

Growing like Topsy

SHARON MCKIE and **SIMON MCKIE** discuss the statutory residence test in the Finance Bill.

On budget day, it was confirmed that a statutory residence test (SRT) would be included in the Finance Bill but that it would include “amendments to the concepts of full-time work, international transportation workers and split year status”. When the Finance Bill was published, in addition to the announced amendments, the SRT provisions contained changes to the second automatic UK test, a new fifth automatic overseas test and numerous smaller changes.

This article explains the major changes and notes some important areas where the legislation has not been changed, despite the inadequacies which have been identified by the professional bodies.

Sufficient hours

In the draft legislation published on 11 December 2012 (December schedule), both the third automatic UK test and the third automatic overseas tests used the concept of “full-time work” which was defined in part II of the draft schedule. The FB schedule adopts the same approach, but has replaced the phrase “full-time work” with “sufficient hours”. The rules for calculating “sufficient hours” are now found in the automatic tests, but they use the phrase a “reference period” which is defined in part II. The definition of a “significant break” from work has been moved out of the automatic tests in part I and into the key concepts in part II.

The December schedule, in calculating whether an individual works full time in a period, took account of periods of annual leave, parenting leave and sick leave. It did not take account of weekends which related to such leave. For example, in calculating average weekly hours, where a person takes ten days of annual leave, consisting of two periods of five days divided by a weekend on which he is not required to work under his employment contract, the divisor in the calculation was reduced by the ten days of leave but was not reduced by the weekend falling in the middle of them.

KEY POINTS

- Changes to “sufficient hours”.
- Issues for international transportation workers.
- What is a home?
- The accommodation tie should be clarified.



It is clear that HMRC were not aware of this fault at the time they published the draft guidance on 18 December 2012, because the examples, which were based on the December schedule, calculated the reduction by reference to complete weeks, thus effectively including a reduction for related weekends.

Paragraph 28 of the FB schedule contains provisions to take account of what it calls “non-working days embedded within a block of leave” and to provide for the reduction of annual leave, etc to be rounded down to the nearest number of whole days. These provisions, however, are restrictively drawn because they will not apply where the number of leave days which surround the embedded days is less than six. They also do not take account of non-working days preceding and following a period of leave; for example, no reduction would be made for the weekends on either side of ten days of annual leave covering two consecutive working weeks. It is only the weekend in the middle of the ten days that is taken into account.

What is more, the provisions in respect of embedded days do not deal adequately with the self-employed. This reflects a larger problem with the provisions concerning what we must now call “sufficient hours”. No significant changes have been made by the government in response to the representations which it received in this area.

The provisions also do not deal with periods of absence from work other than annual leave, parenting leave, sick leave or embedded non-working days. Therefore they do not provide a reduction for leave which is agreed ad hoc, for compassionate leave or for leave for other reasons, such as leave granted to allow employees to take examinations, or to take part in major sporting events.

The provisions regarding gaps between periods of work are also highly restrictive, applying only where the gap is one between two employments. They do not apply to gaps between

working in a trade and working in an employment or between working in two separate trades. In fact, in one way the provisions have been made even more restrictive than they were before. The December schedule restricted the reduction which could be made for gaps between employments to a maximum of 15 days in respect of any one gap. To this, the FB schedule adds a further restriction to 30 days for the aggregate reduction in respect of all such gaps.

Third automatic UK test

Changes have been made to the third automatic UK test to take account of days on which the individual concerned does more than three hours work overseas, even if he also does work in the UK on that day. An additional condition has been added. This requires that there be at least one day in the fiscal year concerned on which the individual does more than three hours work in the UK.

Rather bizarrely, under the December schedule, it had been possible for an individual to meet the test in a year in which he did no work in the UK whatsoever. The reason for that is that the test operates by reference to a 365-day period, which need fall only partly within the fiscal year concerned. It is still possible, however, for the test to be met in respect of a fiscal year in which an individual works in the UK for just over three hours on one day.

No other significant changes are made to the third automatic UK test other than the changes in respect of “a relevant job” which are discussed below.

Third automatic overseas test

The application of the significant breaks rule to the third automatic overseas test had been criticised because it could result in the test not being met in circumstances where a person works for very long hours for a period followed by an extended break or where a break is due to unforeseen and uncontrollable circumstances. These faults in the legislation have not been addressed.

A relevant job

The December schedule included a series of provisions relating to “international transportation workers” as defined in part II. In particular, the third automatic UK test and the third automatic overseas test could not be met by such a worker. There were a number of difficulties in the definition of an international transportation worker.

The draftsman has now replaced the term “international transportation worker” with “a ‘relevant’ job”. It is not entirely clear why this change of terminology has been made. In relation to the self-employed, “job” is an even less apposite term than “worker”.

A major criticism of the December schedule was that a person whose work was performed entirely outside the UK because he made journeys between two foreign countries could still be an international transportation worker and therefore excluded from meeting the third automatic overseas test. The exclusions of individuals who have “a relevant job” from the third automatic

UK test and the third automatic overseas test now do not apply where “at least six of the trips that [the individual concerned] makes in [a fiscal year] as part of [the relevant job] are cross-border trips that either begin in the UK, end in the UK or begin and end in the UK”.

That provides a very limited relief. Yet it is still the case that an individual who works substantially all of his time outside the UK, but who happens to make more than five job-related trips beginning or ending in the UK, will be excluded from the benefit of the third automatic overseas test. The policy reason for this exclusion is obscure.

“The professional bodies expressed particular concerns about the second automatic UK test.”

Under the December schedule, both the self-employed and employees could be international transportation workers. Whether an employee was one depended on the nature of the duties of his employment. A person was excluded from the third automatic UK and the third automatic overseas tests if he was an international transportation worker at any time in the fiscal year, it was therefore necessary to determine from moment to moment whether a person was an international transportation worker.

The duties of the employment had to be determined at a series of particular points in time. That raised the question of whether to look at the duties of the employment generally or at the duties to which the worker was subjected at the particular point in time concerned. Neither construction worked entirely satisfactorily. The test has been reordered so that it looks both at the duties of the employment and the trips which were actually made in performing those duties.

This change does not entirely resolve the difficulties, but it has made them less acute.

The international transportation worker provisions did not work satisfactorily in relation to the self-employed and no significant changes have been made in respect of these.

Second automatic UK test

In their responses to the December schedule, the professional bodies expressed particular concerns about the second automatic UK test. The Institute of Chartered Accountants in England and Wales (ICAEW) pointed out the anomalies which would result from it; the Society of Trust and Estate Practitioners (STEP) described it as “very unsatisfactory”; and the Chartered Institute of Taxation (CIOT) said “we have a problem understanding the second automatic UK test”.

Particular concerns were expressed about the dual condition. In the FB schedule, the second automatic UK test is slightly reorganised. The relevant parts of the equivalent of the dual condition now provide that:

“There is at least one period of 91 (consecutive) days in respect of which [various conditions are met] ... [and] ...

Throughout that 91-day period, condition A or condition B is met or a combination of those conditions is met.”

Condition B is that:

“(a) [the individual] has one or more homes overseas, but

“(b) each of those homes is a home where [the individual] spends no more than a permitted amount of time [in the fiscal year concerned].”

Although the legislation has been recast, it preserves an ambiguity in the December schedule about which the CIOT made a representation in February. For condition B to be met throughout the 91-day period, is it sufficient that the individual should spend no more than the permitted amount of time at the overseas home during the fiscal year concerned, or must he do so during the part of the 91-day period which falls within that fiscal year?

The answer to that question depends upon whether it is possible to meet a condition “throughout [the] 91-day period” by reference to a state of affairs existing outside that period.

“It is now apparent that the test will not achieve its target of being ‘clear, objective and unambiguous’.”

Fifth automatic overseas test

Under the December schedule, the fourth automatic overseas test applied where the individual concerned died in the fiscal year.

The FB schedule preserves the fourth automatic overseas test, but a fifth automatic overseas test has been added which also applies where the individual dies in the fiscal year.

Unlike the fourth test, the fifth test does not require the individual to have spent fewer than 46 days in the UK in the fiscal year, but contains another requirement. It is, loosely, a test which applies to those who die during the year and who have become non-resident in a previous year because they have gone to work abroad.

The individual must either:

- have been non-resident in the two preceding fiscal years because he met the third automatic overseas test for each of those two years; or
- have been non-resident in the preceding fiscal year by reason of meeting that test, and the year before that must have been a split year within case 1 of the split year rules

and the individual would have met the third automatic overseas test in the fiscal year of death if that test were modified so as to apply to a person who dies during the year.

Split year rules

In the December schedule, the split year rules, which are an attempt to give statutory form to the split year concession ESC A11, contained five cases defining sets of circumstances in which there would be a split year; there are now eight.

Case 4 in the December schedule has now been divided into cases 4 and 5, cases 6 and 7 have been inserted, and what was formerly case 5 has been renumbered as case 8.

The new cases 6 and 7 essentially deal with those becoming resident again after working abroad (case 6) and with their accompanying partners (case 7).

Significant remaining faults

The two most important areas where changes have not been made by the FB schedule are in respect of the accommodation tie and of the definition of a “home”.

The accommodation tie is full of ambiguities and of concepts which are incapable of precise definition including “a holiday home or temporary retreat (or something similar)” and “accommodation [which] is otherwise available” to the individual concerned.

This tie also uses the concept of a “home” which is fundamental to the operation of the SRT more generally, forming a key element of the second automatic UK test and the split year rules in addition to the accommodation tie.

“Home” is a word which can bear a wide range of meanings with small areas of overlap between them. For that reason it is entirely inappropriate to be used as a key concept in a statutory test, the purpose of which is, as the Exchequer Secretary of the Treasury David Gauke, said, to “be clear, objective and unambiguous”. It is for that reason that the CIOT, the STEP and the ICAEW have all strongly criticised the use of the concept in the SRT.

In spite of this, no clear and exhaustive definition of a “home” in the test has been provided.

The SRT is an improvement on the current highly uncertain position, but it is now apparent that the test will not achieve its target of being “clear, objective and unambiguous”. The government started its consideration of the test by rejecting, for reasons which remain opaque, a simple arithmetical test modelled on the Irish and US tests.

By starting in the wrong direction the government has arrived at the wrong destination, missing a once in a generation opportunity to achieve, at no tax cost, a significant simplification of our tax system. ■

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