Institution **CIOT - CTA**
Course **APS Taxation of Individuals**

Event **NA**

Exam Mode **OPEN LAPTOP + NETWORK**

Answer-to-Question-_1_

[CLIENT'S ADDRESS]
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CHARTERED TAX
ADVISERS

2 November 2023

Dear Stefan

We are writing to you today to follow on from our meeting on 31 October 2023 to advise you on the following areas:

- Your UK residency and domicile status and claiming of the remittance basis.
- The disposal of your half share in your property in Leipzig and the disposal of your Kremet GmbH shares.
- Advice on pension contributions.

EXECUTIVE SUMMARY

- You are UK resident for the 2023/24 tax year.
- You are non-UK domiciled under general law and can claim the remittance basis in respect of your overseas income and gains.
- The remittance basis will tax your UK income and gains on the arising basis but will only tax your overseas income and gains when it is remitted to the UK.
- Claiming the remittance basis will mean that you lose eligibility to claim the personal allowance and the annual exempt amount in the year of claim and remitted income will be taxable at the non-savings tax rates.
- You should make a claim under the remittance basis for 2023/24 and you will save income tax of £722.

- By making the remittance basis claim you will also save capital gains tax of £1,916 that have arisen in Germany.
- You will also not pay capital gains tax in Germany on the diposal of your property under the double taxation agreement.
- The disposal of your shares in German will give rise to a loss in the tax year. This loss will be lost as we have advised you to claim the remittance basis in 2023/24 which will mean that you will not be subject to UK CGT on any overseas disposals.
- You have the opportunity to claim an election under s.16za in respect of your overseas losses. This election must be made within 4 years of the first year that you claim the remittance basis. We would only advise making this election if you generate substantial losses overseas to offset against gains in the UK. This is because the overseas losses offset against historic gains in priority, being your German property disposal.
- Following the disposal of your shares and property we recommend that you hold your proceeds in a new overseas account and avoid remitting any of these gains to the UK. If these gains are remitted to the UK an capital gains tax charge will arise even if you are no longer claiming the remittance basis.

<u>Pension</u>
- Individuals have an annual allowance of £40,000 per tax year to input into their pension scheme, less subject to tapering.
- We have calculated that you have unused annual allowance to carry forward, and including 2023/24 of £123,308.
- If you claim the remittance basis, your gains and losses arising in German will not be subject to tax in the UK or in German. This gives you net proceeds to invest of £187,500. Only invest up to £123,308 in the tax year.
- You can make a contribution into either pension schemes, however if you contribute into your UK pension scheme this will give rise to a remittance on the value that you contribute.
- If you make an investment into your German pension then this will not be a remittance and will be outside of UK tax.

Inheritance tax

- Non-domiciled individuals are outside the scope of UK IHT on their overseas assets.
- Only your UK situs assets will give rise to IHT in the event of your death.
- You should therefore keep as many assets outside of the UK to reduce exposure to UK IHT on your estate for your nephew.
- You could also consider setting up an overseas excluded property trust for the benefit of your nephew as this would be outside the scope of UK IHT.

Other recommendations

- We recommend that you amend your 2022/23 tax return as you have under 31 January 2024 to do so. You can save income tax of £1,306.
- If you wish to save further income tax you can make investments in EIS/SEIS/VCT or other tax efficient investment streams by remitting income or capital to the UK and investing within 45 days under the business investment relief. If you do not invest the funds within 45 days you will suffer a remittance charge in the UK.

SECTION A: RESIDENCY AND DOMICILE

Individuals in the UK a liable to income tax based on their UK residency status. UK residency status is determined by the statutory residency test. On the basis that you arrived in the UK on 1 September 2020 and have been working full time in London from this date, and have a home in the UK, you are considered to be UK resident.

UK resident individuals are liable to UK income tax on their worldwide income and gains on as they arise. This means that you are liable to UK income tax on your German income as well as UK capital gains tax ("CGT") on disposals made overseas.

Domicile is a slightly more complex area. The domicile of an individual is a concept under general law and is determined based on your father's domicile at birth. You have informed us that your domicile is German and therefore you are not domiciled in the UK.

There are instances where your domicile can change and that would be if you choose to be domiciled in the UK (domicile of choice). This would mean that you server all of your ties with German and choose to settle permanently in the UK. On the basis that you have stated that you plan to return to Germany in the future, this will not apply to you.

Secondly, if you are a long-term UK resident you will become deemed domicile in the UK under general law. You will become deemed domicile in the UK when you have been UK resident for 15 of the preceding 20 tax years. As you have only been a resident in the UK since 2020/21, this will not apply to you until the start of the tax year 6 April 2036.

<u>Remittance basis</u>

If you are UK resident but not UK domiciled there are special rules which apply to your foreign income and gains. In these circumstances you have a choice as to whether to use the arising basis of taxation or the remittance basis of taxation. If you choose the remittance basis for a tax year you will pay UK tax on the following:

- Any income or gains that arise in the UK
- Any foreign income and gains that you or another relevant person, brings into the UK, even if that remittance occurs in a later year when you are not claiming the remittance basis.

The remittance basis is a claim that is made year on year and should be made by the 12 year anniversary of 31 January following the end of the tax year. Therefore, for 2023/24 you have until 31 January 2026 to make a claim to be tax on the remittance basis.

If you choose to claim the remittance basis of taxation it will mean that you lose eligibility to claim your personal allowance of £12,570 and your annual exempt amount for capital gains tax of £12,300.

When income is remitted to the UK from overseas regardless of the source of income, you will pay income tax under the non-savings tax rates of 20%, 40% and 45%. Capital gains tax are remitted will be liable to tax under the CGT rates 20% and 28%.

If unremitted income income in a year is less than £2,000 the remittance basis will be applied automatically and you will still be entitled to your personal allowance and annual exempt amount.

Based on your income tax position alone, we would recommned that you claim the remittance basis in 2023/24 as you will save income tax of £722 please see Appendix 1.

Due to the level of your taxable income if you did not claim the remittance basis, your personal allowance has suffered tapering. When total your income exceeds £100,000, your personal allowance will be reduced by £1 for every £2 exceeded. As a result if you did not claim the remittance basis your personal allowance would be tapered to £2,750.

<u>Remitting funds to the UK</u>

As you came to the UK on 1 September 2020 (2020/21 tax year) you were no resident for the years prior to this date. This means that any income or capital that arose outside of the UK before you became UK resident will be treated as "clean capital" and can be remitted to the UK without any tax implications.

Further points to note - the remittance basis charge

The remittance basis charge can be reconsidered every year depending on what is most beneficial for you in that tax year. Once you have been UK resident for 7 out of the preceding 9 tax years you will be subject to the remittance basis charge of £30,000. Once you have been resident for 12 out of the preceding 14 tax years you will be subject to a charge of £60,000. Neither of these charges will impact you for a while however it is important for us to mention.
If do find that you are still a resident on 6 April 2028, this will be the first year that you would be subject to a charge.

SECTION B: DISPOSAL OF YOUR ASSETS

When paying tax on the arising basis, you are liable to UK income tax on your worldwide income and gains as they arise. This would mean that as a UK resident individual you would be liable to UK CGT on the disposal of your property in Germany.

Disposal of your property in Leipzig and Kremet GmbH shares

General principals

As you own your property in Germany with your Brother as joint owners and you are selling your share of the property to your brother (a connected person). This transaction will be deemed a disposal between connected parties.

The proceeds that you receive from your brother of £150,000 will be disregarded and your share of 50% of the market value of the property at the date of disposal will be used when determining your gain. As you are selling 50% of the property back to your brother, you are able to claim a 10% tenanted deduction to reduce the market value of the property as the property is noy physically being sold on the open market.

The base cost of the property will be the probate value of £270,833 at the date that you both inherited the property on 1 November 2007. You will be able to claim 50% of this cost against the deemed proceeds to arive at your gain.

As you occupied the property as your main residence for a period of time between 1 November 2007 to 1 March 2010, private residence relief ("PRR") is available. This relief will restrict all or part of the gain that arises on the property. Additionally, as you occupied the property as your main residence at some point during your ownership you can also claim the final 9 months as deemed occupied.

As you never rehabited the property, you are not able to claim any other periods of absense as deemed absense and therefore we have calculated that your total deemed occupation of the property is 37 months see Appendix 2. We have calculated disposal of the property as if it were to take place in December 2023. The gain that is subject to tax in the UK under the arising basis would be £38,309. As this is a disposal of a UK residential property and you are a higher rate tax payer the capital gains tax due will be 28%.

As the value of your shares in Kremet GmbH have decreased in value we have also reviewed their position should you wish to dispose of these shares, see appendix 2. When a disposal of shares arises, the share matching rules will apply. These rules match a disposal of shares as follows:

- first matched with a purchase of shares on the same day
- matched with shares purchased within 30 days
- shares are accumulaed in a s.104 share pool and the diposal will be treated as a part disposal from the total value of the pool at that date.

As your shares give rise to a loss, and you also have losses on the shares from 1 August 2015, on the basis that these losses have not been offset against any other gains these losses can be offset against the disposal of your German property. The net taxable gain is £3,509 see Appendix 3.

This gain would be liable to UK CGT if you claim the arising basis and you would be able to claim the annual exempt amount of £12,300.

Claiming the remittance basis

Alternatively, if you claim the remittance basis as advised above based on your income position you will not be liable to UK CGT on the disposal of your German property. You will only be exposed to UK CGT if you remit any of the proceeds to the UK. This would apply if you remit the proceeds to the UK in a tax year that you are not claiming the remittance basis.

Therefore by claiming the remittance basis in 2023/24 you will save income tax and capital gains tax of £722 + £1,916 = £2,638.

The proceeds that you receive from the disposal of your property and shares should be paid into a new account set up in German. It is important to keep different sources of income in seperate accounts so as to not create a mixed fund account. If income or gains are remitted to the UK from a mixed fund account they will be taxable under the mixed fund rules.
These rules tax income and gains in the following way:

- current year income that has not been subject to tax
- current year gains that has not been subject to tax
- current year income and gains that have been subject to tax
- previous years income and gains
- clean capital

We therefore advise that your gains are paid into a seperate bank account and not remitted to the UK whilst you are UK resident.

Claiming losses

When claiming the remittance basis in the UK, it means that you are not subject to UK CGT on overseas gains. It also means that overseas losses are not allowable.

An election can be made under s16za to allow all overseas losses to be carried forward and offset against any gains that arise in the UK.

This election must be made within 4 years of when you start claiming the remittance basis. Therefore, if your first year claiming the remittance basis is 2023/24 you have until 2026/27 to make an election to utilise your losses.

If this election is made, historic gains will be offset by your overseas losses in priority, therefore the loss that has arisen on your German property disposal will be offset first. We therefore only recommend that you make this election if you make any large investments overseas that generate a large overseas loss will make the election beneficial.

If this election is claimed you will need to inform HMRC of all of your historic capital disposals which may be something that you wish to consider.

Future year self assessment tax return

Following on from the disposal of your German property and German shares you will no longer have overseas rental income and dividends. If you income levels in 2024/25 remain consistant with 2023/25 and your savings are £500 it may not be advisable to

claim the remittance basis in 2024/25.
This is because you will lose eligibility to claim your personal allowance, albeit it will likley be tapered slightly. The £500 of interest income if you remain a higher rate tax payer will be covered by your personal savings allowance and no income tax will be due in the UK.

SECTION C: CONTRIBUTION TO PENSION SCHEME

Pension contributions can be made in a tax year to a registered pension scheme.

Pension contributions made by your employer are an exempt benefit but will be included in your total contributions when considering the annual exempt amount and any pension savings tax charge.

Pension contributions made by you into your pension scheme via your gross salary will offer you income tax relief at source.

Individuals have an annual allowance of £40,000 per tax year to make contributions into a pension scheme. This allowance will suffer tapering if your threshold income exceeds £200,000 in the tax year and your adjusted income exceeds £240,000. As your income levels for each tax year are below £200,000 your annual exemption will not be tapered.

Additionally, any unused annual exemption from the previous three tax years can also be carried forward and offset against contributions made. The carried forward unused allowance will start from the furthest year in priority, in your case 2020/21.

We have calculated that, you have unused annual allowance carried forward of £94,308 and £29,000 in the current year. This means that you can make a contribution into your pension scheme of £123,308 in 2023/24 without triggering a pension charge.

If you make contributions into your UK pension, these should be made from UK employment income that has been taxed in the UK, or from overseas income and gains that arose prior to becoming resident in the UK in 2020/21. This income will be clean capital and can therefore be remitted to the UK tax free.

If you wish to use the proceeds from the sale of your German assets you will have total proceeds of £150,000 for the property and £37,500 for the shares. You will not suffer tax in Germany on these disposals and therefore have total proceeds of £187,500 to invest should you wish to.

We recommend that you invest your proceeds into your German pension scheme as this will not give rise to a UK remittance. As you do not plan to stay in the UK permanently you will be able to enjoy the proceeds from your German pension when you are no longer UK resident without triggering a remittance in the UK.

Please note that we cannot advise you on the return on your investment, this advise should be sought by a pensions adviser. We can however state that if you remit the proceeds received from the disposal of your German assets to the UK to invest in your pension scheme, this will give rise to a remittance and you will be liable to tax on this amount in the UK.

SECTION D: INHERITANCE FOR HIS NEPHEW

You have mentioned that you would like to leave your whole estate to your nephew as you do not have any children.

Non-domiciled individuals are only liable to UK inheritance tax ("IHT") on their UK situs assets. Any assets situated overseas will not be within scope of your UK IHT.

Based on your current assets this would be your UK ISA, your UK property in London and your UK pension.

If you become deemed domicile under the long term residence rules, which is when you have been UK resident for 15 of the preceding 20 tax years you will be deemed domicile for UK IHT purposes and your worldwide assets will be within scope for UK IHT.

If you plan to leave the UK before this time then your overseas assets will not fall within scope for UK IHT.

You could transfer the funds in your ISA to an overseas bank account and then put these funds into an overseas trust. This would create an excluded property trust ("EPT") and would be outside of the scope of UK IHT. Your nephew can then benefit from the trust.

When/if you become deemed domicile under the long term residence rules this will not trigger the trust to become UK resident and it will retain the EPT status should you wish to continue investing.

Additionally, we further encourage our recommendation to invest your funds in your German pension as a non-domiciled individual the pension will be outside of the scope of IHT.

SECTION D: OTHER RECOMMENDATIONS

We have reviewed your income tax position for 2022/23.

Individuals have until 31 January 2024 to amend their 2022/23 tax return and thus make a claim to be taxed on the remittance basis.

If you have not remitted any of your overseas income from 2022/23 to the UK yet, you can amend your tax return and claim the remittance basis. If you do so you will save tax of £1,306, see appendix 5.

If you would like our assitance amending your tax return, please let us know.

Business investment relief

If you have excess proceeds after contributing into your pension scheme you can remit them to the UK if you are doing so to invest in a qualifying company in the UK.

This company must be unlisted and can qualify for EIS/SEIS/VCT relief.

You can remit proceeds and income to the UK free of tax if you then invest the income within 45 days to the qualifying company.

If you choose to make an investment under EIS/SEIS/VCT for example you will be able to claim income tax relief on your investment at 30%/50%/30% respectively. This may be something that you wish to consider to reduce your tax liability further.

If the shares are disposed of, you must take the remittance out of the UK within 45 days or reinvest it. If you do not this will be a remittance and you will be subject to a remittance charge on the value.

Yours Sincerely

Chartered Tax Advisers

Appendix 1

UK income tax computation 2023/24 on the arising basis NO remittance basis election

	NSI	SI	DIV
	£	£	£
Salary	110,000		
Overseas rental income	7,000		
Overseas savings		500	
Overseas dividends			2,500
Total income	**117,000**	**500**	**2,500**
Personal allowance	(2,570)		
Taxable income	**114,430**	**500**	**2,500**
NSI	37,700	20%	7,540
	76,730	40%	30,692
SI	500	0%	-
DIV	2,000	0%	-
	500	33.75%	169
		Tax liability	38,401
		DTR on rental	(1,050)
		DTR on divs	(169)
		Income tax due	37,182

Personal allowance tapering:
Total income 120,000

1/2 x (120,000 - 100,000) = £10,000
PA: £12,570 - £10,000 = £2,570

Double tax relief:
The relief is the higher of the tax paid overseas (or the

restricted amount) and the tax due in the UK.

- Rental income 15% paid overseas which is lower than the amount paid in the UK 20%/40% therefore DTR on rental:
15% x 7,000 = £1,050

- Dividend income:

Tax paid overseas: £2,500 x 15% = £375
Tax paid in the Uk: £169

UK income tax compuation with a claim for the remittance basis

	NSI	SI	DIV
	£	£	£
Salary	110,000		
Total taxable income	110,000	-	-
NSI	37,700	20%	7,540
	72,300	40%	28,920
		Income tax due	36,460

Appendix 2

Disposal of property in Germany

	£	50% share	
Deemed proceeds	406,250	203,125	
Less: 10% tenanted deduction		(20,313)	
		182,812	
Probate value	270,833	(135,417)	
Gain		47,395	
PRR: 47,396 x 37/193		(9,086)	
Revised gain		38,309	

Private residence relief:

Owned the property from 01/11/2007 - 01/12/2023 = 193 months
Occupied the property from 01/11/2007 - 01/03/2010 = 28 months
Final 9 months of ownership allowable

Disposal of German shares

s.104 share pool:

Date	Description	Number of shares	Base cost £
01/07/2008	Purchased	1,000	50,000
01/03/2010	Purchased	2,000	120,000
		3,000	170,000
01/08/2015	Sale	(2,000)	(113,333)
06/04/2023	c/f	1,000	56,667
		(1,000)	(56,667)
		-	-

Disposal in August 2015	£		
Proceeds £55 per share	110,000		
Less: cost	(113,333)		
Loss	(3,333)		

Disposal in 2023/24	£		
Proceeds £37.50 per share	37,500		
Less: cost	(56,667)		
Loss	(19,167)		

Appendix 3

Capital gains under the arising basis in the UK

	£		

Disposal of German property	38,309		
current year losses	(19,167)		
Gain	19,142		
Annual exemption	(12,300)		
	6,842		
Taxable	6,842		
CGT @ 28%	1,916		

Net position: £149,017 - £1,916 = £147,101

If Remittance basis is claimed then no tax in the UK as the disposal is of overseas assets.

Appendix 4

Pension contributions

Tax year	Salary	Contributions made in the year	Annual allowance	Unused
2020/21	58,020	5% EE 2,901 5% ER 2,901 5,802	40,000	34,198
2021/22	93,995	5% EE 4,670 5% ER 4,670 9,340	40,000	30,660
2022/23	105,500	5% EE 5,275 5% ER 5,275 10,550	40,000	29,450
2023/24	110,000	5% EE 5,500 5% ER 5,500 11,000	40,000	29,000
			Carry forward Available	94,308

Appendix 5

	NSI		
	£		
Salary	105,500		
NSI	37,700	20%	7,540
	67,800	40%	27,120
		Tax due	34,660
		Tax paid	(35,966)
		Refund	1,306