Savills puts at 64,000 homes per year. Lead indicators suggest that 41,000 homes were completed in 2016.

Over the past five years, private housebuilding starts have raced ahead of completions, supported in large part by rising volumes of off-plan sales, which assist cash flow and give certainty to funders. However, over the next few years, private sector completions are forecast to fall sharply, the result of rapidly falling home starts, as developers adjust to lower rates of sale. Savills say that policy intervention is required, in order to reach the level of development needed and shift the focus to the lower-value end of the market.

Sales have started to slow, meaning more homes will remain unsold on completion, particularly in the prime market.

New tax allowance could reduce IHT bills

An increasing number of families are being hit with a 40% Inheritance Tax (IHT) bill when a relative dies. Rising house prices have pushed many estates over the £325,000 IHT-free entitlement, called the nil-rate band. In 2011/2 the government's inheritance tax (IHT) take was £2.9bn, but it is forecast to rise to £6.2bn in 2021/22.

However, the introduction of the residence nil-rate band this month should help some families at risk of incurring IHT. The residence nil-rate band will boost individual IHT-free entitlement by £100,000, upon death, if they plan to leave a family home to children or grandchildren. And this allowance will rise by £25,000 each year over the next three tax years, so that it will be £125,000 per person in 2018-19, £150,000 per person in 2019/20 and £175,000 per person in 2020/21.

Married couples are allowed to pass assets to each other during their lifetime or when they die without having to pay IHT, no matter how much they pass on. Additionally, if one spouse dies without using their nil-rate band or residence nil-rate band allowance, the surviving person can claim their spouse's allowance. This means a married couple have a combined nil-rate band allowance of £650,000. And by 2020, when the full residence nil-rate band has come into force, couples will have an additional £350,000 available to them. This will allow them to pass on a £1m family home to direct descendants – such as children, grandchildren, adopted children, step-children or foster-children – completely IHT-free. Spouses of direct descendants, such as sons and daughters-in-law, are also eligible beneficiaries. However, siblings, nieces and nephews, and other relatives are not.

The residence nil-rate band will be gradually withdrawn, or tapered away, for an estate valued at more than £2m, even if a home is left to direct descendants. It will be reduced by £1 for every £2 that the value of the estate is more than the £2m taper threshold.

But if an estate includes multiple properties, the deceased's family can decide which property should qualify for the residence nil-rate band. The only requirement is that the property was owned by and lived in by the deceased at some stage before their death. A property that the deceased owned, but never lived in, such as a buy-to-let property, won't be eligible for the residence nil-rate band. However, the home doesn't have to be a person's main home, or been lived in or owned for a minimum period, and it doesn't have to be in the UK. But it does have to be within the scope of IHT and it must be included in a person's estate.

And the residence nil-rate band will still be applicable if the deceased downsized to a less valuable home, or sold their home on or after 8 July 2015, for example to pay for care home fees. As long as the former home would have qualified for the residence nil-rate band, and the deceased left the downsized property or equivalent assets to direct descendants, then the allowance would still be available. Generally, this allowance will be equal to the residence nil-rate band that has been lost because the former home is no longer in the estate.

The residence nil-rate band does not apply to homes held in discretionary trusts. Many wills written before 2008 are likely to include arrangements for discretionary trusts to be established to the value of the nil-rate band since this was common practice at the time for IHT purposes.

Many people still use discretionary trusts because of the flexibility they provide in terms of controlling what happens to assets after death. This type of trust gives trustees discretion over how, when and who will benefit from the trust proceeds. And they can be useful for planning for the future needs of your children or grandchildren, including those not yet born. As you can describe the beneficiaries simply as 'the grandchildren', as your family grows all the grandchildren can be included and be treated equally.

Assets within discretionary trusts are outside the settlor's estate for IHT purposes. But because these trusts do not benefit from the residence nil-rate band clients should think twice as to whether discretionary trusts are still the right approach.

Contact us

If you require further information about our services and how we can assist your clients, then please call us on the number below, or send us an email about how and when we can contact you.

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