Forewarned is forearmed: Preparing for the abolition of the existing non-dom regime

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When the Conservative Party announced their proposal to abolish the existing non-dom regime in March 2024, there was an audible sharp intake of breath from clients and practitioners across the tax, private client and trust industries. Just as we were starting to consider what the changes would mean and when they would take effect, (the then) Prime Minister Rishi Sunak announced that a general election would be held on 4 July 2024.

By the time this article is published, the election will be over. Regardless of who's in power, significant changes to the non-dom regime are inevitable and they look likely to have an impact on foreign trusts.
In this article, we consider what trustees of foreign trusts can do now to ensure that they are best placed to respond to the changes.

What are the proposed changes?

Under the existing non-dom regime, certain UK residents with a permanent home/domicile elsewhere (so called non-doms) are not required to pay UK tax on foreign earned income and gains unless and until they receive it in the UK. This has historically led some individuals to settle a foreign "protected trust" prior to becoming UK resident, so that any income and gains arising on the assets settled are not taxed in the UK unless and until they are remitted to the UK.

Under the proposals, UK-resident non-doms will pay UK tax on all foreign income and gains, subject to certain provisos, time periods, transitional rules and double taxation treaties.

Significantly, the new residency-based regime will also capture foreign income and gains arising within trust structures, resulting in a potential tax liability in the hands of a non-dom settlor of a foreign trust. Inheritance tax in respect of trusts is also subject to review and further consultation.

What steps can trustees take now?

1. Undertake a full health-check

As a starting point, trustees should review their existing structures to identify those trusts which may be affected based on where the settlor resides (this includes all individuals that have settled assets into the trust). These trusts can then be prioritised later in the year in terms of considering potential changes once we have clarity on the effect of the new regime.

Undertaking a health-check also provides an opportunity to review the structure with fresh eyes to ensure everything is as it should be including, for example, that accounts are up to date, 10-year anniversaries are diarised where relevant and supplemental instruments are fully executed.

2. Consider the class of beneficiaries and their requirements

As part of the health-check trustees should determine which of the trusts that might be impacted have a closed class of beneficiaries and which include remoter issue and unborns. Knowing this will impact the trustee's fiduciary considerations and potentially the options available to them. Trusts with a closed class of adult beneficiaries will likely prove easier to deal with should significant decisions need to be made quickly in circumstances where those beneficiaries are willing to provide the trustee with a release.

3. Open a dialogue with the settlor

For trusts that have UK-resident non-dom settlors, now is a good time to discuss with them what their intentions are and whether this is reflected in their letter of wishes.

- Do they intend to remain in the UK for the time being due to family and/or business circumstances, or are they considering exiting in view of the proposed changes?
- Are they discussing the changes with an advisor and have they received any initial advice on how the changes might impact them and the trust?
- Are they considering taking any steps with regard to their financial affairs in order to mitigate the impact of the new regime, such as becoming an Excluded Person who is unable to benefit from the trust in the future?
- If this is a potential consideration, do they understand the ramifications of being excluded, namely that they can no longer benefit from the trust directly or indirectly?

This conversation should be started as soon as possible and used as an opportunity to reconfirm the settlor's intentions for the trust – for instance, is the primary purpose tax planning or is it driven by other factors such as asset protection and succession planning.

4. Review the trust deed

Excluding one or more beneficiaries, particularly a settlor who has to date been regarded as a principal beneficiary, is something a trustee may be asked to consider in light of the abolition of the existing non-dom regime. Settlors should be advised that this is not something a trustee would do at short notice without careful thought and advice.

Some concern has been expressed in relation to the volume of clients who will need advice and changes to be made to their trusts at short notice. Potential time pressures may be alleviated by the trustee reviewing the relevant provisions of their trust deeds now to see whether any improvements can be made at this stage to increase flexibility. For instance, does the trust deed enable a beneficiary to disclaim their interest in the trust and to declare themselves to be an Excluded Person or could such a power be introduced? This would allow beneficiaries to make this decision of their own volition, taking pressure off the trustee being asked to exercise their power of removal.

Another power that trustees may be asked to exercise at short notice is to make significant distributions from the trust thereby reducing the trust fund and potential tax exposure. Alternatively the trustee may be requested to distribute the whole of the trust fund to a beneficiary who is resident in a more favourable jurisdiction, with the intention that they then re-settle the trust. Again, the drafting of the trust deed should be checked to ensure that the powers of appointment are clear and that they can be exercised in favour of one or more beneficiaries to the exclusion of the others (following careful consideration).

In reviewing the trustee's powers, it is important to ascertain whether the trustee can exercise the power solely or if the consent of another power holder (such as the settlor or the protector) is required. Where the trustee does not have sole discretion over the

exercise of the power to remove a beneficiary or make an appointment, contact should be made with the power holder now to alert them to the fact that their input may be required at short notice and to agree how best this can be obtained.

5. Take professional advice

To understand the effect of any legislative changes surrounding the non-dom regime so that the trustee can properly consider what actions to take, it is critical that tax advice is obtained. Where the settlor and/or a beneficiary has taken their own tax advice, the trustee should request a copy of this to satisfy itself that the advice is appropriate and based upon a correct understanding of the facts.

It would be a breach of fiduciary duty for a trustee to simply rely on an oral confirmation that a beneficiary has received tax advice, and ideally the trustee should always obtain their own independent advice which will take into account the varying interests of the beneficiaries in light of the power they are considering exercising. Most trusts will have incumbent advisors but it is essential to check that any trusts with UK resident non-dom settlors have advisors in place now who are able to assist promptly.

6. Consider preparing legal documents that may be required at short notice

Similarly, instructing lawyers now might be prudent to enable relevant legal documentation to be pre-prepared so it is available at short notice should the trustee decide to take a particular course of action. This could include documents such as supplemental instruments of exclusion of beneficiaries, instruments of appointment of capital, or instruments of amendment to the terms of the trust deed, as well as potentially breach of trust style indemnities which might assist in circumstances where the trustee is asked to make a momentous decision in circumstances where time constraints mean a court blessing is not possible.

While some time pressures on trustees are inevitable as the year progresses, planning and preparing ahead of time will certainly ease the process.

This article by Victoria Yates and Bonnie McPartland was first published in issue 15 of ThoughtLeaders4 Private Client magazine. See here.

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