

UK Tax Facts

Introduction

Taxation in the UK is mostly at a national level with property taxes (rates) being raised by local authorities at a regional level. The national UK tax system is administered by the Inland Revenue.

Tax Year

6th April to 5th April.

Assessment Basis

Individuals who are UK resident, ordinarily UK resident and domiciled in the UK are taxable on their worldwide income. The UK requires all tax payers to file a tax return and operates a self-assessment regime. Although individuals who are only in receipt of employment and savings income are not usually required to file a return. Married couples are treated separately for taxation purposes and are responsible for completing their own tax returns.

Income Tax

Individuals are subject to income tax on all their taxable income. Individuals benefit from tax free allowances, dependent upon age and marital status. In addition certain expenses are allowable against taxable income, for example pension contributions. Income from married couples is not aggregated, each being taxed on an individual basis, although couples do receive an additional tax free allowance if either spouse is 65 or over.

A progressive tax scale is applied to successive bands of taxable income with income tax rates ranging from 10% to 40%. The progressive tax scale is applied to three income bands, namely the 'starting rate band' (the first £2,020 of taxable income), the 'basic rate band' (the next £29,380) and the 'higher rate band' (taxable income in excess of £31,400) (limits are in respect of the 04/05 tax year). The actual rate of tax applied to income depends upon the type of income being taxed. Income from employment and other income (excluding dividends, savings income and capital gains) are taxed at 10%, 22% and 40% in respect of each of the three income bands. Different rates may apply to other types of income (i.e. dividend, savings income and capital gains), as detailed below.

Taxation of Investment Income

In general, investment income is taxable and is included with other income when calculating an individual's income tax liability. However, the rate of tax applied to investment income depends upon the type of income and into which tax band it falls. In determining which band investment income falls into, the different types of income are layered with employment and other non-savings income being considered first, then non-dividend savings income, and finally dividend income.

Dividends are taxed at 10% in respect of the starting rate and basic rate bands with 32.5% applicable to higher rate band dividend income (04/05 tax year). UK company dividends are paid net of 10% tax with an attaching tax credit. The tax credit may be used to offset any tax due.

Other savings income is liable to income tax rates of 10%, 20% and 40% in respect of the three taxation bands (04/05 tax year). Interest credited by banks and building societies is paid net of 20% tax.

Tax on Property Rental Income

Rental income is taxed on the same basis as employment income with tax being applied to rental income received, less any allowable expenses incurred. In determining into which tax band rental income falls it is considered after employment income but before savings income and dividend.

Wealth Taxes

There are no wealth taxes in the UK.

Capital Gains Tax

Capital gains are aggregated with taxable income and added to an individual's taxable income. The first £8,200 (04/05) of capital gains in a tax year is exempt. Gains on an individual's principal residence are also exempt.

Capital gains are taxed according to the income tax band into which the gain falls and may be taxed at up to 40%. In determining the tax band into which capital gains falls it is layered on top of all other types of income. The rate of tax applied to capital gains is reduced according to the length of time the individual has held the asset. If a business asset has been held in excess of 2 years the maximum rate of capital gains tax is 10%.

Inheritance and Gift Tax

Inheritance tax is a cumulative levy on lifetime gifts and assets (including the principal residence) passing between owners on death. Cumulative transfers are taxed at 40%, although the first £263,000 (04/05) is free from inheritance tax. Gifts are generally included in the value of the estate for inheritance tax purposes although they are generally subject to a decreasing tax charge if the donor survives 3 years and will generally be exempt if the donor survives 7 years following the date of gift.

Transfers between spouses are generally exempt, unless the spouse has a foreign domicile in which case only the first £55,000 is exempt. Certain lifetime gifts are also exempt up to £3,000 per annum. Other exemptions may apply, for example with regard to wedding gifts.

In certain circumstances lifetime gifts may be subject to inheritance tax and/or capital gains tax.

Regional and Municipal Taxes

There are no regional taxes in the UK.

Property Taxes

Council Tax on residential property and Business Rates on non-residential property are charged by the local authorities. Rates vary according to the region.

Stamp Duty/Transfer Tax

Stamp duty is charged in the UK on the execution of documents transferring property. The standard rate for share sales is 0.5%.

With effect from 1st December 2003 Stamp Duty on real property was replaced by the Stamp Duty Land Tax (SDLT). This new tax is not dependent upon documents being stamped but is directly enforceable on an acquisition of land. The purchaser is liable to pay SDLT. The rate of SDLT varies between nil and 4% depending upon the value of the property. Residential property valued less than £60,000, or £150,000 in respect of non-residential property, is taxable at the nil rate, with the 4% rate applying on properties valued at £500,000 or more. Non-residential property located in certain disadvantaged areas of the UK is exempt.

Lease duty is payable on the lease of property at the rate of 1% for residential properties with a rental net present value of over £60,000 and £150,000 for non residential properties.

Sales Tax

Sales tax (VAT) of 17.5% is generally added to the sale price of goods. Some sales are outside the scope of VAT or are taxed at a lower rate.

Social Security Contributions

In the UK social security contributions are known as National Insurance Contributions (NIC). Individuals are liable to pay social security contributions based upon their earnings. Social security rates on successive bands of earnings are 0%, 11% and 1%.

Unlike a number of other countries social security contributions in the UK are not deductible from taxable income.

Taxation of Expatriates Living in the UK

The scope of UK taxes with regard to an expatriate individual living and working in the UK will depend upon the individual's residency, ordinary residence and domicile status. There are a number of tests to determine an individual's classification in the UK.

Residence

In order to be tax resident in the UK an individual must be physically present in the UK at some time during a tax year. An individual's residence status in other countries is irrelevant to determining UK tax residency. In order to be classified as tax resident in the UK an individual must meet one of the following criteria:

- If an individual is physically present in the UK for at least 183 days in the current tax year they will be classed as resident.
- If an individual intends to work in the UK for 2 years or more they will be classed as resident from the day of arrival in the UK.
- If an individual visits the UK, for any reason, in four consecutive tax years and the visits average more than 90 days per year they will be classed as resident from the start of the fifth year. Alternatively if an individual arrives in the UK with the intention of spending more than 90 days per year in the country they will be treated as resident from their day of arrival.

Whilst an individual's tax residency elsewhere is irrelevant in determining UK tax residency, if an individual is classed as resident in another country, the terms of any tax treaty may determine where the individual is taxed.

Ordinary Residence

The definition of ordinary residence considers the longer-term, compared to residence. Ordinary residence considers an individual's 'habitual' residence rather than an individual's residence in a particular tax year. In order to be classified as ordinarily resident in the UK an individual must meet one of the following criteria:

- If an individual arrives in the UK with the intention of staying three years or more they will become ordinarily resident in the UK from their day of arrival in the UK.
- If at the time of arrival an individual intends to stay less than three years, or has no intended fixed length of stay, they will not be classed as ordinarily resident and will normally retain this status for the first four tax years in the UK. Such an individual would become ordinarily resident at the start of the tax year following the third anniversary of their arrival in the UK.
- If an individual acquires accommodation (by buying a property or acquiring a lease of 3 years or more) available for his/her use then they will normally acquire ordinary residence status either from their date of arrival in the UK or the start of the tax year in which such accommodation becomes available.

Domicile

An individual's domicile indicates the country which an individual considers to be their permanent home. Under UK law every individual has a country of domicile and this impacts upon their liability to certain taxes, such as inheritance tax. Domicile is different to residence and rarely changes. An individual usually acquires their father's domicile at birth and then retains this for life unless an individual severs their ties with their original country of domicile and establishes a permanent home in another country.

An expatriate working in the UK for a limited period, with no intention to settle in the UK, will generally be regarded as non-UK domicile. An individual may, however, be deemed to be domiciled in the UK if they are UK tax resident for 17 out of the last 20 tax years.

The taxation basis applicable to the different types of income and gains depends upon an individual's status with regard to residence, ordinary residence and domicile. An individual who is UK resident, UK ordinary resident and UK domicile will be taxed on worldwide income and gains, as well as inheritance tax being based upon the value of their worldwide assets.

With regard to an expatriate non-UK domiciled person living and working in the UK, the tax treatment of their employment income and gains will depend upon their UK tax residence status and whether the income is generated by UK or non-UK employment duties:

	Non-resident	Resident but not ordinarily resident	Resident and ordinarily resident
UK employment income	Taxable in UK	Taxable in UK	Taxable in UK
Non-UK employment income	Not taxable in UK	Not taxable in UK unless remitted into the UK.	Taxable in UK

Non-UK employment income in respect of a resident and ordinarily resident expatriate may, if the non-UK employment is subject to a separate employment contract and no duties under the contract are performed in the UK, only be subject to UK tax if remitted into the UK.

Non-UK domicile expatriates living in the UK will be taxed upon all of their UK sourced investment income. Non-UK sourced investment income will only be subject to UK tax if it is remitted into the UK, subject to any relief which may be due in respect of foreign tax paid.

Any capital gains arising from UK situated assets will be liable to capital gains tax if the non-UK domicile expatriate is resident or ordinarily resident in the UK. Any capital gains arising from non-UK situated assets will not be liable to UK tax unless the gains are remitted into the UK.

An expatriate's liability to UK inheritance tax depends upon their domicile. An individual who is UK domiciled will be liable to inheritance tax on their worldwide assets, whilst a non-UK domicile expatriate living in the UK will only be liable to UK inheritance tax on their UK situated assets.

An expatriate's liability to pay National Insurance Contributions (social security) generally depends upon the expatriate's country of origin and length of stay in the UK. The countries of origin are split into the following groups:

- EEA/EU – generally an expatriate will continue to pay social security contributions in their home state if they only expect to stay in the UK for less than 12 months. Under certain circumstances this period may be extended up to a maximum of five years.
- Countries with a social security treaty with the UK – the situation will be dependent upon the terms of the treaty but in general an expatriate will not pay UK National Insurance Contributions if they are continuing to contribute in their home country.
- Any other country – an expatriate may not have to pay National Insurance Contributions for the first 52 weeks but will be required to pay UK contributions once this period has ended.

Expatriate Financial Planning

As a whole, the UK tax regime is less onerous for expatriates who are not resident, not ordinarily resident or not domiciled in the UK, compared to the regime for individuals who are UK resident and domiciled, with generally only UK sourced income and gains being subject to UK tax. An expatriate should take care to plan when they move to the UK and also the number of days they spend in the UK in a tax year.

In addition, if you are an expatriate currently living in or considering moving to the UK, you should review your finances with a suitably qualified financial advisor. In particular, if you are about to move to the UK, you should plan and review your finances before making the move. You may wish to consider offshore investments, including offshore life products, in order to manage your tax liability and/or control when tax charges are made, as well as considering options available to you for estate planning.

Whilst the specific benefits of an offshore life product will depend upon your individual circumstances they do offer a number of potential benefits:

- Investments in an offshore life product grow virtually free of tax throughout the time the product is held, suffering only a small amount of irrecoverable withholding tax on investment funds located in certain countries.
- They allow you, in general, to manage when you take benefits and potentially to defer the benefits to a period that may be more advantageous to you from a taxation perspective.

- Offshore products often feature a strong range of the life company's own individual offshore funds and managed offshore funds specifically tailored to fit with the spread in clients' attitudes to risk. Offshore products also offer access to household name fund managers, including many international and specialist fund managers.
- An offshore product has the flexibility to adapt to changes in your individual circumstances, including changes in your residency status.
- Most companies offering offshore life products are subsidiaries of global financial services companies.
- The offshore life companies are regulated in first class jurisdictions which benefit from strong regulatory controls.

Your independent financial adviser can help you ensure that you maximise the financial benefits of your expatriate status and help you to assess if offshore life products are right for your individual circumstances.

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