

UK STATUTORY DEFINITION OF TAX RESIDENCE ... BREAKING NEWS

1. Introduction

As foreseen in the UK Budget on 23 March, a 37-page document was issued on 17 June 2011 – “Statutory Definition of Tax Residence . . . A Consultation”. Recent tax cases and HM Revenue and Customs practise has led to considerable confusion among people coming to and leaving the UK. Indeed the Consultative Document accepts that the present “residence rules are vague, complicated and perceived to be subjective. In certain circumstances it is not possible for a person to be sure whether they are tax resident in the UK or to know what activities or circumstances would make them tax resident.” In our view certainly the current proposals clarify the situation quite considerably and it is proposed still that the new rules would take effect from April 2012. The UK is certainly not alone in having a statutory definition of tax residence and one has long existed for UK limited companies. However we have to express surprise at the proposals and their prescriptive nature.

2. Leaving the UK

Many recent tax cases have focused on whether a UK resident has truly left the UK for tax purposes and assumed non resident status. This of course can be crucial as if still UK resident, the individual will be liable to UK tax in principle on their worldwide income and gains. Thus in ascertaining tax residence it has been important to assess whether a “clean break” has been made and what continuing connections there have been with the UK.

The new proposals assert that someone will be *not* resident in the UK for a tax year if they fall under any of the following conditions:

- If they were not resident in the UK in all of the previous three years and they are present in the UK for fewer than 45 days in the current tax year; or
- Were resident in the UK in one or more of the previous three tax years and they are present in the UK for fewer than ten days in the current tax year; or
- Leave the UK to carry out full time work abroad provided they are present in the UK for fewer than 90 days in the tax year and no more than 20 days are spent working in the UK in the tax year.

There are proposed definitions for “full time work abroad” and “working day”. However the provisions can be regarded as being quite generous in that an individual will know exactly where they stand and may be able to plan their affairs carefully. There are anti-avoidance provisions if an individual leaves the UK and is not away for five complete tax years. In a measure similar to that adopted for capital gains, an individual who has assumed non resident status may still be liable to UK tax upon return on certain UK investment income, namely dividends paid by closely controlled companies that reflect profits that are built up during a past period of UK residence.

Example – Alan leaves the UK in March 2014 and returns to the UK in May 2015. He takes care to be in the UK for less than ten days in the year to 5 April 2015 but receives a dividend of £1 million from his family company representing accumulated profits made prior to March 2014. Although not resident in the UK under the “ten day test” he will be taxed on the dividend in the year of return under this proposed five year rule.

Where an individual is not conclusively non-resident due to the “day count” provision set out above, it will be important to look at other “connection” factors namely:

- Whether the individual’s spouse or civil partner or common law equivalent or minor children are still resident in the UK.
- Whether the individual has accessible accommodation in the UK and makes use of it during the tax year.
- Whether the individual does substantive work in the UK.
- Whether the individual spent 90 days or more in the UK in either of the previous two tax years.
- Whether the individual spends more days in the UK in a tax year than in any other single country.

There are quite complex provisions that mean that these “connection factors” need to be evaluated and compared with the number of days spent in the UK. For example if an individual is in the UK for between 45 and 89 days in a year, he will be resident if the individual has three or more connecting factors.

Example – Brian leaves the UK in March 2014 and returns in May 2015, but comes back for 98 days in the year to 5 April 2015. He is single, does not work in the UK, has no UK accommodation and spends the remainder of his time equally between France and Belgium.

Present treatment – he almost certainly would be resident in the UK in 2014/15 due to level of return visits.

Proposed treatment – as he has been in the UK for between 90 and 119 days in the year to 5 April 2015, he needs only to have two connecting factors or more to be UK resident. His only connecting factor is that he was in the UK for 90 days or more in 2013/14 and hence he is non resident in the UK for 2014/15.

3. Arriving in the UK

Again the law has been unclear as to when an individual became resident and again the “conclusive non residents” tests outlined in (2) above will be adopted to determine whether he or she has become resident in the UK. If none of these tests apply it will be important to look at certain connecting factors, namely:

- Whether they have a UK resident family.
- Whether they have substantive UK employment duties.
- Whether they have accessible accommodation in the UK.
- Whether they spent 90 days or more in the UK in either of the previous two tax years.

4. Conclusions

The new proposals seem to us to be admirably clear and therefore give considerable assistance to taxpayers. It has to be said that perhaps they give opportunities for tax avoidance, particularly for those leaving the UK. Although we need to be mindful of certain anti avoidance provisions, they do not apply, for example, to bonuses paid by captive UK companies.

Individuals need to consider their position carefully as there will need to be a gentle transition to the new rules which may need to be considered carefully in individual cases. Individuals leaving and coming to the UK will need to plan their tax affairs especially carefully to minimise their tax exposure both in the UK and any other jurisdiction.

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