UK Tax for Dual Residents –

making sense of the tax rules

Expert knowledge means success

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Introduction

In these days of increasing international competitiveness, more and more Executives are taking up employment in foreign countries - knowing that they can return to the UK if required in only a few hours.

There are special tax rules to deal with people who pay tax in two countries with which the UK has Double Taxation Agreements - these are referred to as DTA and are made between the UK and many foreign countries and cover most situations. This publication provides information to help you to decide whether you're a resident of the UK or another country for the purpose of these Agreements.

Statutory Definition of Tax Residence – But not until 2013

The Government announced at Budget 2011 its intention to introduce a full statutory definition of tax residence for individuals. Its objective is to replace the current uncertain and complicated residence rules with a clear statutory residence test that is simple for the taxpayer to use. A consultation was launched on 17 June 2011and ran to 9 September 2011.

The draft legislation was due to be published prior to the UK Budget 2012. However, following consultation, the Government announced in the UK Budget 2012, that it has decided to allow further time to finalise the detail of the test. The SRT will be introduced with effect from 6 April 2013 and legislated in the Finance Bill 2013. Draft legislation will be published shortly.

The Government's proposals are covered in this section. Existing rules, until 2013, are covered on page 3 onwards in this publication.

Why is this issue important?

Tax residence has a significant bearing on an individual's UK tax liability, especially if they have non-UK ("overseas") income or capital gains. In most circumstances residents are liable to tax on some or all of their overseas income and capital gains whereas non-residents are not liable. Residence can also affect how much tax is paid on income and capital gains from UK sources.

At present there is no full statutory definition of tax residence. There is some very limited legislation but the definition largely rests on legal cases decided in the courts over a very long period of time and based on facts arising in a very different world from today's globalised economy, technology, travel and working patterns. Court decisions have not provided clear or specific principles that are applicable to all taxpayers. The result is that 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. Tax and professional bodies and other interest groups have long argued that this is unsustainable and unfair to the taxpayer.

The statutory residence test (SRT) is designed to provide a simple process and clear outcome for the vast majority of people whose circumstances are straightforward. For most individuals the SRT will have no impact on their residence status, however, for those with complicated affairs, such as those who travel to and from the UK frequently or who have connections with a number of different countries, there will likely be some impact.

Proposals[1]

The Government are proposing that the SRT should take account of both the amount of time the individual spends in the UK and the other connections they have with the UK. The SRT will make a distinction between:

- ***Arrivers*** – defined as individuals who were not UK resident in all of the previous three tax years; and
- ***Leavers*** – defined as individuals who were resident in one or more of the previous three tax years.

The test will have three parts:

- ***Part A*** – contains conclusive non-residence factors that would be sufficient in themselves to make an individual not resident.

  Where an individual satisfies any of the following conditions of Part A for a tax year they will definitely not be UK tax resident:

  - Non UK resident in all of the three previous tax years, and present in the UK for fewer than 45 days in the current tax year;
  - UK resident in one or more of three previous tax years, and present in

the UK for fewer than 10 days in the current tax year; and

- Leaves the UK to carry out full-time work abroad, providing he/she is 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 during the tax year.

- ***Part B*** – contains conclusive residence factors that would be sufficient in themselves to make an individual resident.

  Where Part A does not apply, an individual will be conclusively UK resident for the tax year under Part B if they meet any of the following conditions:

  - Are present in the UK for 183 days or more in a tax year; or
  - Have only one home and that home is in the UK (or have two or more homes and all of these are in the UK); or
  - Carry out full time work in the UK.

  Where both Part A and Part B apply then Part A will take precedence and the individual will be regarded as non UK tax resident.

- ***Part C*** - contains other connecting factors and day counting rules which will only need to be considered by those whose residence status is not determined by Part A or B.

  Where an individual's residency status is not determined by Part A or Part B, then Part C needs to be considered. Under Part C an individual would simply need to compare the number of days they spend in the UK against a small number of clearly defined connected factors. The connected factors are:

  - Family – the individual's spouse or civil partner or common law equivalent (provided the individual is not separated from them) or minor children are resident in the UK;
  - Accommodation – the individual has accessible accommodation in the UK and makes use of it during the tax year (subject to exclusions for some types of accommodation such as short–term accommodation in hotels);
  - Substantive work in the UK – the individual does substantive work in the UK (but does not work in the UK full-time);
  - UK presence in previous year – the individual spent 90 days or more in the UK in either of the previous two tax years;
  - More time in the UK than in other countries – the individual spends more days in the UK in the tax year than in any other single country.

  These connected factors would be combined with days spent in the UK into a "scale" to determine whether the individual is UK resident or not.

There will be separate scales for arrivers and leavers, reflecting the principle that it should be harder for leavers to relinquish residence than for new arrivers to acquire UK tax residency.

Arrivers – Individuals not resident in all of the previous 3 tax years

Days spent in UK	Impact of connected factors on residence status
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 (otherwise not resident)
120-182 days	Resident if individual has 2 factors (otherwise not resident)
183 days	Always resident

Leavers – Individuals resident in 1 or more of the previous 3 tax years

Days spent in UK	Impact of connected factors on residence status
Fewer than 10 days	Always non-resident
10-44 days	Resident if individual has 4 factors (otherwise not resident)
45-89 days	Resident if individual has 3 factors (otherwise not resident)
90-119 days	Resident if individual has 2 factors (otherwise not resident)
120 – 182 days	Resident if individual has 1 factors (otherwise not resident)
183 days or more	Always resident

"Dual" Residents

Some people are resident for tax purposes in more than one country. See if this applies to you:

- Are you a UK resident?
- Will you be resident in the UK for the whole or part of the tax year?
- Are you resident for tax purposes in a country with which the UK has a DTA?

If you answer "yes" to the above questions, then the chances are that you have a "dual resident" status for tax purposes. Please check with us for a list of the countries with which the UK has a DTA that enables you to claim either full or partial relief from UK tax on your income arising in the UK.

Even if you don't qualify for tax relief because you are dual resident in a country with which the UK has no DTA, you may be entitled to claim relief from UK tax by way of credit for foreign tax paid on overseas income or gains.

DTAs are complicated things (what did you expect!) and one DTA is not the same as another, so it's necessary to check the text of the particular agreement concerned to see if there's any relief in your own circumstances.

"Residence" - what does it mean?

Different countries use different criteria to decide whether someone is a taxable resident or not. It's quite possible to be regarded as a resident for tax purposes under the laws of more than one country (see "dual" residents above).

Most modern DTAs have "tie-breaker" rules to decide which of two States should claim the taxpayer as their own. The "tie-breaker" tests don't appear in the same order in all DTAs and in some Agreements they don't appear at all - good reason to contact us to examine the terms of a particular DTA to see if it applies to you.

Tie-breaker - Residence under the DTA to another country

If the tie-breaker rules award residence under the DTA to another country, then your UK tax liability is usually affected. People who are resident in another country under DTA rules are entitled to make claims to relief from UK income tax on the basis of that overseas residency status - this means that income or gains of a type that are covered under the relevant DTA and which arise in the other State, are exempt from UK tax.

Any income arising in a third country will also be exempt if the DTA contains an article dealing with "other income". But not all DTAs do - it depends on the terms of the particular DTA with the country of which you are treated as a resident. So your UK income might remain fully taxable in the UK, or be taxable in the UK at a lower rate than usually applicable under UK domestic law - or if you're really lucky, it might be exempt from UK tax altogether.

Special rules, however, apply where any income (including foreign income) is connected with a business or profession which an individual carries on in the UK. Again it is important to look closely at the provisions of the DTA in question, since no two DTAs are identical.

If, in accordance with the rules referred to above, you decide that you are resident for tax purposes in a country other than the UK, the Charity, Assets & Residence (CAR) can supply information about the effect of the provisions of the particular treaty on income from UK dividends, interest, royalties, pensions and annuities. They can also supply forms to allow you to make an application to allow future payments of interest, royalties, pensions and annuities to be paid together with the appropriate amount of double taxation relief.

Their contact details are:

HM Revenue & Customs Residency
Fitz Roy House
PO Box 46, Nottingham NG2 1BD, UK
Telephone
+44 (0) 151 210 2222 (or 0845 070 0040 if you are calling from the UK)

Tie-breaker - Residence under the DTA in the UK

If the tie-breaker rules award residence for the purpose of the DTA to the UK, you will remain liable to UK tax on the whole of your worldwide income and gains. You may however be entitled to relief from tax in the other country as a resident of the UK for the purposes of the DTA. The precise terms of the particular Agreement must be consulted since no two Agreements are exactly the same. CAR Nottingham (see previous page)

has stocks of some overseas forms on which claims for relief from foreign tax can be made, if appropriate.

Although a DTA overrides some of the normal consequences of being a UK resident, it doesn't override the fact of UK residence itself for purely domestic law purposes. So, even if by virtue of the tie-breaker provisions in a DTA, you are resident in another country for the purposes of the DTA between the UK and that State, you'll still have to complete UK Tax Returns and fulfil any similar obligations imposed by the UK Taxes Acts.

You may also be UK resident for the purpose of claiming relief from foreign tax under DTAs between the UK and other countries. And you will remain entitled to any personal allowances due on account of your status as a UK resident under domestic law.

The OECD Model Tax Convention Residence Tie-Breaker Rules

The residence tie-breaker rules in most recent UK DTAs closely follow those in the Model Tax Convention of the Organisation for Economic Co-operation and Development (OECD). They comprise a series of tests to be applied successively until residence for the purposes of the Agreement is allocated to one State or the other. In other words, once a test is conclusive it's unnecessary to apply subsequent tests. The tests usually appear in the order of:

- permanent home
- centre of vital interests
- habitual abode
- nationality

Let's examine these four tests separately:

1. Permanent home

You will be a resident only of the State in which you have a 'permanent home' available to you for the period of dual-residence. A permanent home is any form of accommodation that is continuously available to you for your personal use. It doesn't necessarily have to be owned by you. But a property which you let out will not be a permanent home because the fact that it is let to someone else means that it is not continuously available for your own use.

The test will be inconclusive if you have a 'permanent home' in both countries. In those circumstances you should move on to the next test ('Centre of vital interests'). If you have a 'permanent home' in neither country, move on to the next but one test (Habitual abode').

2. Centre of vital interests

You will be a resident of the State with which your 'personal and economic relations' are most close. This is known as your *'centre of vital interests'*. 'Personal and economic relations' is a wide expression intended to cover the full range of social, domestic, financial, political and cultural links. The whole range of these factors must be taken into account, but considerations based upon your personal acts are given special weight.

For example, if you have a home in the UK and set up home in another State while retaining the first home, the fact that you have retained your home in the UK (where you have lived, worked and where your family and possessions are) can, together with other factors, go to demonstrate that your centre of vital interests remains in the UK.

If it is not possible to determine with which of the two States your personal and economic relations are closer, perhaps because the range of factors is broadly balanced between the two, then the test will be inconclusive and you should move on to the next test.

3. Habitual abode

You will be a resident of the State in which you have an 'habitual abode' (broadly, this means the State in which, over a reasonable period, you stay more frequently). The comparison must be made over a sufficient length of time for it to be possible to determine whether residence in either of the two countries has become 'habitual'.

If you can't be said to have an habitual abode in either of the two countries, you should move on to the next test.

4. Nationality

You will be a resident of the State of which you are a national. Ultimately, since in theory **all** these tests may prove inconclusive (even the last, since it is possible to have dual nationality, or to be a national of neither State), DTAs normally provide for the tax authorities of the two countries to settle the matter by negotiation. In practice, very few claims reach this stage.

Tax changes for “non-doms”

UK residents who are non-domiciled and have been taxed on their foreign income on the remittance basis will have to pay an annual charge of £50,000 from 6 April 2012 (previously £30,000) to stay within the remittance basis if they have been UK resident for seven out of ten years. Alternatively, they will be taxed in the UK on their worldwide income.

Users of the remittance basis also lose their tax free personal allowances, but they will be able to opt in for personal allowances if they decide not to use the remittance basis in any year.

For more information see our publication 193 – Tax Residence and Domicile

Other forms of Residence Articles in DTAs

Some of the UK's older DTAs, mainly with former colonies in the Caribbean, but also including the agreements with Guernsey, and the Isle of Man, define a resident of one country as a person who is resident there for the purposes of that country's tax and not resident for tax purposes in the other country. If, therefore, you are dual-resident in the UK and one of the countries below, you will only be able to obtain relief by way of credit for one country's tax against the other's:

Antigua	Isle of Man	Myanmar
Belize	Jersey	St. Kitts
Brunei	Kiribati	Sierra Leone
Greece	Lesotho	Solomon Islands
Grenada	Malawi	Tuvalu
Guernsey	Montserrat	

Certificate of Overseas Residence

If you:

- are resident in the UK under domestic law, and
- are also resident in another country under that country's rules, and
- wish to claim that you are a resident of the other country for the purposes of the DTA between the UK and that other country then you need to obtain a certificate from the overseas tax authority confirming that it regards you as resident there under its domestic law for the period in question, which must be stated on the certificate.

Special rules - the USA

Special rules apply where the other county is the United States of America, if you are claiming to be a resident of the United States for the purposes of the UK/US DTA. Statements concerning residence should not normally be sought from the United States Internal Revenue Service. This is because the United States operates a special system whereby it taxes its 'citizens' on their world-wide income, wherever they may be resident. US citizens are not, however, necessarily 'residents' of the United States for the purposes of the DTA.

Article 4(2) of the DTA provides that a citizen or green card holder will be treated as a resident of the United States for purposes of the DTA, and, thereby entitled to treaty benefits, only if two conditions are met.

Example

If you spent 48 days in the US in 2006, 250 days in 2005 and 366 days in 2004, the calculation would be as follows:

Year of test - 2006 (more than 31 days spent in US)

2006	48 days	x 1/1	= 48
2005	250 days	x 1/3	= 84
2004	366 days	x 1/6	= 61
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Both legs of the substantial presence test are passed and you will be regarded as resident in the US under that country's domestic law.

- You must have a substantial presence (see below), permanent home or habitual abode in the United States;
- You must not be treated as a resident of a state other than the United Kingdom under any treaty between the United Kingdom and a third state.

Substantial presence test

You will have a substantial presence if:

- you were present in the US on at least 31 days in the calendar year under test; and
- the sum total of days on which you were present in the US in the year under test and in the two preceding years adds up to at least 183 days. For the purposes of this calculation a day spent in the US in the year preceding the year under test counts as 1/3, and a day in the year before that counts as 1/6. Part days of presence in the US should be treated as if they were whole days for this purpose.

Residence tie-breaker provisions

If you are UK resident and also, by virtue of the above tests, resident in the US, you will need to determine your residence status for the purposes of the UK/US DTC by applying the tie-breaker provisions described earlier. If you wish to make a claim as a dual UK/US resident who is a resident of the US for the purposes of the DTA, the procedure to be adopted depends upon whether or not you are a US citizen.

Further Information

HMRC have provided an online tool which provides a step-by-step guide on whether someone is resident or non-resident. It is available online at:
http://www.hm-treasury.gov.uk/d/consult_statutory_residence_online_tool.xls

This publication is for general interest - it is always essential to take advice on specific issues.

We believe that the facts are correct as at the date of publication, but there may be certain errors and omissions for which we cannot be responsible.

If you would like to receive further information about this subject or other publications, please call us – see our contact details on the next page.

Acknowledgements

[1] The text in this section is derived from:
http://www.skandiainternationalknowledgedirect.com/Financial-Planning-Solutions/Country-Specific/Statutory-definition-of-tax-residence-%E2%80%93-a-summary.html

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Important Notice

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