DOMICILE IN FEDERAL STATES AND THE CONCEPT OF A UK DOMICILE

Peter Vaines[1]

This article addresses the application of the concept of domicile to Federal states such as the United States, Australia and Canada and also examines the related concept of a UK domicile.

The traditional view is that a person's domicile connects him with a particular country, or perhaps more accurately, with a territory subject to a single system of law. That is comparatively straightforward with a sovereign state such as Holland but becomes more difficult when we look at a Federal State such as the United States. In The Conflict of Laws, 13th Edition, Dicey and Morris say that there is no doubt that each state within the United States is a separate country for the purposes of the conflict of laws. The same applies to Canada, Australia and some other countries. However, they also observe that Wales is not a country because its system of law is the same as that of England in contrast with a Federal State where each state has its own system of law.

I do not find this easy to follow because in Canada for example the Federal Government has the law making power for the entire country and although the provinces have some legislative responsibility, it is difficult to regard that as enabling the provinces to be regarded as systems of law sufficient to support a separate domicile any more than Wales with its separate legislative assembly. However, it has long been accepted that one cannot be domiciled in Australia, Canada or the United States; one can only be domiciled in a particular state or province, each of which has to be regarded as a separate country for the purposes of domicile and all the rules relating to the acquisition and loss of a domicile.

Related but rather different, considerations arise in connection with the concept of a UK domicile, a term which has enormous UK tax significance but is not defined, and although everybody knows what it means, the authority for the concept is

1 Peter Vaines, Squire Sanders & Dempsey LLP, Tower 42, 25 Old Broad Street, London EC2N 1HQ; pvaines@ssd.com

extremely vague. I shall come to that later but first I should like to consider the implications regarding domicile in a Federal State.

It is necessary to set out a few of the key rules enunciated by Dicey and Morris.

Rule 10 deals with the acquisition of a domicile of choice as follows:

> *"Every independent person can acquire a domicile of choice by the combination of residence and intention of permanent or indefinite residence, but not otherwise".*

Rule 13 (1) deals with the abandonment of a domicile of choice as follows

> *"A person abandons a domicile of choice in a country by ceasing to reside there and by ceasing to intend to reside permanently or indefinitely, but not otherwise".*

Rule 13(2) introduces the concept of revival:

> *"When a domicile of choice is abandoned (i) a new domicile of choice is acquired; or (ii) the domicile of origin revives".*

So in the simplest example if an individual with a English domicile of origin and a French domicile of choice leaves France and goes to live in Australia, the question arising from Rule 13 is whether the individual acquires a new domicile of choice in Australia or whether his English domicile or origin revives. Unfortunately, I think that the question is much more complicated than that, as I shall explain. However, the position is even more difficult when you introduce a federal state into the picture.

The classic problem with the concept of revival is set out in an example provided by Dicey & Morris in the commentary to Rule 13. They postulate an individual with an English domicile of origin who emigrates to the USA and acquires a domicile of choice in New York. He never revisits England. At the age of 65 he decides to leave New York and settle in California. He sets out for California but dies on the way. He dies domiciled in England.

The reasoning here is that at the time of his death he no longer resided in New York and he had ceased to intend to reside there permanently. Accordingly, his New York domicile was lost at the moment he ceased to reside there with the intention of ceasing to reside there permanently. This is the inevitable conclusion from Rule 13(1).

When his domicile of choice was lost, either a new domicile of choice was acquired or his domicile of origin revived. That is the effect of Rule 13(2). Unfortunately, he had not yet taken up residence in California, although it was his clear intention to do so. He could not therefore satisfy Rule 10 so a claim to have acquired a domicile of choice in California at the time of his death could not succeed. Accordingly, his English domicile of origin revived.

He may never have been to England (his domicile of origin may have derived solely from his father being domiciled in England at the time of his birth) and he may have no UK assets. That does not matter – he is still fully chargeable to IHT on his worldwide assets. This may sound academic on the basis that nobody may realise the possibility and make any notification to HMRC. However, he might have a sister or other family in the UK who inherit his estate and they could become liable for the inheritance tax to the extent of their inheritance by reason of section 199 IHTA 1984.

This apparently bizarre conclusion is really no more than the application of the long standing rules on the acquisition, loss and revival of a domicile. It may be thought that this is just one anomaly out of many in the tax system and it is not a circumstance which arises with sufficient regularity to cause difficulty. After all, how many people die en route from one territory to another in these circumstances causing their domicile of origin to revive? Unfortunately, on further consideration, the matter is rather more serious.

The above analysis is based on the premise that the individual moving from one state to the other dies in transit at a time when he resides in neither state. The introduction of a death brings a dramatic flavour, but does not really affect the analysis. Let us assume that our traveller leaves New York and arrives safely in California to take up his residence there. Whether or not he died on the way, the effect on his domicile will be the same. As soon as he left New York, his New York domicile would have been lost and until he arrived in California, he could not acquire a domicile of choice in California. Accordingly, during his journey' his UK domicile of origin would have revived whether he died or not.

The significance of this is that the revival of his UK domicile of origin brings him back into the inheritance tax net and once inside he cannot escape for a further three years. By reason of section 267 IHTA 1984 an individual who was domiciled in the UK within the last three years is treated as continuing to be UK domiciled for the purposes of inheritance tax. This may come as a surprise and may represent a risk of which the individual is both unaware and unprepared.

So when he arrives in California and takes up residence there, he will be deemed to be UK domiciled for inheritance tax purposes. This rule does not apply to

income tax and capital gains tax because the deemed domicile concept has no application to those taxes for which his domicile will be determined by the general law. Accordingly we have to look at the position afresh on his arrival in California and it is certainly not automatic that he becomes domiciled there; he needs to satisfy the tests for the acquisition of a domicile of choice all over again. It is likely that he would do so, although one could expect a degree of uncertainty because having not lived there before, he may not find it entirely to his liking and he may not be able to make an informed decision about his future intentions until he has been there for a while.

Now this is by no means an unusual situation; indeed, it may the most frequently occurring circumstance in this area. It must be rare for one domicile of choice immediately to be followed by another unless the two territories share a common border so that the individual remains within the territory of his domicile of choice until he crosses the border into the territory of his new residence. If he has to travel through another state or country, the domicile of origin will revive during the transit period. Even if the states do share a common border the position is not wholly clear because having packed up and left his home, one might say that he ceased to reside in that territory (in the sense of an inhabitant) even though he had not yet crossed the state border. Furthermore, the second territory must be one where he had already established his actual residence – and he must already be intending to reside there permanently; otherwise the first limb of Rule 10 would not be satisfied. This just shows how difficult it is likely to be to avoid the revival of the domicile of origin whenever an individual moves leaves his domicile of choice.

In the Report of the Law Commission in 1988, they made reference to the position of a Federal State such as Australia, the USA or Canada not being a country for the purposes of domicile and that an individual can only be domiciled in a particular province or state and not domiciled in the country as a whole. They highlight the anomalies which arise from this conclusion and put forward their own example (similar to that in Dicey & Morris) of a person with a domicile of origin in Scotland who leaves Scotland intending never to return but rather to settle permanently in Canada. He spends one month in Ottawa trying to decide which Canadian province to make his home but dies before he has reached a decision. He would die domiciled in Scotland.

This is perhaps an ambiguous example because the individual's indecision about his place of residence could be a reason for saying that his decision to settle in Canada was insufficiently firm to justify the acquisition of a domicile of choice there in any event. It is not the intention never to return to Scotland which is important, but the positive intention to reside permanently in a particular Canadian province.

The concept of revival was certainly a matter of concern to those who were considering the revision to the law of domicile in the Law Commission and they recommended it be abolished. I would suggest that the absurdities created by the doctrine of revival may be even greater than had been recognised, giving rise to an even more urgent need for reform in this area.

The position is scarcely easier when one looks at the concept of a UK domicile. The traditional view is that a person may be domiciled in England and Wales, or in Scotland, or in Northern Ireland but not the UK as a whole. Indeed this was the view of the Law Commission whose Report specifically highlighted that a composite state such as the UK is not a country for the purpose of domicile. However, the UK inheritance tax legislation refers specifically to persons domiciled in the UK (IHTA 1984 section 267) and this would indicate that some development must have taken place with this concept because otherwise the Inheritance Tax Act would make no sense. The absence of any explanation or definition regarding the concept of a UK domicile indicates that no such qualification is necessary because the UK (and not its constituent parts) is a sufficiently singular system of law to enable a domicile to exist in respect of it. It seems likely that this wording was deliberate because the predecessor concerning estate duty referred to an individual being domiciled in part of Great Britain. Furthermore, in the Income Tax (Earnings and Pension) Act 2003 Section 721(3) the issue is specifically addressed as follows:

> *"Any reference in this Act to being domiciled in the United Kingdom is to be read as a reference to being domiciled in any part of the United Kingdom".*

The provision is clearly an acknowledgement of the unsatisfactory position but it may be too much to suggest that this is correcting a previously untenable position.

A similar development may be said to have taken place in Australia where for family law purposes the Australian Family Law Act 1975 refers to divorce proceedings being competent if either party to the marriage is "domiciled in Australia". This would seem to indicate that the traditional approach may no longer applies in Australia either at least for this purpose.

For practical reasons it is obviously not possible for an individual domiciled in England to escape inheritance tax by claiming that he does not have a UK domicile on the grounds that such a domicile does not exist – however attractive the argument be and despite the support he could derive from the Law Commission. But it is difficult to articulate the legal analysis in support of this conclusion. The reasoning must be that either the term UK domicile is a collective noun encompassing all or any of the systems of law or countries comprised in the UK or

it is a concept which aggregates a number of different systems in law into a single domicile known as UK domicile.

This seems to be the view of HMRC. In paragraph 1302 of the Inheritance Tax Manual they say

> "*In general your domicile will be in a country as a whole. However, where there is for example, a federal system your domicile will relate to the individual state, province or canton e.g. Texas, Ontario and Zurich.*
>
> *So, despite the wording in the [Inheritance Tax] Act you cannot be domiciled in the UK but in one of England and Wales, Scotland or Northern Ireland. However, you should take the reference in the Act and this Manual to "domiciled in the UK" to mean domiciled in some part of the UK."*

And further in paragraph 1608 of the Inspector's Manual they say that an individual is domiciled in the particular state of province in which he has his permanent home:

> *"A similar situation exists in the United Kingdom. An individual is not domiciled in the United Kingdom as a whole but in one of its constituent countries namely England (meaning England and Wales), Scotland or Northern Ireland."*

This may be convenient shorthand and no doubt a way to make sense of the position, but it does seem to be just a way of fudging the issue.

If one can have the flexibility under English law to say that although the UK is not a country for the purposes of domicile, it should be still be treated as a single country, why should the same treatment not apply to Canada, Australia, the United States and other federations at least for the purposes of domicile. After all Dicey & Morris Rule 8 says that matters pertaining to domicile should be determined by reference to English law.

In conclusion, I would submit that the traditional view regarding the domicile of an individual in a country with a federal system can no longer be supported and that a person domiciled in any one of the states of a federation should be regarded as domiciled in the country as a whole. This is not a matter of mere esoteric debate because whilst HMRC continue to deny people living in Australia, Canada and the USA as having a domicile in any of those countries because they have moved, or intend to move around within the country, the issue remains one of a real practical importance.

Furthermore, (or perhaps alternatively) if it is asserted that the UK should be treated as a single country, not by any principle or enactment, but merely out of expedience because the federal argument is too long established to be overturned, one does have to ask how the continuity of the concept of a UK domicile can be sustained – other than in the case of ITEPA where the position is specifically addressed. The concepts are in conflict – or perhaps more accurately, the concept of a UK domicile is simply unsupportable on the traditional view of the law relating to federal states – and at the very least a provision similar to that in section 721(3) ITEPA 2003 ought to be enacted for tax purposes generally.