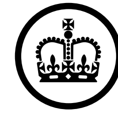

Reform of the taxation of non-domiciled individuals:

summary of responses to consultation

December 2011

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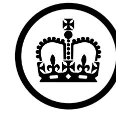

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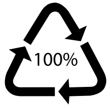

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1 Introduction

Aim of the response

1.1 The Government published *Reform of the taxation of non-domiciled individuals: a consultation* on 17 June 2011 and the consultation closed on 9 September 2011. This document sets out the Government's response to the consultation. The aim of this response is to make clear how the feedback received during the consultation has informed policy development and to confirm how the Government intends to take forward issues raised during the consultation.

Policy intention

1.2 As set out in the consultation document, the Government's policy objectives are to:

- ensure a greater tax contribution from non-domiciled individuals ("non-domiciles") who have been resident in the UK for many years and claim the beneficial tax regime available to them ("the remittance basis");
- promote inward investment in business by removing barriers in the non-domicile tax regime that actively discourage it; and
- simplify the current remittance basis rules in line with the Government's wider commitment to creating a tax system that is more certain, efficient and supportive of growth.

Description of the policy

1.3 The policy changes included in the consultation were:

- increasing the existing £30,000 annual charge to £50,000 for non-domiciled individuals who claim the remittance basis in a tax year and who have been UK resident in 12 or more of the 14 years prior to the year of claim;
- enabling non-domiciles to remit overseas income and capital gains tax-free to the UK for the purpose of commercial investment in businesses; and
- making technical simplifications to some aspects of the current remittance basis rules to remove undue administrative burdens.

Overview of the consultation

1.4 The consultation requested evidence on the impact of increasing the annual charge.

1.5 Views were sought on two main policy changes: encouraging business investment and simplifying the existing remittance basis rules. Respondents were invited to give their responses on these issues via eight consultation questions which are set out below.

Encouraging business investment

1. Are the proposed exclusions from the incentive appropriately drawn? Should other types of business be included or excluded?
2. What would be the impact on both investment and complexity of extending the incentive to listed companies?
3. Are the proposed anti-avoidance provisions suitable? Would it be appropriate to require remitted income or capital gains to be taken out of the UK or reinvested within two weeks of the disposal of the investment?
4. Would a mandatory requirement to claim the relief for business investment on a Self Assessment tax return be an appropriate way of monitoring the policy? If not, what alternative monitoring approach would be appropriate?
5. Would the policy as outlined be an effective means of encouraging investment in the UK?

Simplifying the existing remittance basis rules

6. (a) Do you think the proposed solution for each simplification would be effective?

   (b) Can you propose other ways in which the remittance basis rules could be simplified, provided they meet the principles described in paragraph 2.63 (of the consultation document)?

Taxation of assets sold in the UK

7. Would two weeks be a suitable period of time before which the proceeds of the sale of an exempt asset should be taken out of the UK?

Statement of practice 1/09 – employees with duties in the UK and overseas

8. Should the situations outlined in paragraphs 2.98 to 2.101 (of the consultation document) fall within the new statutory treatment for employees who are not ordinarily resident and carry out duties in the UK overseas? Are there any other situations which are not covered by SP1/09 and might require legislative provision?

2 Summary of responses

2.1 The Government is grateful to those who submitted responses for their time and effort and for the constructive comments made. A total of 83 responses were received from a mix of organisations and individuals. Over 85% were from advisors, businesses or representative bodies. Annex A contains a full list of respondents.

2.2 Overall, respondents welcomed the proposals and felt that they would send a positive signal to non-domiciles who are resident in the UK or who are considering coming to, or investing in, the UK. The commitment to making no further substantive changes for the rest of this Parliament was seen as a clear indication that the Government recognises the importance of providing certainty. There was a mixed response to the increase in the remittance basis charge, with some respondents concerned about the potential impact. The proposed business investment relief and simplifications to the remittance basis were positively received.

Increasing the remittance basis charge

2.3 Comparatively few respondents commented on the proposal to increase the remittance basis charge (RBC) to £50,000.

2.4 Of those who commented a small number were strongly opposed to the increase. These were all representatives of the UK maritime industry and they raised concerns about the possible impact on that sector. They indicated that non-domiciles, mostly of Greek nationality, are particularly important to the maritime industry and argued that a significant proportion of the Greek ship-owning community had left the UK since the previous Government's reforms to the non-domicile regime in 2008. They contended that the rise in the RBC could have a similar effect by prolonging uncertainty as well as increasing tax. One response suggested that, as a way of mitigating the impact, years spent by non-domiciles in the UK before the age of 18 should be excluded when assessing liability to pay the RBC. There were no specific representations from other business sectors.

2.5 Other respondents were less strongly opposed but felt that, in general, the increased RBC could make the UK less attractive and have a negative impact on non-domiciles, possibly affecting the number of non-domiciles choosing to be resident in the UK.

2.6 Others felt that the increase to the annual RBC was reasonable and that the proposed level of the increase was unlikely to have a significant impact on the number of non-domiciles in the UK.

2.7 A number of responses requested confirmation that the level of the RBC will not be increased again.

Government response

2.8 The Government continues to believe it is right to require an increased contribution from those non-domiciles who have been resident in the UK for many years or all their lives and who benefit from the remittance basis of taxation.

2.9 While the Government recognises that the UK maritime sector faces competition from other jurisdictions and notes its concerns, it does not accept that the increase to the RBC will have a

critical impact on that industry. It believes other factors, such as the wider tax landscape, will continue to be influential and that the UK will remain an attractive location for maritime business despite commercial changes in the global shipping industry. It is right that all non-domiciles should be subject to the same rules and that there should be no special treatment for particular sectors.

2.10 The suggestion to exclude time spent as a minor in the UK when assessing liability to pay the RBC would have a significant Exchequer impact. It would also provide a relaxed tax treatment for wealthy individuals who may have spent a significant period in the UK. The Government does not believe this could be justified and will not take this suggestion forward.

2.11 The Government will therefore implement the increase to the RBC as outlined in the consultation document and legislation will be included in Finance Bill 2012 to take effect from 6 April 2012.

2.12 The Chancellor made a commitment at Budget 2011 that there would be no further substantive changes to non-domicile taxation for the rest of this Parliament. This commitment applies to the level of the RBC. The Government believes this will provide certainty and stability for non-domiciles.

Encouraging business investment

Types of business

Box 2.A: Question 1

Are the proposed exclusions from the incentive appropriately drawn? Should other types of business be included or excluded?

Qualifying businesses

2.13 All respondents welcomed the proposed relief for business investment and the intention to draw the policy widely.

2.14 A significant number of respondents felt the requirement that trading on a commercial basis must constitute a "substantial proportion" of the overall activities of a business needed further explanation in respect of what was meant by "substantial" and how this would be calculated.

2.15 Clarification was sought on whether a company would be able to carry out a small amount of non-qualifying activity and whether investment into a company carrying out a mixture of trading and other activities would qualify for relief. Similarly, some asked whether a business in which a substantial proportion of overall activities consist of a mixture of trading and the development or letting of commercial property would be a qualifying business.

2.16 Some respondents asked whether investments in start-ups or companies preparing to trade would qualify for relief. They also asked about the impact on a claim to relief if a company ceased to meet the qualifying conditions during the period of investment (for example by ceasing to be a trading company or diversifying into non-qualifying activity), or following the commercial failure of a company. It was suggested that once relief had been given, it should not be withdrawn as a result of changes in the status of a company, except in cases of abuse.

2.17 It was also proposed that a time limit for investments to be made should be introduced, with any money brought to the UK for investment not treated as a taxable remittance if it was either used as a qualifying investment or taken back offshore within the time limit.

2.18 Under current legislation, an individual is regarded as having remitted overseas income or capital gains if a benefit is received by a UK resident "relevant person". This includes a spouse, civil partner, a partner living with the individual as their spouse/civil partner, minor children or grandchildren, close companies or trustees. A small number of respondents asked whether relief would be available to the individual regarded as having made the remittance if the qualifying investment was made by a "relevant person".

Government response

2.19 The Government's intention is to encourage active investment in a broad range of businesses and sectors. However, this must be consistent with ensuring it is not open to avoidance or used to provide a personal benefit to the individual.

2.20 As stated in the consultation, qualifying activities will be a business which is either a trade or which develops or lets commercial property. A trade will be defined as anything that is treated for corporation tax purposes as the carrying on of a trade. Investment in a company which combines trading activity with developing or letting commercial property will be eligible for the relief.

2.21 The Government will require all, or substantially all, of the company's activities to be qualifying activities. Investments will therefore be eligible for the relief provided any non-qualifying activities do not form a substantial part of the company's total business activities. For these purposes this will mean that the non-qualifying activities constitute no more than 20% of the company's business activities. For companies that have yet to start trading at the time the investment is made, the relief will be available where it is reasonable to expect that non-qualifying activities will not be substantial. For most companies, determining whether non-qualifying activity breaches this condition will be based on the company's turnover but this may not be applicable in all cases. HM Revenue & Customs (HMRC) will provide guidance on how total business activity should be measured.

2.22 As the Government wishes to encourage new businesses, it will not require that a qualifying business must be trading at the time of the investment. However, it will require that the business should commence qualifying activities within two years of the investment being made. If a company fails to commence trading, the investment will not be treated as a taxable remittance provided the investor disposes of it, and takes the full proceeds offshore, within 45 days of the end of the two-year period. Companies undertaking Research and Development (R&D) will be treated as carrying on a commercial trade and will be eligible for the relief.

2.23 The company will need to meet the qualifying conditions at the point of investment and throughout the period of investment. However, the Government recognises that it is important to allow individuals to take appropriate mitigating steps if, at any point, the company ceases to meet the qualifying conditions. Therefore, where a non-domicile invests in a company that subsequently changes its activities to such an extent that its qualifying activities are no longer substantial or it fails to fulfil the qualifying conditions, the Government will allow 45 days for the investor to dispose of their investment. This period will start on the date they became aware, or could reasonably have known, that the company had ceased to meet the qualifying conditions. If the investor fails to dispose of their investment within this time limit, the amount of overseas income and gains which remains in the company will no longer qualify for the relief and will be liable to tax in the UK. There will be a further time period to allow the individual to remove disposal proceeds from the UK and details are set out at paragraphs 2.65 to 2.69.

2.24 In some cases, it may be difficult for an investor to know that a company's activities have changed and to dispose of their investment within the 45-day period. The draft legislation therefore contains a provision to allow HMRC to extend this grace period where exceptional

circumstances mean it would be unreasonable to expect the individual to dispose of an investment within 45 days.

2.25 The Government confirms that the relief will be available for all qualifying investments made by any relevant person.

Non-qualifying activity

2.26 Many respondents thought that there should be fewer exclusions or that the proposed exclusions should be modified to ensure the policy achieves its objective of encouraging significant inward investment.

2.27 Around a quarter of respondents commented that the exclusion of residential property was unnecessarily restrictive and would limit the attractiveness of the relief. It was felt that investment in residential property should be allowed where it was on a commercial footing.

2.28 Clarification was sought on whether the relief extended to investments in:

- Businesses which build and develop residential property;
- Businesses whose activities include the use of residential accommodation such as student accommodation, nursing homes, private hospitals and hotels; and
- Furnished holiday lettings.

2.29 Some felt that the proposed exclusion of businesses which lease tangible, moveable property (such as yachts or cars) was unduly restrictive and would prevent legitimate investment in commercial businesses. Clarification was sought on whether the exclusion would extend to items such as plant and machinery, and whether investment in commercial businesses such as shipping or aircraft leasing would be allowed. Similar issues were raised on the exclusion of businesses that provide personal services (such as nannies or cooks) as part of their business activities.

2.30 Although most respondents acknowledged the need to prevent indirect or direct personal benefit arising from any investment, it was felt that such concerns should be dealt with by the specific exclusion of activity which is not carried on as a commercial business or provides a personal benefit to the investor rather than a blanket exclusion of certain types of business.

Government response

2.31 The Government has noted the weight of opinion that there should be no blanket exclusion for residential property. The Government maintains that there is a material avoidance risk associated with residential property but recognises that many non-domiciles see this as an attractive area for investment. The draft legislation will therefore contain rules to target the avoidance risk rather than the wider exclusion for residential property proposed in the consultation document. These rules are set out in detail in the section on anti-avoidance in paragraphs 2.73 to 2.76 below.

2.32 Otherwise residential property will fall within the general rules on qualifying activity (outlined in paragraphs 2.20 and 2.21). This means that residential property companies will be capable of qualifying for relief provided they do not carry out a substantial amount of non-qualifying activity. Therefore, companies carrying out a trade, for example building and developing residential property will be eligible, as will trading companies where the business involves the use of residential property, such as nursing homes, private hospitals, hotels and private student halls of residence. However, activity that is not a trade, such as the letting of residential property, will not qualify unless that activity forms less than 20% of the company's business activity.

2.33 Businesses undertaking furnished holiday lettings (FHLs) will not be qualifying businesses for the purposes of the relief. Although FHLs are treated as a trade for certain purposes, they are not taxed as such and will therefore not meet the qualifying conditions.

2.34 The Government also accepts the view that it would be too restrictive to exclude relief for investments in companies whose business activities include the leasing of tangible moveable property or the provision of personal services. The rules described in the section on anti-avoidance (paragraphs 2.73 to 2.76) will ensure that the exclusion is limited to companies that provide such services for the direct personal benefit of an investor or relevant person. Otherwise there will be no specific exclusion for leasing companies and those that are carrying out a trade will, in general, qualify for relief.

2.35 To summarise, there will be no exclusions for particular business sectors and non-qualifying activity will simply be anything that is not qualifying activity, as defined in paragraph 2.20.

Form of business

Box 2.B: Question 2

What would be the impact on both investment and complexity of extending the incentive to listed companies?

2.36 Over half of respondents commented on extending the relief to include companies listed on a recognised stock exchange ("listed companies"). Views were mixed on this point. Some were opposed, stating that it would only benefit those looking to build an investment portfolio rather than those who wished to support the growth of business and the economy. Others felt that it would reduce the amounts invested in unlisted companies or those listed on exchange-regulated markets. A small number of respondents felt that including listed companies would be likely to result in an increased administrative burden for investors due to the potentially high number of transactions.

2.37 Overall, a small majority of those who commented thought that listed companies should be included because this would make the relief more attractive and would be likely to lead to increased investment. Some suggested that it would prevent difficulties arising if a company listed after investment. A small number felt that, if the relief was extended to listed companies, it should be restricted to newly issued equity or new loans only.

2.38 It was suggested that, if the relief was extended to listed companies, the different nature of such companies should be recognised by revising the qualifying conditions, for example by removing the requirement for such companies to be carrying out a trade.

2.39 Many respondents thought that the relief should not be restricted to companies and should include other forms of business. Most were in favour of extending to all partnerships or at least to Limited Liability Partnerships. Some recognised that extending the relief in this way could lead to an increased risk of avoidance but felt that this should be dealt with by specific provisions rather than a wholesale exclusion. It was argued that allowing relief for investment in partnerships would make the relief more attractive as they are commonly used across a range of sectors such as venture capital, private equity, commercial property, and professional services firms. A small number of respondents suggested extending the relief to allow investment in sole traders.

2.40 Clarification was also sought on what types of foreign entities would be eligible for relief.

Government response

2.41 Although the Government has noted the level of support for extending the relief to listed companies, it has not seen any compelling evidence that doing so would significantly enhance the attractiveness of the relief and lead to increased levels of active investment. In addition, there is a need to balance incentives for investment against complexity. The Government does not think its proposed rules on qualifying companies and avoidance could be applied to listed companies and so additional legislation, including further anti-avoidance provisions, would be required. This would add significantly to the complexity of the relief. The Government therefore will not extend the relief to companies listed on a recognised stock exchange.

2.42 However, the legislation will include provisions to deal with situations where a qualifying investment has been made in an unlisted company that subsequently becomes listed. This will allow investment to be taken out of such a company without creating a taxable remittance provided this takes place within 45 days. This is the same limit that will apply to other situations where a company ceases to meet the qualifying conditions (see paragraph 2.23).

2.43 The Government is not yet convinced of the case for including partnerships within the relief. It remains concerned that extending the relief in this way could lead to large scale avoidance unless complex anti-avoidance legislation was introduced. The legislation which will take effect from 6 April 2012 will not allow investment in partnerships.

2.44 However, in view of the strength of support for extending the relief to investments in partnerships and the increased investment that this might encourage, the Government will consider this issue further to evaluate whether there is any scope for widening the relief to include investment in partnerships in Finance Bill 2013. The Government will not consider extending the relief to sole traders.

2.45 Investment in a foreign entity will be eligible for relief where it is a private limited company and the other conditions on qualifying activities are met.

2.46 To summarise, the Government will initially limit the relief to companies that are either unlisted or quoted on exchange-regulated markets such as AIM or PLUS quoted.

Channel of investment

2.47 There was strong support for the Government's proposal to allow investment through a variety of investment vehicles, including offshore companies and trusts.

Form of investment

2.48 Some respondents sought clarification on whether it would be possible to take out a loan to invest in a qualifying company before 6 April 2012 and subsequently remit overseas income or gains after 6 April 2012 to repay the loan without creating a taxable remittance. It was argued that this would effectively allow non-domiciles to make use of the relief sooner than April 2012 and this would enhance the policy.

Government response

2.49 The Government agrees that, in principle, there is a case for allowing non-domiciled investors to repay loans taken out prior to 6 April 2012 to invest in a qualifying company in the way proposed. However, it believes that doing so would add undue complexity to the legislation. In addition, because the draft legislation for the business investment relief will not be finalised before April 2012, making investments before then would entail risk for potential investors and the Government believes it is unlikely that it would generate a material amount of additional investment in that period. The Government therefore does not intend to take forward this proposal.

2.50 The legislation will allow investment in the form of money or any other property, whatever the underlying overseas income and gains.

UK businesses

2.51 A small number of respondents felt that the proposal to restrict relief to UK companies or overseas companies with a UK permanent establishment (PE) was unnecessary and appeared intended to prevent abuse that should be dealt with by specific rules. A concern was raised that the requirement for a UK PE could result in inadvertent taxable remittances by investors who were unsure whether a company met this condition.

Government response

2.52 The Government agrees that restricting investment to non-UK resident companies with a UK PE is not necessary and has decided not to include this restriction. As there is generally no need to remit overseas income and gains to the UK to invest in a non-UK business, the Government believes the business relief will primarily encourage non-domiciles to remit overseas income and gains to the UK for investment in UK business.

Companies holding shares in other companies

2.53 Further information on the tests to be applied to holding companies was requested, including the extent to which the holding company would be allowed to carry on its own business and how the qualification of the holding company would be assessed.

Government response

2.54 The Government does not intend to widen the relief for holding companies beyond the proposal set out in the consultation document. However, as confirmed at paragraph 2.52 above, the Government considers that the requirement for a UK PE is unnecessary and so this will not be a qualifying condition for investment in a holding company.

2.55 Holding companies will be eligible for relief where they exist wholly for the purpose of making investments in companies which carry on qualifying activities (see paragraphs 2.20 and 2.21). However, the Government recognises that it would be too restrictive to require that the activities of a holding company consist entirely of the holding of shares in qualifying companies, so minor or incidental activities of the holding company will be disregarded when determining whether an investment in a holding company qualifies for relief.

Size of investment

2.56 Respondents fully supported the absence of any restrictions on the size of investment permitted in a tax year.

Anti-avoidance

Box 2.C: Question 3

Are the proposed anti-avoidance provisions suitable? Would it be appropriate to require remitted income or capital gains to be taken out of the UK or reinvested within two weeks of the disposal of the investment?

Taking disposal proceeds out of the UK

2.57 The consultation proposed a requirement for overseas income or gains remitted for investment in a qualifying business either to be taken out of the UK or reinvested in another

qualifying business when an individual disposes of the investment. This was broadly seen as an appropriate measure.

2.58 However, a majority of respondents thought that the proposed time limit of two weeks was too short, failing to take into account the commercial realities of investment disposals and the sometimes complex affairs of investors. There was no consensus on, or clear argument for, any specific alternative time limit, but suggestions ranged from 30 days to 6 months.

2.59 It was suggested that there should be flexibility for HMRC to take into account exceptional circumstances that would prevent an individual meeting the time limit, for example, due to a bank's failure to comply with instructions or serious illness of an investor.

2.60 The policy defines the time limit with reference to receipt of the proceeds generated by the disposal of the investment. A number of respondents sought clarification of the meaning of "receipt" and suggested that the time limit should commence at the date funds are unconditionally available to the investor. This may not immediately follow the disposal of an investment if, for example, funds are paid into escrow.

2.61 Clarification was requested on what precisely would be required to be exported, and whether the requirement for export or reinvestment would apply to any gains arising that were chargeable to capital gains tax (CGT).

2.62 Clarification was also requested on how the rules on disposals would interact with the mixed funds rules and other remittance basis rules. A small number of responses raised concerns around the possible complexity in identifying whether the sources of a remittance were income, gains or capital, either where the proceeds were retained in the UK and became a taxable remittance, or where a loss arose.

2.63 Questions were raised about how any CGT due on the disposal of an investment would be paid if a vendor had insufficient other UK-source funds available and whether any funds remitted to pay the tax would be liable to a UK tax charge. It was suggested that the rules should be relaxed in such circumstances, allowing an individual to retain in the UK an amount equal to the tax charge without this constituting a taxable remittance.

2.64 A small number of respondents suggested that there should be a minimum period of investment after which the original remittance should be considered to have become clean capital and the requirement to remove or reinvest the proceeds on disposal should be dropped. The suggested period of investment required ranged from three to seven years.

Government response

2.65 The Government accepts that the two-week limit is too short. It therefore proposes to amend the time limit to 45 days and believes that this higher limit will strike an acceptable balance between recognising the commercial reality of disposing of an investment and ensuring that HMRC can track money from disposals where necessary for compliance purposes.

2.66 The Government recognises that there may be circumstances beyond the control of an investor that will prevent them reinvesting or exporting any proceeds within this time limit. The draft legislation therefore contains a provision to allow HMRC to extend the grace period where exceptional circumstances mean it would be unreasonable for an investor to reinvest or export the proceeds within 45 days.

2.67 The Government confirms the following points relating to disposals:

- The time limit will apply from the point at which the funds are unconditionally available to the individual.

- The 45 days for reinvestment or export of any proceeds will be in addition to the 45-day time limit for the disposal of an investment where a company no longer qualifies for relief (paragraph 2.23 refers).
- As outlined in the consultation, the Government will require that the overseas income or gains used to fund the qualifying investment is identified with the first amount of value taken out of the business until the total amount invested has been matched. This means that, in general, the investor will not be required to take chargeable gains which arise on disposal out of the UK in order to benefit from the relief. However, if an investor disposes of part of their investment, it may be necessary for them to take the gain arising on that part disposal out of the UK, or to reinvest it in a qualifying business, to meet this requirement.
- In situations where an investor disposes of a qualifying investment but retains all or part of the proceeds in the UK beyond the permitted time limit, the amount which will become liable to tax as a remittance of overseas income and gains will be determined by the existing rules for mixed funds and offshore transfers. Where only part of the proceeds is retained in the UK after a disposal, those existing rules would apply only to that part of the proceeds remaining in the UK and taxed accordingly.
- The Government intends that all qualifying investments into, or out of, an eligible company will be treated as an offshore transfer rather than a payment under a mixed fund. The effect of this will be to treat the money used to make the investment, and funds received from the investment, as containing the same proportion of income, gains and capital as was in the overseas account immediately before the investment was made.

2.68 As described above, in many cases investors will be able to retain a capital gain arising from the disposal of their investment in the UK and there will therefore be no difficulty in meeting the CGT due on that gain. However, the Government recognises that this will not be the case in all circumstances, for example where they make a part disposal, and is giving further consideration to including provisions to enable an individual who disposes of a qualifying investment to meet the CGT due on a gain from the investment without there being a taxable remittance. The Government intends to include legislation to this effect in Finance Bill 2012 and will aim to make draft legislation available for comment early in 2012.

2.69 The Government considers that allowing overseas income and gains remitted for a qualifying investment to become clean capital after a specified period of time would have a material Exchequer cost and does not intend to take forward this proposal.

Personal benefit

2.70 There was clear recognition of the need for a rule to prevent an investor deriving a personal benefit from a qualifying investment.

2.71 As set out in paragraph 2.30, many respondents felt that such a rule should be used to address the risk of avoidance from investments in businesses involved in residential property, the leasing of tangible, moveable property, or the provision of personal services.

2.72 Clarification was also sought on what types of benefit or payments would be targeted by this rule and whether it would apply to benefits provided on commercial terms.

Government response

2.73 The Government reiterates that it is critical to ensure that the policy is not used for tax avoidance or to provide a personal benefit for the investor. The legislation will include two rules

to prevent the value of an investment leaking from a company to an investor either directly or indirectly. These will apply if:

- the invested company provides a personal benefit to the investor or a relevant person on terms which are not arms length or commercial. This rule will apply if any portion of the business, however small, provides such a benefit; or
- the investment is made as part of a scheme or arrangement where the purpose, or one of the main purposes, is the avoidance of tax.

2.74 An investor who breaches either of these rules will be required to take the full amount of overseas income and gains invested, and any proceeds, out of the UK or to reinvest them in a qualifying company.

2.75 The Government confirms that this will not prevent an individual or relevant person from receiving a commercial salary, other commercial remuneration, dividends, interest or other income in respect of their rights as a shareholder or lender, provided UK tax is paid on such payments. The Government does not intend to prevent the provision of benefits on arm's length or commercial terms.

2.76 The Government believes that these provisions will prevent abuse but ensure that the relief is as widely drawn as possible to encourage significant inward investment.

Claiming the relief

Box 2.D: Question 4

Would a mandatory requirement to claim the relief for business investment on a Self Assessment tax return be an appropriate way of monitoring the policy? If not, what alternative monitoring approach would be appropriate?

2.77 Many respondents commented on the proposal that an individual should be required to make a claim for this new relief on their Self Assessment (SA) tax return. A significant majority thought that such an approach would be an appropriate way to monitor the policy. A small number felt that making a claim would be inappropriate or unnecessary, and that the requirement to report non-taxable remittances would be a departure from current practice.

2.78 Clarification was requested on how individuals who were not otherwise required to make a SA return would make any claim to relief.

2.79 A small number of respondents thought that the proposed requirement for an individual to state whether they had remitted income or capital gains to the UK for investment would be unnecessarily onerous and could discourage individuals from using the relief to invest in the UK. It was suggested that the individual should only be required to identify the total amount invested.

2.80 A number of respondents highlighted the potentially significant consequences for any individual who remitted substantial sums of overseas income and gains to the UK for an investment that was subsequently found not to qualify for relief. It was felt that to help mitigate these concerns, and encourage investment, HMRC should introduce a voluntary pre-investment clearance procedure to provide investors with certainty that an investment would qualify.

Government response

2.81 The Government confirms that it will introduce a requirement that any non-domicile wishing to use this relief should make a claim on a SA tax return. This will include individuals

who would not otherwise have to complete a return. However, the Government believes that in the vast majority of cases the individual will in any case be claiming the remittance basis in the year of investment. Claimants will be required to state:

- whether they have remitted overseas income and gains to the UK for investment in a qualifying company;
- how much has been invested in total (but without a requirement to show the constituent elements of the funds invested); and
- the names of the companies in which they have invested.

This information will help the Government to monitor the effectiveness of the relief.

2.82 The Government agrees it would be beneficial to provide a voluntary pre-clearance procedure to provide investors with certainty that an investment will qualify for relief before they remit overseas income and gains to the UK. HMRC is exploring how a pre-clearance procedure might be structured.

Effectiveness of the policy

Box 2.E: Question 5

Would the policy as outlined be an effective means of encouraging investment in the UK?

2.83 A significant number of respondents felt that the relief would be an effective means of encouraging non-domiciles to invest in the UK, subject to removing or amending some of the restrictions and increasing the time limit for export or reinvestment of any proceeds.

Other issues raised during the consultation

2.84 A number of respondents sought clarification on whether the relief would:

- be available to individuals who were taxed on the arising basis in a given tax year but wished to invest overseas income or gains in that year which had arisen under the remittance basis in previous years;
- be available to long-term UK resident non-domiciles who become temporarily non-resident;
- require a qualifying investment to be transferred directly from a non-domicile's offshore bank account to the bank account of the recipient company;
- affect entitlement to other UK tax reliefs, such as the Enterprise Investment Scheme (EIS) and Venture Capital Trust (VCT);

2.85 A small number of respondents raised concerns about the compliance of the proposals with EU law and whether they complied with State Aid rules. It was felt that any lack of certainty on this aspect could result in individuals being reluctant to bring overseas income and gains to the UK to invest as the possible consequences of the relief being withdrawn at a later date would be significant.

Government response

2.86 The Government confirms that relief will apply to a qualifying investment using overseas income and gains that arose in any year in which the non-domiciled individual claimed the

remittance basis, regardless of their basis of taxation in the year the qualifying investment is made.

2.87 Individuals covered by the rule for temporary non-residents will be able to use the investment relief in the same way as other remittance basis taxpayers.

2.88 The Government will not require a qualifying investment to be transferred directly from a non-domicile's offshore bank account to the bank account of a recipient company. Overseas income and gains may be brought to the UK up to 45 days in advance of making a qualifying investment and will not be treated as a remittance. Any bank interest arising on the funds when they are in the UK prior to investment will be taxable in the UK in the normal way.

2.89 A claim to relief under this incentive will not affect entitlement to other UK reliefs. An individual who brings overseas income and gains to the UK to invest under this relief will still be able to claim other tax reliefs, such as EIS or VCT, if the conditions for such reliefs are met.

2.90 The Government is satisfied that the draft legislation to be published in Finance Bill 2012 is compatible with EU law and the State Aid rules.

Philanthropy

2.91 A number of responses from the arts and charity sectors suggested that the business investment relief should be extended to allow non-domiciles to bring overseas income and gains to the UK tax-free for the purpose of making donations to, or investments in, UK charities.

Government response

2.92 The Government is committed to encouraging philanthropy. However, there are already tax-efficient ways for non-domiciles to make donations to UK charities and the Government has not seen any compelling evidence that extending the business investment relief in the way suggested would lead to a significant increase in the level of donations to UK charities by non-domiciles. It is also very likely that complicated legislation and anti-avoidance provisions would be required. The Government therefore does not intend to take any further action on this issue at the present time but it will consider how to increase awareness of ways for non-domiciles to make tax-efficient donations under the existing rules.

Simplifying the existing remittance basis rules

Box 2.F: Question 6

(a) Do you think the proposed solution for each simplification would be effective?

(b) Can you propose other ways in which the remittance basis rules could be simplified, provided they meet the principles described in paragraph 2.63 (of the consultation document)?

Nominated income

2.93 The proposal to simplify the nominated income rules was widely welcomed.

2.94 There were some suggestions for modifying the proposal. In particular, a small number of respondents felt that the proposed limit of £10 was too low and should be raised.

2.95 Some also requested that the change be backdated to 6 April 2008 on the grounds that this would provide a further administrative simplification with little or no Exchequer cost.

2.96 A number of respondents commented on the overall complexity of the nominated income rules and suggested that either all the nominated income legislation or the identification rules that apply when nominated income is remitted to the UK should be removed.

Government response

2.97 The Government will proceed with the proposal as outlined in the consultation document. Its purpose is to enable an individual to nominate a small amount of their overseas income or gains without becoming subject to the complex identification rules and the individual can determine how much income they nominate. There would therefore be no practical effect in increasing the limit from £10.

2.98 The Government has considered the possibility of backdating the change to 2008 but concluded that it would not be appropriate to do so because it would not be to the benefit of the taxpayer in all circumstances.

2.99 The Government sees no case for more fundamental simplification of the nominated income rules. The identification rules ensure that non-domiciles cannot gain a tax advantage by remitting their nominated income or capital gains to the UK before other income and capital gains on which they would be taxed. Removing the nominated income rules would call into question the creditability of the RBC for US tax purposes. Therefore, wider simplification of these rules would carry an unacceptable risk.

Foreign Currency Bank Accounts (FCBAs)

2.100 There was widespread support for the proposal to remove all sums within FCBAs from the scope of CGT. Respondents viewed it as offering a significant simplification for those who use bank accounts held in a foreign currency. However, a clear majority felt that the proposal should be extended to accounts held by offshore trusts. Some also suggested the exemption should apply to accounts held by companies and partnerships. Many requested that the change be backdated to April 2008 or, if that was not possible, to April 2010.

2.101 A small number of respondents requested that consideration should be given to extending the definition of a foreign currency bank account to include investments in constant NAV money market or liquidity mutual funds.

Government response

2.102 The Government notes the evidence that the complexity of the current rules causes significant difficulties for trusts as well as individuals and accepts this argument. It will therefore extend the policy to bank accounts held by trustees of settled property and personal representatives of deceased persons. However, it is not necessary for partnerships to be specifically included in the exemption because partnerships are not liable to CGT and individual partners are treated as holding a part share in the partnership bank account. There is no need to include companies in the exemption because companies' returns from FCBAs are not liable to tax on capital gains.

2.103 The exemption will be confined to bank accounts. The Government believes investment funds and other similar vehicles should remain within the charge to CGT and is concerned that exempting them would carry avoidance risks.

2.104 The Government understands the desire to backdate the change to tax years prior to 2012-13. However, it has concluded that it would not be appropriate to do so because it would prevent taxpayers using capital losses that might have arisen from foreign currency transactions to offset against chargeable gains on other disposals. It would, therefore, not be to the benefit of all taxpayers.

2.105 The Government no longer considers that new anti-avoidance measures will be needed to prevent abuse of this exemption.

Taxation of assets sold in the UK

Box 2.G: Question 7

Would two weeks be a suitable period of time before which the proceeds of the sale of an exempt asset should be taken out of the UK?

2.106 There was a significant response on this proposal and universal support for the objective of encouraging sales of assets in the UK.

2.107 There were a variety of comments on the proposed requirement for proceeds of a sale to be taken out of the UK within two weeks:

- A clear majority of those who commented felt that the two-week time limit was too short. Proposals for a longer time limit were made, ranging from four weeks to three months.
- It was also proposed that the amount required to be taken offshore should only be the net amount received after deduction of any associated costs of sale, such as auctioneer's fees.
- Payments for expensive items sold through auction houses or the art markets are often staggered over a period of time e.g. at 30, 60 and 90 days from the date of sale. A number of respondents suggested that the time limit for taking proceeds offshore should be from the date proceeds were unconditionally received rather than the date of sale and that the time limit for taking proceeds offshore should apply separately to each instalment.

2.108 Some respondents also felt that the current rules that enable assets purchased with overseas income or gains to be temporarily imported to the UK for 275 days without incurring a charge as a taxable remittance were too short. It was suggested that this limit should be extended to two years in cases where the asset had been brought to the UK to be sold rather than used for other purposes.

2.109 A significant majority of those that commented on this proposal felt that it would fail to achieve its objective unless the charge to CGT on any gain realised on the sale of an exempt asset was also removed.

2.110 Other suggestions made by respondents included:

- extending the relief to allow the proceeds of a sale to be used to purchase other works of art in the UK;
- allowing relief for exempt assets that are lost, stolen or destroyed, subject to the condition that any insurance money received is also removed offshore within the specified time limit;
- allowing proceeds arising from the sale of an exempt asset to be directly invested in a qualifying company under the new business investment relief without triggering a charge to tax as a remittance; and
- making pre-eminent objects and works of art gifted to the nation exempt assets when remitted to the UK.

2.111 A number of respondents stated that paragraph 2.85 of the consultation document was unclear and requested clarification that there would be no requirement for any asset that had been sold to be retained in the UK by the purchaser in order to qualify for the relief.

Government response

2.112 The Government accepts that the proposed time limit for taking sale proceeds out of the UK is too short and will therefore increase this limit to 45 days.

2.113 It also confirms a number of other aspects of the policy:

- The time limit for taking proceeds out of the UK will only apply from the date on which the proceeds of sale are unconditionally available to the individual.
- All proceeds of sale, whether in a single payment or in instalments, must be paid to the vendor within 95 days of the date on which the sale takes place.
- In cases where proceeds are paid in instalments, the 45-day limit will only apply from the date on which the final instalment is received.
- Individuals will only be required to take out of the UK the sale proceeds less any legitimate costs incurred by the vendor in making the sale.
- The exemption will be available to all "relevant persons" who remit and sell exempt assets in the UK.
- It will be possible for the proceeds of selling an exempt asset to be reinvested directly in a qualifying UK business without a requirement for the proceeds to be taken out of the UK before reinvesting. It will also be possible to invest part of the proceeds directly in a qualifying business provided the remainder of the proceeds are taken out of the UK within the time limit.

2.114 The Government accepts that the effectiveness of the policy would be significantly enhanced by a corresponding relaxation of the charge to CGT on any gain realised on the sale. It will therefore introduce legislation in Finance Bill 2012 to treat such gains as foreign chargeable gains which will be subject to the remittance basis and so, in general, only liable to UK tax if they are subsequently remitted to the UK. Draft legislation on this aspect will be made available for comment early in 2012.

2.115 The Government considers that the existing 275-day limit for temporary import of assets is sufficient and will not extend it.

2.116 Other than the changes outlined in paragraphs 2.112 to 2.114 the Government will implement the policy as outlined in the consultation document.

2.117 The Government will undertake further work to consider whether the existing legislation on exempt assets can be extended to cover situations in which assets are lost, stolen or destroyed. It will also consider whether there are other aspects of the exempt asset rules that can be simplified. If it decides to proceed, legislation will be included in Finance Bill 2013 to take effect from April 2013.

2.118 The donation of pre-eminent objects was the subject of a separate consultation. The Government is publishing its response to that consultation on 6 December and this confirms that objects brought to the UK for donation under that policy will not constitute a taxable remittance if purchased out of overseas income or capital gains.

2.119 The Government confirms that there is no requirement for an asset that has been sold to be retained in the UK by the purchaser in order for the individual to qualify for the relief.

Statement of Practice 1/09 – employees with duties in the UK and overseas

Box 2.H: Question 8

Should the situations outlined in paragraphs 2.98 to 2.101 (of the consultation document) fall within the new statutory treatment for employees who are not ordinarily resident and carry out duties in the UK and overseas? Are there any other situations which are not covered by SP1/09 and might require legislative provision?

2.120 The proposal to place SP1/09 on a statutory footing was broadly welcomed, as it is widely used by expatriate employers and employees to reduce the complexity and administrative burden of applying the mixed fund rules to earnings.

2.121 A number of responses suggested that the circumstances in which the simplified treatment offered by SP1/09 is available should be widened to allow:

- joint accounts with a spouse, where the spouse makes no economic addition to the account;
- accounts containing pre-existing funds or where receipts from more than one employment are paid in;
- genuine errors where amounts are inadvertently paid into SP1/09 accounts, possibly subject to a requirement that the payments are either below a specified limit or transferred out of the account within a certain period of time; and
- a change of employer without the requirement to open a new SP1/09 account.

2.122 Some respondents felt that the wider reform of non-domicile taxation provided an opportunity for more major changes to remove administrative burdens and simplify the relief.

2.123 The consultation document sought views on whether the simplified legislative treatment should apply in two specific circumstances:

Employee becomes not UK resident part way through a tax year and continues to deposit money into a bank account

2.124 Most respondents felt that the simplified treatment should be applied to such accounts. Some concerns were raised over the interaction of SP1/09 with the conditions for split year treatment on departure contained in the proposed statutory residence test.

Employee holds bank accounts containing employee share scheme transactions in respect of non-UK situs assets

2.125 In general, responses indicated that the simplified treatment should continue to apply in such circumstances on the grounds that many employees have little control over which account employers will pay such transactions into. Respondents also suggested that excluding such transactions could be administratively burdensome for employers, for example if they automatically make such payments into the same account as an employee's salary as part of the payroll process.

Government response

2.126 The Government notes the various suggestions and concerns raised, and agrees that it is important to ensure that the legislation does not depart significantly from the way in which SP1/09 currently works. It will therefore give further consideration to these issues and take forward legislation of SP1/09 in Finance Bill 2013 to take effect from April 2013. This will have

the further advantage of tying in with the implementation of legislation on ordinary residence which the Government has announced separately will be effective from April 2013. The Government confirms that SP1/09 will continue for the 2012/13 tax year.

Other simplifications

2.127 The Government received a number of proposals for other simplifications to the remittance basis rules. Some of these proposals failed to meet the principles outlined in paragraph 2.63 of the consultation document and the Government does not agree that they should be pursued. In particular, the Government will not look further at the following:

Table 2.A: Examples of simplifications which will not be taken forward

Simplification	Government response
Reviewing and simplifying the mixed fund rules	Although the Government appreciates that these rules can be complicated to operate, it is essential to be able to identify different types of income, gains and capital as they are remitted from a single account. The Government cannot envisage an alternative approach to achieve this purpose which would not entail similar complexity or a significant Exchequer cost.
Definition of a remittance and the derivation rules	The Government recognises that the definition of a taxable remittance is widely defined but believes any change to narrow the rules would open up opportunities for abuse and an unacceptable risk to the Exchequer.
Increasing the £2,000 de minimis limit to align with the income tax personal allowance	The Government considers that this would be likely to have a material Exchequer cost. It would also restore the income tax personal allowance and CGT Annual Exempt Amount (AEA) to some individuals with a significant level of income or capital gains and the Government does not think that this can be justified.

2.128 However, the Government does accept that there is value in giving further consideration to the following suggestions:

- Excluding minor grandchildren from the definition of a 'relevant person'; and
- Removing the charge to tax on inadvertent remittances.

2.129 The Government will undertake further evaluation of these areas with a view to implementing any changes from April 2013. This will be done alongside the further consideration of the exempt assets rules described in paragraph 2.117. The Government will only proceed with changes if it is satisfied that there is no risk to the Exchequer.

3 Summary and next steps

3.1 The Government will introduce legislation in Finance Bill 2012 on the proposals described in paragraph 1.3 and including the changes outlined in this document. Draft legislation has been published on 6 December for a period of consultation which will close on Friday 10 February. The draft legislation can be found at http://www.hm-treasury.gov.uk/finance_bill_2012_consultation.htm and includes Explanatory Notes and Tax Information and Impact Notes (TIINs). Comments on the draft legislation should be sent to offshorepersonal.taxteam@hmrc.gsi.gov.uk and copied to non-doms@hmtreasury.gsi.gov.uk.

3.2 Following consultation on the draft legislation the Government will publish final legislation in Finance Bill 2012 shortly after Budget, and it will then be subject to parliamentary scrutiny in the normal way.

3.3 There are elements of the legislation on business investment and assets sold in the UK which will be included in Finance Bill 2012 but for which draft legislation will not be available on 6 December. However, the Government will seek to publish draft legislation on these elements early in 2012 to allow a period of scrutiny before final legislation is published. These are:

- Encouraging business investment: legislation to enable an individual disposing of a qualifying investment to meet the CGT due on a gain from the investment without this constituting a taxable remittance (described in paragraph 2.68);
- Assets sold in the UK: legislation to relax the charge to CGT on any gain realised on the sale of an exempt asset (described in paragraph 2.114).

3.4 The Government will take forward legislation of Statement of Practice 1/09 in Finance Bill 2013.

3.5 The Government will give further consideration to the following issues with a view to possible legislation in Finance Bill 2013:

- Extending the business investment relief to partnerships;
- Further simplifications to the remittance basis rules:
    - Exempt asset rules in general;
    - Exempt assets that are lost, stolen or destroyed;
    - Excluding minor grandchildren from the ‘relevant person’ definition;
    - Removing the charge to tax on inadvertent remittances.

3.6 As a result, the policy measures announced at Budget 2011 will be implemented in a two-stage process that will be completed in Finance Bill 2013. There will not be a rolling programme of further changes.

3.7 The main changes and clarifications which the Government will make to its proposals in Finance Bill 2012 following consultation are summarised below.

Encouraging business investment

- There will be no general exclusion for residential property or leasing. However, there will be anti-avoidance rules to disqualify investment in any company where the investor or another relevant person derives a personal benefit on non-commercial terms or where the investment is made as part of an arrangement whose purpose is the avoidance of tax.
- The Government will require all, or substantially all, of the company's activities to be qualifying activities. Non-qualifying activities should constitute no more than 20% of the company's activities.
- Companies undertaking Research and Development (R&D) will be treated as carrying on a commercial trade and will be eligible for relief.
- The relief will be confined to companies which are unlisted or are quoted on an exchange-regulated market such as AIM or PLUS quoted.
- There will be no requirement for a qualifying company to be UK resident or to have a UK Permanent Establishment.
- The time limit for the proceeds generated on disposal of an investment to be taken out of the UK or reinvested will be increased from two weeks to 45 days from the date that the investor has unconditional access to the funds.
- Investors will be allowed a period of 45 days to dispose of their investment if the company in which they invest ceases to meet the qualifying conditions for the relief. In addition to this they will have 45 days to take the proceeds of disposal out of the UK or to reinvest them, as described in the point above.
- There will be provisions to enable an individual disposing of a qualifying investment to meet the CGT due on a gain from the investment without this constituting a taxable remittance.

Simplifying the remittance basis rules

Foreign currency bank accounts (FCBAs)

- The exemption for FCBAs will be extended to trustees of settled property and personal representatives of deceased persons.
- There will not be any specific anti-avoidance provisions.

Taxation of assets sold in the UK

- The time limit for taking proceeds of sale out of the UK will be extended to 45 days.
- As an alternative, vendors will be allowed to invest the sale proceeds in a qualifying business without a requirement to take the funds out of the UK.
- The charge to CGT on any gain realised on the sale of an exempt asset will be relaxed and the gain will be treated as a foreign chargeable gain.

A List of respondents

A.1 The Government would like to thank all organisations and individuals who responded to this consultation. Responses were received from 11 individuals and from the following 72 organisations

Association of Chartered Certified Accountants
Arts Council England
Association of Private Client Investment Managers and Stockbrokers
Association of Taxation Technicians
Baker Tilly
Baltic Exchange
Barclays Wealth
BBA
BDO LLP
Berkeley Law
Berwin Leighton Paisner LLP
Bircham Dyson Bell LLP
Boodle Hatfield
British American Business
British Art Market Federation
Buzzacott LLP
British Private Equity & Venture Capital Association (BVCA)
Caldwell and Braham
Confederation of British Industry
Charles Russell LLP
Charter Tax Consulting Ltd
Chartered Institute of Taxation
City of London Law Society
Commercial Estates Group (CEG)
Council of British Chambers of Commerce in Europe
Coutts (Tax, Trust & Estate Planning)
Crowe Clark Whitehill LLP
Deloitte LLP
Ernst & Young LLP
Fladgate LLP
Frank Hirth Plc
Grant Thornton LLP
Harwood Hutton Ltd
Institute of Chartered Accountants in England and Wales
Institute of Chartered Accountants of Scotland
IK Investment Partners
Ince & Co LLP
Institute for Philanthropy
Institute of Economic Affairs
Investment Management Association
J P Morgan
James Cowper LLP

KPMG LLP
Kreston UK
Linklaters LLP
Law Society of England and Wales
London Society of Chartered Accountants
Low Incomes Tax Reform Group
Maritime London
London Maritime Arbitrators Association
Maritime UK
Maurice Turnor Gardner LLP
Mazars LLP
Mishcon de Reya
Moore Stephens LLP
National Farmers Union
National Museums
New Quadrant Partners LLP
PWC LLP
Quoted Companies Alliance
Rawlinson and Hunter
Royal National Theatre
Royal Opera House
RSM Tenon
Sotheby's
South Bank Centre
Society of Trust and Estate Practitioners
Stonehage Law Ltd
Tate
Taxaid
TUC
White & Case LLP

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This document can be found in full on our website: http://www.hm-treasury.gov.uk

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