PUMP COURT
TAX CHAMBERS

COMMON TAX AND SUCCESSION PROBLEMS FOR FOREIGN DOMICILES

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Structure

- Types of domicile
- Domicile enquiries and succession issues
- Reservation of benefit and trusts created by non-domiciled individuals
- The 2020 legislation and its impact on settlements
- Onward gifts regime

Domicile – three categories

- **Domicile of origin** – everyone must have a domicile at birth which is generally the domicile of the father if legitimate and that of the mother if illegitimate. However, this can be hard to apply for same sex couples.

Note the position on federal states. You must fix domicile in a particular country that is a territory subject to one body of law. UK/Australia/USA/Canada. Time for a change of approach?

Domicile of origin prevails until acquisition of domicile of choice in a particular country even if you leave and there is no intention to return to country of origin

- **Domicile of dependency** – children under 16 (21 until 1 January 1970 and then 18 until 1 January 1974). Previously included wives marrying before 1 Jan 1974- can still trap a wife who married an English person and then remained here
- **Domicile of choice** *Re Fuld's Estate* 1968 "a man fixes voluntarily his sole or chief residence in a particular place with an intention of continuing to reside there for an unlimited time." Burden of proof on the person who seeks to show a change of domicile

Domicile – three types of deemed domicile for tax purposes

(a) the long stayer - UK resident for 15 out of the last 20 years – deemed domiciled in the 16th year even if not UK resident. IHTA s267 However you lose IHT deemed domicile at the start of the 4th tax year of non-residence. If you return in 5th or 6th years you reacquire deemed domicile for IHT purposes then (but gifts in 4th year undisturbed).

(b) the returning foreign dom – while UK resident and had a UK domicile of origin and born here then deemed domiciled here for income tax and CGT purposes (and IHT purposes from the second tax year of UK residence).

Note that deemed domicile as a long stayer does not mean you lose your common law domicile. This means a foreign dom still has access to certain transitional reliefs such as 2008 trust rebasing and 2017 personal rebasing (although this is denied to a returning foreign dom).

(c) Elected domicile for spouses – a non-dom spouse can elect to be domiciled in the UK for IHT purposes only: that domicile is lost only after 4 consecutive tax years of non-residence. May have limited application under DTTs for US purposes S267ZA

Domicile – acquiring a domicile of choice

- Dicey states: Every independent person can acquire a domicile of choice by the combination of residence and intention of permanent or indefinite residence, but not otherwise. Thus there are two requirements: residence and intention. Rule 10. The substantive law is well-established – applying it is another matter
- The dispute is generally about intention. The test is strict: "... the true test is whether he intends to make his home in the new country until the end of his days unless and until something happens to make him change his mind."
- Scarman J said in the leading case of In the Estate of Fuld, Deceased (No 3) v AG: "What has to be proved is no mere inclination arising from a passing fancy or thrust upon a man by an external but temporary pressure but an intention freely formed to reside in a certain territory indefinitely." [note not to the end of his days]
- Action on validity of Will and four Codicils - whether the instruments were entitled to be admitted to probate in England and allegations of undue influence and in some cases lack of testamentary capacity.
- Held he had retained his German domicile of origin until death. Acquisition of domicile of choice was a serious matter not to be lightly inferred. Predominant feature of his life was indecisiveness. He felt the pull of Canada, of London, of Germany. "In truth his complex hesitant mind may never have made its final option between them."

Domicile – case law – Ramsay v Liverpool Royal Infirmary & Others House of Lords (1930)

- Testator died in Liverpool in 1927 aged 82 and unmarried. Left a holograph Will valid in Scotland but invalid in England. Domicile of origin was Scottish. Lived greater part of his life in Glasgow. Originally employed there as a commercial traveller but gave up in 1882 and never worked again. Lived in Liverpool for the last 35 years of his life. With the exception of family ties he had few if any ties in either England or Scotland. Held that the burden of proving that he had abandoned his domicile of origin had not been discharged. He is reported to have said he never wished to set foot in Glasgow again and he refused to go to Scotland when his sister, Isabella, desired to remain there in 1915.
- An intention to change a domicile of origin is not to be inferred from an attitude of indifference or a disinclination to move with increasing years. The residence was "colourless". Mere length of residence by itself is insufficient evidence from which to infer the necessary animus.

Domicile – IRC v Bullock 1976

- Taxpayer's domicile of origin was Canadian Nova Scotia, lived in Canada, born in Nova Scotia in 1910, arrived in England in 1932 serving with the Royal Air Force. Whilst still serving in the RAF he married an English woman in 1946 aged 36. Retired in 1959 aged 49 and took civilian employment. Father died in 1960 at which point he retired at the age of 50 and went with his wife to live in Dorset.
- He wished to return to live in Canada after leaving the RAF but did not do so because his wife disliked the idea. Made a Nova Scotia Will. No children. Retained Canadian citizenship. Did not vote in the UK.
- Left gifts to Canadian churches on last death. All his assets were in Canada. His wife bought the UK home. Maintained it was wrong to vote in Parliamentary elections and had never considered obtaining a UK passport. Regular reader of the Toronto newspaper and maintained contact with Canadian relatives and friends.

Domicile –Bullock

- Court of Appeal reversed the High Court decision and held that although the matrimonial home was important, it was not conclusive and as the taxpayer had maintained a firm intention to return to Canada should he survive his wife who was similar age and health he could not have had the intention of establishing a permanent home in the UK.

"He had in his contemplation some event upon the happening of which his residence will cease. It is not necessary to show his intention to make a home in the new country as irrevocable or that the person whose intention is under consideration believes that for reasons of health or otherwise had no opportunity to change his mind. In my judgment the true test is whether he intends to make his home in the new country until the end of his days unless and until something happens to make him change his mind."

Domicile –Steiner v CIR [1973] STC 547

- An individual(s) born in 1889 in what is now Czechoslovakia but was then part of the Austrian Empire. Moved to Berlin in 1906 and established a textile business there. Came to England in 1939 to escape Nazi persecution and in 1947 successfully applied for British nationality. Held by Special Commissioners and upheld by Court of Appeal that he had acquired an English domicile of choice.
- This was despite the fact that he had visited Berlin in period from 1948 to 1951, was there for a total of 6 months. From 1951 to 1963 onwards he spent about 6 months in each year in Berlin. In January 1967 he was taken ill whilst in Zurich, gradually retired from business after his second operation in London. Held to have acquired a domicile of choice here in the early 1950s.
- May 1970 suffered a stroke whilst at his flat and has not been able to travel. Did not speak good English. Had a flat in Berlin around 1954 and made contacts in the Jewish community in Berlin with a list of former friends. Wanted to be buried in Israel. Procured a burial plot for two graves in Israel. Younger son spent most of his time in the flat in Berlin. Wife and other son in the UK

Domicile –more recent cases

- *Agulian v Cyganik* [2006] EWCA Civ 129 *Holliday v Musa* [2010] and *Barlow Clowes International Ltd v Henwood* [2008] [domicile of choice in Isle of Man abandoned and Mauritius domicile not acquired]
- Many cases not on tax but jurisdiction or succession. *U v J* [2017] EWHC Fam 449 *Ray v Sekhri* [2014] EWCA Civ 119 *Proles v Kohli [2018]*
- Remember that anything other than English real estate must be covered by a Will valid under the law of that person's domicile. Ensure that proper advice is obtained e.g. on forced heirship; testamentary succession Under the law of that other country you may be able to opt for English law to apply.
- UK real estate – may want to own in joint names with spouse or left under a separate English will that covers English real estate only. Could leave on a revocable immediate post death interest trust for the spouse

Domicile enquiries and domicile status – HMRC targets

- Those with UK domicile of origin who return to the UK e.g.to die, work or for health care reasons – *Gulliver* [2017] UKFTT 222(TC)
- 2nd or 3rd generation children who have never lived outside the UK *Henderson v HMRC* [2017]
- Long term UK residents–no home in the claimed country of domicile *Proles v Kohli* [2018]
- Weak domicile of choice or origin e.g. never lived there but inherited – the British Empire type
- Where there is doubt about whether the immigrant parent who had a claimed foreign domicile lost it on arrival in the UK -did he intend to leave?
- If he did not, then the child acquired a UK domicile of dependency which became a UK domicile of choice and this cannot be lost until he physically leaves the UK

Domicile enquiries

- HMRC approach now more centralized
- Look at the information given: how far is it still relevant? E.g. if the person said he would leave at 60, did he do so?
- Increased litigation and enquiry – can wreck previous planning especially inheritance tax where trusts have been set up or there has been reliance on transitional reliefs such as 2008 rebasing and large capital payments have been made from trusts
- Long inheritance tax lead of 20 years
- Compile chronology and examination of key life events e.g. acquisition of property here.
- Pack of documents listed at RDRM 23080
- Naturalisation

Domicile enquiries – how to deal with them

- Do not say something that cannot be evidenced
- Should the taxpayer go for an interview?
- Avoid being forced into a straitjacket when answering their questions
- Know your client. His or her hobbies and interests. Are they compatible with leaving? What about friends, social ties? Language Business interests.
- How much time is actually spent in the place of claimed domicile
- Is there a home there?
- When was the last enquiry into domicile; have circumstances changed since then?
- Retirement – when realistically will s/he ever leave?
- Remember domicile may be challenged in terms of succession planning and under the 1975 Act not just a tax issue- consider *Schaffer*

IHT and settlements and reservation of benefit issues

1. Problems aggravated by the charge on indirect interests in UK residential property under Sched A1 IHTA.
2. Can be avoided by investing in excluded property. But the proceeds from selling/repaying indirect interests remain non-excluded property for 2 years: see para 5 Sched A1 IHTA. However, the sale of the underlying UK property can result in excluded property status: IHTM04313, IHTM04314 and s 65(7C)-(7D) IHTA.
3. Except for formerly domiciled residents, HMRC now accept that a change of domicile status after the property is settled does not impact on the excluded property status if there is a reservation of benefit: IHTM14396 and s48(3E) and s 65(7B) IHTA.
4. With new acquisitions consider commercial debt charged on the property: s 162(4) IHTA, but note Schedule A1 IHTA, para D28 GAAR guidance, 103 FA 1986, *Shelford v HMRC*. If the property is owned indirectly, para 2(5) of Schedule A1 IHTA 1984 attributes liabilities rateably.

IHT and settlements and reservation of benefit issues (2)

5. HMRC now accept that spouse/charity exemption may apply if the reservation continues until death and the settlement terminates in favour of the spouse/charity: IHTM14303 (as undated on 9/3/01). Could presumably apply to a disabled interest for a spouse under a trust.
6. HMRC do not accept that spouse exemption can be relied upon to prevent a charge under s 102(4) FA 1986 on a lifetime termination which is a deemed PET: IHTM14303.
7. Also note on a transfer from a trust to a spouse of the settlor:
   (i) the reservation of benefit could continue after the appointment to the spouse: see FA 1986 Sched 20 para 5(2);
   (ii) if the reservation continues until death there are also likely to be problems in claiming spouse exemption since no property probably "becomes comprised in the estate" of the spouse if he/she already owns it nor is his/her estate increased. Note IHTM14303 suggests HMRC shares this view since it states the exemptions "may be applicable…. if, on death, the property passes to an exempt beneficiary" .

IHT and settlements and reservation of benefit issues (3)

(iii) if winding up the trust does not tigger material chargeable gains, there may be benefits in transferring the assets to the donor to secure spouse exemption and/or a capital gains tax uplift on death. Note:

(a) FA 1986 Sched 20 para 5(2) does not apply if the property reverts to the donor;

(b) HMRC accept there is no charge under s 102(4) IHTA because they consider the PET to be of no value: see Answer 17 to matters on which HMRC's view is sought in relation to pre-owned assets income tax. Paper submitted on behalf of STEP, CIOT and LITRG (14 July 2005).

Finance Act 2020 IHT Changes

1. Intended to reverse the Court of Appeal's decision in *Barclays Wealth Trustees (Jersey) Ltd v HMRC* [2017] STC 2465. The Court considered that the time when "the settlement was made" was to be assessed from a trust law perspective. But Henderson LJ left open whether there could be charges if fresh funds were added after a change of domicile status: para 58.
2. S 73 FA 2020 amends Part III IHTA so that the focus is now on when "property became comprised in the settlement" and not when "the settlement was made".
3. Legislation makes express provision for accumulated income which is treated as having been settled when the property from which it derives from was settled: s 48(3F) IHTA and changes made to s 64 - s 65 IHTA.
4. HMRC's views likely to be similar to those on whether transactions impact whether there is a continuing s 49 IHTA interest in possession: see IHTM16075 - IHTM16078 (note criticisms in the texts).

Finance Act 2020 IHT Changes (2)

5. New statutory wording could be significant in relation to loans:

   (i) IHTM16077 views loans as an issue of difficulty. IHTM14317 states that HMRC view interest-free loans as gifts of the interest foregone for GWR purposes;

   (ii) is anything new "comprised" in a settlement, since any property added is matched by a liability, and if so when? Note *St Barbe Green and another v IRC* [2005] STC 288.

6. The changes made by s 73 do not impact on chargeable events prior to the FA 2020 coming into force on 22 July 2020. However, they do impact on how events that occurred prior to that date should be analysed when assessing subsequent charges: see s 73(11) FA 2020.

Finance Act 2020 IHT Changes (3)

7. These retroactive changes could be significant from a reservation of benefit perspective if the settlor has acquired a UK domicile when funds were transferred to a new settlement. This is because the settlor will have acquired a UK domicile at the time the funds become comprised in the new settlement so the revised wording of s 48(3) IHTA suggests the funds may no longer be excluded even if both settlements were created when he was non-domiciled (note s 81, s 82 and s 82A IHTA just apply for the purposes of Chapter III (i.e. relevant property charges).
8. Is any retroactive change ECHR compliant?
9. S 74 FA 2020 inserts a new s 81B (when a settlor or spouse have a S 49 initial IIP) and s 82A IHTA directed at transfers between settlements after 22 July 2020.

Finance Act 2020 IHT Changes (4)

10. New s 82A imposes additional conditions on transfers if the property would otherwise be excluded for the purposes of the relevant property regime:

    (i) if the transfer is effected by an assignment by a beneficiary or the exercise of a general power, the beneficiary/person exercising the power must not be domiciled in the UK or a formally domiciled resident at the time of the transfer/ exercise of the power;

    (ii) in other cases where a transfer occurs and the settlor is alive or the transfer is caused by his death, the settlor must remain non-domiciled;

    (iii) in other cases if the settlor has died, the property will retain its excluded property status.

Onward gifts rule – FA 2018 sch 10

- There are three sets of onward gift rules. There are rules that apply to the transfer of assets benefits charge (ITA 2007 section 731); rules that apply to the Trust gains matching regime (TCGA 1992 section 87); and rules that apply to the settlements code benefits charge (ITTOIA 2005 section 643A).
- The intention was to stop the avoidance of tax by trusts distributing assets or benefits – out of capital or income - to a non-taxable individual (e.g. someone who is non-resident or foreign domiciled). The non-resident or foreign domiciled recipient (A) could then make a tax free onward gift of the assets to another person B who is UK resident. Bowring decision seemed to make it more difficult for HMRC to attack onward gifts without specific legislation
- One could obviously deal with the problem in a different way – simply tax all lifetime gifts on the recipient B whatever the source and whether received from A's personal funds or from a Trust. However, the UK does not tax straightforward gifts between individuals provided the donor survives 7 years (and in the case of a foreign domiciled donor A, a gift of non-UK situated assets to B is generally not taxed at all in the UK subject to this rule). The intention is that the recipient B is taxed as if they had received the distribution direct from the Trust itself. The status of A is ignored.

Onward gifts rule – FA 2018 sch 10

Five conditions:

(a) the original recipient A of a capital payment or benefit from a trust (before or after 2018) is non-resident or a remittance basis user

(b) A makes a gift to another person B after 5 April 2018

(c) The gift is made within three years following receipt of the capital payment or benefit from the trust

(d) The gift derives from the trust distribution or is made in connection therewith

(e) At the time of the trust distribution or benefit there are arrangements or an intention to pass it on.

If the conditions are satisfied the broad effect is to attribute the capital payment or benefit to B and tax B accordingly as if they had received it from the trust.

Onward gifts rule – FA 2018 sch 10

However, the onward gifts rule cannot apply if:

(a) a gift is made by A to B more than 3 years after the capital payment or benefit received by A from the Trust. Thus the simple way round the rule is to make a large capital distribution from a Trust to A who then waits 3 years before giving it on. [A cannot get round it by making a gift to another non-resident who then makes an onward gift to the UK resident within 3 years from the Trust distribution.]

(b) Even if A makes a gift to B within 3 years of receiving a Trust distribution there is no tax if it can be shown that there was no intention or arrangement to hand on the capital payment or benefit to the UK resident – but there is a rebuttable presumption that there was such an intention.

(c) If A the recipient of the Trust distribution pays tax on the distribution e.g. is UK resident and UK domiciled or UK resident and foreign domiciled but remits, then B pays no tax.

(d) If A is a non-resident settlor or the settlor is deceased and A is non-resident and the Trust makes an income distribution to A generally the rule cannot apply if A gives it on to B. There is no protected foreign source income and if the distribution is income it is not a capital payment charged to CGT

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