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Rosamond McDowell

Rosamond McDowell is a partner at Payne Hicks Beach Solicitors where she advises individuals, their families and their trustees, both offshore and onshore the UK, on all aspects of tax and estate planning. Email: rmcdowell@phb.co.uk; tel: 020 7465 4300.

Spring Budget 2017: Private client perspective

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Author(s): Rosamond McDowell

In a Budget where the big surprise was a national insurance contribution increase for the self-employed, for private clients, there has been no unexpected change of course, writes Rosamond McDowell (Payne Hicks Beach).

The chancellor's first and last Spring Budget contains few surprises for private clients. The changes to non-dom tax rules have long been trailed, and the draft legislation was already in print. New sanctions will now apply to those failing to report offshore tax liabilities – we have come a long way from disclosure facilities! UK land remains a hot topic; IHT will now apply irrespective of any offshore envelope, and the FA 2016 rules that subjected offshore property developers to tax in the UK have been tightened up.

Non-dom changes: As expected, from 6 April 2017 non-doms will be deemed domiciled in the UK for all tax purposes if they have been UK resident for at least 15 of the past 20 tax years, so they will lose the use of the remittance basis of taxation for income and capital gains tax, and inheritance tax will apply to their worldwide assets. But:

- non-UK based assets may be rebased to their market values on 5 April 2017; and
- offshore trusts set up before becoming deemed domiciled are protected (see below).

Individuals with a UK domicile of origin will be deemed UK domiciled for all tax purposes while they are UK resident.

Non-doms will also be able to 'clean up' mixed funds during the two year window of the tax years 2017/18 and 2018/19. This may enable individuals to release clean capital (which can be remitted to the UK without a tax charge) from accounts which currently contain a mix of clean capital and foreign income and gains.

Inheritance tax on land: Coming again as no surprise, from 6 April 2017, IHT will be charged on all UK residential property even where indirectly held by non-doms or trusts they have created through an offshore company. The rules are not simple, as the charge does not apply to the property itself but to the interest in the holding structure (be that a company or a partnership), as well as the benefit of loans to those structures if used to finance such property. 'De-enveloping' planning is already widely underway, and will continue to be effected after 5 April, ideally before the occurrence of any significant taxable event! No reliefs were offered to assist people in de-enveloping their residential property structures, and none have materialised in the Budget.

Protection of overseas trusts: The changes to the tax rules affecting offshore trusts have been in draft since December 2016 (for CGT) and January 2017 (for income tax). Essentially, non-doms will continue to be protected from capital gains tax charges under TCGA 1992 s 86 and income tax under the Settlement Code (ITTOIA 2005) and the Transfer of Assets Code (ITA 2007), even if they become deemed domiciled, but the protection is withdrawn if property is added to the trust after 6 April 2017 (subject to the clarification of proposed transitional rules). Attribution and matching of income under ITA 2007 s 731 and gains under TCGA 1992 s 87 will continue to apply, though payment to non-residents will no longer be matched against gains after 5 April 2017. When the draft legislation was first published, it was feared that gains washed out to non-residents prior to 6 April 2017 would be added back to the capital gains pool to be matched on UK residents receiving a benefit in the future. HMRC has commented that this is not the intention, and that only unmatched payments to non-residents will be ignored post 5 April 2017, but this clarification has not yet materialised in the draft Finance Bill.

Offshore non-compliance and the requirement to correct: The draft Bill establishes a new legal 'requirement to correct' for those who have failed to declare UK capital gains tax, income tax or inheritance tax on offshore interests, with the intention of motivating these persons to make a disclosure to HMRC before information is passed to it under the common reporting standard. Punitive sanctions will apply for those who fail to put their houses in order before 1 October 2018, to include penalties of up to 200% of the unpaid tax. Also, HMRC may name and shame the worst offenders. The new requirement will apply to all taxpayers who are in default as at 5 April 2017.

Reduction in the dividend allowance: Dividend income that is charged to income tax on individuals (though not trustees) at 0% by ITA 2007 s 13A will reduce from £5,000 to £2,000 from 6 April 2018. This reduces the tax advantage offered to those who work through a personal service companies in being able to receive their income at dividend rates. Together with an increase in class 4 NICs (to 11% in April 2019), it will reduce the tax differences applying to employees and the self-employed.

QROPs: Since FA 2004, it has been popular for UK individuals to transfer their pensions to a qualifying recognised overseas pension scheme (QROPS), potentially avoiding tax. As a result, the draft Finance Bill 2017 contains legislation subjecting transfers to QROPS requested on or after 9 March 2017 to tax at a rate of 25% unless, broadly, both the individual and the pension savings are in the same country, both are within the European Economic Area, or the QROPS is provided by the individual's employer. The charge is to be withheld by the scheme administrator. Tax charges will also apply to distributions out of the funds transferred within the five tax years following the transfer.

Life insurance policies: Life insurance policies are currently subject to special rules, so that surrenders or assignments annually of up to 5% of the premium paid do not incur a tax charge. Surrenders or assignments in excess of the cumulative annual allowance may generate a charge to income tax. It is, however, possible to generate a huge charge to tax by making a large surrender or assignment early in the life of the policy, so that the gain subject to charge is far in excess of any underlying economic gain on the policy. New draft legislation means that, with effect from 6 April 2017, policyholders in this position may apply to HMRC to have their gain recalculated on a just and reasonable basis.

Non-resident companies consultation: Originally announced at Autumn Statement 2016, the government will be consulting on the rationale and options for bringing non-UK resident companies within the scope of corporation tax. These companies are already subject to income tax on UK source income (e.g. rent on UK properties), and to non-resident capital gains tax on residential property. Let's see what is to follow!