

RESIDENCY, DOMICILE AND UK TAXATION



This paper will explain in summary the key issues of residency in respect of UK taxation, and the effect it has on the individuals who arrive and leave the UK throughout the fiscal year. Residency can be a baffling area with many nuances. HMRC in recent years have strived to reduce the complexities of the rules surrounding residency and have made major changes to the associated legislation.

WHAT MAKES YOU A RESIDENT IN THE UK?

There is no special definition of the word "residence" for tax, it simply takes its every day meaning. It is important to remember that residence is not just about whether you have a house in the UK or about how much time you spend here, it's more important to consider your connection to the UK. The more connections you have the greater the likelihood that you will be a resident.

It is important to understand that if you come to the UK to work or live on a continuing basis you will be resident from the date you arrive.



There are other factors that will also affect your residency such as whether you've been a resident before, family and work connections and the pattern and purpose of your visits to the UK.



HOW DOES HMRC DETERMINE YOUR RESIDENCE STATUS?

HMRC have a series of test to determine you residence status.

If you spend more than **183** days in the UK in any tax year you will be a resident for tax purposes.



If you spent less than 183 days in the UK **you are not automatically a UK resident** therefore the next test to consider is the automatic overseas test...

Here HMRC will try to determine whether you are automatically a non-resident. They will look at what time you have spent overseas and will consider if you have been a non-resident in the previous 3 tax years, how many days you will spend in the UK, where you work etc. If your residency status can't be determined from these factors you move to the next stage.



The next stage is the automatic UK test. Here HMRC will try to determine if you are automatically a UK resident by reviewing the time you spend in the UK, whether you own a home here, if you work here etc. Again if your residency can't be determined at this stage you move to the final stage of testing.

The final stage is the sufficient ties test. Here HMRC try to determine what ties you have to the UK and will look at factors such as whether you have a spouse or child (under 18) living in the UK, where you spend the most time over the course of the tax year and whether you will work more than 40 days in the UK.



WHAT'S THE DIFFERENCE BETWEEN RESIDENCY AND DOMICILE?

Domicile is defined as your "place of belonging" – the place you consider to be your permanent home.

Whilst residency is determined on your specific circumstances at any point in time (as outlined above) domicile is usually inherited from your father and can only be changed through a complex application process.

You cannot be without a domicile and you can only have one at any time.

WHAT ARE THE TAX IMPLICATIONS OF MY RESIDENCY / DOMICILE?

Your residency / domicile status effects three different types of taxation; these are "Income Tax", "Capital Gains Tax" and "Inheritance Tax".

Income Tax

Income tax is the taxation of your general income for example; employment earnings, self-employed income, investment income (bank interest, dividends and property income) etc. If you are a UK resident you pay UK tax on your worldwide income.

If you are non UK resident you would normally only pay UK tax on your UK income (from UK employment, interest on UK savings, dividends on UK investments etc.)

However if you are resident but non-domiciled in the UK you can choose to use the remittance basis of taxation (see "What is the remittance basis?" below).

Capital Gains Tax

Capital gains tax is the taxation of gains made from selling assets such as shares or property. If you are a UK resident you pay UK capital gains tax on your worldwide gains.

If you are non UK resident you would normally only pay UK capital gains tax on gains made from the sale of UK assets (although the rules around this are complex and have recently changed so please contact us for further advice).

As with income tax though, if you are resident but non-domiciled in the UK you can choose to use the remittance basis of taxation (see "What is the remittance basis?" below).

Inheritance Tax

Inheritance tax is the taxation upon your death of assets either within your estate at that point in time or gifted by you within the seven years before that date.

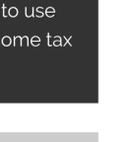
If you are a UK resident and domicile your worldwide assets are subject to UK inheritance tax. However if you are not domiciled in the UK only your UK assets are subjected to UK inheritance tax.

Under current UK legislation assets passed to your spouse on death are not subject to UK inheritance tax. However if you were UK domiciled and your spouse was not this relief is capped to £325,000.

WHAT IF I ARRIVE AT OR LEAVE THE UK PART WAY THROUGH THE TAX YEAR?

If you have arrived in the UK part way through the current tax year you're now a UK resident and technically have to pay UK tax on your worldwide income for the full tax year.

However under certain circumstances HMRC offer an "extra statutory concession" (ESC) known as the "split year treatment" which allows you to only pay UK tax on the overseas income received whilst in the UK. You would still have to pay UK tax on UK income received for the full year, as a non-resident would.



This treatment can be applied during a year you become UK resident and / or a year you cease to be UK resident.

WHAT IS THE REMITTANCE BASIS AND HOW DOES IT AFFECT TAX ON OVERSEAS INCOME?

We spoke about when you can apply the remittance basis earlier in the paper.

In the UK you pay tax on what is known as the "arising basis". This simply means you pay tax as and when the income is earned. The remittance basis contrasts with this and means you pay tax on foreign income or capital gains that you bring (or "remit") to the UK.

The remittance basis can only be claimed by an individual who is UK resident but not domiciled in the UK. If you meet this criteria you do not have to use the remittance basis of taxation but if you choose to do so the rules vary depending on your situation:

If you have less than £2,000 of foreign income and/or gains that you leave abroad during the tax year you can use the remittance basis without making a claim to do so or incurring a charge.

If you have over £2,000 of foreign income and / or gains that you leave abroad during the tax year you have to make a claim to use the remittance basis and you will lose your UK personal income tax and capital gains tax allowances.

If you have over £2,000 of foreign income and / or gains that you leave abroad during the tax year and you have been resident in the UK for at least seven of the preceding nine tax years you have to make a claim to use the remittance basis, you will lose your UK personal income tax and capital gains tax allowances and you will be subjected to a "Remittance Basis Charge" from HMRC of £30,000.

If you have over £2,000 of foreign income and / or gains that you leave abroad during the tax year and you have been resident in the UK for at least twelve of the preceding fourteen tax years you have to make a claim to use the remittance basis, you will lose your UK personal income tax and capital gains tax allowances and you will be subjected to a "Remittance Basis Charge" from HMRC of £50,000.

As you can see, the cost of using the remittance basis can be high and so an informed decision needs to be made as to whether this cost is outweighed by the tax savings.

WHAT IF I'M TAXED LOCALLY ON MY FOREIGN INCOME?

If you're UK resident and have already been taxed on your foreign income then you will still need to pay UK tax but you will in most circumstances be able to apply "double taxation relief" (DTR) which should reduce your UK tax liability and avoid you pay tax on the same income twice.

The terms of this relief will be dependent upon the double taxation treaty in place between the UK and the country where the income has already been taxed but in practice you would usually get a credit against your UK tax liability equal to the amount of overseas tax suffered but limited to the amount of UK tax payable on that particular source of income. The claim is made through your self-assessment tax return.



WHAT TO DO NEXT?

Hopefully you have made it to the end of this paper and are a little less confused than when you started. Residency is a complicated area of tax and the above is just an overview of what we consider the key areas.

Contact Chaddesley Sanford and speak to Rachel Elvin, our Tax specialist on 01483 802 895 or email Rachel at rachel.elvin@chadsan.com.