

Should I stay or should I go?

Steve Bougourd on the increasing UK tax burden on UK resident, non-domiciled high net worth individuals



ABOUT THE AUTHOR

Steve Bougourd TEP is Associate Director, Trust & Corporate, Legis Group

Attempting to provide topical comment, in advance of publication, on rising taxes, spending cuts and the desirability of remaining in the UK, I was almost inclined to re-title this article 'Back to the Future'. Or, with unemployment at a 16-year high and the Trade Unions massing to confront the cuts, perhaps, 'I Predict a Riot'.

By the time you read this the honeymoon period for the UK's newly formed Coalition government will be over. The cold reality of June's emergency budget will start to bite and England will have just lost on penalties in the World Cup. Despite the gloom, hopefully we in the UK will be enjoying the start of a hot summer!

The story so far

It would be fair to say that non-domiciled UK residents (non-doms) have borne the brunt of new tax rules in recent years. For those wise enough to settle their non-UK assets in offshore trusts, the opportunity to receive tax-free capital distributions in the UK consisting of capital gains realised after 5 April 2008 has gone. In addition, individuals resident in the UK for more than seven years now have to pay an annual fee of GBP30,000 if they still wish to be taxed on a remittance basis on their non-UK assets, a status that was previously enjoyed at no charge. More generally, we have also seen the introduction of the 50 per cent tax rate for those earning more than GBP150,000 a year, a hike in national insurance contributions and a tax on bank bonuses.

There has been some relief for non-doms however. After a short spell of speed-dating the Coalition government was formed and the two parties agreed a compromise. For now at least, the Tories have dropped their GBP25,000 non-dom fee payable from year one. And the Lib Dems have shelved their plan to abolish non-dom status for seven year residents. But this is subject to a further review, so watch this space.

Domicile

Let's rewind...what is domicile? Very simply, if you are a born and bred Brit, you are likely to be domiciled in the UK. An individual normally takes their 'domicile of origin' from their father and attaining a new 'domicile of choice' is possible, but is notoriously difficult. An individual can only have one domicile. Any change in status will essentially require the severing of family ties, businesses and assets and re-establishing the same in another country with the intention of remaining there indefinitely. The purchase of a burial plot is often recommended.

Individuals with a UK domicile of origin that have left the UK to become resident elsewhere are often advised to test their domicile status by establishing a trust with assets just in excess of the nil rate band (exemption limit) currently at GBP325,000 to potentially trigger a tax charge.

Residency broadly applies to the days spent in the UK, although inevitably the rules are complicated as illustrated in the recent Gaines Cooper case. He (a Brit), argued that he left the UK and became domiciled in the Seychelles over 30 years ago and spent less than 91 days a year in the UK. However, as he still maintained businesses, owned property and frequently

visited immediate family in the UK, the Court of Appeal stated that England remained 'the centre of gravity of his life and interest'. HMRC won the case and he was ruled UK domiciled. Fair enough. However, despite the fact that he left the UK in 1976 and had spent less than the widely assumed threshold of 91 days per tax year in the country, he was also ruled UK resident. The decision was predicated on the application of the tax authorities' published guidelines. As Gaines Cooper did not leave the UK to take up full time employment, he needed to demonstrate that he had left the UK 'permanently' AND had spent less than 91 days in the UK. The Court of Appeal ruled that he had never really left the UK permanently in the first place and therefore remained resident in the UK for tax purposes.

What does this all mean? If you are UK domiciled and resident you are fully taxable whereas if you are non-domiciled and UK resident, tax is paid on UK income/gains with the option not to be taxed on other income/gains but only if kept out of the UK. If non-resident, you are taxed on UK income only. And, finally, in terms of inheritance tax which is payable at 40 per cent, if UK domiciled (or deemed-domicile – see below), tax is payable on your worldwide assets. If non-domiciled, tax is limited to UK assets only, although structures can be used to help mitigate liability.

Trusts and tax-planning

And this is where trusts can play a key part in non-dom tax inheritance tax planning. Given the domicile rules, it is perfectly conceivable to retain non-dom status and be resident in the UK for a generation and



beyond. As illustrated above, if a 'domicile of origin' is maintained there are no grounds for attaining a new 'domicile of choice', so the UK tax authorities cannot have it both ways. However, there is also a 'deemed domicile' rule for UK inheritance tax purposes only. If an individual is tax resident in the UK in any part of 17 of the previous 20 tax years, they will become liable to tax on their worldwide estate. However, if an individual settles non-UK assets into trust before becoming deemed domiciled, the assets will be 'excluded property' and therefore out of scope.

Of course, any tax planning arrangement should be underpinned by UK and relevant foreign tax advice and it would be prudent for trustees looking to take on tax planned structures to have such advice on file. Thereafter, they should remain very aware of beneficiaries' tax status and any changes in the tax rules, so they can be proactive and engage with them and their tax advisors when required.

Cuts ahead

With the UK Government having to tackle a record deficit of GBP163 billion (the largest of the G20 countries), public sector cuts totalling over GBP6 billion have been announced. But to bring this into context, this still represents less than 1 per cent of public spending.

By the time you read this article, the emergency budget will have come and gone. It has already been announced that the capital gains tax rate (18 per cent) will rise in line with income tax rates on non-

business assets, although this is likely to be capped at 40 per cent. That said, its impact will be limited as currently the amount of capital gains tax collected represents less than 1 per cent of the entire tax take. I would expect to see significant increases in fuel, tobacco and alcohol, but again, relatively speaking, this will not amount to very much. Building on the Coalition's momentum, and with the Labour Party currently leaderless, an increase in Value Added Tax from 17.5 per cent has to be a real possibility, to say 20 per cent, bringing the UK more into line with its EU partners.

Whilst turning the screw on the rich has populous appeal and with deeper pockets they can arguably afford to pay more, the past and new UK governments point to the wealthy and ask them to pay their fair share. I am sure that higher tax payers would already argue that 50 per cent in excess of GBP150,000 is considerably more than 20 per cent on GBP35,000. To my mind, higher earners can only be squeezed so much and there will be a tipping point. The UK rich list suggests that about 50 per cent of the top 100 are either non-doms or are Brits that have left the UK to live elsewhere. These people are wealth generators, they build businesses, employ people and those businesses pay taxes on profits. Working people do not receive state benefits, they pay taxes and spend money; which creates a ripple effect across the economy.

Voting with your feet

The wealthy and their businesses can

afford to vote with their feet and move to lower tax jurisdictions such as the Channel Islands and Switzerland. We have seen Guy Hands and his firm, Terra Firma move to Guernsey, while BlueCrest, another hedge fund manager has left the City and set up its head office in Guernsey and located its trading arm in Geneva. If a levy is also imposed on banks in the UK without it being applied globally, affected banks will also consider changing their tax domicile.

Rhetoric often refers to tax haven abuse, but tax competition is actively pursued by EU countries such as Belgium and the Netherlands that offer tax breaks to encourage relocation. The UK government's Foot Report states that 'the Crown Dependencies make a significant contribution to the liquidity of the UK market'. In addition, both Guernsey and Jersey are recognised, alongside the UK, as 'jurisdictions that have substantially implemented the internationally agreed tax standard' regarding transparency and exchange of information for tax purposes. The Channel Islands are also 'All Crimes' jurisdictions, which effectively means that business cannot be accepted if it is or appears to be contrary to domestic laws. This includes tax evasion, which is a criminal offence.

In conclusion, in the UK there is little doubt that it is going to get worse before it gets better and the wealthy will carry much of the burden. So back to the words of The Clash, 'Should I stay or should I go now?'... 'If I go there will be trouble, if I stay it will be double'. ■