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Budget Note

Removal of Domicile Rules and Employment Tax

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The Government's plans to end the special treatment of non-UK domiciled individuals with effect from 6 April 2025 have been well publicised and commented on in terms of their general effect. What is less obvious from the Treasury's Technical Note is the impact for individuals in the context of employment tax save that "Overseas Workday Relief" (i.e. treatment under s.26 of ITEPA) will be preserved in a new form.

This article sets out the current status quo for non-UK domiciled individuals (**"non-doms"**) in the context of employment tax and discusses areas that are currently not addressed by the Technical Note.

The present treatment of non-doms

ITEPA currently provides for non-UK doms as follows:

(1) General Earnings: there are two alternative bases for which a non-dom can claim the remittance basis:

- s.22 (Chargeable Overseas Earnings) for non-doms who have been UK resident for more than 3 years and
- s.26 (Overseas Workday Relief) for non-doms who have not been UK in the previous 3 tax years.

(2) Part 6: no remittance basis at all – in other words for charges under s.394 (EFRBS) and s.401 (termination/change of employment) the proposed charge will have no impact.

(3) Part 7: the rules for internationally mobile employees set out in Chapter 5B (ss.41F to 41L) – these rules applied to apportion income under Part 7 for periods of both non-UK residence and for periods of UK residence where the remittance basis applied. In terms of the latter, this created "chargeable foreign securities income". Income could qualify as chargeable foreign securities income under either s.41H(3)-(5) or s.41H(6)-(7) which essentially repeated the tests in s.22 or s.26. All of this was subject to a just and reasonable apportionment override in s.41L.

(4) Part 7A: the rules set out in in s.554Z9 to s.554Z11A – in broad terms these rules allowed income treated as arising under Part 7A to be subject to the remittance basis rules if on an apportionment of the income some of it would have been "for" a tax year where conditions equivalent to either s.22 or s.26 would have applied.

The above is also set out in s.809F of ITA 2007 which summarises the effect of the remittance basis. Note that the employment income is completely outside the definition of "relevant foreign income" in s.830 ITTOIA 2005.

By contrast for National Insurance contributions (**"NICs"**), domicile has never been a relevant concept and indeed the NICs rules have their own separate rules on residence (i.e. not using the statutory residence test for income tax) and are therefore unaffected.

The proposed changes

Domicile and the remittance basis will be scrapped from 6 April 2025. Instead the remittance basis will be replaced by a Foreign Income and Gains ("FIG") Regime which will be available for individuals who become UK tax resident after a period of 10 tax years of non-UK residence.

The FIG Regime will allow qualifying individuals to be totally exempt from UK tax on "foreign" income or gains – they will be able to bring such income and gains (or their proceeds) without any tax charge.

In terms of employees, the Technical Note only makes the following comment:

> "Relief will continue to be available for employees who opt to use the new 4-year FIG regime. The new Overseas Workday Relief (OWR) will be like that currently available, providing relief on earnings for employment duties performed outside the UK. The new OWR will be available for the first 3 tax years of UK residence. Employees who are eligible for OWR in 2023-24 or 2024-25 for their first year since returning to the UK should still be able to claim OWR for the full three years. However, those re-entering from 2025-26 will not be able to claim OWR, if they are not eligible for the FIG regime.
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> The new OWR will provide relief from income tax whether or not these earnings are brought to the UK. As under the current rules, the new OWR will not provide relief from National Insurance contributions (NICs), so any NICs liabilities on these earnings will be determined as usual."

By implication, it is suggested that the only employment income to which the FIG Regime will apply will be that treated as "foreign" under an amended s.26. However, given how s.26 currently feeds through to provide a remittance basis for Part 7 and Part 7A, I would imagine that accommodation will be made under these regimes as well – i.e. the FIG Regime for any income apportioned to when the new s.26 would have applied. However, the Treasury might be concerned about too great a windfall if a blanket exemption applies (rather than the remittance basis) since the Part 7/Part 7A have the potential to be in respect of years stretching many years back.

By contrast, it is clear that the current s.22 regime will be scrapped entirely. This is not much of a surprise given the increasing number of restrictions which had been imposed on it in recent years (e.g. the revised s.24 and s.24A).

Overseas Workday Relief – the old and the proposed compared

Under the current s.26 regime the following were the key criteria:

(1) The remittance basis applies for the year (under ss.809B, D or E) – this by definition also means the individual is UK resident but non-dom;

(2) The requirements of s.26A are met – essentially a test that the individual has not been resident in the UK for more than 3 tax years prior to becoming UK resident and has not been UK resident for the 3 tax years prior to the year in question;

(3) All or part of the individual's General Earnings are (i) not in respect of duties performed in the UK and (ii) not from overseas Crown employment subject to UK tax;

(4) To the extent that the year is a "split-year" the earnings are attributable to the UK part of the split-year (if they were attributable to the non-UK part, there would be no need for this relief – instead one would only have to consider s.27).

In summary, new arrivers get s.26 treatment for the first 3 years but in the fourth year they are taxed like all other UK residents (unless they could avail themselves of s.22).

Under the current rules, where s.26 applied the non-dom would only be taxable on employment income attributable to non-UK duties on a remittance basis (i.e. they would be taxed on the income if remitted).

The new proposed regime is significantly different in the following respects:

(1) It is available to everyone regardless of their domicile status;

(2) Instead of needing to be non-UK resident for 3 years prior to arrival, the new rule will now be 10 years (as this is a requirement of the FIG Regime);

(3) The new regime will operate as a complete exemption from income tax in terms of earnings attributable to overseas duties as opposed to being chargeable on remittance.

The transitional provision

The Technical Note states that those who are eligible in 2023/24 or 2024/25 for s.26 (i.e. under the current rules) will be able to claim treatment for the full 3 years. For years 2025/26 onwards, this presumably will mean that they will enjoy a windfall in the form of an outright exemption as opposed to being taxed on the remittance basis.

Temporary Repatriation Facility

The Temporary Repatriation Facility (**"TRF"**) is summarised at 3.6 of the Technical Note as follows:

> "A new 12% rate of tax will be introduced for remittances of FIG made in tax years 2025-26 and 2026-27 where the FIG arose to the individual personally in a year when the individual was taxed on the remittance basis and the individual is UK resident in the relevant tax year.
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> There will be some relaxation of the mixed fund ordering rules to make it easier for individuals to take advantage of the TRF if, for example, they have FIG in a mixed fund or they are unable to precisely identify the quantum of their FIG.
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> From 2027-28 remittances of pre-6 April 2025 FIG will be taxed at normal tax rates."

This essentially is an incentive for individuals to remit income and gains arising before 2025/26 to access a new 12% tax rate which will apply to the first two years of the new regime. Individuals who currently enjoy the remittance basis are therefore potentially incentivised to trigger foreign employment income now and then remit such income post-2025/26 if realistically they will need to remit at some point in any event.