

Megxit maelstrom

A case study by **Sharon McKie** and **Simon McKie** illustrates the importance of understanding the tests involved in determining statutory residence status.

We know that determining residence status can be difficult and the critical factor is having all the relevant facts. Much has been written in the popular press about ‘Megxit’ and many facts concerning the Duke and Duchess of Sussex are in the public domain so let us use them as an example of how an adviser would go about determining residence status. The ‘transition’ of the couple throws an interesting light on the complexities of the statutory residence test (SRT), particularly in the areas of determining the activities that will constitute ‘work’, how the concept of a ‘home’ can cause uncertainty, the split year cases, and the necessity of detailed record keeping.

As a brief recap, under the statutory residence test an individual is resident in the UK for a tax year if, for that year the ‘automatic residence test’ or the ‘sufficient ties test’ is met. If neither of those tests is met, the individual is not resident in the UK for that year. The ‘automatic residence test’ is met for a year if the individual meets at least one of the four ‘automatic UK tests’ and none of the five ‘automatic overseas tests’.

Clearly, we do not have the exact details, but some information is available. From the court circular records up to 16 January 2020, it seems that Prince Harry has been outside the UK on official business on 16 days. Various newspapers report that during the summer he went to Ibiza and Nice and attended a Google conference in Sicily. He left the UK on 20 January 2020 after returning to the UK on or before 6 January following his six week ‘sabbatical’. We shall assume that up to 20 January 2020 he had spent 220 days in the UK.

Prince Harry then returned to the UK on 25 February to undertake various official duties intending to stay until, we are informed, 9 March 2020. We shall assume that he will leave as planned on 9 March 2020. Further, all references are to FA 2013, Sch 45 unless otherwise stated.

Key points

- The statutory residence test comprises several different elements.
- The application of the split year rules.
- Are the overseas work criteria satisfied?
- Voluntary work is not ‘work’ for the purposes of the test.
- Determining the departure date.
- Does an individual have a sufficient link with an overseas country?
- Reviewing the automatic overseas tests.
- The importance of record keeping.



2019-20 and split year treatment

First, what of his residence status for the current fiscal year, 2019-20? Unsurprisingly, he does not satisfy any of the five automatic overseas tests (para 11) because of the number of days he has spent in the UK.

Does he satisfy any of the automatic UK tests? He satisfies the first because he has spent at least 183 days in the UK in the fiscal year and so is resident in the UK for 2019-20 (para 7).

The next question is whether the split year treatment will apply. The application of these rules will not change his residence status because a person who is resident under the SRT for a fiscal year is to be ‘taken for the purposes of any enactment relating to relevant tax to be resident ... there at all times in that tax year’ (para 2(3)). Instead, the rules modify the taxation of specific types of income.

Paragraph 43 provides that a tax year will be a split year if the individual is resident in the UK for that year and their circumstances fall within one of the eight split year cases. Cases 1, 2 or 3 may be relevant for 2019-20.

Case 1

Although the legislation does not use the phrase ‘full-time work,’ case 1 (in para 44) is aimed at an individual starting full-time work overseas. Under this case, an individual must have been resident in the UK in the preceding year. For Prince Harry, the relevant preceding year is 2018-19 and we assume he was then UK resident. Second, there must be at least one ‘period’ (the ‘consideration period’) which satisfies the overseas work criteria. The consideration period satisfies this criteria provided:

- the individual works sufficient hours overseas as assessed over that period;
- during that period, there are no significant breaks from overseas work;
- the number of days in that period on which he does more than three hours work in the UK does not exceed the permitted limit; and
- the number of days in that period falling within para 44(6) does not exceed the permitted limit.

'Work' is not defined in the legislation, but para 26 defines when a person is considered to be working or doing work. An individual is considered to be working at any time when he is doing something in the performance of duties of an employment held by him or in the course of a trade carried on by him. Paragraph 26(8) provides that voluntary work is not 'work' for the purposes of SRT. We have been told that Prince Harry 'intends to work to become financially independent'. One can only guess at how he will achieve this, but we assume he will be undertaking some sort of trade. Paragraph 26 provides that time spent travelling may count as work but only if the cost of the journey could, if it were incurred by the individual, be deducted in calculating his trading profit. Prince Harry has also said that he intends to 'launch [a] new charitable entity', but, of course, those activities will not constitute 'work' under the SRT. On occasions, it will, no doubt, be difficult to distinguish between his voluntary work and the work done in the course of a trade carried on by him. Detailed records of all his activities will be essential.

The consideration period

So when does the consideration period begin? It starts with a day on which the individual does more than three hours work overseas and in Prince Harry's case that would be work done in the course of his trade.

Determining when a trade starts is difficult, particularly in respect of such ill-defined activities as those he is likely to undertake. Will his trade have started before he has actually performed an engagement but when he arranges, with his management team, possible speaking engagements at, for example, global banking organisations for a fee? This again illustrates the importance of keeping records to provide evidence of his various activities. We shall assume that the consideration period began on 4 January 2020.

One must then determine, using the rules set out in the third automatic overseas test with modifications, whether sufficient hours overseas have been worked. Further, there must be no significant breaks from overseas work. Paragraph 29 provides that there is a significant break if at least 31 days go by and not one of those days is a day on which an individual does more than three hours work overseas or would have done so but for being on annual leave, sick leave or parenting leave. Again, keeping records of all activities will be essential.

In addition, the number of days in that consideration period on which the taxpayer does more than three hours work in the UK must not exceed the permitted limit as calculated under para 44(8). For example, on the assumption that the consideration period began on 4 January 2020, the permitted limit will be seven days ($30 \text{ days} - (9 \div 12) \times 30$) rounded (para 52(5)). On that basis, therefore, Prince Harry should have been advised to ensure that he does no more than three hours work in the UK on more than seven days on or after the first day on which he worked more than three hours overseas which we assume was 4 January 2020.

The number of days in the consideration period which are days spent in the UK must also not exceed the permitted limit which will be 22 days as calculated under para 44(8) and (9). If the consideration period began on 4 January, this limit will have been exceeded taking into account his time spent here in January, February and March 2020.

The third automatic overseas test

Finally, Prince Harry must not be resident in the UK in 2020-21 on the basis that he meets the third automatic overseas test for that year (para 44(4)).

It is not clear whether case 1 will apply if he is non-resident because he satisfies another automatic overseas test. Due to this uncertainty it would be prudent to ensure that the third automatic overseas test is satisfied. That is that in 2020-21 he must work sufficient hours overseas assessed over that fiscal year without any significant breaks from that overseas work, the number of days on which he does more than three hours in the UK must be less than 31 and he must spend less than 91 days in the UK in the fiscal year.

If he wishes 2019-20 to be a split year under case 1, therefore, he must ensure that in 2020-21 he spends less than 91 days in the UK and must not do more than three hours' work in the UK on more than 30 days.

“Determining when a trade starts is difficult, particularly in respect of such ill-defined activities as those he is likely to undertake.”

Case 2

Paragraph 45 sets out case 2, which applies to the accompanying spouse of someone starting full-time work overseas under case 1. It would appear that the prince and his wife's financial independence is a joint venture, so we shall assume for the purposes of this article, that the duchess satisfies case 1. In that case, would case 2 apply to the prince?

Case 2 has five elements.

First, he must be resident in the UK in the preceding year 2018-19 which we have assumed he was.

Second, he must have a partner whose circumstances fall within case 1 for the fiscal year 2019-20 which we have also assumed he does.

Third, during the 2019-20 year he has to move overseas so that he can continue to live together with the duchess while she is working overseas. Whether this condition is fulfilled is uncertain, but we shall assume that it is possible that it will be.

Fourth, in the part of the relevant year (2019-20) beginning with the deemed departure date he must not have a home in the UK at any time (the 'first limb') or he must have homes in both the UK and overseas, but spend the greater part of the time 'living in the overseas home' and the number of days that he spends in the UK must not exceed the permitted limit (the 'second limb').

Determining the departure date

Paragraph 45(7) provides that the deemed departure date is the later of:

- the day on which he moves overseas so that he and his wife can continue to live together; and
- the first day of his partner's overseas part of the relevant year as defined for case 1.

The concept of moving overseas is not a precise one so, in practice, it will often be uncertain when a person ‘moves overseas’; however, we assume that he moved overseas on 20 January 2020 so this is his deemed departure date. At that time, did he still have a home in the UK? The palace has stated that Frogmore Cottage ‘will remain their UK family home’, but is it a home for the purposes of the SRT? The difficulty is that a ‘home’ has a range of meanings. Paragraph 25 provides that ‘somewhere that ... [the individual] ... uses periodically as nothing more than a holiday home or temporary retreat (or something similar) does not count as a home of [the individual]’. So if an individual spends only a few weeks a year in a property that has been his home, does it remain his home or has it become a holiday home or temporary retreat? There are no clear principles by which this question can be determined, but it is arguable that a property’s function determines its nature.

One might, therefore, argue that Frogmore Cottage will not be his home in the period from 20 January to 5 April 2020 and that when he stays there in February and March 2020 it functions merely as temporary accommodation. If that were the case, he would satisfy the first limb of the test. On the other hand, if Frogmore Cottage were his home, the second limb must be considered: does he have homes in both the UK and overseas but spends the greater part of his time in the overseas home? One has to ask, is the property on Vancouver Island, which does not belong to him and he is occupying temporarily, a home? Again there is uncertainty.

“ Having considered cases 1 to 3, it can be seen that there is at least a reasonable possibility that none of the cases will apply.”

Further, he must not spend more days in the UK than the permitted limit, namely 22 days, calculated in the same way as under the case 1 provisions. Because the period is calculated from his departure date, 20 January 2020, he is unlikely to exceed the permitted limit.

The fifth element

The fifth element of case 2 is that he must not be resident in the UK in 2020-21. Unlike case 1, that does not have to be by virtue of meeting the third automatic overseas test. There is a nasty trap here, however, because, in the event that the duchess does not satisfy the condition of case 1, namely that she is not resident in the UK in 2020-21 because she satisfies the third automatic overseas test, not only will she not fall within case 1 but it will mean that Prince Harry will not satisfy case 2.

Case 3

Paragraph 46 sets out case 3 which is aimed at an individual who leaves the UK, makes a substantial break in his connection with it, and creates a sufficient link with another country. The first condition of case 3 to be satisfied is that Prince Harry was resident in the UK in the previous fiscal year, 2018-19, which we have assumed he was.

The second condition is that, at the start of the relevant year, 2019-20, he has had one or more homes in the UK but has ceased to have any home in the UK during that year and from that time, he has no home in the UK for the rest of that year. At the start of 2019-20 he had a home, Frogmore Cottage, in the UK but did he cease to do so during this year? Again we are back to the question of what is a home. If Frogmore Cottage remains his home, case 3 will not be satisfied.

If he ceased to have a home in the UK, for example from 20 January 2020, the third condition is that he must not spend more than 15 days in the UK in that part of the year which began when he ceased to have a home in the UK. On the assumption that he returned to the UK on 25 February and he left on 9 March he will have spent 13 days in the UK. Therefore, as long as his stay is not extended this condition will be satisfied.

The fourth condition is that he must not be resident in the UK in 2020-21.

The fifth condition is that at the end of the period of six months beginning with the day he ceased to have a home in the UK, he has a sufficient link with a country overseas. We shall assume that that date is 20 July 2020.

An individual has a sufficient link with a country overseas if and only if:

- he is considered for tax purposes to be a resident of that country in accordance with its domestic laws;
- he has been present in that country at the end of each day of the six-month period (this condition will not be satisfied because he was in the UK in February and March); or
- his only home is in that country. Again we are back to the concept of what is a home and whether his only home is in Canada.

Having considered cases 1 to 3, it can be seen that there is at least a reasonable possibility that none of the cases will apply.

The fiscal year 2020-21

Taking each automatic overseas test in turn, he will satisfy the first automatic overseas test if he does not spend 16 or more days in the UK in 2020-21 and stays alive. He will not satisfy the second automatic overseas test because he was resident in the UK in all of the three fiscal years before 2020-21. The third automatic overseas test will be satisfied if:

- he works sufficient hours overseas as assessed over 2020-21;
- during the fiscal year there are no significant breaks from overseas work;
- he spends less than 31 days doing more than three hours work in the UK; and
- he spends less than 91 days in the UK.

The fourth and fifth automatic overseas tests, which apply only if the individual dies during the fiscal year concerned, are not considered.

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With regard to the automatic UK tests, the first test will not be satisfied provided the prince spends less than 183 days here.

The second UK automatic test will be satisfied if Frogmore Cottage is his home in the UK and the following conditions are satisfied, namely:

- a) that home is one where he spends a sufficient amount of time in the fiscal year, that is at least 30 days when he is present there on that day for at least some of the time; and
- b) there must be at least one period of 91 consecutive days in respect of which the following conditions are satisfied:
 - i. the 91-day period in question occurs while he has that home;
 - ii. at least 30 days of that 91-day period fall within 2020-21; and
 - iii. throughout that 91-day period condition A or B (or a combination) is met.

Conditions A and B

Condition A is that he had no home overseas.

Condition B is that he has one or more homes overseas, but each of those homes is a home where he spends no more than a permitted time.

As we can see, the questions of whether he will continue to have a home in the UK is complex.

As long as he does not work sufficient hours in the UK he will not satisfy the third automatic UK test. The fourth automatic UK test applies only when an individual dies in the year and is not considered.

We shall assume that he will not meet any of the automatic overseas tests or any of the automatic UK tests in 2020-21. We, therefore, need to consider the sufficient ties test. Because Prince Harry has been resident in the UK in one of the three preceding fiscal years there are five UK ties to consider, namely:

- the family tie;
- the accommodation tie;
- the work tie;
- the 90-day tie; and
- the country tie.

The UK ties

Prince Harry is unlikely to have a family tie because the duchess and his son, Archie are likely not to be resident in the UK.

He will satisfy the accommodation tie, having a place to live in the UK – namely Frogmore Cottage – which will be available to him during 2020-21 for a continuous 91-day period, if he spends one night in the cottage. We shall assume that he will have this tie.

As long as there are less than 40 days on which he does more than three hours of work in the UK he will not have a work tie in 2020-21.

He will have a 90-day tie for 2020-21 because he will have spent more than 90 days in the UK in both 2018-19 and 2019-20.

Planning point

If the automatic tests are not satisfied, consideration of the sufficient ties test will be required to determine the length of time that a taxpayer can spend in the UK without becoming resident here.

He will satisfy the country tie if the country in which he meets the midnight test for the greatest number of days in 2020-21 is the UK (he will meet the midnight test in a country for a day if he is present in that country at the end of that day). If he spends most of his time outside the UK he will not satisfy this tie so we shall assume that he will not have a country tie.

So, based on our assumptions, it is likely that Prince Harry will only have two ties in 2020-21: the accommodation tie and the 90-day tie. If so, he could spend up to 120 days in the UK without satisfying the sufficient ties test but that, of course, will be qualified if he wishes the split year treatment under case 1 to apply to him for 2019-20.

Conclusion

The factors above demonstrate the difficulties for any taxpayer, even a member of the royal family, in obtaining any kind of certainty in relation to the application of the SRT. A particular complication in the case of Prince Harry is his ability to occupy Frogmore Cottage. Our usual advice to our clients who wish to cease to be UK resident is to sell or let what has previously been their UK home on commercial terms so that they cannot occupy it and to obtain a permanent home, whether it be purchased or on a long term rental, in the overseas country.

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In all residence cases, the importance of record keeping is paramount, especially when distinguishing between what is work and what is not. This will be particularly significant in Prince Harry's case. It is important to take advice well in advance of any proposed change of residence and, because of the imprecision of many of the conditions by which fiscal residence is determined, an individual should make the fullest possible disclosure to HMRC of the facts that are relevant to determining his residence status. ●

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