A TALE OF TWO DOMICILES

By Nikhil V. Mehta

There was once a Martian pupil who was a keen student of comparative fiscal jurisprudence. While on a sponsored sabbatical from Mars, he asked his supervisor a number of questions relating to the India/UK Estate Taxes Double Tax Avoidance Treaty 1956 ("the Treaty").

Question 1:

"If neither the United Kingdom nor India have estate duty any more, what's the point of a double tax avoidance convention between the two countries relating to estate duties?"

"Ah," said the supervisor with a twinkle in his eye. "A very good question, which baffles many. And in the answer hangs a tale. Pull up a chair and let me tell you."

The supervisor began by saying that India had done away with estate duty in 1985 and not replaced it with any other form of tax on death. In the UK, he explained the devolution of death taxes from estate duty to capital transfer tax and then to inheritance tax. He then referred his pupil to Section 158 of the Inheritance Tax Act 1984 and took him through how the UK had extended the application of the Treaty to inheritance tax ("IHT"). India had done nothing comparable as there was nothing in tax terms to which the Treaty could be extended. But the Treaty was not terminated.

"Does that mean that the Treaty, which deals with double taxation between the two countries, applies even though there is only single taxation?"

"Er, yes, but if India brings back estate duty, it would double up again".

The pupil was a little nonplussed by this reply, but went on to ask about domicile.

Question 2:

"I see that the Treaty divides taxing rights between the two countries by reference to an individual's domicile at death and that the country of domicile is determined by the law in force in that country relating to duty. What happens if an individual is deemed domiciled in the UK but his actual domicile is in India?"

"Another very good question", said the supervisor. "The answer is that deemed domicile, which is a post-Treaty unilateral definition created by the UK, cannot trump the definition of domicile under the Treaty. That is made clear by Section 267(2) of the Inheritance Tax Act 1984."

Question 3:

"You mean that someone who dies deemed domiciled in the UK but is domiciled in India under the Treaty will not suffer IHT on his offshore assets?"

"Absolutely, but subject to one catch. This only applies if the foreign assets pass under a foreign will and not under a will made here. So, it is important for such an individual to have appropriate wills made both in the UK and India – and perhaps even in other countries depending on where the assets are."

The Martian looked at his supervisor slightly agog, but had all the information he needed, so thanked his supervisor and got up while browsing through his hard copy of the Treaty.

He had an afterthought:

Question 4:

"Just one more question, if I may. If India no longer has estate duty, how do you determine whether someone had Indian domicile at death? Which Indian law determines this since there is no law which relates to estate duty?"

The supervisor smiled and said: "I think you had better sit down again. This question has created a lot of confusion and generated some misleading answers.

The confusion arises in part because Article 3 of the Treaty

talks about someone being domiciled "in some part of" India and "in some part of" Great Britain. It's easy to see that for Great Britain, the word "part" makes sense because an individual can have, for example, an English domicile or a Scottish domicile. The word as it applies to India is misleading because it suggests that an individual could have a domicile in one state as opposed to another and not a single domicile for the whole of India. But the Indian Courts have generally rejected this federal approach to domicile in favour of a national concept based on private international law. The word "part" does not make sense as a federal concept under the Treaty. There are situations where "domicile" has been used in a state context-for example, for student university admissions where priority is given to students domiciled in a particular state. But the Supreme Court, in the leading case of *Dr Pradeep Jain v Union of India [1984] (3) 942* said:

> "The concept of domicile has no relevance to the applicability of municipal laws, whether made by the Union of India or by the States. It would not, therefore, in our opinion be right to say that a citizen of India is domiciled in one state or another forming part of the Union of India. The domicile which he has is only one domicile, namely, domicile in the territory of India. When a person who is permanently resident in one State goes to another State with the intention to reside there permanently or indefinitely, his domicile does not undergo any change: he does not acquire a new domicile of choice. His domicile remains the same, namely Indian domicile."

"Part", therefore, in the Treaty, should not be given any undue significance insofar as it applies to India. One's suspicion is that the draftsman was simply trying to achieve parity when describing India and Great Britain.

But given that "domicile" is used in different areas of law, which meaning applies to the Treaty? The logical starting

point is the Estate Duty Act 1953. Even though that has been repealed, it gives some strong pointers. Section 3 of that Act said that a domicile of an individual should be determined as if the Indian Succession Act 1925 applied to him.

The good news is that the 1925 Act is still in force, so it forms a more than persuasive basis for determining domicile under the Treaty.

Section 7 of that Act says:

> "The domicile of origin of every person of legitimate birth is in the country in which at the time of his birth, his father was domiciled; or, if he is a posthumous child, in the country in which his father was domiciled at the time of the father's death."

The Martian pupil interjected: "This is very similar to the English law concept of domicile!".

"Not only that", said the supervisor, "but the Indian courts have consistently followed English cases in looking at domicile even though the cases only have persuasive value. So, the exercise of determining domicile under Indian law has many similarities with English law. Hardly surprising, really, given the common law origins of both legal systems. But let's just go on with the Indian Succession Act. Incidentally, that was of course drafted by the British. The Act acknowledges that a domicile of origin can change, and become a domicile of choice. So, another similarity! And the beauty of the Indian position is that all of this is enacted, so the law is clear-although of course its correct application to any given set of facts remains the province of lawyers and the courts. One cannot, incidentally, assume that the courts will blindly follow English case-law, although they will give it great importance. They will also do the same with leading publications like Dicey & Morris.

There is one peculiar provision which I should mention, which is Section 11. That states:

> **"11. Special mode of acquiring domicile in India.**

> Any person may acquire a domicile in India by making and depositing in some office in India, appointed in this behalf by the State Government, a declaration in writing under his hand of his desire to acquire such domicile; provided that he has been resident in India for one year immediately preceding the time of his making such declaration."

Read literally, anyone could acquire an Indian domicile under this provision by being resident in India for at least a year and depositing the written declaration with the specified office of the Indian Government. But before one gets too carried away with the planning potential of this, I must tell you that it is toothless for the simple reason that the Indian Government do not have such offices. The provision is linked to the British Domicile Act 1861, which was repealed many years ago. Section 1 of that Act provided that a British subject dying in a foreign country did not acquire a foreign domicile unless he had properly made and filed the written declaration in the designated office in that country. For all practical purposes, this procedure is dead and can be ignored.

One last point: where an individual who is deemed domiciled here dies and has a domicile of origin in India, that domicile still has to be substantiated with HMRC. I gather that sometimes this has been attempted by providing so-called certificates of domicile from Indian state authorities. But these do not address the question of domicile under the Indian Succession Act, which is the only relevant test of domicile. And, as I have said, a state domicile is insufficient anyway and involves an incorrect use of the legal expression "domicile". The best way of substantiating domicile in India is a legal opinion from a suitably qualified lawyer based on evidence. HMRC will rightly question whether someone who lived most of his life in England had in fact acquired a domicile of choice in England. Viewed from the Indian side, the fewer connections someone like that

had in India, the harder it will be in practice to show that the domicile of origin subsisted-no matter how theoretically adhesive its character."

The supervisor thought they had finished their conversation, but he could see that his young pupil was looking troubled. "Come on, tell me, what's on your mind?"

Question 5:

"Well", said the pupil, "I started wondering about something slightly different. Do people with English domiciles ever go to India to live and if they do, how easy is it to get an Indian domicile and fall outside inheritance tax for offshore assets?"

"How long is a piece of string?!" Exclaimed the supervisor. But he immediately regretted saying that as he saw the baffled look on his pupil's face. Either he was not familiar with the expression, or, more likely, he was about to answer the question based on his knowledge of the average length of all the string in the world at that point in time. "Let me think", the supervisor hurried on. "We need to split people who might do this into two realistic categories. The first category is the Indian origin individual. This could be someone who was born into a family the head of which came to settle in the UK from India a couple of generations ago. Our individual, a grandson in the family – let's call him Sachin-acquired an Indian domicile of origin by virtue of being born legitimately to a father who had a domicile of origin in India at Sachin's birth. It's interesting that the location of a domicile of origin is adhesive both in relation to an individual but also in the way in which it is passed down the generations. For example, a fourth-generation Indian origin family member who was born in the UK could still have a domicile of origin in India by virtue of his father's domicile at the individual's birth. And the father could have inherited his Indian domicile in the same way from his father and so on up the family tree. Now, Sachin could have kept that domicile and then moved to India-in which case it would

be relatively straightforward to show that Sachin's domicile of origin never changed-subject of course to having good evidence to support that. But we are not talking about that scenario as you want to know what happens to an English domiciliary. So, we must assume that Sachin managed to give up his domicile of origin in India and to acquire a domicile of choice in England. But strong – indeed magnetic – factors drew him to India where he has lived on a permanent basis.

The second category is the Englishman with a domicile of origin in England and with absolutely no Indian connections in the early years of his life. Let's call him Alastair. Alastair met and fell in love with an Indian girl and moved to Mumbai. He now lives there with his wife and 3-year old son, who was born there. Let's consider both of these.

The first point is which country's domicile law do you look at to determine the question? The deemed domicile IHT classification was irrelevant to Sachin and Alastair before they moved to India because they were already actually domiciled in the UK. If the Treaty did not exist, the question of a change in their domicile and their domicile at death for IHT purposes would be governed by English law. But because the Treaty does exist, we need to look at that and determine the question under Indian law. Of course, the issue only becomes relevant on the death of either of them as the Treaty looks at domicile at death. But where there has been a change in domicile during the life of the individual and the result of that change prevails at death, inevitably both the situation at death and the previous history involving the change must be looked at under the same law.

We are so far only talking about death. Note that the Treaty does not apply to lifetime chargeable transfers for IHT purposes. If Sachin or Alastair were to make any lifetime transfers in relation to non-UK assets after they moved to India, those transfers could be transfers of excluded property if they were not domiciled in England at the time. In that

scenario, the question of domicile would be governed by English law. We would also need to consider the deemed domicile tests in Section 267(1) as they would remain relevant for lifetime transfers. For example, if Sachin made a transfer within three years of losing his English domicile, he would still be deemed domiciled here and the Treaty would not help even if his Indian domicile of origin had revived.

So, we need to be clear about which law is relevant and to what. I am only concerned with the situation at death at present as we are discussing the Treaty.

Sachin

Sachin's family has a huge multinational business. He has relatives stationed in different parts of the world who run different parts of the business. Sachin originally helped his father run the London arm, and indeed, had never been to India until he was in his late twenties. He is now 45, and moved to Bangalore (or Bengaluru) seven years ago. He was asked by his father to move there to set up a new tech business, which he did and which is really going places. His wife and two children have now also moved there although he still keeps a flat in London. HMRC took the view that Sachin had acquired a domicile of choice in the UK in his early thirties, and Sachin never challenged that as it seemed to make sense. After all, he had very little interest in India and had no Indian assets. But now he is well-settled in India and has very little reason to go back to the UK. Sachin needs to consider what his ultimate intentions are. If these include making India his permanent home, he may want to take steps to sever his ties with the UK so as to abandon his domicile of choice. As a matter of law, if the domicile of choice is abandoned, then the domicile of origin automatically revives. But it would be prudent for Sachin to ensure that his Indian ties are strong so as to reinforce this proposition, particularly given that he had no ties with India himself before he acquired his English

domicile of choice. There is no hard and fast rule as to how long someone like Sachin has to be in India so as to revive his domicile of origin. But undoubtedly Sachin can accelerate the timetable by breaking off significant links with the UK and shoring up his Indian profile. In pure theory, if Sachin had left the UK with a view to emigrating to India and staying there irrespective of the success of the new business, he could get his domicile of origin back in the year of arrival in India. Practically speaking however, there is likely to be a period after leaving the UK where Sachin keeps his options open-and until the options have been closed, it would be difficult to say that the domicile of choice had been abandoned.

Alastair

In Alastair's case, it would be quite natural for him to keep his options open for a long time. No doubt he wants to make a go of things, but India is not the easiest place in the world to move to, and it takes time to adjust. There is a world of difference between visiting on holidays and living there. Further, he has strong ties with the UK and he would really need to consider if he is prepared to give these up. There is nothing inconsistent between living in India for a long period of time and retaining an English domicile of origin. It is sometimes said that a domicile of origin is harder to shake off than a domicile of choice. For one thing, a domicile of origin, as I said earlier, automatically revives when a domicile of choice is abandoned whereas a former domicile of choice does not revive when a subsequent one is surrendered.

Section 9 of the Indian Succession Act states:

> "A man acquires a new domicile by taking up his fixed habitation in a country which is not that of his domicile of origin."

This is essentially the same as acquiring a domicile of choice. A fixed habitation connotes taking up residence in a country with the intention of living there permanently. Alastair may

well develop that intention once he is comfortable with his new life in India. But until that intention develops and is backed up by steps to loosen his links with England and to strengthen his Indian ties, Alastair will retain his English domicile of origin. For him, the move to India involves a greater upheaval than for Sachin, and Alastair's position is the opposite of Sachin's: Alastair stands to lose a domicile of origin to gain a domicile of choice whereas Sachin gives up a domicile of choice to regain what he had viz. his Indian domicile of origin.

It would be too simplistic to say that it will take longer for Alastair to switch domiciles than for Sachin, but I think we can say that there are more things for Alastair to do (both in England and in India) than Sachin in order to achieve the change.

Question 6:

"If Sachin or Alastair were to die within three years of losing their English domicile, would their deemed domiciled status under Section 267(1) of the 1984 Act have any impact?

"You really have been looking into this deeply, if I may say so", said the supervisor. "As this is another deemed domicile test created by UK tax legislation, again it cannot override an individual's domicile at death under the Treaty. This would mean that he would be regarded as domiciled in India. As I said earlier, the deemed domicile status remains relevant to lifetime transfers."

Question 7:

"And presumably there would be a similar result for Alastair if he became a formerly domiciled resident here and then died?"

"Let's see. Suppose Alastair has lived in India for ten years, having acquired a domicile of choice there five years earlier. He is then posted to the UK for five years. He will become a formerly domiciled resident in year two of his posting, assuming that he is UK resident in that year and in the previous year. If he were to die as a resident in year 3 without losing his actual

domicile of choice in India, he would still be treated as Indian domiciled under the Treaty. As you say, the result is the same because the formerly domiciled resident is also a category of deemed domicile which cannot override the Treaty. But it is relevant for lifetime transfers."

A tax lawyer gets a bit too used to seeing domicile as a bad thing if the upshot is a potential tax liability. The categories of deemed domicile simply reinforce that viewpoint. We should not lose sight of the fact that real domicile is both a right and a privilege. It is harder to get than citizenship in some countries. The Indians would certainly not grant domicile to a foreigner unless the person has taken serious steps to commit to living in India and staying there to the exclusion of other countries. So, domicile-switching is not easy. It is certainly not as easy as residence-switching by limiting days spent in a country and so forth. Of course, if India brings back estate duty, both Sachin and Alastair may get an Indian domicile more easily than I have suggested!"

"Thank you", said the pupil. "Perhaps I should investigate what the chances are of India bringing in estate duty or something similar."

"If you find the answer", chuckled the supervisor, "Let me know. There is a small matter of a General Election to get out of the way this year but after that, who knows? And you better not use time travel to answer that!"

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