Welcome certainty

A statutory definition of tax residence in the UK

17 June 2011

"…*the 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. … Given that tax residence is an essential prerequisite for determining an individual's tax liability, the Government agrees that this lack of certainty is unsatisfactory. It undermines its wider ambition of developing a tax system that is more certain, efficient, and easy to comply with. … It is also a deterrent to individuals and businesses looking to invest in the UK.*"

With these words the Treasury launched its consultation on a new statutory test of what constitutes tax residency in the UK. The new test is designed to provide certainty for taxpayers in assessing their residency treatment. While this certainty will be welcomed, it does come at a price and some of the permissiveness of the current regime will be lost. For many individuals this will be a price worth paying. The new rules are intended to be introduced with effect from 6 April 2012.

Overview

For the purposes of the new test a distinction is to be made between three classes of taxpayer:

1. '**Arrivers**' – individuals who have not been resident in all of the previous three tax years;

2. '**Leavers**' – individuals who have been resident in one of or more of the previous three tax years; and

3. '**Full time workers abroad**' – individuals who leave the UK to work abroad.

   Full time workers are classified as those who work aboard for at least a tax year, who do a 35 hour working week and spend less than 20 days working in the UK (a working day being at least three hours work!).

Each class will have its own set of rules and 'safe-harbours' – clear guidelines that confirm when individuals will not be regarded as UK resident. This contrasts with the current position where it is not possible to say that, even an individual who does not step foot in the UK during a tax year is not UK resident.

While these rules are clear (for the most part) they cannot always be described as generous.

Safe Harbours

The rules are still based on a day count and will take the existing "presence at midnight" test as to whether an individual was present in the UK on a particular day. For each class of individual there is then a safe harbour day count, within which an individual will not be treated as resident.

Arrivers	Fewer than 45 days in the UK
Leavers	Fewer than 10 days in the UK
Full time workers abroad	Fewer than 90 days in the UK (up to 20 working days)

For those seeking to establish residency in the UK there are two factors that will show UK residency conclusively:

1. being resident in the UK for 183 days or more in one tax year; and

2. having your only home (or homes) in the UK.

Residency factors

Between these safe harbours, there is a sliding day count scale for 'Arrivers' and 'Leavers' that sets out when individuals falling with those categories will be treated as resident. In contrast to the current position, where all the facts of an individual's life were relevant (from homes to shotgun certificates), only five defined factors are relevant:

1. **Whether your family is UK resident**

   Family means in this context your spouse, civil partner (but also including unmarried partners), but not if separated (by court order, or where it is likely to be permanent!). It also includes your minor children, unless they are only in the UK to go to school and spend less than 60 days of the holidays in the UK.

2. **Whether you have 'substantial' employment in the UK**

   This is a different test to the full time work abroad, and means working in the UK for more than 40 days in a tax year (again a day is three hours work).

3. **Whether you have 'accessible' accommodation in the UK**

   The test here is not ownership, but accessibility, so if accommodation can be used by you it will count, even if it is owned (and occupied) by someone else. The accommodation must, however be used as a residence.

4. **Whether you have been resident for more than 90 days in the previous two years**

5. **Whether you spend more days in a single other country than you do in the UK**

   This is only relevant for Leavers.

The residency tests

Using these factors, a sliding scale is then set out for each of ‘Arrivers’ and ‘Leavers’ dictating when they will be resident based on their day counts and the number of factors that they meet

Arrivers

Days in the UK	Test
Fewer than 45 days	Always non-resident
45 – 89 days	Resident if individual has 4 factors (otherwise not resident)
90 – 119 days	Resident if individual has 3 factors or more (otherwise not resident)
120 – 182 days	Resident if individual has 2 factors or more (otherwise not resident)
183 days or more	Always resident

Leavers

Days in the UK	Test
Fewer than 10	Always non-resident
10 - 44 days	Resident if individual has 4 factors (otherwise not resident)
45 – 89 days	Resident if individual has 3 factors or more (otherwise not resident)
90 – 119 days	Resident if individual has 2 factors or more (otherwise not resident)
120 – 182 days	Resident if individual has 1 factor or more (otherwise not resident)
183 days or more	Always resident

By using these tests individuals will be able to determine when they will be resident. The Government’s hope is that this “*will allow individuals to assess their residence status simply and without the need to resort to specialist advice*”.

Anti-avoidance rules

While the consultation is refreshingly light in terms of anticipating abuses, there is a proposal to extend the temporary non-resident rules. These currently tax capital gains and offshore income gains made by an individual who is non-resident for less than five tax years on their return (where such an individual was resident in the UK in four out of the seven years before leaving). It is proposed that they should be extended to some types of investment income; dividends from close companies are mentioned, while bank interest and dividends from listed companies are excluded. It would seem likely that profits from insurance policies may also be caught by this rule when enacted.

Ordinary residence

The Government seems less clear about what it wants to do with ordinary residence, but has proposed q new narrower statutory definition of ordinary residence that will apply so that if an individual is resident, you will be ordinarily resident unless he has been non-resident for the previous five tax years and doesn't have his only 'home' in the UK. Non-ordinarily resident status will only be available for a maximum of two tax years.

The consultation also considers whether non-ordinarily resident status should be restricted just to non-domiciliaries (in 2008/09 it seems that there were just 300 non-ordinarily resident UK domiciliaries who used the status to claim the remittance basis) or just for the purpose of overseas workday relief (whereby they are not taxed on part of their employment income.

Summary

While analysis of each of the individual factors and day counts is in itself straightforward, applying them to an individual's life may be more difficult. There are also some inequities in the legislation.

For example:

- If an individual, who has a home in the UK, is lucky enough not to work for a living and spends 110 days in the UK a year he will not be considered resident (satisfying only two factors). However, if he falls in love with a UK resident and they want to live together, he will immediately have to reduce his days in the UK to less than 90 as he will satisfy a third factor. A bad result for romance!

- This also applies so that a single person will always have one less factor than a family, giving them more time in the UK. A bad result for marriage (surely not a Conservative policy!).

- Non-resident families who have children at school in the UK will need to make sure that they take their holidays outside the UK to avoid falling foul of the 60 day test. A good result for foreign holidays![1]

- For families who fail the 60 days test, the eighteenth birthday of their youngest child may be a cause for even more celebration than previously as one factor will fall away. A good result for parties!

Overall however, the clarity of the proposed tests is to be welcomed as is the manner in which they are introduced. It is to be hoped that the consultation period will allow time to ensure that the final rules are as clear, coherent and fair as possible.

[1] A non-scientific analysis of a well known public school's calendar would indicate that in the tax year 2011/12 there are 161 days of holidays, at least 101 of which would need to be spent outside the UK.