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Moving to the UK: key considerations for US citizens

The US and the UK are separated by the vast and tumultuous waters of the Atlantic Ocean. Individuals with connections to both countries will often find themselves rowing against the tide between two very different and complex regimes. With the right specialist advice, they can navigate the cross-border challenges safely and make the best use of planning opportunities.

Understand the issues, avoid the traps, and uncover ways to plan ahead in our Navigating the Atlantic series for US-connected clients.

MOVING TO THE UK

In this instalment, we explore some of the key considerations for US citizens who are moving to the UK for the first time.

MANAGING THE RISK OF DOUBLE TAXATION FROM "DAY ONE"

Upon becoming tax resident in the UK, individuals will become exposed to UK taxation in respect of their worldwide income and gains (subject to the remittance basis of taxation, discussed below).

US persons, unlike those moving from most other jurisdictions, will also carry with them an exposure to US income tax on their worldwide income and gains. This leads to the risk of double taxation.

WELCOME RELIEF UNDER THE US-UK INCOME TAX TREATY

The double taxation agreement between the US and the UK (also known as the "income tax treaty") is designed to provide relief from double taxation. Broadly, the treaty operates by allocating taxing rights between the two countries and, to the extent that both countries have a right to tax, providing for a system of credits that allows tax paid in one country to be credited against the liability arising in the other.

WHERE TREATY RELIEF WON'T HELP!

Although double taxation can generally be avoided through use of the treaty, the dual exposure can nevertheless have a significant impact on the tax-efficiency of certain types of investments – for example, where an asset is treated favourably for US purposes but is subject to higher tax rates in the UK.[1] A classic example are US mutual funds that do not have "reporting" status in the UK. While profits on those investments will typically be subject to capital gains rates (currently 20%) in the US, they will be subject to income tax rates (currently up to 45%) in the UK. For this reason, the UK's remittance basis of taxation can still play an important role for US persons.

[1] To be a reporting fund, a fund must register with HMRC as such. In doing so, the managers of the fund must agree to comply with onerous reporting obligations regarding the performance of the fund and the distributions that are made to investors. Most non-UK mutual funds will be non-reporting funds unless they have been designed with UK resident investors in mind.

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MOVING TO THE UK: KEY CONSIDERATIONS FOR US CITIZENS

BENEFITTING FROM THE "NON-DOM" TAX REGIME

For so long as UK resident US persons maintain a non-UK domicile for UK tax purposes, they should be eligible to claim the remittance basis of taxation. By doing so, they can shelter their non-UK source income and capital gains from UK tax, provided those income and gains are not "remitted" to (i.e. brought to or used in) the UK.

Many US persons will claim the remittance basis for at least the first seven years of UK residence, when it is available free of charge. This offers a degree of administrative ease when compared to claiming treaty relief. After the seven-year point (when an annual charge becomes payable to access the remittance basis), the taxpayer will need carry out a mathematical exercise each year to determine whether payment of the annual charge is worthwhile.

In many cases, it won't be worthwhile for US persons to pay to access the remittance basis because the global tax saving can be marginal once the residual exposure to US taxation is taken into account.

However, it could be helpful for taxpayers who wish to maintain holdings in investments that are not tax-efficient in the UK (provided they can afford not to remit the income or gains arising on those assets to the UK).

US persons who choose to claim the remittance basis will need to take extra care around the timing of remittances and tax payments to ensure that tax credits are available. This is a complex accounting issue on which US remittance basis users will require specialist advice.

WHAT STEPS SHOULD BE TAKEN AHEAD OF TIME?

Maximise "clean capital"

Anyone who plans to take advantage of the remittance basis of taxation should explore ways to maximise "clean capital" (i.e. funds that can be brought to the UK without triggering a taxable remittance). They might do this by crystallising capital gains and/or accelerating income to be paid to them prior to their arrival in the UK. However, US persons will need to be mindful of the US income tax consequences of such planning and execute a careful balancing act between US and UK considerations.

Consider risks associated with existing trusts

Any existing trusts of which the individual is a settlor, trustee and/or beneficiary should be examined before the individual becomes UK resident. For instance, it is common for US citizens who are moving to the UK for the first time to already hold assets in revocable living trusts, which they have been advised to put in place in the US as a probate avoidance vehicle. The individuals will very commonly be the trustees of those trusts themselves. Consideration ought to be given to how the trusts will be characterised for UK tax purposes, as there can be risks of tax inefficiencies resulting from a mismatch in the US and UK treatment.

The double tax risks for UK resident beneficiaries of US trusts are considered in detail in our article, "Welcome Relief".

Consider risks associated with existing company interests

It is common for US persons to hold assets through Limited Liability Companies ("LLCs"), which can produce tax traps for the unwary. Again, there is a likely mismatch between the US and UK treatment of these entities, which can give rise to double taxation. Broadly, this is because the US generally treats LLCs as partnerships (i.e. transparent entities) for tax purposes, whereas the default position in the UK is to treat LLCs as companies (i.e. opaque entities).

As a result, the US will typically tax the members of the LLC on their respective shares of the underlying profits of the LLC as they arise, whereas the UK may seek to tax distributions of profits from the LLC as dividends. This mismatch can cause treaty protection to be lost, with the result that the same income or gain suffers tax twice. The options for mitigating this risk will need to be considered.

MOVING TO THE UK: KEY CONSIDERATIONS FOR US CITIZENS

Consider planning opportunities before purchasing a UK home

Many US citizens who move to the UK will acquire a home there. This raises various tax, estate planning and other considerations, including mitigating exposure to UK inheritance tax and putting in place a UK will. We explore these issues in detail in our separate guide for US purchasers of UK residential property.

CONTACT US

It is essential to plan in advance of a move to the UK, to take advantage of available tax reliefs and ensure arrangements are as efficient as possible. This is particularly pertinent for those with connections to the US due to their global exposure to US income tax, regardless of where they live. It is therefore important that advice is taken from advisors with an understanding of how the two legal systems interact; ideally before any action is taken. Please contact a member of our specialist US/UK team to find out more.

Disclaimer: The members of our US/UK team are admitted to practise in England and Wales and cannot advise on foreign law. Comments made in this article relating to US tax and legal matters reflect the authors' understanding of the US position, based on experience of advising on US-connected matters. The circumstances of each case vary, and this article should not be relied upon in place of specific legal advice.

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