Certified B Corporation

GUIDE

UNDERSTANDING DOMICILE

Domicile is an important concept to consider whenever you are tax planning, and especially if you have ties in the UK and overseas.

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WHAT YOU'LL LEARN IN THIS GUIDE

Domicile is an important concept to consider whenever you are tax planning, and especially if you have ties in the UK and overseas.

Domicile ultimately defines whether or not you'll be caught in the UK Inheritance Tax net, and likely to face a possible, and substantial, 40% tax charge on your UK (and even worldwide) assets.

There are other consequences too. All the while you're UK tax resident, your exposure to UK Income Tax and UK Capital Gains Tax is ruled by your domicile status.

Understanding domicile, and how it affects your wealth, is a crucial step in any solid financial plan. This guide is here to help.

In March 2024, reforms were proposed to how domicile affects taxation, tying it more closely to your residency status. This is still a work in progress, with further announcements expected in October. Full certainty will follow the Finance Act in 2025.

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WHAT IS DOMICILE?

Domicile is a legal concept used to define your 'homeland'. It's a fairly adhesive device and generally applies to the country to which you are rooted – usually decided by where you were born.

So if you were born in the UK, and so was your father who had a UK domicile at the time of your birth, it's highly likely you will be UK domiciled, regardless of where you now live in the world.

Here's an example of domicile in action:

Joe was born in London to an English father and Hong Kong mother. He grew up in the UK, then lived in Hong Kong for 15 years, and he now lives in Thailand.

- He is a UK national
- He has a UK domicile
- He has a Hong Kong permanent residency
- He is a Thailand tax resident

All at the same time

Domicile is a separate tax consideration to your nationality, residence or citizenship and is not automatically reflective of the country you are currently living in.

WHY IS DOMICILE SO IMPORTANT?

Every individual has a domicile status throughout life. This status determines how much UK tax we pay.

If you are considered to be UK domiciled and UK tax resident, then normally you are charged on an ‘arising basis’. This means that you pay tax on your worldwide income and worldwide capital gains as they arise. You’re allowed to use your personal tax allowances and any annual exemptions to offset those income and gains.

However, individuals who are resident in the UK but not UK domiciled can choose to be taxed on a ‘remittance basis’, if that treatment is more favourable than the arising basis. By choosing the remittance basis, you’ll only be taxed on UK sourced income and gains, not worldwide income, unless you decide to ‘remit’ those funds.

If you are UK tax resident and UK domiciled

You pay UK tax on all worldwide income and gains as they arise, regardless of whether the income and gains stay outside of the UK (arising basis). You don’t have the ability to shelter overseas income and gains from UK tax.

If you are UK tax resident and not domiciled in the UK

You pay UK tax on any UK sourced income and gains in the year in which they arise (arising basis). You can choose to pay tax on your foreign income and foreign gains or you can choose to exclude your foreign income and foreign gains by claiming the ‘remittance basis’ of taxation. The remittance basis of taxation allows your overseas income and gains to be excluded from UK tax as long as various conditions are met.

Domicile in action

Nadia, is domiciled in Dubai but she has been living in the UK for six years. She earns an income arising from the letting of her property in Dubai. To follow are two different scenarios assuming her overseas income is £10,000.

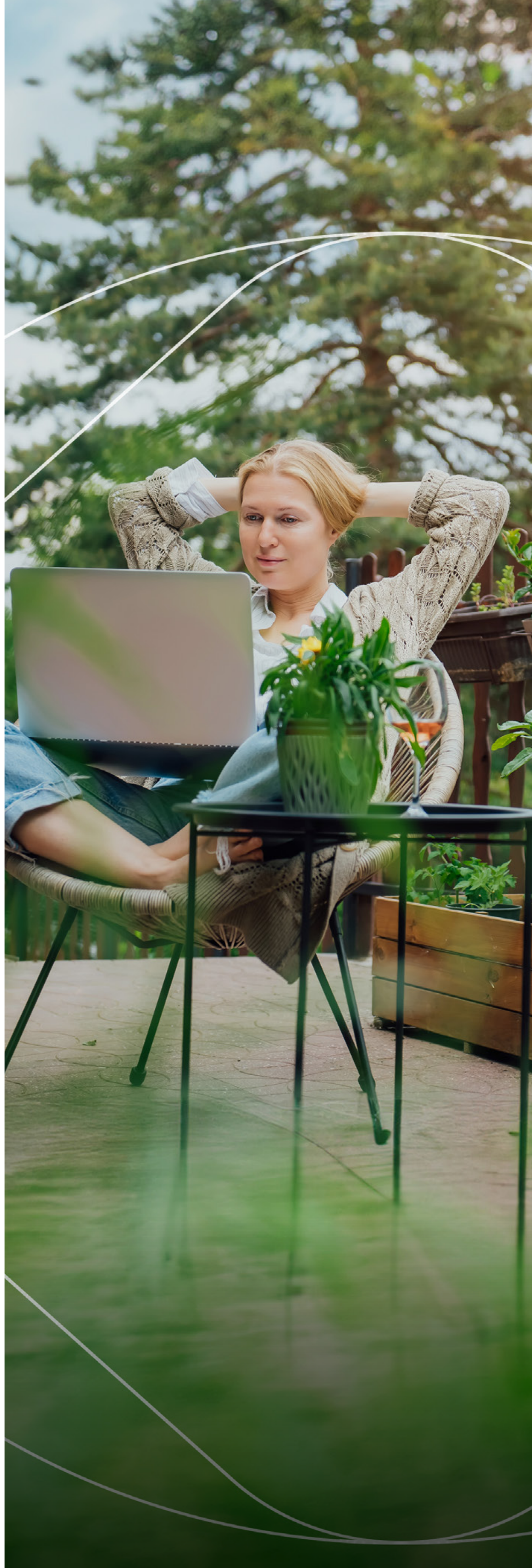
Scenario 1:

She transfers (remits) £1,000 of her overseas income to the UK - she can chose to pay UK tax on the full £10,000 overseas income as it arises, which will then allow her to keep her UK Income Tax personal allowance. If however she chooses to claim the remittance basis, she will only pay tax on the £1,000 transferred, but she will lose her UK Income Tax personal allowance to set against this or any other taxable income. If she transfers any of the remaining £9,000 to the UK she will then be taxed on it.

Scenario 2:

Nadia transfers (remits) £8,500 to the UK - she can have the benefit of the remittance basis, and pay tax only on £8,500 and not pay tax on the remaining £1,500 she has kept overseas. If at the end of the tax year her unremitted income/gains are less than £2,000, therefore she can use the remittance basis and still keep her UK Income Tax personal allowance.

There may be different treatment for particular types of income and gains if a double taxation agreement applies.



How domicile affects Inheritance Tax (IHT)

When someone dies, domicile is the key factor in assessing the extent of their estate's exposure to UK Inheritance Tax.

Estate when UK domiciled

UK Inheritance Tax is due in the UK on all worldwide assets.

40% Inheritance Tax charge applies.

A tax-free allowance, currently of £325,000 plus a £175,000 'family home allowance' generally applies.

Estate when not UK domiciled

UK Inheritance Tax is due only on assets held in the UK.

Overseas assets escape any UK tax charge (you'll need to be aware of any taxes due elsewhere).

UK assets generally enjoy a tax-free allowance, currently of £325,000 plus a £175,000 'family home allowance'.

The only way to control your exposure to IHT, and that of your heirs, is to create a comprehensive tax-efficient strategy tailored to your specific assets, residency and domiciliary status.

Here's an overview of when UK taxes are typically charged:

	Income & capital gains		UK investment property			Inheritance Tax – other assets	
Residence domicile	UK	Non-UK	Income Tax	Capital Gains Tax	Inheritance	UK	Non-UK
Non-UK resident, non-UK domicile	✓	✗	✓	✓	✓	✓	✗
UK resident, non-domicile	✓	✗ * **	✓	✓	✓	✓	✗
UK resident, UK domicile	✓	✓	✓	✓	✓	✓	✓
Non-UK resident, non-UK domicile	✓	✗	✓	✓	✓	✓	✓

*If using remittance basis ** Non UK chargeable events are always subject to tax in the UK even if the taxpayer is on remittance basis.

NON-TAX MATTERS

Every individual has a domicile status throughout life. This status determines how much UK tax we pay.

Not every country gives you the right to leave your assets as you wish, and you ought to take advice from local lawyers on what this means for you. Generally, we think you should consider having a Will on the country of your domicile, and another for each country in which you have houses or land. It is important that all the advisers are aware of the other Wills to avoid unintentional revocations.

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THE DIFFERENCE BETWEEN YOUR DOMICILE AND TAX RESIDENCE STATUS

Simply put, residence is based on your physical presence in the UK over the course of a tax year, whereas domicile is generally determined by your father's domicile or homeland.

It's highly unlikely that your domicile will change if you move to another country for a short to medium period, but if you live in another country your tax residence status is likely to change.

There are two key areas which define your exposure to UK tax:

1. UK tax residency – determined each year under the complex Statutory Residence Test

2. Your domicile status

WHERE AM I DOMICILED?

Working out which country you are domiciled in can be complicated and there are a number of factors that need to be considered.

There are three main types of domicile. You may also be 'deemed UK domiciled' depending on how long you've been resident in the UK.

1. Domicile of origin

This is acquired at birth, usually based on the domicile of your father. If your circumstances remain unchanged it's likely that you will retain your domicile of origin throughout your life.

2. Domicile of dependence

This domicile is acquired, generally when your father's domicile changes before you reach 16 years of age. Before 1974, women who married automatically acquired the domicile of their husband.

3. Domicile of choice

It's possible to acquire a domicile of choice in a certain jurisdiction. If you have a home overseas and want to move there permanently, you may be able to acquire a domicile of choice.

Changing domicile is a very significant step and you will need to show that you have left your original home country behind you forever, and chosen another country which is going to be your permanent home for the rest of your life. The onus is on you to prove that you have acquired a domicile of choice in another country.

Deemed domicile

From 6 April 2017, the rules changed for long-term UK tax residents who had a non-UK domicile of origin. From that date, these long-term UK tax residents are now deemed to be UK-domiciled for UK tax once they've held this status for 15 out of the 20 previous tax years.

CHANGING YOUR DOMICILE STATUS

Switching domicile away from the UK by choosing to be domiciled in another country is possible, but it's very hard to do and you should always seek specialist advice. In previous guidance the UK tax authorities shared the following about someone with a UK domicile acquiring a domicile of choice overseas:

"You have the capacity to acquire a new domicile (a domicile of choice) when you reach age 16. To do so, you must broadly leave your country of domicile and settle in another country. You need to provide strong evidence that you intend to live there permanently or indefinitely. Living in another country for a long time, although an important factor, is not enough in itself to prove you have acquired a new domicile."

So, if you are planning to leave your UK domicile behind, you need to demonstrate that you have severed your ties to the UK, with no intention to return, and, in addition, have chosen another country as your permanent home. Both conditions need to be fulfilled and can be difficult to prove.

It's important to note that if you become UK tax resident again in the future you'll be treated as though that domicile of choice had not been acquired.

If you're unsure of your domicile status, a domicile review can help you understand your exposure to UK tax. This can be very important for estate planning, especially if you have complex personal and financial circumstances.

DOMICILE IN ACTION

The case of Richard Burton

This fascinating case study illustrates the difficulties when trying to show you've acquired a domicile of choice outside of the UK (and replaced a UK domicile of origin) and the impact it can have on your Inheritance Tax bill.

Welsh Actor, Richard Burton CBE, moved to Switzerland in 1957, initially to escape UK tax, and spent the remaining 27 years of his life living there in the hope of claiming that he had acquired a domicile of choice. He died in Switzerland and was buried there, but his request for the burial of his body in a red suit, together with a copy of Dylan Thomas' poems and his coffin being draped in the Welsh flag, scuppered his plans to avoid Inheritance Tax. The result was an Inheritance Tax bill of £2.4 million, after the UK tax authorities successfully claimed that he had always kept his affection for Wales.

So, although it's possible to displace your UK domicile with a domicile of choice somewhere else, it's very hard to prove. Specialist advice is needed; particularly over how to provide evidence of your change in domicile status.

Contact us

We can help you with all aspects of your financing planning affairs.
Click here to contact us.

HOW WE CAN HELP

Domicile is an important topic for those with both UK and overseas connections.

Our global team of experts can help you understand your options by discussing your personal circumstances. They will guide you through the steps which you may need to take to protect your wealth and prepare for the future.

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