



RESTRICTING NON-RESIDENTS' ENTITLEMENT TO THE UK PERSONAL ALLOWANCE

ICAEW welcomes the opportunity to comment on the consultation paper [Restricting non-residents' entitlement to the UK personal allowance](#) published by HM Treasury on 17 July 2014 and revised on 4 August 2014.

This response of 9 October 2014 has been prepared on behalf of ICAEW by the Tax Faculty. Internationally recognised as a source of expertise, the Faculty is a leading authority on taxation. It is responsible for making submissions to tax authorities on behalf of ICAEW and does this with support from over 130 volunteers, many of whom are well-known names in the tax world. Appendix 1 sets out the ICAEW Tax Faculty's Ten Tenets for a Better Tax System, by which we benchmark proposals for changes to the tax system.

Contents

	Paragraphs
Major points	
Introduction	1-3
Key point summary	4-11
Responses to consultation questions	12-30
Ten Tenets for a Better Tax System	Appendix 1

ICAEW is a world-leading professional accountancy body. We operate under a Royal Charter, working in the public interest. ICAEW's regulation of its members, in particular its responsibilities in respect of auditors, is overseen by the UK Financial Reporting Council. We provide leadership and practical support to over 142,000 member chartered accountants in more than 160 countries, working with governments, regulators and industry in order to ensure that the highest standards are maintained.

ICAEW members operate across a wide range of areas in business, practice and the public sector. They provide financial expertise and guidance based on the highest professional, technical and ethical standards. They are trained to provide clarity and apply rigour, and so help create long-term sustainable economic value.

Copyright © ICAEW 2014
All rights reserved.

This document may be reproduced without specific permission, in whole or part, free of charge and in any format or medium, subject to the conditions that:

- it is appropriately attributed, replicated accurately and is not used in a misleading context;
- the source of the extract or document is acknowledged and the title and ICAEW reference number are quoted.

Where third-party copyright material has been identified application for permission must be made to the copyright holder.

For more information, please contact ICAEW Tax Faculty: taxfac@icaew.com

icaew.com

MAJOR POINTS

Introduction

1. We welcome the opportunity to comment on the proposals in HMRC's consultation document of 4 August 2014.
2. We should be happy to discuss any aspect of our comments and to take part in all further consultations on this area.
3. Along with other professional bodies we attended a meeting with HM Treasury on 29 July and joined a conference call on 30 July in which we were able to put forward some key comments and concerns and discuss aspects of the consultation document. We were disappointed to note that Hugo Gillibrand was dropping out of the consultation before the responses were even collected.

Key point summary

4. In our view the entitlement to personal allowance (PA) should be retained in its current format. While we understand the desire for tax to be collected in the UK on income received in the UK rather than the tax being collected in a different jurisdiction the additional administrative burden is not justified.
5. The cost of compliance is likely to outweigh the tax collected, especially in the case of low paid workers. It will increase direct and indirect (ie compliance) employment costs especially in shipping and oil/gas and low paid sectors such as tourism/leisure/entertainment/hospitality and agriculture, in many cases for the sake of tax worth pennies. This could give rise to undesirable economic impacts because the prospect of paying UK tax at source and having to complete a tax return in an unfamiliar language to settle the liability is likely to discourage people from coming to the UK to work. The additional costs incurred by employers will be passed on to customers by way of higher prices which will increase inflation.
6. The PA usefully reduces the compliance burden. The allowance of £10,000 (£10,500 from 6 April 2015) plus inflation adjustments is not so high that it warrants the hassle of restrictions and instead it can be promoted as good incentive for international businesses to locate in the UK.
7. If the government chooses to make a significant increase in the PA in the future the same effect could be achieved by introducing a 0% tax rate band of a sum equal to the proposed increase in the PA and keeping the PA at the same level. The 0% tax band could then be restricted to just UK residents.
8. Employers will have their administration burden increased significantly if they have to determine the residence status of employees. They may need to pay for professional help to help determine the residence status of employees and frequently it will be impossible to determine the residence status until after the end of the tax year. Employees arriving in or leaving the UK may unexpectedly discover that they are resident in either a year of arrival or departure, resulting in unwelcome PAYE underpayments for those individuals and an additional administrative burden for HMRC to calculate and collect such underpayments.
9. The circumstances of employees may change; we would welcome confirmation that employers will not be expected to monitor the on-going residence status of all employees.
10. DWP would need to operate PAYE on state pensions to ensure that the right amount of tax is collected from expatriates living overseas. The pensioner's code number would have to take into account his country of residence because although most double tax treaties tax state pensions in the country of residence others tax them in the UK. PAYE would also need to be applied to any other taxable social security payments made by government departments including local government to collect tax on payments to non-residents.

11. Has consideration been given to the possibility that other jurisdictions will follow the lead if the PA is restricted for non-residents in the UK to restrict the PA equivalent in their country for UK nationals working there?

RESPONSES TO CONSULTATION QUESTIONS

Q5.1: Do you agree that, if the government decides to introduce any restriction on non-residents' entitlement to the Personal Allowance, this should not apply in circumstances where individuals have strong economic connections to the UK? If you do not agree please explain your reasoning.

12. We agree that if the PA is restricted then those with strong economic connections to the UK should not have their PA restricted but the measure for economic connections has to be simple to understand and apply; if they are difficult the inevitable result is non-compliance.
13. An alternative approach would be to pro rata the PA to only allow the PA for periods of residence so for an employee a Wk1/Mth1 tax code would collect approximately the right amount of tax. This would work well for employees but a different approach would be needed for recipients of pensions and rental income who could perhaps qualify for the PA or a proportion of it based on nationality.

Q5.2: Is a percentage test for the location of income the simplest and least burdensome basis upon which to identify circumstances where individuals have strong economic connections to the UK? Do you have any views on what level such a percentage should be set at? Please explain your reasoning.

14. Whilst we are not sure judging the position solely on the location of income gives a fair result in all cases it is a reasonable measure; a 75% level would be preferable. The problem is that the location of the income will not be known until the end of the tax year and this will necessitate completing a self assessment to either reclaim tax or pay additional tax adding administrative burden to the taxpayer and to HMRC.

Q6.1: Are there unfair outcomes for those with globally low incomes from a broader policy of restricting non-residents' entitlement to the UK Personal Allowance? Could a de minimis limit of global income below which non-residents would automatically be entitled to the UK Personal Allowance help mitigate these unfair outcomes? If so, is there a way to design this so that the administrative burdens are not disproportionate?

15. The loss of the PA would impact unfairly on the low income group. Setting a global income de minimis below which non-residents are automatically entitled to keep the PA would help mitigate the position and setting a level of between one and two times the PA would be appropriate.

Q6.2: Do you agree that retaining the UK Personal Allowance in respect of the income of non-residents which is by treaty subject exclusively to UK taxation would help mitigate unfair outcomes from a broader policy of restricting non-residents' entitlement to the UK Personal Allowance?

16. Where income of the non-residents is exclusively liable to UK taxation under the treaty then in fairness the PA should be retained in full for the individual.

Q6.3: Are there any other hard cases or unfair outcomes you believe that the government may not have considered if the Personal Allowance for non-residents were to be withdrawn?

17. The additional compliance costs that would be placed on non-resident landlords in order to account for what in most cases will be a small tax liability would be very unfair. In many cases the professional costs could be more than their profit.

Q6.4: In practice are non-resident individuals claiming the UK Personal Allowance on the basis of criteria other than UK residence or EEA nationality?

18. We are not aware of significant numbers of such individuals.

Q6.5: If the government were to remove the entitlement to the UK Personal Allowance by virtue of EEA nationality to what extent would non-residents you are familiar with claim the UK Personal Allowance on the basis of other criteria currently in Section 56 Income Tax Act 2007? Please provide what evidence you can in support of your answer.

19. We are not aware of significant numbers of such individuals.

Q6.6: Which, if any, of the criteria other than UK residence or EEA nationality in Section 56 Income Tax Act 2007 do you think are relevant to the in the 21st century? Should these criteria be repealed? Are there any other criteria in Section 56 on which individuals should be entitled to the UK Personal Allowance? Please provide evidence in support of your answer.

20. It will depend on what other changes if any are made to the PA for non-residents.

Q6.7: How widespread is knowledge of residence status amongst PAYE scheme operators, particularly employers? How easy would asking employees to declare their tax residence be for employers?

21. In our view employers are not aware of the residence status of their employees. Determining residence is a very complex issue and it is unlikely that many employers would have the ability or the inclination to determine the residence status of the employees.

22. The average employee from overseas is likely to be even less familiar with the UK's statutory residence test (SRT) rules and so however easy it is for the employer to ask his employee and the employee to declare residence status, the employee will probably not provide the right answer.

23. Most employers running a small business are content to check that potential employees have the right to work in the UK but would not want to assess the employees' residence status they simply want to be given a code to operate by HMRC. If the employer assesses the residence status and it is wrong who would be liable for any tax underpaid, the employee or the employer?

24. Employers who employ internationally mobile employees in numbers often do assist in working out employees' residence status, with systems for tracking days in and out of the UK etc. However other employers are unlikely to have the systems to do this. Coupled with the problem that it is frequently not possible to determine the status until the end of the tax year makes the suggestion that employees "declare" their tax residence e.g. at the start of the year nonsensical.

Q6.8: How could the PAYE starter process be best used to ensure that most people get the correct tax code at the start of the employment if the government decides to restrict the availability of PAs to non-residents? What questions could be used to indicate residence status? Is the new starter process a sensible way to identify non-residents? What other processes could be adapted, with minimal additional burden, to identify non-residents?

25. If the burden is to be placed on employers, in our view it should not be, then the starter form would seem to be the place to include questions on residence for new employees. This would involve adding SRT questions to which employers would have to find out the answers. In many cases it is hard enough for employers to find out the answers to the basic questions already included.

26. If employers have to ask questions relating to residence status then they should be instructed to send the answers to HMRC so HMRC can issue the appropriate code number. Pending the

issue of an appropriate code number by HMRC, employers would follow current PAYE processes for new employees. This would minimise the additional burden on employers and enable a code number to be applied from the start of the employment.

27. HMRC setting out standard questions and reviewing the answers and issuing the tax codes would ensure consistent treatment across all employees. Questions would need to be carefully worded, so questions like: 'Do you live permanently in the UK' would need the meaning of the word 'permanently' defined.
28. If employers have to ask questions about residence then a change in statute or Regulation will probably be required. Employers are already concerned about asking questions that might be perceived as discriminatory under the Equality Act; asking more and more personal data could infringe the Equality Act.
29. Assuming the employee is accepted as non-resident, the availability of the personal allowance could only be determined with the knowledge of the individual's worldwide income. Normally this information is a matter between HMRC and the individual and would not generally be disclosed to the individual's employer.

Q6.9: Although the government will consult on detail if it decides to restrict non-residents' entitlement to the UK Personal Allowance do you have any preliminary views as to whether any system should lean toward restriction or entitlement?

30. As noted above we do not think there should be any change at this time but if there is a change it should lean toward entitlement.

APPENDIX 1

ICAEW TAX FACULTY'S TEN TENETS FOR A BETTER TAX SYSTEM

The tax system should be:

1. Statutory: tax legislation should be enacted by statute and subject to proper democratic scrutiny by Parliament.
2. Certain: in virtually all circumstances the application of the tax rules should be certain. It should not normally be necessary for anyone to resort to the courts in order to resolve how the rules operate in relation to his or her tax affairs.
3. Simple: the tax rules should aim to be simple, understandable and clear in their objectives.
4. Easy to collect and to calculate: a person's tax liability should be easy to calculate and straightforward and cheap to collect.
5. Properly targeted: when anti-avoidance legislation is passed, due regard should be had to maintaining the simplicity and certainty of the tax system by targeting it to close specific loopholes.
6. Constant: Changes to the underlying rules should be kept to a minimum. There should be a justifiable economic and/or social basis for any change to the tax rules and this justification should be made public and the underlying policy made clear.
7. Subject to proper consultation: other than in exceptional circumstances, the Government should allow adequate time for both the drafting of tax legislation and full consultation on it.
8. Regularly reviewed: the tax rules should be subject to a regular public review to determine their continuing relevance and whether their original justification has been realised. If a tax rule is no longer relevant, then it should be repealed.
9. Fair and reasonable: the revenue authorities have a duty to exercise their powers reasonably. There should be a right of appeal to an independent tribunal against all their decisions.
10. Competitive: tax rules and rates should be framed so as to encourage investment, capital and trade in and with the UK.

These are explained in more detail in our discussion document published in October 1999 as TAXGUIDE 4/99 (see icaew.com/en/technical/tax/tax-faculty/~media/Files/Technical/Tax/Tax%20news/TaxGuides/TAXGUIDE-4-99-Towards-a-Better-tax-system.ashx)