

TREATIES WHICH OVERRIDE THE IHT DEEMED DOMICILE RULES

by Patrick Soares

Practitioners must be aware that with regard to taxpayers who are domiciled in India and Italy that the death duty treaties with those countries restrict the operation of the IHT deemed domicile rules. The restrictions may result in major inheritance tax (IHT) savings.

If a taxpayer who is domiciled within the UK dies, he is liable to IHT on all his assets regardless of where the same are situated (IHTA 1984 s.4(1)). If the individual is not domiciled in the United Kingdom at the time of his death, then all assets situated outside the United Kingdom are not chargeable to inheritance tax (IHTA 1984 s.6(1)). However, an individual may be deemed to be domiciled in the United Kingdom for inheritance tax if he was tax resident in the United Kingdom in not less than 17 of the 20 years of assessment ending with the year of assessment in which the death takes place (IHTA 1984 s.267(1)).

The deemed domicile rule is ignored for the purposes of the above four treaties in certain circumstances (IHTA 1984 s.267(2) and s.158(6)).

India

Article III of the UK/India Treaty of 3rd April 1956 (SI 1956/998) states thus:-

“Duty shall not be imposed in Great Britain on the death of a person who was not domiciled at the time of his death in any part of Great Britain but was domiciled in some part of India on any property situate outside Great Britain: provided that nothing in this paragraph shall prevent the imposition of duty in Great Britain on any property which passes under a disposition or devolution regulated by the law of some part of Great Britain.”

Thus, to take a simple case, if Mr X dies domiciled in India in accordance with English and Indian law, but he is deemed to be domiciled in the United Kingdom for the purposes of UK inheritance tax (under IHTA 1984 s.267), he will not pay UK inheritance tax on any property of his which is located outside the United Kingdom and which passes under a disposition or devolution regulated by a law other than that of Great Britain. Thus if he dies owning property in Portugal, and that property devolves according to a Portuguese will, no IHT will be in point in spite of the fact that he is deemed to be domiciled in the UK.

Italy

The terms of the Italian Treaty are similar, but there are some significant differences, and the Treaty is less likely to be as useful in practice as the UK/Indian Treaty. The relevant treaty is the UK/Italian Treaty of 15 February 1966 (SI 1968/304). Article V states that where duty is imposed by the UK on the death of a person who at the time of his death was not domiciled in any part of the UK but was domiciled in Italy (according to Article

43 of the Italian Civil Code “the domicile of a person is the place where the person has established the main centre of his affairs and interests”), then no account shall be taken in determining the IHT payable “of property situated outside the (UK) provided that this (exemption) shall not apply to duty imposed (in the UK) on property passing under a settlement governed by its (UK’s) law,”

Thus – to take a simple case – if the deceased was domiciled in Italy according to UK law (albeit deemed domiciled in the UK under IHTA 1984 s.267) and according to Italian law at the date of death, all his free estate which is located outside the UK – e.g. land in Portugal – is free of UK inheritance tax; that is the case even though the devolution is governed by English law. Only if the overseas property is in a settlement which is governed by English law does a problem arise.

The other point with regard to the Italian treaty is there is a tie-breaker clause determining domicile in Article II(2)(b). If the deceased had strong UK ties, Italian law may treat him as having a UK domicile, and the tie-breaker clause the tie-breaker may also point to him having a UK domicile. If that is the case, then the special relief in Article V(2) would be of no help, as that envisages the deceased not being domiciled in the UK under the terms of the treaty.

The conclusion is if a taxpayer is domiciled in one or other of the above mentioned four jurisdictions but at the same time he is deemed to be domiciled in the United Kingdom for the purposes of inheritance tax then it is vital that practitioners look at the terms of the treaties

and this may involve actions being taken during the lifetime of the taxpayer to ensure that he comes within the terms of the treaty on his death.