home and dry?

February 2008

Colin Jelley assesses the proposed amendments to the residence and domicile tax rules.

The package of measures issued on residence and domicile in the Pre-Budget Report (PBR) on 9 October 2007 were designed to 'strike the right balance between competitiveness and fairness' to ensure the UK tax system remains modern – but also works in a fast-moving global economy.

The Government's latest consultation document, issued on 6 December 2007, adds further points to the PBR statement on the tax position for UK resident non-UK-domiciles.

There are three key areas affected:

- The remittance basis
- The availability of personal allowances
- The residency rules

The consultation document runs to 27 pages, but the key points for advisers with clients potentially affected are summarised below.

summary of key points

Resident non-domiciles who have been in the UK for longer than seven out of the past ten years will only be able to access the existing remittance basis of taxation on payment of an annual charge of £30,000.

However, if the remittance basis is adopted by a resident non-domicile, they will lose automatic entitlement to personal income tax allowances and the Annual Exempt Allowance (AEA) for capital gains.

In practice this will mean a non-domicile suffering income tax at 40% whose unremitted income (and/or gains) is in excess of £80,435 will be better off paying the £30,000 charge.

The decision whether to pay the annual charge or not can be reviewed from one year to the next. Paying the charge will not impact the individual's domicile status.

A de minimis level of £1,000 will be introduced, which means that those whose unremitted income (and/or gains) is below this threshold will continue to benefit from the remittance basis without paying the £30,000 charge.

counting the days

The draft legislation also proposes amendments covering 'day counting' – something that attracted much attention following the Special Commissionaire's decision in Gaines-Cooper (2006). The case highlighted specific residence and planning strategies to minimise any potential liability to UK tax by spending as much time in the UK as possible without impacting the taxpayer's resident or ordinarily resident status. Although the appellant was unsuccessful, much debate centred on HMRC's interpretation of what did or did not count as a 'resident' day.

Following the uncertainty this case caused on this issue, it is no surprise that the Government has taken this opportunity to change the rules. Changing the method for counting 'resident' days will clearly affect many individuals who regularly fly in and out of the UK to manage their affairs. As the example on the next page shows, this can have the impact of significantly increasing the number of days a person is resident in the UK.

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example

what a difference a day makes

Consider Robin Banks, who lives in Jersey and normally works and resides there. In 2007/08 Robin began a three-year project in London for his Jersey employer, which involved spending three working days each week in London.

Robin arrives on Monday evening, works a full day on Tuesday, Wednesday and Thursday, and returns to Jersey on Thursday evening. Under existing practice the days of arrival and departure are not counted, so each week spent in the UK counts as two days.

Over the working year Robin makes 46 trips on this basis. He therefore spends 92 days in the UK. This is not enough to make him a UK resident under either the 183 days in one-year rule, or the 90-day average over four years rule.

Under the rules, which take effect from 2008/09 onwards, the days of both arrival and departure will be counted. For each working week Robin will be deemed to have spent four days in the UK – a total of 184 days for the tax year 2008/09.

There are also further proposals to change certain aspects of the current tax regime which enable individuals to reduce the tax payable. In recent years we have seen specific anti-avoidance legislation to address such issues and these changes follow suit.

Included in these are the 'cash only' and 'ceased sourced' rules.

Under the 'cash only' rule, foreign savings and investment income could only be taxed if it was remitted as 'cash'. If the income was converted into an asset outside the UK (eg a Ferrari, and then driven to the UK) no UK tax could have been applied until the asset was sold or turned into cash.

Under the 'ceased sourced' rule, foreign interest was only taxed if the source of that interest existed at the time it was remitted to the UK.

A common practice was for a foreign bank account, which generated interest, to be closed at tax-year end and for the interest to be transferred to a new account. This would then be remitted to the UK tax-free as the source of the interest (the closed bank account) no longer existed.

Draft legislation to address these and other issues will be addressed in the 2008 Finance Bill. While the hope is that it only impacts the deemed avoidance identified, HMRC have left the door open for further changes!

adding value

The deadline for responses to the consultation paper is 28 February 2008. For any adviser working in this area it is clear that change is on the way. Current planning practices will need to be reviewed and new strategies possibly adopted. Again, the Government has presented advisers with another clear opportunity to underline the value of quality advice.

This article is based on Skandia's interpretation of the law and HM Revenue & Customs practice as at 31 January 2008. We believe this interpretation to be correct but cannot guarantee it.

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Registered and Head Office: Skandia House, King Edward Road, Onchan, Isle of Man, IM99 1NU, British Isles. Phone: +44 (0)1624 655 555 Fax: +44 (0)1624 611 715.
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