



## Government issues proposals for a statutory residence test

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Christopher Sly, Partner, and Freddie Bjorn, a Solicitor in the Private Client department, summarise the framework of the proposed statutory residence test for individuals.

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Following the announcement by the Chancellor in the 2011 Budget, the Government published a consultation document in the summer of 2011 containing proposals for a new statutory definition of tax residence with a view to bringing legislation in to take effect from 6 April 2012. However, in December 2011 the Government announced they would allow further time to finalise the detail of the test. The test is now to be introduced with effect from 6 April 2013 and legislated in the Finance Bill of that year. Draft legislation is to be published around the time of the Budget 2012. The Government is not proposing to allow individuals to apply the test retrospectively to calculate tax for prior years and consequently the current rules will continue to apply.

Residence is a crucial element in the tax liability of an individual in the United Kingdom, but currently it does not have a full legal definition. The present rules, based on a mixture of statute, case law and guidance published by HM Revenue & Customs (HMRC), are uncertain and complicated, so much so that the Government considers that they deter some businesses and individuals from investing in the UK.

### PROPOSED FRAMEWORK FOR A STATUTORY RESIDENCE TEST

The analysis below is based on the initial Consultation document issued in the summer of 2011. There may be material changes when the draft legislation is published around the time of the Budget 2012.

The proposed test is designed to provide a simple process and a clear outcome for the vast majority of people in straightforward cases. HMRC is even looking at providing an interactive online tool to allow individuals to self-assess their tax residence status.

The proposed test is composed of three parts.

Part A contains conclusive non-UK residence factors that would be sufficient in themselves to make an individual non-UK resident.

Part B contains conclusive residence factors that would be sufficient in themselves to make an individual resident in the UK.

Part C contains other connection factors and day counting rules which only need to be considered by

an individual whose residence status is not determined by Parts A or B.

**Part A:** conclusive non-UK residence

Part A of the proposed test would conclusively determine that an individual is non-UK resident for a tax year if that individual:

- was non-UK resident in all of the previous three tax years and he is present in the UK for fewer than 45 days in the current tax year; or
- was resident in the UK for one or more of the previous three tax years and he is present in the UK for fewer than 10 days in the current tax year; or
- leaves the UK to carry out full-time work (i.e. a 35 hour week) abroad, provided he 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 in the tax year.

An individual who does not fall within Part A would not necessarily be resident in the UK, but would instead need to consider Parts B or C of the test.

**Part B:** conclusive UK residence

There are a large number of people who are clearly tax resident in the UK because they spend almost all of their time in the UK, work exclusively or predominantly in the UK, or have their home in the UK and base their life and family in the UK. Part B is intended to give certainty to this group.

Provided Part A of the test does not apply, an individual would be conclusively UK-resident for the tax year under Part B if that individual:

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

An individual who does not meet any of the conditions in Part B would not necessarily be non-UK resident; instead he would need to consider Part C of the test.

In exceptional cases, an individual may satisfy the conditions of both Parts A and B. In such circumstances, it is proposed that non-UK resident status will prevail.

**Part C:** other connection factors and day counting

Part C would only apply to those individuals whose residence status is not determined by Parts A or B and therefore whose circumstances are less straightforward. Residence is determined by considering how many connection factors an individual has with the UK, together with the number of days he spends in the UK.

This part of the proposed test reflects the principle that the more time someone spends in the UK, the fewer connections he can have with the UK if he wants to be non-UK resident. In consequence, it puts forward different rules for those arriving in the UK and leaving the UK.

The Government proposes that the following connection factors should be relevant to the residence status of an individual, but only when linked to the amount of time he spends in the UK. These factors can be summarised as follows:

- **family** - the spouse or civil partner or common law equivalent (provided they are not separated from the individual) or minor children of an individual 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);
- **substantive work in the UK** - the individual does substantive work in the UK (but does not carry out full-time work in the UK);
- **previous UK presence** - 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 connection factors would be combined with days spent in the UK into a "scale" to determine whether the individual is UK-resident or not. It is proposed to have separate "scales" for arrivers and leavers, reflecting the principle that it should be more difficult for leavers to relinquish residence than for new arrivers to acquire it.

Days spent in the UK	Minimum number of connection factors needed to make an individual UK-resident in a tax year	
	Individuals arriving in the UK	Individuals leaving the UK
Fewer than 10 days	Always non-UK resident	Always non-UK resident
10-44 days	Always non-UK resident	4
45-89 days	4	3
90-119 days	3	2
120-182 days	2	1
183 days or more	Always UK-resident	Always UK-resident

**Connection factors for individuals coming to the UK (non-UK resident in all of the previous three tax years)**

If the individual was non-UK resident in all of the three tax years preceding the year under consideration, four of the five connection factors may be relevant to his residence status, if they occur at any point in the tax year. These are that the individual:

- has a UK-resident family;
- has substantive UK employment (including self-employment);
- has accessible accommodation in the UK;
- spent 90 days or more in the UK in either of the previous two tax years.

### **Connection factors for individuals leaving the UK (resident in one or more of the previous three tax years)**

If they occur at any point in the tax year, all five of the connection factors listed above may be relevant to the residence status of an individual if that individual has been UK-resident in one or more of the three tax years immediately preceding the tax year under consideration.

### **OTHER ASPECTS OF THE PROPOSED TEST**

#### **Split years**

Currently, an individual is either resident in the UK for a full tax year or non-UK resident for a full tax year. However, by concession, it is possible to split a tax year so that an individual is treated as UK-resident for only part of a tax year.

The proposed test incorporates a split year test, but whereas the current test relies on the vague concept of a person becoming "permanently" resident in the UK or elsewhere, the new rules will treat a tax year as being split into periods of UK residence and non-UK residence if an individual:

- comes to the UK to take up permanent residence;
- leaves the UK to take up permanent residence abroad; or
- loses UK residence when leaving to work full-time outside the UK.

A tax year will not be treated as split where the residence status of an individual changes due to changes in the number of connection factors under Part C, such as the arrival or departure of his family.

If an individual becomes non-UK resident by virtue of leaving the UK to work full-time abroad and is accompanied by his spouse or civil partner, split year treatment would also apply to the spouse or civil partner provided their sole or main home is outside the UK. Under the existing practice, the main home does not have to be moved.

#### **Anti-avoidance provisions**

The proposed test includes an income tax anti-avoidance rule in relation to some forms of investment income. This is similar to the existing capital gains tax temporary non-UK residence provision, which broadly allows chargeable gains realised while an individual is non-UK resident for a period of less than five years to be taxed in the year of his return to the UK. This is to deter people from becoming non-UK resident for short periods of time to avoid UK tax liability on expected income.

#### **Ordinary residence**

Ordinary residence is a different concept to residence, but similarly has no statutory definition.

Currently, individuals who are resident but not ordinarily (habitually) resident in the UK can use the remittance basis to shelter foreign income from UK tax. Ordinary residence is uncertain and difficult to apply in practice, and the Government proposes to re-define the concept or abolish it altogether. "Overseas work days relief" will be retained for not ordinarily resident employees. This allows not ordinarily resident individuals to claim the remittance basis on employment duties carried on outside

the UK, even if for a UK employer. It is likely to cease to apply for UK domiciled employees who might be not ordinarily resident.

## **CONCLUSION**

Neither overly complicated nor too subjective, the long-awaited statutory residence test, if adopted, is likely to provide far greater certainty for individuals in determining their tax residence.

This new test will not be able to provide clear answers for all taxpayers, however, and the application of Part C, in particular, is unlikely to be straightforward. As a result, obtaining specialist advice is still to be recommended in almost all cases.

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If you wish to discuss how this proposal could affect your tax situation please contact your usual contact in the Private Client department at Payne Hicks Beach or Christopher Sly at [csly@phb.co.uk](mailto:csly@phb.co.uk) or Freddie Bjorn at [fbjorn@phb.co.uk](mailto:fbjorn@phb.co.uk)