Chartered Institute of Taxation.

30 Monck Street
London SW1P 2AP
T: +44 (0)20 7340 0550
E: technical@ciot.org.uk

Simplifying the Taxation of Offshore Interest – HMRC Consultation[1]

Response by the Chartered Institute of Taxation

1 Executive Summary

1.1 The Chartered Institute of Taxation (CIOT) is the leading professional body in the UK for advisers dealing with all aspects of taxation. We are a charity and our primary purpose is to promote education in taxation with a key aim of achieving a more efficient and less complex tax system for all. We draw on the experience of our 20,000 members, and extensive volunteer network, in providing our response.

1.2 We agree that the current system of taxing investment income received from overseas is problematic, and support HMRC's attempts to find a workable solution to the problems it causes for both taxpayers and HMRC. However, in our view the better solution would be to align the UK tax year to the calendar year, albeit the one-off costs of change would be significant, as highlighted in the 2023 report by the Office of Tax Simplification[2]. We would encourage the Government to look again at this as it could potentially simplify the UK tax system in the long term and make compliance easier, particularly since more and more data is being shared internationally as new exchange of information agreements are developed, eg through the OECD. Also, multinational businesses and internationally mobile persons would no doubt find it easier if the UK's tax year end mirrored the vast majority of global tax year ends, ie 31 December.

1.3 We are cautiously in favour of the proposal to change the assessing period for offshore interest to a calendar year, since we consider that it will help mitigate the issues caused by the mismatches outlined in the consultation document. However, we are not in favour of it only applying to bank interest received from overseas. If introduced, it should apply to all overseas investment income (interest and dividends) and capital gains/losses shared under Automatic Exchange of Information Agreements (AEOI).

1.4 The technical detail will be important and should be kept as simple as possible. It will not be worth doing if it results in myriad exceptions, exclusions, transitional, grandfathering and anti-avoidance rules.

[1] https://www.gov.uk/government/consultations/simplifying-the-taxation-of-offshore-interest/simplifying-the-taxation-of-offshore-interest

[2] Office of Tax Simplification: The UK tax year end date: exploring the potential for change – September 2021 https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/1016718/Tax_year_end_date_report___web_copy_.pdf.

1.5 For it to mitigate the mismatch issues described in the consultation, and to keep it as simple as possible, the change should probably be mandatory. However, we have also received feedback that calendar year reporting should be optional – for example, by election – as that will provide taxpayers with the flexibility to choose the option that suits their personal circumstances best. If it is optional, there would have to be a decision made about whether it should be an irrevocable choice or not. Potentially complex rules would be required should the decision not be an irrevocable one. Ultimately, it would be about striking an appropriate balance between flexibility and simplicity.

1.6 A change to the basis of assessment could lead to confusion for taxpayers with offshore interest income and other sources of income being taxed on different bases, so any change must be clearly communicated through guidance, in the tax return supporting notes and via online prompts in tax return software.

1.7 It will be important that HMRC factor in planned changes such as Making Tax Digital (MTD) in deciding on any wider extension and make sure that they consider how information is played back to taxpayers / pre-populated in tax estimates and PAYE codes etc.

2 About us

2.1 The CIOT is an educational charity, promoting education and study of the administration and practice of taxation. One of our key aims is to work for a better, more efficient, tax system for all affected by it – taxpayers, their advisers and the authorities. Our comments and recommendations on tax issues are made solely in order to achieve this aim; we are a non-party-political organisation.

2.2 The CIOT's work covers all aspects of taxation, including direct and indirect taxes and duties. Through our Low Incomes Tax Reform Group (LITRG), the CIOT has a particular focus on improving the tax system, including tax credits and benefits, for the unrepresented taxpayer.

2.3 The CIOT draws on our members' experience in private practice, commerce and industry, government and academia to improve tax administration and propose and explain how tax policy objectives can most effectively be achieved. We also link to, and draw on, similar leading professional tax bodies in other countries.

2.4 Our members have the practising title of 'Chartered Tax Adviser' and the designatory letters 'CTA', to represent the leading tax qualification.

3 Introduction

3.1 This consultation is seeking views on how the taxation of offshore investment income can be simplified. Individuals are taxed on investment income, including interest, arising in a tax year. Where the investment income is from a non-UK ('offshore') investment the individual will often receive details on a calendar year basis. HMRC also receive details on a calendar year basis under international exchange of information agreements. This is because many countries use the calendar year as their tax year. The mismatch between the UK tax year and the calendar year reporting causes issues for both HMRC and taxpayers.

3.2 The consultation explores whether the assessing period for offshore interest might be changed to a calendar year basis rather than the existing tax year basis, so that income received in the calendar year that ends in the

tax year would be taxable in the UK in that year. This could help reduce administrative burdens for taxpayers and improve the efficiency and focus of HMRC's compliance work.

3.3 The CIOT's stated objectives for the tax system, relevant to this consultation, include:

- A legislative process that translates policy intentions into statute accurately and effectively, without unintended consequences.
- Greater simplicity and clarity, so people can understand how much tax they should be paying and why.
- Greater certainty, so businesses and individuals can plan ahead with confidence.
- A fair balance between the powers of tax collectors and the rights of taxpayers (both represented and unrepresented).
- Responsive and competent tax administration, with a minimum of bureaucracy.

4 Question 1: Do you agree with the issues caused by the mismatch as set out above?

4.1 Yes. However, further issues arise with data inconsistencies and processing mismatches, which will not be resolved by changing the assessing period. These mean that, for example, the incorrect recipient taxpayer is identified by HMRC or income is classified differently by the overseas jurisdiction compared to the UK. We sometimes hear from our members that HMRC have issued One to Many nudge letters to taxpayers regarding foreign bank interest, dividends etc, where the income had been correctly reported on their UK tax return. In one case, the income had been correctly reported as interest but had been classified as dividend income by the overseas jurisdiction, leading to confusion and several rounds of correspondence.

4.2 We agree that resolving the mismatch would help HMRC match the data they receive under automatic exchange from overseas jurisdictions with entries on UK tax returns better. However, exchange rate differences will still mean the data does not tie in exactly.

5 Question 2: Are there any other issues this mismatch causes?

5.1 No.

6 Question 3: How would you mitigate these issues?

6.1 We agree that aligning the assessment period for overseas income to the calendar year would appear to help overcome these issues.

6.2 We are aware anecdotally that in practice a lot of people already report typically small amounts of overseas investment income on a 31 December basis, either informally or with a note in Box 18 of the tax return ('any other information'). We believe that this approach, albeit technically incorrect, is rarely challenged by HMRC. HMRC could therefore consider whether a discretionary power already exists for them to allow taxpayers to report informally on a calendar year basis, if they want to, perhaps with a de minimis limit, rather than introducing a change in the law. However, this is probably not a satisfactory solution because it makes the

rules more complex and does not resolve the situation for larger amounts of income or any amounts of capital gains.

6.3 The consultation suggests that PAYE codes could be used to collect small amounts of tax on offshore income, reducing the need for a taxpayer to submit a Self-Assessment tax return. We support this but note that coding out can be imperfect because it sometimes relies on assumptions about a person's income that may be incorrect, for example that an income source continues year on year producing similar levels of income, or exchange rate conversions. Also it does not apply if, as the consultation notes, the taxpayer is not in PAYE.

6.4 Third party software providers should be included in plans for pre-population of this type of data, so that all taxpayers can be included (both taxpayers in MTD for Income Tax and for those that will remain in Self-Assessment). If pre-population is adopted then taxpayers must be able to over-write the figures to correct them if they appear wrong. Sometimes the banks deliver incorrect reports of investment income. If the taxpayer cannot simply over-write the figures, they will either be knowingly submitting an incorrect return or unable to file (and thus incurring penalties) if they have to wait for the bank to correct the data, send the data to HMRC and HMRC to process it to update the taxpayer's record/pre-population.

6.5 We know that the plan is that over time more and more information will be pre-populated into the MTD systems / Personal Tax Account. HMRC should make sure that they are thinking about if and how offshore interest information will be included in that pre-population, so that systems are built in a joined-up way and everything is as clear as it can be. We do not know whether offshore interest is a candidate for true pre-population (ie third party figures being pulled through), but if not, HMRC might pull through an estimate based on previous years. In that case HMRC would need to be clear a) that it is an estimate and b) which period the estimated figure covers, so that it is easy for taxpayers to check against the actual figures once they have them. Careful consideration should be given to the 'customer journey' so that it is as clear and intuitive as possible and minimises the risk of error.

6.6 Any change to the assessing period should be clearly communicated, through guidance, in the tax return supporting notes and via online prompts in tax return software.

7 Question 4: Which changes could be prioritised to drive improvements in the taxpayer experience?

7.1 As noted above, aligning the assessment period for overseas income to the calendar year could be prioritised, although we think that this is a second best option compared to changing the UK tax year itself from 5 April to the calendar year.

8 Question 5: Is it right to focus on offshore interest only at this stage or should all offshore investment income be considered at the same time?

8.1 No. It should be all offshore investment income (interest and dividends) and capital gains/losses reportable under automatic exchange of information (AEOI). Once the cryptoasset reporting framework (CARF) is implemented, the related income and gains should similarly be included in this approach as CARF is effectively an update to the Common Reporting Standard (CRS). This would be the simplest and most consistent approach. We would suggest that rental income is not included since it is not generally reportable under AEOI (although some may be reportable via digital platform reporting (eg Airbnb)).

8.2 If the change is only for offshore interest, 'offshore interest' would need to be carefully defined to make it clear which type of income is in scope and which is not. We would anticipate that this will be difficult, if not impossible, because of the large number of overseas investment income sources that exist. Therefore, limiting it to offshore interest is likely to cause confusion and errors. All of a taxpayer's offshore investment income and gains will usually be in the same broker's / investment company's / financial institution's report so it makes sense that they all should be reported on the same tax return.

8.3 If the assessment period is only changed for offshore interest, we foresee there being a particular issue with excess reportable income (ERI) and whether the deemed distributions would be interest for the purpose of this consultation. Offshore funds are normally corporate vehicles. Any distributions they do make are legally dividends, but they are deemed to be interest if more than 60% of the underlying investments are interest-bearing (broadly – often referred to as bond funds – see s378A ITTOIA for conditions). A deemed distribution from such a fund would go in the foreign interest box on the foreign pages and would be indistinguishable from interest on a bank account in, say Luxembourg. In addition, a non-UK broker would have no reason to split distributions from the fund up based on whether they meet the conditions in s378A ITTOIA and should be taxed as interest rather than dividends. Rules would also be needed to determine what happens if the s378A status of the fund changes (probably rare in practice, but it could theoretically happen if the composition of the fund changed). These are all further reasons for dividends being treated the same way as interest, but having different forms of interest on different bases would be even more confusing.

8.4 It would be helpful if both dividend and interest income from foreign investment partnerships was included. We do not know if this data is shared under AEOI agreements or not. Some taxpayers hold substantial interests in mainly US Investment partnerships and fiscal year data is not usually available so the US calendar year data (usually from the form K1) will be used to prepare the UK return.

9 Question 6: Do you think the idea of aligning taxation of offshore interest to a calendar year has merit?

9.1 Yes. But see our response to Question 5.

10 Question 7: Do you agree the issues identified with this solution are the right ones?

10.1 Yes.

11 Question 8: Are there other issues that have not been covered?

11.1 Whilst some taxpayers will receive overseas investment income from just one other country (eg, their home country), there will be many who will receive investment income from multiple overseas jurisdictions. Anyone who has a portfolio of investments (even a small one) could have securities and offshore funds in any number of jurisdictions (although the most common offshore funds are typically from Ireland, Luxembourg or the USA). We would suggest that all overseas investment income would need to be taxed on the same basis regardless of where it originates. Taxing investment income differently depending on where it originates would be unnecessarily complicated.

11.2 Issues could arise where the overseas jurisdiction does not use the calendar year as its tax year, meaning that changing the UK basis of assessment to 31 December would not appear to help. We understand, for example,

that there are a very small number of overseas jurisdictions which do not have a calendar tax year and which do not report CRS data on a 31 December basis[3], so the impact of moving to a 31 December assessing basis would not necessarily be an improvement on the status quo for taxpayers in receipt of income from this small number of countries, or for HMRC.

11.3 The majority of CRS data (including from the UK) is exchanged on a 31 December basis, regardless of the tax year of the jurisdiction concerned, as per the OECD rules – but we believe that this is not well understood. As a general point therefore, it would be helpful if there was more transparency about how each overseas jurisdiction reports its data under AEOI, so that taxpayers and agents can have a better understanding about how they report and any differences that exist.

11.4 We note that the OECD's digital platform reporting process includes a step requiring the platform to provide the taxpayer with a copy of the data exchanged. It would help if the CRS reporting requirements (including the CARF) could be updated to include a similar requirement. The UK could consider raising this as a recommendation for the OECD to consider.

11.5 There could be issues involving residence where a person leaves the UK part way through the tax year. This is best illustrated by an example. A calendar year basis starts to apply from 2025/26 and an individual, in receipt of overseas bank interest which is paid monthly, leaves the UK on 1 February 2026 and has split year treatment from that date (so they are non-resident in 2026/27). The January 2026 interest should be taxable because it arises when the individual is UK resident. If a calendar year basis is being used, the January 2026 interest would be taxable in 2026/27, but foreign interest is not in the territorial scope for a non-resident. It is therefore possible that pushing the assessment of the interest into the subsequent tax year could result in it being untaxed. A solution would be to force people back onto the fiscal year basis if they cease UK residence but it obviously adds complexity. In the above example, the 2025/26 return would therefore include the January 2026 interest.

11.6 Where an income source ceases / an account is closed and the individual continues to be UK resident in the following tax year, it would make sense for the January to March interest to be taxed in the next year if that is what would have happened if the account had remained open. We suspect that it is only residence status and the new foreign income and gains (FIG) status that will create some issues.

12 Question 9: How would you deal with the transitional year?

12.1 We agree with the suggestion in paragraph 3.5 of the consultation. In addition, this could be used as a model for later alignment of other sources of income and gains to the calendar year, perhaps as part of a long term plan to change the UK tax year to align to the calendar year.

12.2 Only taxing 9 months' worth of interest, rather than a full 12 months' worth, will result in less tax in the transitional year. The lower tax take in the transitional year could potentially be counterbalanced by improved compliance from taxpayers and better targeting of HMRC's compliance activity in future years. We would encourage HMRC to look at quantifying the impact that the removal of the problems caused by mismatched data is expected to have over the longer term. Any possible negative public reaction arising from the change could be mitigated by clear communication of the impact of the changes.

[3] Most countries, including the UK, report CRS data on a 31 December basis (per the OECD rules) but South Africa and New Zealand report CRS data to their own tax years (28/29 February and 31 March and respectively).

12.3 Some taxpayers will be already reporting their overseas investment income on a calendar year basis (see above) and will report a full 12 months' worth of interest in the transitional year, so there will be no Exchequer loss - although we suspect that the impact of that may be difficult to quantify in isolation.

13 Question 10: Do you receive tax information from your Financial Institute on a calendar basis?

13.1 Taxpayers / clients not tax agents usually receive this information. We do not know how frequently tax information reports are prepared on a calendar year basis (as opposed to the UK tax year of 5 April or on the tax year basis applicable to the overseas jurisdiction in which the financial institutions/investments etc are located, where that jurisdiction does not use the calendar year as its tax year). We suggest that HMRC would need to consult with the industry about what might be involved in preparing reports of overseas investment income for their clients on a 31 December basis instead.

13.2 As noted above, a taxpayer's offshore investment income and gains will usually all be in the same tax information pack so it makes sense that they all should be reported on the same tax return.

14 Question 11: How often is tax deducted at source on payments of offshore interest?

14.1 Tax is deducted at source on payments of offshore interest whenever required by the home jurisdiction. This does not seem particularly relevant to the issues under consultation.

15 Question 12: Should the proposed solution be mandatory if it did go ahead?

15.1 For it to mitigate the mismatch issues described in the consultation, and for simplicity, it should be mandatory. However, we have also received feedback that calendar year reporting should be optional – for example, by election – as this will provide taxpayers with the flexibility to choose the option that suits their personal circumstances best. If it is optional, we think there should be some flexibility for taxpayers about when they can use it, perhaps in limited circumstances (which would need defining). We recognise that this means that potentially detailed and complex rules would be required. The rules for switching to and from the 'cash basis' might provide some assistance in this regard. The alternative is to make it an irrevocable decision at the start, with no ability to swap to and from once started, which would be less complicated and less open to abuse. Ultimately, it would be about striking an appropriate balance between flexibility and simplicity.

15.2 There may be situations where certain taxpayers would benefit from it being optional, for example under the new FIG regime, an individual claiming FIG in their 4th tax year after becoming UK resident should be able to claim relief for the interest credited in the period from 1 January to 5 April. If there is an irrevocable election to use calendar or fiscal year basis, potentially everyone on the FIG regime will elect to be on the fiscal year basis to avoid being disadvantaged on the year 4 interest.

15.3 If it only applies to overseas interest and it is an optional choice, many taxpayers could choose not to opt in if they have a variety of different overseas income sources in a portfolio because otherwise it could be too complicated to identify and pull out the interest from other types of income.

16 Question 13: Do you think this measure could cause issues for financial Institutions, agents and taxpayers when considered alongside basis period reform?

16.1 We can foresee that the change could lead to confusion for taxpayers (and their agents) with different sources of income being taxed on different bases, so it will be important that any change is clearly communicated through guidance, in the tax return supporting notes and via online prompts in tax return software.

17 Question 14: Do you have any ideas on how reporting requirements can be further simplified for individuals with offshore income?

17.1 HMRC need to consider what to do about the other information they receive from overseas jurisdictions on a calendar year basis, ie they will start getting the digital platform data on that basis this month, as well as the cryptoasset data in due course. HMRC will experience similar matching issues due to non-coterminous periods unless these sources are also switched onto a calendar year basis. That is why we think it would be better to change the UK tax year itself from 5 April to 31 December.

17.2 Having said that, it is unfortunate that basis period reform has unhelpfully taken the assessing rules for the taxation of trading income in a different direction. This could make it more difficult to undertake more fundamental reform (changing the UK tax year) but as we have already noted, we think it should be a long term ambition which would simplify the UK tax system and have long term benefits, so it should not be ruled out.

17.3 There are situations when changing to a 31 December basis of assessment could cause issues with MTD and basis period reform. The most obvious one is the digital platform reporting where the relevant income (property or trading income) would potentially (depending on turnover) be MTD income. Allowing reporting to 31 December for trades or businesses covered by the digital platform reporting would make MTD reporting more complex and it is not clear how it would be impacted by basis period reform. It would be particularly problematic for anyone with a business covered by the digital platform reporting and also one that is not, anyone moving in and out of use of a digital platform (for example, a business starting on Etsy and then moving to its own website as it scales up), or anyone moving into MTD because they go over the turnover threshold for the first time.

18 Question 15: Are there any other challenges you have with reporting requirements for offshore income?

18.1 HMRC should publish the details they receive from reporting funds, because it is currently very difficult, and often impossible, for taxpayers and agents to find this information. HMRC know the Excess Reportable Income (ERI) per unit and the deemed distribution date, but they do not publish it. The law allows the funds to meet their obligations in informing taxpayers by publishing the figures on the internet. In practice these are almost impossible to find via a search engine (there is usually a pdf that is not indexed on Google). You need to know where to look on each provider's website. If HMRC published a list with the name, international securities identification number (ISIN), ERI and reporting date (and/or deemed distribution date, which is six months later), it would help taxpayers get their tax returns right. It would be even better if HMRC put the figures in the digital tax account or pre-populated them into tax returns, rather than needing to use a One to Many letter approach after the fact.

18.2 When the remittance basis applies, oversights with ERI do not usually matter, as there is no remittance if the fund is sitting there rolling up. But the consultation notes that with the removal of the remittance basis there is going to be an increased number of individuals with offshore investment income who will be required to report it on a UK tax return. If a taxpayer is on the foreign income and gains (FIG) regime going forward, they need to quantify the income and make a claim. Many of these people risk getting caught out by this once the protection of the remittance basis falls away.

18.3 Another challenge to compliance, as has been already noted, is that data shared with HMRC by overseas jurisdictions under the CRS is not automatically provided to the taxpayer. We would support HMRC sharing the data that they receive from overseas jurisdictions with taxpayers and their agents, particularly when they send the taxpayer a nudge letter. This will make compliance checks more efficient for both HMRC and taxpayers because the taxpayer will know which account HMRC are asking about and in which jurisdiction.

19 Acknowledgement of submission

19.1 We would be grateful if you could acknowledge safe receipt of this submission and ensure that the Chartered Institute of Taxation is included in the List of Respondents when any outcome of the consultation is published.

The Chartered Institute of Taxation

20 January 2025