



**Response from ICAS to the
HM Treasury and HMRC Consultation
'Implementing a capital gains tax charge on
non-residents: Consultation'**

24 June 2014

Implementing a capital gains tax charge on non-residents: Consultation

About ICAS

1. The Institute of Chartered Accountants of Scotland (ICAS) is the oldest professional body of accountants. We represent over 20,000 members who advise and lead businesses. Around half our members are based in Scotland, the other half work in the rest of the UK and in almost 100 countries around the world. Nearly two thirds of our members work in business, whilst a third work in accountancy practices. ICAS members play leading roles in around 80% of FTSE 100 companies. ICAS is also a public interest body.

General introductory comments

1. ICAS welcomes the opportunity to comment on the consultation 'Implementing a capital gains tax charge on non-residents', issued by HM Treasury and HMRC on 28 March 2014.
2. In broad terms, ICAS appreciates the Government's desire to extend capital gains tax to non-residents. Within this broader position however, there are aspects of the proposals which cause concern. Our concerns centre on:
 - The potential effects on private residential relief
 - Restricting the charge to residential property
 - The collection mechanism
 - Rebasing to April 2015.

These are expanded upon below.

3. More generally, ICAS members have serious reservations about the way in which this policy has been considered as a one-off, piecemeal extension. In our discussions with the Office of Tax Simplification, ICAS members regularly note the complexity of CGT whether this is in partnerships, companies or for individuals. ICAS also notes the comments in the recent IFS working paper 'Tax without design: recent developments in UK tax policy'¹. Before proceeding with the proposals in this consultation paper, ICAS recommends that a road map for overall CGT reform would be beneficial for policy makers, taxpayers and HMRC. Accordingly, ICAS recommends that the timetable should be extended, and the policy should be reconsidered as part of a wider review of CGT.
4. If this is to proceed, ICAS also suggests that the recommendation put forward by the Office of Tax Simplification in its final report 'Review of Tax Reliefs'², in relation to Principal Private Residence relief should be acted upon. The recommendation was as follows:

Principal private residence

3.18 This relief is clearly of considerable importance and is itself a simplification on the basis that it keeps many taxpayers outside the CGT net. However, there has to be scope for simplification due to the numerous conditions and sub-reliefs causing complexity in anything other than straightforward cases. It is therefore proposed that these conditions be:

- Reviewed to test which are still appropriate;
- Researched to see whether any can be streamlined; and
- Rewritten in a simpler format.

¹ IFS Working Papers (W14/09) 'Tax without design: recent developments in UK tax policy'
<http://www.ifs.org.uk/publications/7203>

² Office of Tax Simplification final report 'Review of Tax Reliefs, March 2011, page 21
https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/198570/ots_review_tax_reliefs_final_report.pdf

Private residence relief (PRR)

5. There may be good policy reasons to review private residence relief but ICAS members strongly believe that it should not simply be as a side issue of extending CGT to non-residents.
6. Paragraph 3.3 of the consultation paper notes that 'Under the current system an individual with more than one residence can choose, for any given period, which of those properties they would like to qualify for PRR. They do this by notifying HMRC of their election.' This is a choice afforded by the law and should remain in place. For example, when an individual works in Edinburgh 5 days a week and owns a residence, but also goes 'home' to a residence in the country each weekend there can be a genuine question mark over which is the main residence. It is simpler that it should rest with the taxpayer to make this clear.
7. It would be a matter of considerable concern if the test of main residence was changed to require detailed, daily record keeping of where the taxpayer stays; this would not only be a highly intrusive measure but compliance would be difficult to establish and confirm.
8. The existing Private Residence Relief election provides the taxpayer with certainty and should remain in place as long as there is such a relief. More broadly, however, PRR should be examined as a part of CGT reform, with the review of PRR centred on those taxpayers who are the main users of the relief, in other words, UK residents.

Restricting the charge to residential property

9. There are potential difficulties if the CGT charge proposed in the consultation paper is to be on residential property but not on other property owned by non-residents. This raises questions of 'fairness': if fairness between non-residents and UK residents is a policy objective, this extension of CGT could equally well be applied to any other UK based property owned by non-residents. Questions may also be asked about why a non-resident who invests in the UK should be subject to different tax treatment depending on whether the investment is, say, a farm with some residential property, or any other commercial property.
10. The proposal fails any 'simplicity' test. Wherever there is a dividing line, such as that between what is and is not a residential property, there is scope for disputes. Difficulties may also arise when development work changes the use and nature of a building, or if a residential building is purchased, demolished and redeveloped as a commercial property. Such disputes are likely to be time consuming for all concerned, fee consuming, and may still appear arbitrary even when settled.
11. The complexities arising from defining boundaries will be aggravated if the definition of 'residential property' is different from that used in other UK taxes, such as for ATED.
12. For the above reasons ICAS requests clarification about why the policy is limited to extending CGT to the residential property of non-residents.

The collection mechanism

13. The collection mechanism for a capital gains tax charge on a non-resident needs further consideration. Whilst the tax liability rests with the non-resident and a self-assessment and collection method could be established, any necessary enforcement measures would be difficult to impose on a non-resident outwith the UK. Nor is there necessarily an on-going UK source of income or capital from which to levy any outstanding tax. Because of this, making the solicitor who is responsible for handling the sale of the UK based property also responsible for tax would seem to be the only practical choice.

14. The solicitor will already have to operate within the anti-money laundering requirements and if the sale is conducted by a UK based solicitor the proceeds are likely to pass through its client account. If this is the case, a collection mechanism could be built upon the non-resident landlords scheme rules, whereby the selling agent would be required to identify the taxpayer and withhold tax.

The commencement date and rebasing

15. It is not clear from the consultation whether it is proposed that tax should be levied on a gain that crystallises after 5 April 2015; or whether it should only be in relation to the portion of the crystallised gains that have accrued from 6 April 2015. If it is the latter, further complexity and costs would arise with the need for rebasing and valuations at that date. However this would avoid retrospection issues, and be consistent with other CGT changes over the years.
16. However, bringing in a charge to CGT on non-residents who dispose of a UK property from April 2015 onwards, could lead to a 'fairness' question for UK residents, about whether all UK residential property should be rebased to April 2015 or time apportioned to only tax the element of gain after April 2015.

Unintended consequences

17. A number of the proposals in this consultation paper have complexity implications in relation to capital gains tax as discussed above. There may also be significant unintended consequences in relation to double tax treaties which may be affected.
18. There may also be broader unintended consequences, for example, on investment decisions by non-resident investors. Investment may be made in commercial property instead of residential property, such as the redevelopment of old industrial buildings into offices rather than redeveloping into housing. Investment may be in greenfield sites rather than redevelopment of, say, old, disused housing stock which could be very suitable for investment properties. Brownfield sites within city centres needing investment and redevelopment may also be affected if there is an unintended consequence of this tax measure refocusing investment on commercial property instead of housing. This tax policy may not sit comfortably with other government policies in relation to the provision of housing stock.
19. Competent advice may become more difficult and expensive to obtain if taxes on property have a number of intricacies and different nuances. Whilst CGT is in theory a self-assessed tax, this proposal will be very difficult for taxpayers to comply with especially if they are based outwith the UK. It will push taxpayers towards the larger, international tax agents, make it more challenging for smaller agents to offer their services, and lead to a polarising of the tax advice market.

Specific questions

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

In principle, no. However, the policy objective of simplicity will not be met if the exclusions differ within one tax (CGT) to another (SDLT and ATED). Nor is it clear why, say, student halls of residence should differ in treatment from a house in multiple occupation by students. There needs to be clarity of principle and clarity of legislation. As currently proposed, however, the consequence around this will be complexity with a need to apply rules all of which are similar, but not the same, to different taxes.

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

Not obviously. If sustainability and simplicity are both sought then consideration should be given to drafting a more principles-based charge so that it is clear what principles underlie exclusions. Listing specific exclusions simply results in some being on the list, whilst others are not.

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

No comments

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

The unintended consequences from including non-resident trustees will be the additional complications of dealing with such trusts; it may also impact on the section 91 TCGA 1992 charge.

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?

It is questionable whether there should be such an exclusion. It is noted in paragraph 2.4 of the consultation paper that the final sentence states in bold 'The government also believes that gains made on disposals of residential property used as an investment should be subject to CGT.' Such an exclusion is inconsistent with the policy objectives; it certainly does not lead to fairness or simplicity.

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

Such a test may be difficult to manage; for instance, with ownership across many there will need to be monitoring in place to retain the GDO qualification, which may be affected by sales of unit holdings or the death of a unit holder. If there is to be such a test it is hoped that it would be operated on a pragmatic basis with, say, a period of six months in which the conditions if failed can be re-met.

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?

Consideration may need to be given to whether umbrella structures would be developed as an alternative means of holding residential property to circumvent this.

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?

Such a measure may discourage foreign investors from investing in UK let property, or in property with a view to residential letting over the longer term. A wider impact associated with this is that residential planning applications frequently have conditions attached to provide social housing and therefore tax measures that encourage investment in commercial property may be counterproductive in relation to wider housing policies within 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?

There is an existing income tax mechanism for such entities, and this could be built upon to charge gains arising. Alternatively, double tax treaties could be reviewed and amended so that UK situs property would be liable to the appropriate tax regime as in other OECD countries.

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

ICAS considers that it is the wrong approach to change the PRR election rules simply to bring non-residents into the CGT charge. If these rules require examination and potential amendment this should be done as a separate exercise. See above for further discussion of this under 'General Introductory comments'.

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?

In a self-assessment regime a level of certainty is preferable and therefore, if the election is to be removed, ICAS members would prefer the second option in the consultation paper of having a fixed rule. Nevertheless, there are significant concerns about this because it would need an intrusive level of record keeping showing where the person stays every day, which is unlikely to be complied with in practice, and overall tests of what makes it the main principal residence.

An exclusion might be needed to provide consistency with job related accommodation. If, for example, a contractor worked at a client site for two years, in a rented flat, but kept the family home for weekends, that should not disturb the main residence test, but could. Maintaining the flexibility of the United Kingdom workforce is key and residential property tax should support this, not add complications or costs where none now exist.

Question 12: Are there any other approaches that you would recommend?

As noted in our general comments above, our preference is not to have the PRR election changed.

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

Care should be taken in placing duties that may be onerous on others.

It should also be noted that in general accountants do not hold client moneys due to the regulatory aspects of doing so.

A collection mechanism could be designed building upon the non-resident landlord scheme rules, whereby the selling solicitor would be required to identify the non-resident taxpayer and withhold tax. Of course, this may be more difficult if the solicitor was not UK based.

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

A withholding tax is generally applied where a fixed percentage is levied on the income or receipt that is taxable. With CGT however, the amount chargeable is based, broadly, on proceeds less cost. So if a withholding tax is charged this may bear little connection with the tax bill. Issues may also arise in agreeing rebasing valuations and those transactions that are not at arms length.

However, a withholding tax of an average effective amount could be charged (say, 5%) as a default rate, which could be displaced by the submission of the self-assessment. The rate could be determined by HM Revenue & Customs as the effective rate paid on residential property disposals.

Question 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, this would be helpful for those who wish to be compliant and settle their affairs promptly.

Question 16: Is it reasonable to ask non-residents to use self-assessment or a variant form to submit final computations within 30 days? If not, what processes would be preferable?

30 days would appear to be a tight deadline and one that might lead very quickly to penalties. Enforcement of this may prove difficult and therefore a longer submission period of, say, three months may be more practical for both the taxpayer and for HMRC.

