# CHAPTER 42

# TAXATION OF FOREIGN INCOME

## 42.1 Introduction

The taxation of overseas income is entirely dependent on the residence and domicile status of the recipient. We shall take a detailed look at the taxation of overseas employment income in the next chapter, but in this chapter we will concentrate on overseas investment and property income.

## 42.2 Definition of terms

*"Arising basis"*

This means that income is taxed in the year in which it arises or is received. It makes no difference whether such income is brought back to the UK or kept offshore.

*"Remittance basis"*

This means that foreign income is only taxed in the UK if it is brought back to the UK or is enjoyed in the UK.

*"UK income"*

This means income deriving from a source in the UK (eg, interest on a UK bank account, dividends on shares in UK companies, rents from UK properties etc).

*"Foreign investment / foreign property income"*

This means interest on foreign stock, foreign debentures and foreign bank accounts and dividends from non-UK companies. Foreign property income includes rents from foreign properties.

## 42.3 UK income

The way in which income is taxed, largely depends on where it arises.

UK income – i.e. **income arising from a source which is situated in the UK - is taxed on everybody, regardless of their residence status.**

This means that if an individual is **resident and domiciled outside the UK**, but they have a **UK property** which is let out and produces rental income, that rental income **will be charged to UK income tax** as UK property income. The non-resident individual therefore will have a responsibility to file a Self Assessment return and pay UK income tax.

There is an exemption in respect of "FOTRA" securities:

There is **no tax on UK "FOTRA" securities** which are held by individuals who are not ordinarily resident in the UK. "FOTRA" stands for "Free of Tax to Residents Abroad". An example of a FOTRA security is UK Government Treasury Stock. ITTOIA 2005, ss. 713 -716

As the interest on this stock is UK source income, it should normally be taxed on all individuals, including non-residents. However, by exception, because the stock has "FOTRA" status, if the interest is received by an individual who is **not ordinarily resident in the UK**, the interest will escape UK tax. HMRC has a published list of FOTRA securities.

In every other instance, if the income arises in the UK it will be taxed in the hands of the recipient, irrespective of his residence or domicile status.

## 42.4 Limit on UK tax liability for non-UK residents

S.811 ITA 2007 places a limit on the tax liability for an individual who is not resident in the UK.

The maximum tax liability for a non-UK resident is ITA 2007, s.811

| | £ |
|---|---|
| Tax deducted from interest & dividends (including notional tax) | X |
| Plus: | |
| Tax in respect of other income (ignoring personal allowances) | X |
| Maximum tax liability | X |

Individuals who are not ordinarily resident in the UK who provide their bank or building society with a declaration to that effect, can have their interest paid gross (ie, without deduction of tax at source). Therefore if the only source of UK income is interest which is paid gross, the individual will not have a UK tax liability.

However, if a claim for personal allowances is made, the tax liability is calculated as normal.

**Illustration 1**

Jacob is resident in Germany. He owns a property in the UK from which he receives rental income (after expenses) of £6,000 per annum. He also has a UK bank account on which the amount of interest (usually paid net) is £8,000 per annum.

Jacob has elected to have his UK bank interest paid gross. He will therefore receive gross interest of £8,000 x 100/80 = £10,000 per annum.

His UK income tax liability in 2010/11 will be: £6,000 @ 20% = £1,200

There will be no liability in respect of the bank interest (HMRC will not seek the 20% tax on the interest paid gross). However Jacob will not be able to deduct the UK personal allowance when calculating the tax due in respect of the rental income.

Alternatively Jacob's tax liability for 2010/11 could be calculated under the "normal" rules; ie:

| | £ |
|---|---|
| Rental income | 6,000 |
| Interest | 10,000 |
| | 16,000 |
| Less: Personal allowance | (6,475) |
| Taxable income | £9,525 |
| | |
| £9,525 @ 20% | £1,905 |

It is therefore not beneficial for Jacob to claim the personal allowance.

## 42.5 Foreign income: R, OR and D in the UK

Foreign investment and property income arising to individuals who are resident and domiciled in the UK, is **taxable on an arising basis.**

UK resident individuals who are domiciled in the UK, are therefore taxable on their worldwide income.

## 42.6 Foreign income: R but NOR

Now consider individuals who are resident in the UK but are not ordinarily resident. This will apply to visitors to the UK who have not yet acquired ordinary resident status.

If an individual is resident but not ordinarily resident in the UK, **foreign income is also taxed on an arising basis.** However, the **individual can make a claim for the "remittance" basis to apply**. This means that the individual will only pay tax on his foreign income if he brings it into the UK. This is a very important rule and will be discussed in more detail later on. ITA 2007, s.809B

## 42.7 Foreign income: R and OR but ND

The most important rule as far as the taxation of foreign income is concerned, concerns individuals who are resident and ordinarily resident in the UK but are domiciled somewhere else. This will apply in the case of a foreign national who is living in the UK but will return to his homeland at some point in the future.

For people who are resident in the UK but domiciled abroad, their **foreign income is taxed on an arising basis,** but again a **claim for the remittance basis** can be made.

## 42.8 Foreign income: NR and NOR

Finally, consider foreign income arising to individuals who are neither resident nor ordinarily resident in the UK.

**Foreign income** arising to non-resident individuals **is not taxable in the UK**. For example, the UK Government have no authority to tell a Spanish citizen that he or she should pay UK income tax on his or her Spanish income. This means that in the case of a non-resident individual, as long as the income arises outside the UK, it cannot be taxed in the UK in any circumstances.

## 42.9 Summary

Here is a summary of what we have covered so far;

| | UK INCOME | FOREIGN INCOME |
|---|---|---|
| **R, OR & DOM** | ARISING | ARISING |
| **R but NOR** | ARISING | ARISING (Possible remittance basis claim) |
| **R & OR but NON-DOM** | ARISING | ARISING (Possible remittance basis claim) |
| **NR & NOR** | ARISING | NOT TAXABLE |

## 42.10 Personal allowances

ITA 2007, s. 56

Personal allowances (including age allowances & married couples' reliefs) are available to all individuals who are **resident in the UK.**

The following **non-resident individuals** may also claim UK personal allowances;

- Citizens of the European Economic Area ("EEA"). The EEA essentially comprises the European Union plus a few additional nations (Norway, Iceland and Liechtenstein);
- Residents of the Channel Islands or the Isle of Man;
- Employees (past & present) of the British Crown (including widowers and widowers of Crown Servants).

There will therefore be some non-resident taxpayers who pay UK income tax on UK source income who will not receive a personal allowance.

Also remember that personal allowances for ALL taxpayers (whether resident or not) will be tapered away when net income exceeds £100,000.

## 42.11 Foreign pensions

Foreign pension income is either taxed;

a) on a receipts/arising basis if the recipient is UK resident and UK domiciled; or

b) on a remittance basis if the recipient is UK resident but not UK domiciled (or resident and not ordinarily resident) and has made a claim for the remittance basis.

Where foreign pensions are taxed on a receipts basis, **a 10% deduction is available**. ITEPA 2003, s. 575

The 10% deduction simply means that **only 90% of the pension is taxable in the UK.** For example, if an individual is resident and domiciled in the UK, and receives a pension from abroad of £10,000, only 90% of it – i.e. £9,000, will be taxable in the UK.

The **10% deduction is not available if the foreign pension is taxed on a remittance basis.**

## 42.12 Individuals not domiciled in the UK or not ordinarily resident – the remittance basis

Where an individual is resident in the UK but is not UK domiciled or not ordinarily resident in the UK, as a general rule both UK source and foreign income is taxed on an arising basis.

However, a claim can be made for **foreign income to be taxed on the remittance basis**. In this case, the foreign income of non-UK domiciled taxpayers (or those who are not ordinarily resident) is **only taxed in the UK if it is brought in, used or enjoyed in the UK**. If it is kept offshore, it is free of UK income tax.

If an individual wishes to use the remittance basis, he must generally **make a claim every year** under S.809B ITA 2007 (usually via the SA return). Otherwise, if no claim is made, the foreign income for the tax year should be fully reported and will be taxed as it arises (as for UK domiciled and ordinarily resident taxpayers). ITA 2007, S.809B

Non-domiciled individuals can opt in and out of the remittance basis year-by-year if they so choose.

Where an individual's "unremitted foreign income and gains" are less than £2,000, the remittance basis applies automatically, **without the need to make a claim under S.809B**. The individual will be treated as having used the remittance basis unless he notifies HMRC otherwise. ITA 2007, S. 809D

"Unremitted foreign income and gains" means total foreign income and gains for the tax year less amounts actually remitted to the UK in the year.

For example, if a non-UK domiciliary has foreign income of £4,000 (with no foreign gains) and in that year he remits £2,500 to the UK, the "unremitted foreign income" is £1,500. This is less than £2,000 so **the remittance basis will automatically apply** (no formal claim needs to be made). In this case the taxable foreign income will be the amount remitted – ie £2,500.

However if a non-UK domiciliary has foreign income of £4,000 and he remits £1,000 to the UK, "unremitted foreign income" is £3,000. Here the **remittance basis will not apply unless a claim is made** under S.809B. The taxable foreign income will therefore be the total amount arising of £4,000, unless a claim is made under S.809B in which case the taxable foreign income will be the amount remitted – ie £1,000.

The remittance basis also applies automatically if an individual has **no UK income or gains** for a year (other than taxed investment income of less than £100) and he **does not remit any foreign income or gains** to the UK. However, in this situation the individual must either have been resident in the UK for **not more than 6 out of the 9 preceding tax years or be under 18** throughout the tax year. ITA 2007, S. 809E

Where income is taxed on a remittance basis, it is **always taxed as non-savings income.** This will be the case even if the non-domiciliary remits foreign dividends.

The effect of this is that any foreign dividends remitted to the UK will therefore be taxed at 20%, 40% and 50% (as opposed to 10%, 32½% and 42½% for dividends taxed on an arising basis). ITA 2007, S.13

## 42.13 Statutory rules for remittances from "mixed funds"

ITA 2007, S. 809Q

Where the remittance basis is either claimed under S.809B or is applied automatically, taxpayers will only pay tax if they bring either foreign income or the proceeds of foreign capital gains into the UK.

If foreign income is remitted, the remittance is charged to income tax. The current tax rates for remitted income are the non-savings rates of 20%, 40% or 50%.

If foreign capital gains are remitted, the remittance is charged to CGT. The current tax rates for remitted capital gains are 18% or 28%.

**If the source of the remittance is neither foreign income nor foreign capital gains, there is no charge to tax.** This will be the case if the taxpayer remits accumulated "capital" – for example, money accumulated from neither income nor gains sources (eg, loans, gifts, inheritances etc).

Remittances by remittance basis users are self-assessed, so the onus is on the taxpayer to disclose to HMRC whether a remittance is a taxable remittance, and if so, whether that remittance is income or capital gains. The distinction between income and gains is important because **different rates of tax apply to different remittances**. HMRC do have a power to enquire into a taxpayer's SA return to ask the taxpayer to verify the source of the remittance.

**Sometimes it can be difficult to identify the source of the remittance.** For example, assume a non-domiciled taxpayer lives in the UK and sells a foreign asset. The proceeds of sale are paid into an existing foreign bank account. The foreign bank account contains previously unremitted income as well as non-taxable capital. A remittance is made from the foreign bank account to the UK.

What is the source of the remittance? Does it come from foreign income, foreign capital gain or non-taxable capital?

**As the source cannot be identified, HMRC apply S.809Q ITA 2007**. The bank account is designated as a "mixed fund" – ie, a fund containing a variety of different sources. Where a taxpayer makes a claim for the remittance basis and makes a remittance from a "mixed fund", **strict rules apply when determining what type of income or gains have been remitted**.

The order in which remittances from a mixed fund will be regarded as made is:

1) UK employment income;
2) foreign income which has not been taxed in another country;
3) foreign chargeable gains which have not been taxed in another country;
4) foreign income which has been taxed in another country;
5) foreign chargeable gains which have been taxed in another country;
6) income or capital not stated above

The ordering starts with income and gains from the latest year first, and then from each previous year in turn.

The general effect of the rules is that income is remitted before capital gains, and that income and gains without foreign tax credits are remitted before those qualifying for double tax relief. Essentially (assuming the foreign account does not contain UK employment income), this is a "worst-first" system for the taxpayer.

**The mixed fund rules can be avoided by the taxpayer maintaining multiple bank accounts,** each containing different sources such that none of the bank accounts is a "mixed fund".

For example, assume a non-domiciled taxpayer sold a foreign asset and paid the proceeds into a new non-interest bearing foreign bank account. Any remittances from this account can only be remittances of the capital gain as there is nothing else in the account. The remittance would then be taxed at the CGT rates of 18% or 28% (not at the higher income tax rates).

Keeping multiple bank accounts can however be expensive, time consuming and difficult to administer, although this sort of planning is worthwhile for the very wealthy.

## 42.14 Restriction of Personal Allowances where remittance basis claimed

ITA 2007, S.809F

As discussed above, Personal Allowances (PAs) are given to all UK residents and to certain non-residents (eg, EEA citizens, residents of the Channel Islands and Isle of Man etc).

However, where the **remittance basis is claimed under S.809B, no personal allowances** / age allowances / blind persons' allowances will be available for that tax year. In addition, the individual will not be entitled to the annual exemption in respect of capital gains tax.

Where the remittance basis applies automatically, without a S.809B claim (eg, for non-domiciliaries with unremitted foreign income of less than £2,000), full personal allowances and CGT exemptions will be given.

This loss of PAs will be a particular issue for overseas employees seconded to the UK who are "tax equalized" – ie, they have a guarantee from their employer that their net "take home" pay will remain the same regardless of any changes in the UK tax legislation. If these employees lose their PAs, their employer must then increase their salary to leave them with the same net pay.

Some non-domiciled or not ordinarily resident individuals will be put in a position where they will have to **choose between the remittance basis and their personal allowances**.

In simple terms, non-domiciled or not ordinarily resident taxpayers with foreign income in excess of the PA, will be better off claiming to use the remittance basis (and thereby losing the PA).

Do note that taxpayers with capital gains will also need to consider the loss of their annual CGT exemption when making this choice.

Also remember that individuals with net income in excess of £100,000 will see their PAs reduced by **£1 for every £2 of income above £100,000**. Therefore once a taxpayer has income of £112,950, no PA will be available (irrespective of whether a S.809B claim is made or not).

**Illustration 2**

Boris is Ukranian. He comes to work in London on a 4 to 5 year secondment from Kiev. He is resident, ordinarily resident and non-domiciled. His total income for 2010/11 is as follows:

| | £ |
|---|---|
| UK salary | 40,000 |
| UK bank deposit interest (net) | 800 |
| Rental income from house in Kiev | 8,000 |
| Interest on Ukranian bank account (gross) | 4,000 |

He has sufficient UK salary so he does not remit any foreign income to the UK.

We will calculate **Boris's taxable income** for 2010/11.

1) Assume Boris **claims under S.809B to use the remittance basis**. He will not be able to use the remittance basis without a claim as his unremitted foreign income exceeds £2,000.

   His taxable income in the UK will be as follows:

| | £ |
|---|---|
| UK salary | 40,000 |
| UK bank deposit interest (x 100/80) | 1,000 |
| Taxable income | 41,000 |

**He will not receive a PA as he is claiming to use the remittance basis**.

2) Assume Boris does **not** wish to use the remittance basis, so does not therefore make a claim under S.809B.

   His taxable income in the UK will be as follows:

| | £ |
|---|---|
| UK salary | 40,000 |
| UK bank deposit interest (x 100/80) | 1,000 |
| Rental income from house in Kiev | 8,000 |
| Interest on Ukranian bank account | 4,000 |
| Net income | 53,000 |
| Less; PA | (6,475) |
| Taxable income | 46,525 |

**Boris should therefore claim the remittance basis in 2010/11** (even if this means he will lose his PA).

## 42.15 S.832A ITTOIA 2005 – "Temporary non-residents"

The remittance basis for non-domiciled taxpayers **only applies in tax years when the individual is resident in the UK**. Remittances to the UK in a tax year of non-residence are not taxable.

To prevent avoidance of tax by non-domiciled taxpayers, FA 2008 brought in the "temporary non-residence" rules for income tax, now enacted as S.832A ITTOIA 2005. ITTOIA 2005, s.832A

S.832A applies where:

a) an individual uses the **remittance basis** for a year; &
b) he is **UK resident for 4 of the 7 tax years before becoming non-UK resident**; &
c) **he returns to the UK within 5 tax years** and resumes UK residence; &
d) **in the intervening period, he has remitted foreign income** to the UK which arose before his departure.

In this case, S.832A will **tax the individual on the remitted income in the year of return to the UK**.

S.832A is designed to prevent non-UK domiciliaries stacking foreign income offshore, then becoming non-UK resident for a short period (say one tax year), making large remittances to the UK in the non-resident year, then coming back to the UK to enjoy their offshore income free of UK tax.

S.832A only applies to foreign income "for the year of departure or an earlier year". Therefore if foreign income is received following departure and is paid to a UK bank account, S.832A cannot treat that foreign income as being remitted even if the taxpayer becomes resident again within 5 years.

S.832A will therefore only catch individuals who remit existing or "pre-stacked" foreign income in the intervening period.

S.832A only applies to income which is taxable when remitted. It does not apply to income which has already been taxed on an arising basis.

**Illustration 3**

Nathan is Australian. He came to the UK in 2002 to work as a Software Engineer for a UK motor manufacturer. His contract ended in January 2008 and he returned to Australia.

He had always used the remittance basis while living in the UK. His UK salary was sufficient to meet his UK living costs and he made no remittances.

In January 2010 he was offered a contract by a UK bank to work in London. The contract start date was July 2010.

In March 2010, in advance of his move back to the UK, Nathan transferred £50,000 from his bank account in Jersey to his UK bank as a deposit on a flat in London. The £50,000 is made up of accumulated interest and dividend income from offshore investments.

Nathan resumed UK residence in June 2010.

S.832A will apply as;

a) he was UK resident for 4 of the 7 tax years before becoming non-UK resident in 2007/08; &

b) he **returned to the UK within 5 tax years** and resumes UK residence in 2010/11; &

c) in the intervening period, **he has remitted foreign income** to the UK which arose before his departure.

Nathan will therefore be **taxed on a remittance of £50,000 in 2010/11**. This will be the case whether or not he claims the remittance basis for 2010/11, as the income arose in a year when the remittance basis was used. The £50,000 will be taxed as non-savings income.

S.832A was enacted by FA 2008 and therefore **catches remittances from 2008/09 onwards**. However, it can act to tax pre-2008 foreign income.

For example, the £50,000 remitted by Nathan in the above example could have arisen in 2007/08 or earlier. Even though this is pre April 2008 foreign income, as it is remitted after 5 April 2008, this "old" income would still be liable to tax under S.832A.

## 42.16 The remittance basis and the "long term residents" charge

ITA 2007, S. 809H

The "long term residents" charge (also called the "remittance basis charge" or "RBC"), applies if:

- an individual has made a **claim for the remittance basis**; and
- he is 18 or over in the relevant tax year; and
- he has been **resident in the UK for at least 7 of the previous 9 tax years**.

Such individuals can **only use the remittance basis if they agree to pay a tax charge of £30,000 per tax year**.

This tax charge will be in **addition to any UK tax on income and gains actually remitted** in the tax year.

Non-domiciled taxpayers caught by the "long term residents" charge therefore have 2 choices:

1) To pay **UK tax on <u>all</u> their foreign income as it arises** (ie, not to claim the remittance basis); or

2) To claim the remittance basis (and thereby keep their unremitted foreign income outside the reach of UK tax), but at a cost of **£30,000 per annum**.

It is therefore envisaged that:

- very **wealthy** non-domiciled taxpayers will **claim the remittance basis and pay the charge,** rather than having their substantial worldwide income exposed to UK tax; while

- **less wealthy** non-domiciled taxpayers will **not claim** the remittance basis and will instead **pay UK tax on unremitted foreign income** (thereby putting them on the same footing as UK domiciled taxpayers).

Some "moderately wealthy" taxpayers will have to prepare comparative calculations each year to see which option is more beneficial.

The election to use (or not use) the remittance basis must be made every year, so taxpayers can switch year-on-year if it suits them.

The "£30,000 rule" **does not apply** to:

a) Non-domiciled taxpayers who have unremitted foreign income and gains of **less than £2,000 per annum**. As such taxpayers do not have to claim the remittance basis (it applies automatically), they will not be caught by the charge; or

b) Taxpayers who have **not been resident for seven of the last nine years**. Such individuals can claim to use the remittance basis for foreign income **without any tax penalty** (apart from a loss of personal allowances); or

c) Taxpayers **under the age of 18** at the end of the tax year (ie, the charge will start to bite in the tax year in which the taxpayer becomes 18).

The extra tax of £30,000 will be payable via the self-assessment system. HMRC has confirmed that if a taxpayer meets this charge from an offshore source, the **payment of the tax itself will not constitute a remittance** (as long as the payment is made direct to HMRC by cheque or electronic transfer).

The £30,000 charge is a **tax charge on unremitted income or gains**. This means that the taxpayer will "choose" which unremitted income or gains the £30,000 tax is paid on. The £30,000 will therefore **either be income tax or CGT** (and will be treated as such for the purposes of double tax relief).

Long-term residents within the charge will "nominate" income and gains. This means that an individual can decide which unremitted foreign income or gains the £30,000 tax charge is paid on. When those "nominated" income or gains are finally remitted to the UK, there will be no further tax to pay on them.

However, ordering rules set out in the legislation mean that in any tax year, any previously **unremitted foreign income and gains will be regarded as remitted before any of the nominated foreign income and gains**. In practice this will mean that individuals will not get any credit for the £30,000 tax unless and until they bring all their foreign income and gains into the UK.

The £30,000 charge will normally be available for credit in the taxpayer's "home" country. Therefore in many cases, the new rules will not increase the overall worldwide tax bill of the non-domiciled client, but will instead mean that it is the UK Treasury who will pocket the money (rather than the overseas tax authorities!).

**Illustration 4**

Roman is Russian. He has lived in London for the last 10 years running a variety of businesses. He is resident, ordinarily resident and non-domiciled. His total income for 2010/11 is as follows:

| | £ |
|---|---|
| UK directors fees | 100,000 |
| UK rental income | 80,000 |
| UK bank interest (net) | 16,000 |
| Foreign property income | 95,000 |
| Foreign bank interest (gross) | 30,000 |

In March 2011 he remitted £50,000 of his foreign rental income to his bank account in London.

We will calculate Roman's tax liability for 2010/11.

1) Assume Roman wants to use the remittance basis. He therefore makes a claim under S.809B. His UK tax liability will be as follows:

| | £ |
|---|---|
| UK directors fees | 100,000 |
| UK rental income | 80,000 |
| UK bank interest (x 100/80) | 20,000 |
| Foreign property income (remitted) | 50,000 |
| Net income | 250,000 |
| Less; PA | (NIL) |
| Taxable income | 250,000 |
| | |
| *Tax:* | £ |
| £37,400 @ 20% | 7,480 |
| £112,600 @ 40% | 45,040 |
| £150,000 | |
| £100,000 @ 50% | 50,000 |
| | 102,520 |
| Add; long-term residents charge | 30,000 |
| Tax liability (before credits) | 132,520 |

He will not receive a PA as he is using the remittance basis. He is subject to the £30,000 charge as he has been resident for seven tax years out of the last nine.

2) Assume Roman decides **not** to use the remittance basis. His UK tax liability will be as follows:

| | £ |
|---|---|
| UK directors fees | 100,000 |
| UK rental income | 80,000 |
| UK bank interest (x 100/80) | 20,000 |
| Foreign property income (arising basis) | 95,000 |
| Foreign bank interest (arising basis) | 30,000 |
| Net income | 325,000 |
| Less; PA (note) | (NIL) |
| Taxable income | 325,000 |
| | |
| *Tax:* | £ |
| £37,400 @ 20% | 7,480 |
| £112,600 @ 40% | 45,040 |
| £150,000 | |
| £175,000 @ 50% | 87,500 |
| | 140,020 |
| Add; long-term residents charge | NIL |
| Tax liability (before credits) | 140,020 |

He will be entitled to a PA as he is not using the remittance basis. However, this will be reduced by £1 for every £2 of net income over £100,000. As such, the PA will be reduced to nil.
As foreign income is taxed on an arising basis, Roman is not subject to the £30,000 charge.

If we compare the two results, we see that Roman should therefore **use** the remittance basis for 2010/11. In 2010/11 it will be cheaper for him to pay the £30,000 tax charge rather than being taxed on his worldwide income.

You will note that this decision is "marginal" for this taxpayer, so he will presumably have to carry out these sort of comparative calculations each year before deciding whether or not to claim the remittance basis.

## 42.17 Nominating income or gains

If a taxpayer is liable to pay the long-term residents charge, he must **nominate the income (or gains) to be the subject of the charge**. There is a box on the SA return (box 35) whereby HMRC want to see "the precise income and gains nominated including the country of origin and source of income…". This means that box 35 should give details of the **bank account and account number of the nominated income** and the source of the income in that account.

Assume therefore that foreign bank interest is nominated to be subject to the charge and the non-domiciled client pays UK tax at 40%. The client could therefore nominate £75,000 of interest to be subject to the long-term residents charge which (at 40%) would generate a charge of £30,000.

However, taxpayers don't have to nominate £75,000. They could nominate a smaller amount and the legislation (S.809H) will automatically "top-up" the charge to £30,000. Therefore **a nomination of £1 of foreign income is sufficient to generate a charge of £30,000**. ITA 2007, S. 809H

S.809I talks about what happens if **nominated income is actually remitted** – ie, funds from the nominated account are brought into the UK. ITA 2007, S. 809I

If ANY nominated income or gains are ever actually remitted to the UK at a time when the taxpayer has any unremitted income or gains, S.809J will apply. ITA 2007, S. 809J

S.809J lays down "ordering" rules whereby all remittances will be deemed to be made in the following order;

1) foreign income which has not been taxed in another country;
2) foreign chargeable gains which have not been taxed in another country;
3) foreign income which has been taxed in another country;
4) foreign chargeable gains which have been taxed in another country.

In effect, S.809J creates a special deemed mixed fund of all unremitted income and gains from which the taxpayer is then deemed to remit on a "worse first" basis.

This new mixed fund then exists **for the rest of the taxpayers life**, so all future remittances will be deemed to be "income first" irrespective of the actual nature of the remittance. S.809J will therefore take priority over the actual mixed fund rules in S.809Q (explained in paragraph 42.13).

Remember that **S.809J is only triggered by a remittance of nominated income and can therefore be avoided by keeping all nominated income outside the UK.**

The advice to taxpayers is therefore NEVER REMIT YOUR NOMINATED INCOME!

To ensure that nominated income is never remitted (even accidentally), advice to non-domiciled clients to avoid falling foul of S.809J is as follows;

1) set up a **separate interest-bearing foreign bank account** with a notional deposit (say £500);

2) that account will generate some interest (say £5); then

3) if the long-term residents charge applies, **£1 of interest is nominated** from this account to generate the £30,000 charge; &

4) the taxpayer will **NEVER touch this account for any other purpose**.

This plan saves the need to disclose foreign sources (except the foreign account with the notional deposit).

It also ensures that any future remittances to the UK will be dealt with under the normal tracing rules and will not be subject to the automatic "deeming" provisions in S.809J. Therefore an actual remittance of (say) non-taxable capital will be treated as non-taxable capital rather than being a deemed remittance of foreign income.

## 42.18 The long-term residents charge & ESC A11

**Years of arrival and departure count as "resident" for the purposes of the long-term residents charge**, even if the "split year" treatment in ESC A11 applied in either or both of those years.

Therefore for individuals leaving the UK in 2010/11, the long-term residents charge will potentially apply if the taxpayer was present in the UK on 6 April 2010. The fact that he may only have been physically present in the UK for a few weeks of the tax year, doesn't remove him from the £30,000 charge.

**The long-term residents charge therefore takes priority over ESC A11** (which is unsurprising given that relief under ESC A11 is only concessionary).

**Illustration 5**

Assume a non-domiciled individual came to the UK in 2003/04, intending to stay for 5 years. He left the UK permanently on 30 June 2010. He has UK and foreign income but no capital gains.

ESC A11 will split the years of arrival and departure.

The long-term residents will apply from 2010/11 as this is the 8th year of residence. The fact that ESC A11 makes him resident only from 6 April to the date of departure is irrelevant.

His choices for 2010/11 are;

<u>1) To claim to use the remittance basis under S.809B</u>

- From 6 April 2010 to 30 June 2010 – UK income is taxed, foreign income is taxed only if remitted.
- From 1 July 2010 to 5 April 2011 – UK income is taxed, foreign income is not taxed (remittances are irrelevant).
- No Personal Allowances are available.

- £30,000 is added to his tax bill at end of the year. There is no apportionment to reflect that he has only been resident for 3 months of the tax year.

2) Don't claim remittance basis

- From 6 April 2010 to 30 June 2010 – UK income is taxed, foreign income is taxed as it arises.
- From 1 July 2010 to 5 April 2011 – UK income is taxed, foreign income is not taxed (remittances are irrelevant).
- Personal Allowances are given (but abated if income exceeds £100,000).
- There is no £30,000 charge.

## 42.19 Meaning of "remittance to the UK"

ITA 2007, S. 809L

Money which is brought to or received or used in the UK by an individual is "remitted" to the UK. A straightforward transfer of money from a foreign bank account to a UK bank account will obviously constitute a "remittance".

Overseas income can be used in the UK without being directly received or transferred to the UK.

For example, if a non-domiciled person incurs expenditure in the UK on a UK credit card, and eventually pays the bill from an offshore bank account, that will constitute a remittance. This is because the money in the offshore bank account has been "used" in the UK.

Finance Act 2008 introduced rules tightening-up of the meaning of "remittance to the UK".

*Non-cash remittances*

Before April 2008, foreign income could only be taxed as a "remittance" if it was brought into the UK as cash. Therefore a non-domiciled taxpayer could buy a foreign asset with foreign income, and then bring that asset into the UK without it being a "remittance".

This has now changed such that **property brought to the UK, and services provided in the UK which derive from foreign income can be treated as remittances**. There are exceptions for personal effects and assets costing less than £1,000. ITA 2007, S.809X

Assets owned by an individual on 11 March 2008 that were purchased from foreign income will remain exempt from being taxed under the remittance basis, even if such assets are subsequently brought in to the UK.

*Gifts to family*

Before April 2008, a non-domiciled taxpayer could give foreign income to a member of his family, the family member could bring it to the UK and no "remittance" was deemed to have been made.

However, from 6 April 2008 **a taxable remittance will arise if money or other property representing a person's foreign income or gains is brought to the UK** by any "relevant person".

"Relevant persons" include the donor's spouse or civil partner (including a person living with the donor as a spouse/civil partner) and children /grandchildren under the age of 18. ITA 2007, S.809M

*Offshore mortgages*

Some UK resident individuals have used offshore mortgages to purchase property in the UK (often because interest rates may have been lower). Interest on the loan was paid out of foreign income without it being a "remittance".

From 6 April 2008, **interest or capital repayments under such offshore loans will constitute a remittance**.

However, the interest element (not capital repayments) of existing mortgages on residential property will be temporarily protected, such that the **new rules only apply to loans taken out (or old loans varied) on or after 12 March 2008**. Protection for the interest on pre-2008 loans will end on 5 April 2028 (or when the loan ends if before that date). FA2008, Sch 7 Para 90

**Example 1**

**Which of the following individuals are entitled to UK personal allowances ?:**

a) Mr Capello: Resident in the UK, domiciled in Italy
b) Mr Bush: Resident and domiciled in the USA
c) Mr Dundee: Resident and domiciled in Australia
d) Mr Sarkosy: Resident and domiciled in France
e) Mr Beckham: Resident in the USA, domiciled in the UK
f) Mr Abramovich: Resident in the UK, domiciled in Russia.

**Example 2**

**Which of the individuals in Example 1 could claim the "remittance" basis of taxation for foreign income?**

**Answer 1**

Personal Allowances

| | | *Yes* | *No* |
|---|---|---|---|
| a) | Mr Capello | ✓ UK Resident | |
| b) | Mr Bush | | X |
| c) | Mr Dundee | | X |
| d) | Mr Sarkosy | ✓ European | |
| e) | Mr Beckham | ✓ British citizen | |
| f) | Mr Abramovich | ✓ UK resident | |

Note: Commonwealth citizens could claim PAs up to 2009/10. However, from 2010/11, an individual is no longer entitled to UK personal allowances purely by virtue of being a Commonwealth citizen.

**Answer 2**

Remittance basis

| | | *Yes* | *No* |
|---|---|---|---|
| a) | Mr Capello | ✓ | |
| b) | Mr Bush | | N/A |
| c) | Mr Dundee | | N/A |
| d) | Mr Sarkosy | | N/A |
| e) | Mr Beckham | | N/A |
| f) | Mr Abramovich | ✓ | |

Both Mr Capello and Mr Abramovich are UK resident but are not UK domiciled and hence are taxed on the remittance basis.

The other four individuals are not resident in the UK and hence are not taxable on their foreign income and can remit the income tax free.