



PRIVATE CLIENT

KPMG's Private Client Update

TAX

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Agreeing your domicile status with HMRC

There is greater uncertainty for taxpayers who wish to agree their domicile position with HMRC following changes in HMRC policy in March 2009 and August 2010.

With effect from 26 March 2009, HMRC ceased to consider an individual's domicile position for income tax and capital gains tax following submission of a DOM1 form. For income tax and capital gains tax, individuals now have to self-assess their position which HMRC may enquire into subsequently. In August 2010, a new policy was also announced on the circumstances in which HMRC would consider an individual's domicile position for inheritance tax purposes. The new policy may cause greater uncertainty for taxpayers. This update therefore sets out how best to deal with your domicile status.

What is domicile for income tax and capital gains tax purposes?

Domicile is a legal term which connects an individual to a territory that has a distinct system of law, e.g. England and Wales, Scotland, France. There is no precise definition but, broadly speaking, under English law, you are domiciled in the country that is your permanent home. Everyone is born with a domicile of origin (usually taken from their father) and this domicile is "sticky" and very difficult to lose. Someone born in the UK to a UK domiciled father could remain UK domiciled even after living abroad for many years. This is the concept of domicile that applies for income tax and capital gains tax purposes; there is no separate legislative definition.

What about domicile for IHT?

For IHT, there is an additional concept of "deemed domicile". An individual is deemed to be domiciled in the UK for IHT purposes if they have been resident in the UK during 17 of the last 20 tax years (including the current tax year of assessment). Care should be taken in relation to deemed domicile as an individual becoming UK tax resident on 4 April 1996 could be deemed domiciled on 6 April 2011; only 15 years and two days later!

How do you claim to be non-UK domiciled for income tax and capital gains tax?

Following the withdrawal of form DOM1, a claim to be non-UK domiciled is usually made via the self-assessment tax return process. Effectively, the individual self-assesses their non-UK domiciled status by ticking the appropriate box on their UK tax return. HMRC then have a 12 month period, starting with the date of submission, in which to open an enquiry into the tax return.

Once the enquiry window has elapsed, the tax return can be considered final. However, HMRC have an additional period in which they can revisit a tax return if they discover that it has been completed incorrectly. If an error or omission from a taxpayer's return is **not** deliberate nor is it attributable to the taxpayer's failure to take reasonable care, HMRC have up to four years from the year of assessment concerned to raise an assessment. Where the error or omission is deliberate, the time limit is extended to twenty years. Given the limited information required to complete a tax return, individuals will need to consider what additional information, if any, should be included on their tax returns to minimise the risk of HMRC being able to revisit submitted tax returns in later years.

Even if HMRC do not enquire into an individual's domicile position for a given year, this cannot necessarily be taken to mean that they have reviewed and agreed the position. This can be an issue where an individual may want to "test" their domicile position before entering into a significant transaction in a future tax year.

How do you claim to be non-UK domiciled for IHT purposes?

There is no requirement to complete an IHT return where there is no liability to IHT due to the non-UK domiciled (and non-UK deemed domiciled) status of the transferor and the non-UK situs of the assets transferred. Effectively, such transfers simply fall outside the scope of the UK IHT regime. It is therefore extremely difficult to ensure that HMRC have an opportunity to consider an individual's domicile status in relation to IHT. If there is some doubt as to a taxpayer's domicile status then the individual may wish to "test" the position by transferring a relatively modest amount into a trust; the amount should be sufficient to potentially create a charge to IHT. It is then possible to write to HMRC setting out what has occurred and why there is no liability to tax.

However, on 24 August 2010 HMRC issued a new brief (HMRC Brief 34/10) in relation to domicile and IHT. In short, HMRC advised that they are unlikely to consider the validity of a claim to being non-UK domiciled unless there is a significant risk of loss of UK tax. In deciding the risk, HMRC will take account of the information they have about the individual, the amount of tax at stake and the cost of carrying out the enquiry. HMRC also warned that, where they do investigate a claim of non-UK domicile, the questions raised can be invasive due to the type of evidence required to substantiate the claim.

Where are we now?

The taxpayer is left with a higher degree of uncertainty due to the withdrawal of form DOM 1, the vagaries of the self-assessment process and the policy contained in the HMRC brief on IHT. There is no longer any formal process for agreeing domicile status with HMRC outside of an enquiry and tacit acceptance may be the best that can be achieved. It is therefore more important than ever to obtain comprehensive tax advice in relation to domicile status. Advice should be obtained at an early stage so that appropriate information can be recorded to support a claim to non-UK domicile status. KPMG has a domicile questionnaire which may be useful in this regard. KPMG can also advise non-UK domiciled individuals on the significant tax benefits that may be available.

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