

THE REMITTANCE BASIS OF TAXATION IN THE UK

A FUTURE IN THE BALANCE



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The 'remittance basis' of taxation is the UK's favourable tax treatment available to UK resident but foreign domiciled individuals. Broadly, it allows this category of taxpayer to avoid UK tax on many types of foreign income and on capital gains realised on foreign assets, provided that the income and the proceeds of sale are not used in (remitted to) the UK. This tax regime has been a significant factor in the choice of many wealthy foreigners to establish residence in the UK.

The remittance basis of taxation periodically attracts negative publicity on the grounds of 'fairness', and has become something of a political football at the moment. But before we catch up with the present and look forward, it may be helpful to provide some historical context.

The origins of the remittance basis of taxation go all the way back to the Napoleonic Wars, when Pitt the Younger introduced income tax in Britain in 1799 to fund the war effort. Significant profits were generated in the colonies and had it been practical to do so, income tax would have been imposed on those foreign profits as they arose. However, the reality at the time was that Britain was the only trading partner for colonial businesses, and profits could only be crystallised on the importation of produce to Britain. Income tax was therefore imposed on foreign earnings when they were remitted to Britain.



This endured until 1914, when the remittance basis was abolished for overseas income. However, it was decided that there should be a carve-out for UK resident foreigners. It was necessary to adopt a legal definition for this category of taxpayer, and there was a readymade and convenient legal concept of 'domicile' which was adopted. The purpose of identifying a person's domicile is to connect that person to a particular system of law. This is important because the issue determines which country's jurisdiction would apply in matters such as marriage and divorce, legitimacy and succession (such as how an estate devolves on death under a Will or on intestacy). The status of having a foreign domicile was now imported into British tax legislation.

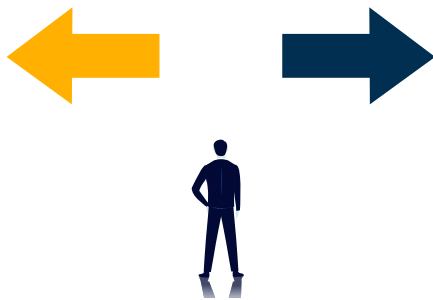
Although the remittance basis of taxation has limped through to the present day in a somewhat curtailed form, it has led a turbulent existence over the last 50 years:

- The 1974 Finance Bill under the Harold Wilson Labour administration included draft 'deemed domicile' provisions which were to apply to a person who had been resident in 9 of the previous 10 tax years. The provisions were mysteriously dropped;
- In 1988, a Consultative Document was published, proposing the replacement of the remittance basis with a provision whereby those resident in fewer than 7 of the previous 14 tax years would be allowed to apply a 2% tax rate to foreign income. This too was abandoned;
- In 2002, there was another concerted campaign by elements of the press to address the perceived unfairness of the remittance basis regime for wealthy foreigners. Forced to respond, the Labour Government published a lukewarm and somewhat superficial document, which (unsurprisingly) led to nothing;

- **The biggest, actual changes occurred in 2008 (the introduction of the Remittance Basis Charge) and in 2017 (the limitation of the remittance basis to those who had been UK resident for 15 or fewer of the previous 20 tax years), along with other significant changes, for example, to the tax treatment of trusts.**

And so to the present day, and what the future might hold. The Labour Party has made a very clear commitment to abolish the remittance basis, if it comes to power. Rachel Reeves, the Shadow Chancellor, made a speech to the Co-op Party conference in October 2022 in which she made clear the Party's view that if you make Britain your home, you should pay your taxes here.

'And that is why as Chancellor in the next Labour government, I will abolish non-dom status'.



Labour's position is very clear, then. The Conservative government has a different view. Jeremy Hunt, Chancellor of the Exchequer, when challenged on why he was allowing £3.6bn to be thrown away because 'he won't make them pay tax here', replied that non-doms pay around £8bn in tax per year and that he would rather that they 'stayed here and spent their money here'.

The differences between the two main political parties might be seen as ideology versus pragmatism, but this would be simplistic. The Labour Party's claim that an additional £3.6bn in tax would be collected if the remittance basis were abolished is based on Cage Policy Briefing no. 38 prepared by Warwick University's Economic and Social Research Council. Its conclusions assume that nearly all non-doms would remain UK resident and pay tax on worldwide income and gains. This is based on a study of what happened after the changes in April 2017, when very few long term resident non-doms who lost the ability to claim the remittance basis chose to depart these shores. However, the 2017 changes left some valuable continuing protections for income and gains arising within trust structures, and it is almost certain that this significantly influenced the low number of departures.

The future of the remittance basis probably rests on which political party wins the next general election, which is a maximum of two years away. As we face economic hardship and a 'Winter of discontent' in the UK, one might speculate that the government in power will struggle to gain much electoral appeal.

But one should never lose sight of Harold Wilson's (possibly misquoted) observation that 'a week is a long time in politics', an observation spectacularly validated by political events here in Autumn 2022.

One last thought on this is that the enactment in 2013 of a detailed test of UK tax residence has provided individuals with the means to work out exactly how many days they can spend in the UK without being UK resident. Many countries offer a favourable tax system to attract new residents and any government, whatever its colour, would do well to remember this. As Adam Smith wrote in 'The Wealth of Nations':

'The proprietor of stock is necessarily a citizen of the world, and is not necessarily attached to any particular country. He would be apt to abandon the country in which he was exposed to a vexatious inquisition in order to be assessed to a burdensome tax, and would remove his stock to some other country where he could either carry on his business, or enjoy his fortune more at his ease.'

If this was the case even in 1776, it is certainly the case now in the era of global mobility!

