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Reforms to the UK's non-dom regime

On 30 October 2024, the UK Chancellor, Rachel Reeves, presented her first Budget. It had been clear for some time that major reforms to the taxation of the UK's population of resident non-domiciliaries (RNDs) would be forthcoming – in a surprise move at the Spring Budget 2024, the previous Conservative Government had announced the abolition of the non-dom regime, to be replaced with a new four-year residence-based foreign income and gains (FIG) regime, as well as reforms to inheritance tax, and the Labour Party had confirmed its broad support for these proposals in the run up to the General Election in July 2024, stating in their manifesto that a Labour Government would "*abolish non-dom status once and for all, replacing it with a modern scheme for people genuinely in the country for a short period*". The 2024 Autumn Budget provided further detail on these reforms, and draft legislation was published which has now been enacted as part of the Finance Act 2025.

This note summarises the key features of the new regime applicable from 6 April 2025, as compared to the previous rules for RNDs, and explores some of the available options, both for new arrivers to the UK and for individuals who have been UK resident for some time.

The "non-dom" regime

Before 6 April 2025, the UK's non-dom regime enabled RNDs to:

- elect to be taxed under the favourable "remittance basis" of taxation during their first 15 years of UK tax residence (whereby, in broad terms, qualifying individuals were subject to UK tax only on UK source income and gains, and any non-UK source income and gains which they "remitted" to the UK);
- be liable to UK inheritance tax only in respect of UK situs assets during their first 15 years of UK tax residence (and, potentially, for a longer period within an "excluded property" trust structure); and
- benefit from advantageous income and capital gains tax treatment in relation to trusts (even after the initial 15 years of UK tax residence) that qualified for "protected settlement status".

The new FIG regime

With effect from 6 April 2025, it is no longer possible to claim the remittance basis of taxation (although the previous remittance rules – albeit with a few specific amendments which widen the meaning of remittance – continue to apply to unremitted FIG which arose prior to 6 April 2025) and the remittance basis has been replaced by a new four-year residence-based FIG regime.

Who is eligible?

Individuals will qualify for the FIG regime if they have been non-UK tax resident for at least 10 consecutive years (assessed by reference to the UK's statutory residence test), regardless of their domicile status.

Accessing the FIG regime

Although there is no charge to access the FIG regime, it does not apply automatically and must be claimed in an eligible individual's UK tax return within 12 months of the 31 January after the end of the relevant tax year.

The amount of FIG for which relief is being claimed must be quantified, and such amounts included in the tax return. It is possible to make a claim for either income or gains, or both, and to select specific sources of FIG on which relief is claimed.

Taxation of personally held FIG

The new regime gives qualifying individuals 100% relief from UK tax on certain categories of FIG (broadly, those that previously qualified for the remittance basis) that arise during their first four years of UK residence (provided, of course, that a claim for relief is made, as set out above). Unlike the previous remittance basis of taxation, such relief applies irrespective of whether the FIG in question is brought to or used in the UK.

Once an individual ceases to qualify for the FIG regime (i.e. after their initial four years of UK residence), they will pay UK tax on their worldwide income and gains on the arising basis.

Taxation of trust FIG

From 6 April 2025, the preferential income and capital gains tax treatment of "protected settlements" was removed from all trust structures (including those already in existence). However, under the new rules, for as long as an individual qualifies for (and claims) the FIG regime, they will not pay UK tax on trust FIG, either as it arises or upon receipt of trust distributions.

Once the individual is no longer eligible for the FIG regime, they will, in general, be liable to pay UK tax on all profits arising within a trust structure which they have established, as well as on benefits received which are matched with trust income or gains.

Overseas workday relief

Before 6 April 2025, overseas workday relief (OWR) was available to certain RND employees for their first three years of UK residence (following a minimum of three consecutive tax years of non-UK residence) who performed at least part of their employment duties overseas, and permitted the apportionment of their salary between UK and non-UK duties, with the latter eligible for the remittance basis of taxation. From 6 April 2025, the OWR rules have been modified, such that:

- it is available for up to four years (increased from the previous three years) to taxpayers who qualify for the FIG regime;
- it is subject to a financial limit of the lower of 30% of the qualifying foreign employment income or £300,000 per tax year; and
- it applies whether or not the qualifying employment income is received in or brought to the UK.

There are specific transitional provisions for taxpayers who started claiming OWR prior to 6 April 2025.

Transitional provisions

By way of recognition that the reforms represent a significant change to the taxation of RNDs, certain transitional arrangements have been made available.

Temporary Repatriation Facility

RNDs who have previously been taxed on the remittance basis will be able to access a three-year Temporary Repatriation Facility (TRF) in respect of FIG that arose (either to the individual personally or within a trust structure which is attributed to the individual or matched to benefits received by that individual) before 6 April 2025.

A special tax rate will apply to a "designated amount" (12% in 2025/26 and 2026/27, rising to 15% in 2027/28) and, once this has been paid, no further UK tax will arise on the designated amount, irrespective of whether it is remitted to the UK (although care may need to be taken in respect of trust distributions which are then remitted to the UK).

Capital gains tax rebasing to 5 April 2017

RNDs who have previously claimed the remittance basis in any one of the 2017/18 to 2024/25 tax years (and were neither UK domiciled nor deemed domiciled (by virtue of at least 15 years' UK residence) by 5 April 2025) will qualify for a rebasing relief. Unless such individuals elect for rebasing not to apply to a specific disposal, assets will be rebased for capital gains tax purposes to their value at 5 April 2017, but only if they (i) are personally held; (ii) have been owned since 5 April 2017; (iii) were non-UK situs from 6 March 2024 to 5 April 2025; and (iv) are disposed of on or after 6 April 2025.

Inheritance tax

Before 6 April 2025, an individual's liability to inheritance tax depended on their domicile status (with an individual being deemed domiciled in the UK once they had lived here for 15 out of the last 20 years) and the location of the asset in question. However, since 6 April 2025, domicile is no longer a connecting factor and has been replaced by the concept of long-term residence.

An individual will be a long-term resident once they have been UK resident for at least 10 out of the last 20 tax years. From year 11, their worldwide assets will fall within the scope of inheritance tax (even if they are not UK resident in year 11), and will remain as such for a certain period (a minimum of three years, rising to a maximum of 10 years for individuals who are UK resident for 20 years or more) following their departure from the UK. There are transitional rules for individuals who left the UK before 6 April 2025 which effectively apply the previous rules in order to ascertain the duration, if any, of the inheritance tax "tail".

One effect of the new rules is that an individual who remains domiciled in the UK but who has been non-UK resident for at least 10 years is, from 6 April 2025, outside the scope of UK inheritance tax as they will not be a long term resident.

As far as the inheritance tax treatment of trusts is concerned, under pre-6 April 2025 rules, non-UK assets, held in trust structures which were established by RNDs before they became deemed domiciled in the UK, were outside the scope of inheritance tax (even after the RND became deemed domiciled). Since 6 April 2025, whether non-UK trust assets are within the scope of inheritance tax depends primarily on whether the settlor is a long-term resident at the time the relevant inheritance tax event occurs or, if the settlor has died, whether the settlor was a long-term resident at the date of their death.

This means that non-UK trust assets can move in and out of the scope of inheritance tax in accordance with the settlor's inheritance tax status. Note that when trust assets move outside the scope of inheritance tax (due to the settlor ceasing to be a long-term resident), an "exit" charge under the relevant property regime (at a maximum rate of 6%) will arise.

There are transitional arrangements for trusts which were established prior to 30 October 2024 (and were outside the scope of inheritance tax at that date). For such trusts, there will (generally) be no inheritance tax charge on the settlor's death (irrespective of the settlor's inheritance tax status on death). However, if the settlor is (or becomes) a long-term resident, the trust assets will not be protected from inheritance tax 10-year or exit charges arising (at rates of up to 6%) under the relevant property regime.

Options for private clients

The reforms will have major implications for private clients. However, the available options and most appropriate course of action will depend on the individual's specific circumstances. We set out some of the key points to be considered below.

New arrivers

Although the duration of the new four-year FIG regime is significantly shorter than the previous 15-year remittance basis of taxation, the complete tax exemption on offer in respect of FIG arising during the four-year period, regardless of whether it is remitted to the UK, means that there is no longer a disincentive to bringing such funds to the UK, and the potential for double taxation due to a mismatch of tax liabilities in the UK and the individual's "home" jurisdiction is also removed. The fact that, unlike equivalent regimes in some other jurisdictions, there is no charge to access the FIG regime and there are no restrictions imposed on qualifying individuals' ability to work in the UK further enhances its flexibility.

New arrivers who qualify for the FIG regime will, where possible, wish to time major disposals (or rebasing) of non-UK assets and the receipt of non-UK income so that these events occur during the four-year tax-free period. If such individuals decide to remain in the UK beyond the four-year mark, consideration can be given to the use of investment vehicles which "roll up" profits within the vehicle.

New arrivers will also remain outside the scope of worldwide inheritance tax for their first 10 years of UK residence. During this period, non-UK trusts may be established without an immediate charge to inheritance tax and, once the settlor becomes a long-term resident, the trust assets will continue to be excluded from inheritance tax on the settlor's death (but not in relation to 10-year and exit charges under the relevant property regime) if the settlor is excluded from benefit under the terms of the trust. Life insurance policies may also be of assistance to cover the potential inheritance tax liability after 10 years of UK residence.

Returning UK domiciliaries

As set out above, an individual's domicile status is irrelevant under the new regime. This means that UK domiciliaries (as well as individuals who would be classed as "formerly domiciled residents" under the previous rules) can benefit from the FIG regime upon their return to the UK, provided that they have the requisite 10-year period of non-UK residence. Accordingly, the considerations set out above in relation to new arrivers also apply to returning UK domiciliaries.

Former RNDs

Although the FIG regime will be an attractive option for new arrivers and returning UK domiciliaries, only a small proportion of RNDs who decided to remain in the UK following 6 April 2025 will be eligible to benefit from it. However, the transitional arrangements may go some way towards mitigating the impact of the reforms.

- **TRF**

  As explained above, the TRF will allow former remittance basis users to bring funds representing pre-6 April 2025 FIG to the UK for spending or investment at a favourable tax rate. In many cases, this will have required careful planning pre-6 April 2025 to ensure that funds are eligible for the TRF – since it applies only to pre-6 April 2025 FIG, it may have been necessary for individuals or trustees to realise latent gains or accelerate receipts of non-UK income before 6 April 2025, with such funds being "designated" under the TRF in the 2025/26 tax year.

- **Rebasing opportunities**

  A rebasing facility is also available for personally held assets which were owned on 5 April 2017; however, the limitations placed on this relief may, in many situations, mean it is of little practical use.

- **Trusts**

  Although the reforms significantly erode the tax benefits associated with many trust structures, this will not be the case in all circumstances. For example, existing trusts whose settlor is already deceased or long-term non-UK resident will, in general, be unaffected by the reforms. Existing excluded property trusts with a living UK resident settlor will, as mentioned above, continue to be protected from inheritance tax on the settlor's death (although this is at the cost of inheritance tax charges under the relevant property regime at a maximum of 6% every 10 years). It may also be possible to mitigate the income and/or capital gains tax exposure for the settlor following the removal of protected settlement status, either by excluding the settlor and their spouse from benefiting from the trust and/or by careful choice of trust investments.

Next steps and further information

These reforms represent a significant change to the way in which private clients with an international connection are taxed in the UK. As set out above, the most appropriate course of action will depend on each individual's personal circumstances so expert advice will be essential.

For further information or specific advice, please get in touch with your usual Macfarlanes contact.

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