

# UK Summer Budget 2015 – Key Issues for Asset Managers and Non-UK Domiciled Individuals

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On 8th July 2015, the UK Government announced several changes to UK tax legislation that will affect those holding carried interest in fund structures which utilise at least one partnership (including a limited partnership), and further changes that will particularly impact UK tax-resident individuals who are not domiciled in the UK for tax purposes ("non-doms").

Two of these changes have immediate effect, so relevant taxpayers should consider their position now and take advice on how their UK tax liability may be affected.

## **1. Carried interest - capital gains treatment and computation**

UK individuals will now be charged capital gains tax, at the current rate of 28%, on the full amounts they receive in respect of their carried interest. Deductions will only be allowed in respect of sums actually given by the individuals as consideration for acquiring the right to that carried interest.

This means that it will no longer be possible to use the so-called "base cost shift", which often resulted in lower effective rates of tax on carried interest receipts. The base cost shift resulted from the long-standing computational rules based on HM Revenue & Customs' published practice. It had the effect of increasing the capital gains base cost of the carried interest holder's interest by some of the amounts subscribed by limited partners, when the profit-sharing ratios changed under the terms of the limited partnership agreement (for example, when the fund started to pay out carried interest).

The current rules on income tax will continue in place so that if the nature of the carried interest return is income (for example, dividends and interest), there will remain a parallel charge to income tax. As a result, a claim would have to be made for a consequential adjustment to reduce the capital gains tax charge under the new legislation so as to avoid double taxation.

This measure will apply to all carried interest which is allocated and made accessible to individuals on or after 8th July 2015, with no grandfathering.

## **2. Carried interest - Non-doms**

Any non-doms receiving carried interest returns will now only be able to claim the remittance basis to the extent that he/she carries on investment management services outside the UK. The remainder will be treated as automatically having a UK source and be UK taxable, whether or not remitted to the UK. The proportion of the gain within the scope of the new rules will need to be calculated on a just and reasonable basis, and will depend on all the facts and circumstances relating to where the relevant duties were carried out and the nature and importance of those duties. This is a major change for UK resident non-doms holding carried interest and seeking to rely on the remittance basis of taxation.

It is not currently clear from the legislation over which period one is required to compute the percentage of time spent on UK/non-UK investment management duties.

Again, this measure will apply to all carried interest which is allocated and made accessible to individuals on or after 8th July 2015, with no grandfathering.

## **3. Consultation on performance-linked rewards**

A consultation process has been launched on performance-linked rewards paid to asset managers. This consultation appears to be driven by a perception that certain asset managers have been structuring their funds to convert what would be a performance fee into a carried interest arrangement, but the effects could potentially be far-reaching.

The consultation will consider the best way to ensure that only carried interest in funds that have a long-term investment strategy are able to benefit from capital gains tax ("CGT") treatment. One option in the consultation is to set out in legislation activities which are to be treated as long-term investment activities – examples given include acquiring controlling equity stakes in trading companies intended to be held for a period of at least three years, and making equity and debt investments in venture capital companies, provided they are intended to be held for a specified period of time. Another option up for consultation is to have a graduated system for access to CGT treatment, with full CGT treatment only available if the average investment holding period exceeds two years.

The consultation will close on 30th September 2015, with the aim being legislation to be effective in April 2016.

#### **4. Long-term non-doms**

From April 2017, the Government proposes that anybody who has been resident in the UK for more than 15 of the past 20 tax years will be deemed UK-domiciled for income, capital gains and inheritance tax purposes. In addition, it will no longer be possible for somebody who is born in the UK to parents who are UK-domiciled to claim non-domicile status if they leave but then return and take up residency in the UK.

Once the non-dom who has become deemed-domiciled under the 15-year rule leaves the UK and spends more than five tax years outside the UK they will at that point lose their deemed tax domicile. If they then return to the UK for a period, but still intend eventually to leave the UK and therefore remain foreign-domiciled under general law, they will be able to spend another 15 years as a UK resident for tax purposes before becoming deemed- domiciled again.

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