


Tax Planning International

European Tax Service

Volume 12, Number 3 – March 2010

INTERNATIONAL INFORMATION FOR INTERNATIONAL BUSINESS

- 
- The background of the cover features a world map with several silhouettes of people in business suits standing on it. The map is partially obscured by the silhouettes and the text. The overall color scheme is a gradient of red, orange, and yellow, with a large globe visible in the upper left corner.
- United Kingdom Budget 2010
 - Belgium: New reporting obligation for payments to tax havens
 - The new Dutch classification decree
 - New rules regarding Slovenian withholding tax on income from financial instruments
 - Tax treatment of photovoltaic business parks in Italy
 - High tax rates triggers high earners to leave

UK: Tax axe on high earners

David Anderson and Graeme Perry
Sykes Anderson LLP Solicitors, London

London is deemed as the most highly taxed financial centre in the world after confirmation of the 50 percent income tax rate in this budget for high earners. Will this dreaded tax rate will fuel the mass exodus of high earners to tax friendly jurisdictions or whether such moves are in fact practical, are questions answered by David Anderson and Graeme Perry.

I. UK Income tax changes

The well publicised 50 percent additional rate of UK income tax, due to come into effect in April 2010, will affect individuals earning in excess of GBP150,000. In addition, those earning over GBP100,000 a year will suffer from a restriction on their personal allowance. This will operate by reducing the personal allowance by GBP1 for every GBP2 earned over GBP100,000. On current figures, this means that those individuals earning at least GBP112,950 a year will have no personal allowance at all from the start of the next tax year.

Many people in these earnings brackets are considering moves to more favourable tax jurisdictions. Although there may be significant tax advantages in such moves, practical issues do arise, in particular for those who need to continue working for their UK based employer.

II. Moving to tax treaty countries

The first hurdle is to establish non-UK residency. People will often be under the impression that so long as they have moved house to a foreign country that will be the end of the matter and they will have escaped the UK tax net. The reality is very different, with HMRC taking an increasingly hard approach to those individuals who seek to leave the country for tax purposes.

Moving to a country which has a double tax treaty with the UK can be helpful in this regard. These treaties will usually contain a residence tie-breaker test to determine in which country you are to be considered resident for tax purposes. When this is the case, One will usually only be considered as tax resident in one of the two countries, i.e. dual residency is usually not possible. Generally it will be more straightforward to comply with this test if one realistically moves ones private life to another country. However, people are often not as keen to move to these countries as, although the personal tax regimes may be more favourable than the UK, they are less likely to receive the

kind of tax exemptions which apply in jurisdictions where they will have no income tax liability such as Monaco.

III. Residency in tax haven jurisdictions

The difficulty with a move to an income tax-free jurisdiction such as Monaco is that there is no treaty protection which establishes that you can only be resident in one or the other states. It is therefore possible to be a dual resident of the UK and say Monaco for tax purposes. In this dual residence position, the worldwide income and gains would still be subject to UK tax. It will be difficult to obtain acceptance from HMRC to the proposal that one has ceased UK residency and become resident only in Monaco. This is because becoming non-resident in the eyes of HMRC is not as simple as moving elsewhere and keeping ones visits to the UK below 91 days per year. HMRC published new guidance in 2009, which sets out their tightened approach to non-residency claims.

Unless one can show that one is moving abroad because of full-time employment outside the UK, a claim that one has ceased to be UK resident will require evidence of a clean break from the UK involving a genuine change in lifestyle. The courts have crucially not defined what is meant by "full-time employment outside the UK". In some cases the employee may work shorter hours than before or have some duties such as meetings which require them to be in the UK from time to time as part of their employment duties. One would, in any event be well advised to cut as many ties with the UK as possible if seeking to establish non-residency.

The difficulty of successfully obtaining a non-residency status has been highlighted by several high profile recent cases involving high net worth individuals. These judgments review the approach of HMRC to non-residency and confirm the necessity for a clean break from family and social ties in the UK in order to be considered as leaving the UK for tax residency purposes. Even where an individual had stringently kept his time in the UK to below 91 days a year for over 30

David Anderson and Graeme Perry are Solicitors and Tax Advisers in the London office of Sykes Anderson LLP.

years, he was still deemed to have never lost his UK residency for tax purposes.

There will not be one determining factor when assessing residency so, for example, keeping a property in the UK would not, on its own, be conclusive of retaining UK residency. Effectively, when an argument is put forward that an individual has ceased to be a UK resident, a balancing act would be required to determine where they are resident. Each of the factors continuing to link one to the UK will be used as evidence that one has maintained residency here and continues to be subject to tax in the country on the worldwide earnings, whereas any action taken to cut ties with the UK will be used as evidence that you have ceased to be resident here. Certainly retaining UK property will be a strong factor against an argument for non-residency and other elements such as family life, doctor registrations, social club memberships and bank accounts will need to be taken into consideration.

IV. Continuing to work in the UK

One of the factors that will continue to link individuals to the UK is work. This can pose particular problems for those individuals who wish to continue UK employment as this will be added to the list of UK ties which HMRC will use to claim that UK residency has been retained. Notably, where an individual continues to carry on duties in the UK it becomes harder to argue that there has been a significant change in lifestyle. Another particular problem which can arise is for those individuals who continue to be directors of UK companies. They will find it difficult to contend the residency position as they have an attachment to a UK company which requires an element of presence here. It should be noted that simply resigning as a director does not automatically detach a director's ties from the company. If one continues to exercise control over the company, one may well still be classed as a shadow director, which for company and tax law has largely the same effect as being a named director.

The idea of a move to Monaco or similar low-tax jurisdiction is likely, therefore, to be more favourable for those individuals whose work is based outside the UK (for example those concerned more with international development and trade) and who dispose of their main residences in the UK. This can fit well with the position of numerous companies who are seeking to expand their operations into new markets. It is highly advisable for any employment contract to clarify that duties are to be carried out solely abroad.

V. UK taxation of non-residents

Even individuals who have been accepted as non-resident will be required to pay UK tax if they spend any time working in the UK, which is more than 'incidental' to their non-UK duties. This will be based on the proportion of work carried on in the UK. Employers will be under a duty to make deductions under the PAYE and NIC systems from salaries paid to these individuals. These deductions will be in respect of the proportion of income attributable to the UK duties.

Where an individual who claims to be non-UK resident receives a salary from a UK company, the situation is likely to be scrutinised by HMRC. This is because they can result in a sum being paid which is deductible from a company's profits for corporation

tax purposes but does not attract income tax in the hands of the individual.

VI. Communicating with HMRC

It may be advisable to approach HMRC voluntarily before beginning to work under such arrangements. Negotiations can then be entered into to determine the proportion of income which is attributable to the UK duties. The default position will be a time spent basis but a qualitative approach can be taken so that, if only less important duties take place in the UK, this can be taken into account when negotiating the tax due. This will result in individuals accounting for some UK tax when they may previously have believed that they would escape this. However, it has the very helpful effect of making the position clear from the outset in that there is an acceptance from HMRC that the taxpayer is a non-resident.

There is a much lower risk of HMRC approaching the taxpayer at a later stage contending that he/she has remained UK resident and owes a large sum of income tax backdated to when he/she claimed to leave the country. It also makes it easier for the employing company to pay the remuneration to its employees without the worry of its corporation tax return being challenged, or a PAYE investigation being initiated.

Once the non-residency position of a taxpayer has been accepted, he/she will need to remain non-resident by complying with the day counting tests and not re-establishing themselves in the country.

VII. Lump sum payments

If any lump sum payments are received by employees

“One of the factors that will continue to link individuals to the UK is work.”

for instance in respect of the employee entering into "golden handcuffs" arrangements with the company, care must be taken to determine whether these are taxable. Even if received in the year following departure from the UK, these can remain fully taxable in the UK as they will be deemed to be in respect of employment from the last tax year. These arrangements are probably best avoided.

Conclusion

Although there are clear benefits of a move to a low-tax or no-tax jurisdiction, careful planning should be undertaken before proceeding with such a move and the practical steps of establishing non-residency must be considered. To force the hand of HMRC, initiating negotiations to pay some UK income tax may be helpful.

David Anderson is Solicitor and CTA, co-founder of Sykes Anderson LLP. He heads up the international tax department, specialising in French tax planning and UK tax. He can be reached by telephone at: +44 (020) 3178 3770 or by email at :david.anderson@sykesanderson.com.

Graeme Perry is Tax Solicitor at Sykes Anderson LLP, specialising in cross-border tax matters and the tax implications and benefits of moving to, and investing in France, Monaco and Switzerland. He can be reached by telephone at: +44 (020) 3178 3770 or by email at: graeme.perry@sykesanderson.com.