Practical Tax People
Association of Taxation Technicians

IMPLEMENTING A CAPITAL GAINS TAX CHARGE ON NON-RESIDENTS

Response by the Association of Taxation Technicians

1 Introduction

1.1 The Association of Taxation Technicians (ATT) is pleased to have the opportunity to respond to the consultation document *Implementing a capital gains tax charge on non-residents* ('the Consultation') published jointly by the Treasury (HMT) and HMRC on 28 March 2014.

1.2 We understand that the Consultation is designed to give an opportunity for interested stakeholders to provide input into how the new tax charge will operate on non-residents from April 2015, including the proposed changes to the main residence election rules that currently exist for individuals to elect between two or more residences as to which one will attract Private Residence Relief ("PRR").

We provide answers to the questions raised in the Consultation in section 2 below. Where appropriate, we reply to linked questions at the same time.

2 Our responses to the questions

2.1 **Question 1: Would an exclusion of communal property from the scope of the new regime result in any unintended consequences?**

We have not identified any unintended consequences of an exclusion of communal property. However, there are aspects of the definition of 'communal property' that require careful consideration.

We note that Box 2.A on page 8 of the Consultation includes a summarised exclusion from the proposals for:

"Accommodation for children and students: use as a home or other institution providing residential accommodation for children; residential accommodation for school pupils; or as a hall of residence for students in further or higher education".

Modern newly built (or newly converted) student accommodation tends to be very different in style and living arrangement to what is traditionally thought of as 'halls of residence'. Modern student accommodation typically comprises clusters of individual 'pods' with a range of

communal facilities for each cluster. The various communal facilities associated with a traditional hall of residence are notably absent.

We understand that many of the modern style student units (as described) are constructed or converted using private funding and then privately operated. This has the beneficial effect of increasing the UK's available housing stock without involving public expense. In order not to discourage investment by non-residents in such student accommodation, this type of accommodation should also be clearly included in the exclusion.

Detailed consideration will need to be given to what constitutes a student. If the university or institution is involved in the allocation of accommodation, that presents no obvious difficulty. Where, however, there is no such involvement (or only very limited involvement), there needs to be a clear and simple test which the landlord can apply. We suggest that this should essentially require the landlord to satisfy themselves at the beginning of each letting period (which we understand is typically around 50 weeks) that the relevant individual is enrolled on a relevant course with a relevant institution. The provision of appropriate standardised certification by the institution to the landlord would constitute evidence of compliance with the test. Such a test would avoid the complications that might otherwise arise from a student dropping out or continuing to live in the accommodation after the completion of their course.

We would envisage a clear distinction being made in the definition of student accommodation so that it included the types of unit referred to above but not houses in multiple occupation that just happen to be occupied by students.

2.2 **Question 2: Are there any other types of communal residential property that should be excluded from scope?**

We believe that box 2.A on page 8 of the Consultation does cover most groups that ought to be excluded from the charge.

We assume that the term 'other communal accommodation' in the third bullet would encompass accommodation for members of religious communities.

2.3 **Question 3: Are there any particular circumstances where including non-resident partners in the scope of the charge might lead to unintended consequences?**

We have not identified any particular unintended consequences from including non-resident partners within the scope of the charge but, more broadly, we think that specific attention will be required to the operation of the proposals in the following circumstances:

- Individual who had incurred a capital loss on the disposal of any asset prior to becoming non-resident - presumably those losses will be available for offset against the proposed charge on the individual?

- Non-resident Individual who had incurred a capital loss on the disposal of an asset that was subject to CGT under section 10, TCGA 1982 – presumably such a loss will be available for offset against a gain arising in the same or any subsequent year under the proposed charge?

- Non-resident Individual who had prior to 6 April 2015 incurred capital losses on the disposal of residential property that would, if disposed of after that date, have been within the scope of the proposed charge – will those losses be available to set against a charge subsequently arising under the new proposals?

2.4 **Question 4: Are there any particular circumstances where including non-resident trustees in the scope of the charge might lead to unintended consequences?**

At the first of the working group meetings, there was discussion about the inter-relationship of the proposed charge with relief under section 225 of TCGA (private residence occupied under terms of settlement). The common view was that the availability of s.225 relief should be determined by reference to the residence status of the occupying beneficiary. Therefore, it would follow that a claim for private residence relief would be available in respect of a gain chargeable under the new proposal on a non-resident trust in relation to its UK residential property where that property was occupied by a UK-resident beneficiary under the terms of the trust.

More generally, HMT and HMRC need to consider the interaction of this new charge with existing sections of legislation and carefully word the legislation for the new charge so that it dove-tails and does not create anomalies or inconsistences. We draw particular attention to the interaction of the new provisions with:

- Section 86 and 87 of TCGA 1992 where the new charge should take precedence, but the above two sections of legislation may require amendment so as to avoid a double tax charge;

- ATED-related gains – please see our comments in section 2.6 below.

2.5 **Question 5: Is a genuine diversity of ownership ("GDO") test an appropriate way to identify funds that should be excluded from the extended CGT regime, and to ensure that small groups of connected people cannot use offshore fund structures to avoid the charge?**

Question 6: Are there any practical difficulties in implementing a GDO test?

Question 7: Is there a need for a further test in addition to a GDO? If so, what would this look like and how would it be policed?

This is not an area upon which we are able to comment.

2.6 **Question 8: What are the likely impacts of charging gains (and allowing losses) incurred on disposals of residential property by non-residential property companies that are not already operating a trade in the UK?**

Question 9: Are there other approaches that you believe would be more appropriate to ensure that non-resident property investment and rental companies are subject to UK tax on the gains that they make on disposals of UK residential property?

We are assuming that the phrase 'non-residential property companies' (in question 8) should actually read 'non-*resident* property companies'.

We are concerned that the Government is considering imposing a charge on non-resident companies owning residential property at the same time as keeping ATED-related CGT charges, for potentially the same properties. This will create double tax charges and much confusion. Except in relation to any pre-April 2015 element of gain, we do not see why an ATED-related CGT charge needs to remain for residential properties that will from 1 April 2015 be within the scope of the new charge.

We would urge HMRC and HMT to put the case to Ministers that to have both systems operating and imposing charges on the same properties would create a very complicated tax system which the relevant taxpayers would struggle to understand and advisers would struggle to explain to clients.

At the very least, we think that consideration should be given to amalgamating the return forms for both the new CGT charge and the ATED-related gain charge so that taxpayers do not have to complete multiple tax forms for the different charges relating to a single transaction. However, this should be considered a last resort solution, with the first aim being to remove ATED-related gain charges on UK residential properties held by non-resident companies.

2.7 **Question 10: Are there any particular circumstances where changing the PRR election rules might lead to unintended consequences?**

We envisage many and varied circumstances in which changing the PRR election rules will lead to unintended consequences. However, until details of the new rules are published, it is impossible to identify these with any precision. Our comments below are necessarily of a somewhat general nature.

We strongly believe that there should be ongoing recognition after 5 April 2015 of all elections that are already in place as at that date. We think it would be possible to structure the legislation so that an election could only now be made in respect of a property that was already potentially within the charge to CGT. Prior to 6 April 2015 (in the case of an individual or trust) that would only be the case where the property owner was UK-resident. Such a measure would accordingly avoid any retrospective charge arising on a UK-resident who had

made a valid election before 6 April 2015 at the same time as preventing a circumvention of the new charge by non-residents.

Even if all existing elections were to become ineffective from 6 April 2015 with the new rules applying for periods of ownership subsequent to that date (which we would certainly not favour), we think that it would be much simpler from an administrative perspective if all such existing valid elections remained conclusive for periods prior to 6 April 2015.

As between a time apportionment calculation and rebasing, our strong preference would be for rebasing as at 6 April 2015. That would ensure that it really was the post 5 April 2015 gain that was being brought into charge under the new provisions. We think that a rebased starting value of 1/6 April 2015 would work equally appropriately in relation to:

- Non-resident owners coming into charge from that date;
- Resident owners who had not made an election between multiple properties so that any change in the determining factors introduced by the new proposals or by any change in circumstances would only apply going forward from that date. (If there were no such changes, there would be no requirement to obtain a rebasing value);
- Resident owners who had made an election before 5 April 2015 if (which we would not favour) all elections ceased to have effect at that date.

We think that rebasing could reduce the complexity of calculations very considerably. It also has the merit of avoiding what under time-apportionment could amount either to a retrospective tax charge or the granting of an arbitrarily generous relief.

As the new rules are set to be introduced from 6 April 2015, we think that timely decisions regarding transitional arrangements need to be taken as a matter of urgency by HMT and HMRC in order to give people affected by the change in the PRR election rules sufficient notice and an opportunity to obtain valuations of their residences, if required.

We foresee potential problems with how to determine which property is the main residence when a person spends equal amounts of time in more than one property, and also where a married couple or civil partners live apart much of the week. We explore these issues further in our response to question 11.

We also foresee issues with making the new legislation fit with existing deemed occupation rules covering absences for work (four years) and any other reason (three years), especially in transitional situations. Changing the PRR election rules has the potential to result in some very complex scenarios with possibly anomalous consequences. Early detailed consideration of such situations could reduce the risk of a large number of appeals going to tribunal.

2.8 **Question 11: Which approach out of those set out in paragraph 3.5 do you believe is most suitable to ensure that PRR effectively provides tax relief on a person's main residence only?**

Paragraph 3.5 of the Consultation identifies two possible methods of determining which of two or more houses should qualify as the main residence of an individual. Briefly stated, the first involves consideration of all relevant factors (in the same way as at present if no election has been made). The second would involve determination by a narrower range of prescribed factors.

Overall, we are not convinced that either of the proposals set out in paragraph 3.5, page 15 of the Consultation would provide a workable substitute for the current election system. Both would unavoidably involve added complexity with more record keeping for the taxpayer and inevitably more intrusive enquiries by HMRC (with significant resource implications for the department). This was amply demonstrated at the working group meeting hosted by HMT/HMRC on 19 May 2014. Every approach discussed at the meeting was found to involve complications and/or 'knock-on' effects. We believe that any method chosen will inevitably lead to much 'tinkering' having to be done to existing legislation in order to maintain a cohesive system.

Whilst there might be good reason for tightening up on the qualifying conditions for a valid election (and a coincidental opportunity to counter any perceived abuses of the election such as 'flipping'), we do not believe that bringing non-residents within the CGT charge should lead to the complete abandonment of the election facility. By way of a simple example of how the existing process could be tightened up, it would we think be possible to make an election irrevocable except in limited and well-defined circumstances. That would avoid the need for every situation where an individual had more than one residence to be considered on a factual basis by both the individual and HMRC and confine the detailed consideration of factors to situations where the individual claimed that their circumstances had permanently changed.

Notwithstanding these comments, if compelled to choose between the two methods identified in paragraph 3.5 of the Consultation, we would have to say that a fixed rule, such as the property in which a person spends the most time in any given tax year, would seem to us to be the simpler to operate and in practice it might in the majority of cases be the fairer of the two. However, we can envisage circumstances when a wider consideration of the facts might produce the fairer outcome, albeit that this would inevitably make outcomes less predictable.

In relation to individuals who were not obviously UK-resident, the time limit for days spent in a property would need to fit in with the time limit that creates a 'tie' to the UK for the purposes of the Statutory Residence Test, so for example more than 90 midnights, although a limit of more than 120 midnights might be preferable in terms of simplifying most cases and avoiding debate about marginal days.

The fixed rule approach would deal with the majority of cases and in situations where an individual spent equal amounts of time in two (or more) residences, then the wider facts of these cases would need to be 'drilled down' and looked at in more detail – such as where does the family reside, where are the children registered for school, for example.

We also propose that consideration should be given to allowing spouses and civil partners to have separate main residences. If we are to go down the route of 'day counting' in order to determine which is the main residence, then it may be necessary to allow separate main residences where spouses live apart for much of the working week. Otherwise, whose day count will have priority in determining which one is the most occupied property? We would envisage any assumption of priority having equality and human rights implications. This is just one of the 'knock-on' effects, referred to above, arising from changing one aspect of legislation. As mentioned, we do not believe that either of the suggested proposals would fully work as a replacement for the existing system as they both involve additional complications and administrative burdens.

We think it would be appropriate to consult separately on how some updated form of election might enable the simplicity of the existing system to be preserved at the same time as countering any perceived abuse and ensuring that non-residents were unable to exploit the election in order to avoid the proposed charge.

2.9 **Question 12: Are there any other approached that you would recommend?**

As mentioned in our response to question 11, we are not convinced that changing the PRR election rules is the correct approach.

We understand the motivation for doing so is to ensure that non-residents, when brought within the charge, do not try to circumvent the new rules by claiming PRR.

However, we favour the approach mentioned at the first workshop held on this subject, which would simply be to amend the Statutory Residence Test ("SRT") to the extent that owning a UK property and making a PRR claim on this property would count as another 'tie' to the UK when determining an individual's residence status. Consideration might even be given to stipulating that a claim for PRR on a UK property would automatically make an individual resident in the UK for the period of the election.

During the first workshop, it was noted that the effect of many DTAs may be to determine that the individual remains non-resident. Many DTAs provide that, if an individual owns property in both contracting states, that individual is a resident only of the state in which he is a national or where his personal and economic relations are closer. This was advanced at the workshop as being the reason for not using the SRT approach. However, we feel that it could still provide a sufficient deterrent to claiming UK PRR, as it would affect other issues pertaining to an individual's tax affairs, such as the remittance basis charge and the need to complete UK tax returns.

Amending the SRT in this way would be a much simpler solution than changing the PRR election rules, which will have many consequences and involve the need to create a transitional system of rules and for other legislation to be rewritten.

We appreciate that the SRT has only just been finalised and brought into use, but we would argue that it must surely be easier to make an amendment to relatively new legislation than to unravel legislation and over-ride associated case-law that has been in place for much longer.

Alternatively, if amending the SRT is not an option, we are of the opinion that HMRC and HMT should seriously consider keeping the election rules as they are (with appropriate modernisation), accept that EEA resident individuals will be able to claim PRR relief in some limited situations, but prohibit non-EEA individuals from doing so. We think this might be the simplest measure all round, and arguably the most cost effective as non-EEA persons are understood to be the main foreign investors in UK residential property.

There is some precedent for such treatment. This has been the approach taken on the extensions of reliefs such as business property relief and agricultural property relief.

2.10 **Question 13: Do you believe that solicitor, accountants or others should be responsible for the identification of the seller as non-resident, and the collection of withholding tax? If not, please set out alternative mechanisms for collection.**

We would expect the greatest responsibility in relation to the withholding mechanism to be with solicitors or licensed conveyancers. We are not therefore responding to this point in detail.

Overall, we believe that the identification process should be the minimum consistent with the policy objectives.

As a point of detail, we think that early attention should be given to instituting a simple procedure under which the relevant solicitor or conveyancer can obtain confirmation from HMRC that someone who is asserting that they are UK-resident is indeed so.

As a separate matter, attention may need to be given to the possible use by non-UK residents of UK-resident nominees. We cannot immediately see how solicitors or conveyancers should be responsible for establishing whether someone is acting as a nominee. Again, it might be appropriate for HMRC to operate a verification process to establish whether a UK-resident was indeed acting on their own behalf. (HMRC could for example satisfy themselves that rental income from the property was disclosed on the individual's self-assessment return.)

2.11 **Question 14: Are there ways that the withholding tax can be introduced so that it fits easily with other property transactions processes?**

We can think of two possible ways:-

- In Spain they use the National Savings system as a means of collection. One approach that might be used as an alternative to self-assessment at the top rate of tax might be a graduated withholding tax at 0% on say the first £50,000 of proceeds, building to 40% on

proceeds over £500,000. The withheld tax would be passed to (say) NS&I by the solicitor acting for the seller.

- Linking the collection method where appropriate with the Non-Resident Landlord Scheme

2.12 **Questions 15: Do you think that the government should offer the option of paying a withholding tax alongside an option to calculate the actual tax due on any gain made from disposal, within the same time scales as SDLT?**

Yes. We believe that there is scope here to offer an incentive to people who opt to calculate the actual tax due and pay ahead of the due date. This incentive could be a discount on the liability due (effectively an interest credit for early settlement). This could help to encourage compliance with this new charge.

2.13 **Question 16: Is it reasonable to ask non-residents to use self-assessment or a variant form.**

Yes, we believe it is reasonable.

Consideration *could* be given to having a non-resident simply complete a variant form requiring the information for the disposal only. This will depend on the rate of tax that will be charged on non-residents, which has not been officially published yet. If the rate is dependent on income levels (such as the system for UK individuals) then entitlement to be taxed at a lower rate (the equivalent of the resident taxpayer's 18% rate) might need to be proved by completing a self-assessment form will full details of the tax position for the year. For any non-resident who did not provide such full detail, it would be assumed that their income was such that they would pay CGT at 28% if they were UK-resident.

Non-resident landlords may already, of course, be completing self-assessment tax returns if they are renting out investment property. Again, we think that there could be scope for some inter-relationship with the Non-Resident Landlords' Scheme.

3 Conclusions

3.1 In our responses to the questions raised in the Consultation, we have shown that there is still much to think about and many details to finalise before the new charge is due to be brought in next April. We consider that further consultation will be essential once the skeleton for the new rules has been constructed.

We also strongly believe that if there is an option to retain the current PRR election rules, by either amending the Statutory Residence Test to prevent or deter non-residents from claiming PRR on a UK property or simply prohibiting non-EEA residents from claiming PRR rules (as EU

law would allow) then this should seriously be considered. We have also suggested a modified version of the election with a rebuttable presumption of irrevocability.

We would be happy to discuss further any issues raised in this response.

3.2 **Contact details:**

Should you wish to discuss any aspect of these comments, please contact our relevant

Yours sincerely

4 **Note**

4.1 The Association is a charity and the leading professional body for those providing UK tax compliance services. Our primary charitable objective is to promote education and the study of tax administration and practice. One of our key aims is to provide an appropriate qualification for individuals who undertake tax compliance work. Drawing on our members' practical experience and knowledge, we contribute to consultations on the development of the UK tax system and seek to ensure that, for the general public, it is workable and as fair as possible.

Our members are qualified by examination and practical experience. They commit to the highest standards of professional conduct and ensure that their tax knowledge is constantly kept up to date. Members may be found in private practice, commerce and industry, government and academia.

The Association has over 7,500 members and Fellows together with over 5,000 students. Members and Fellows use the practising title of 'Taxation Technician' or 'Taxation Technician (Fellow)' and the designatory letters 'ATT' and 'ATT (Fellow)' respectively.