ICAEW
REPRESENTATION 6/25

SIMPLIFYING THE TAXATION OF OFFSHORE INTEREST

Issued 22 January 2025

ICAEW welcomes the opportunity to comment on the consultation on Simplifying the Taxation of Offshore Interest published by HMRC on 30 October 2024, a copy of which is available from this link.

ICAEW does not support the proposal of only taxing overseas interest on a calendar year basis. We would support an optional election for taxpayers to be taxed on a calendar year basis in respect of all of their overseas investment income.

This response of 22 January 2025 has been prepared by the ICAEW Tax Faculty. Internationally recognised as a source of expertise, the ICAEW Tax Faculty is a leading authority on taxation and is the voice of tax for ICAEW. It is responsible for making all submissions to the tax authorities on behalf of ICAEW, drawing upon the knowledge and experience of ICAEW's membership. The Tax Faculty's work is directly supported by over 130 active members, many of them well-known names in the tax world, who work across the complete spectrum of tax, both in practice and in business. ICAEW Tax Faculty's Ten Tenets for a Better Tax System, by which we benchmark the tax system and changes to it, are summarised in Appendix 1.

ICAEW is a world-leading professional body established under a Royal Charter to serve the public interest. In pursuit of its vision of a world of strong economies, ICAEW works with governments, regulators and businesses and it leads, connects, supports and regulates more than 169,000 chartered accountant members in over 146 countries. ICAEW members work in all types of private and public organisations, including public practice firms, and are trained to provide clarity and rigour and apply the highest professional, technical and ethical standards.

ICAEW
Chartered Accountants' Hall Moorgate Place London EC2R 6EA UK
icaew.com

The Institute of Chartered Accountants in England and Wales (ICAEW) incorporated by Royal Charter (RC000246)
Registered office: Chartered Accountants' Hall Moorgate Place London EC2R 6EA UK

KEY POINTS

A. ICAEW considers that any changes should apply to all overseas investment income and not just overseas interest. This is because changing the rules for a single type of overseas income will complicate rather than simplify tax administration for taxpayers with multiple types of overseas income.

B. Not all countries have a 31 December fiscal year end, so ICAEW considers that taxpayers should be able to make an optional but irrevocable election to declare their overseas investment income to 31 December, or a date that aligns with the overseas territory from where most of their overseas investment income derives.

C. Consideration needs to be given as to how a calendar year basis of taxation for overseas investment income would interact with:

- the new foreign income and gains (FIG) regime that will replace the remittance basis from 6 April 2025.
- periods of non-residence.
- Dates of arrival to the UK and dates of departure.
- The year of death.
- Double tax agreements.

D. Will trusts and estates be included in the proposed measures? If they are not, there will continue to be a mismatch between the R185s and what the beneficiaries/heirs have to report.

E. ICAEW would support a further review of the advantages and disadvantages of whether the UK tax year end should be changed to 31 December. As international arrangements for automatic exchange of information (AEOI) extend beyond the Common Reporting Standard (CRS) and Foreign Account Tax Compliance Act (FATCA) to digital platform reporting and the cryptoasset reporting framework, there will be a growing bank of financial data that is not aligned to the UK's tax year.

HMRC'S PROPOSALS AND PREVIOUS ACTIVITY IN THIS AREA

1. HMRC issued a discussion document in 2021, helping taxpayers get offshore tax right. ICAEW responded in ICAEW REP 58/21. HMRC published a summary of the responses it received.
2. There was a separate HMRC call for evidence in 2021 regarding the tax administration framework and HMRC published the responses. ICAEW responded in ICAEW REP 65/21.
3. In 2023, ICAEW was invited to comment on HMRC's overseas investment income proposal which suggested taxing overseas investment income on a calendar year basis. The key points we raised were:
   - Providing for a formal election to choose a different basis of taxation for overseas income would put already existing practice onto a statutory footing.
   - One of the biggest problems with the existing tax year basis is the need to use estimates both of income received and overseas tax suffered on that income when including income on a UK tax return received overseas on a calendar year basis. This then means that those estimates need to be adjusted subsequently, resulting in additional administration for taxpayers, agents and HMRC.
   - UK tax calculations are also made more difficult by the need to pro-rate income received from two different calendar years into a single tax year.
   - The current basis restricts HMRC's ability to enquire into overseas income reported as the information it receives through FATCA and CRS is not received at a time that is most useful for enquiries and interventions.

- Logistical and legislative complications may arise on the transition from one basis of taxation to another. There may also be a deferral of tax to the Exchequer in the transitional year. However, these complications should not be insurmountable.
- One particular difficulty arises from the fact that not every overseas territory uses a calendar year basis of taxation. It will therefore be difficult to design a system that benefits everybody. As such, we recommend that any alternative basis of taxation is made available by election, rather than making this mandatory.

HMRC's proposals

4. Under this consultation, HMRC is proposing that offshore interest should be taxable on a calendar year basis to 31 December, with all other sources of overseas income and capital gains remaining taxable on amounts for the year to 5 April. A clear definition of 'offshore interest' would be needed. For example, US money market funds distribute their income as dividends, but they are often mistakenly treated as interest.
5. HMRC considers that this would have the following advantages:
   - Help to recover more taxes, thus reducing the tax gap, by reducing errors (eg, the need every year to time apportion receipts and foreign taxes to 5 April) and avoidance.
   - Improving the experience for taxpayers, by giving them longer to obtain the information from the overseas financial institution. As an example, a self assessment tax return to 5 April 2024 must be filed by 31 January 2025. The overseas receipts from 1 January 2024 to 5 April 2024 must be included on that return. However, the overseas institution only provides the details in an annual report to 31 December 2024. The taxpayer only has one month to obtain that information from the overseas institution. If the information is not received in time, the taxpayer needs to include an estimate on their tax return and then amend the return once the figures are known.
   - HMRC would be able to reconcile the information it receives under AEOI provisions, such as CRS and FATCA, to the entries on a tax return to confirm if a taxpayer has made accurate and complete disclosures.
   - HMRC has 12 months from the 31 January filing deadline to raise enquiries. Currently, HMRC receives CRS and FATCA data by 31 May following the filing deadline, which only gives HMRC eight months to review the CRS data.
   - HMRC will be able to use the data to pre-populate tax returns and code out tax liabilities.
   - It would reduce the number of disclosures HMRC receives about unpaid tax on overseas interest, which are high volume but low value.
6. HMRC envisages the following potential disadvantages or problems:
   - The number of non-UK domiciled individuals in self assessment is estimated to increase to 80,000 as a result of the abolition of the remittance basis. HMRC's July 2024 figures showed at Figure 3 that there were around 74,000 non-UK domiciled individuals completing tax returns for 2022/23.
   - Not every jurisdiction has a 31 December year end.
   - The interaction with other policies, such as basis period reform and MTD.
   - How to deal with the transitional year.

Should the UK tax year end on 31 December instead of 5 April?

7. We would support a further review of the UK's longstanding tax year end of 5 April and the potential advantages and disadvantages of switching to 31 December. The UK is an outlier globally in not having a 31 December fiscal year end, with Australia (30 June), New Zealand (31 March) and South Africa (28/29 February) being other major exceptions. The latter two dates appear to have been swapped around in the consultation document (para 3.6).
8. There were discussions in 2021 about whether the UK should change its tax year end to 31 December, notably by the Office of Tax Simplification (OTS), which also considered a switch

to 31 March, and at ICAEW's Wyman Symposium (which took place during the OTS' review period).

9. The Republic of Ireland changed to a 31 December fiscal year end in 2002 and ICAEW noted the lessons that the UK might be able to learn from that.
10. However, there are recent or imminent tax changes that have moved the UK closer to a 5 April basis that would need to be addressed should the UK decide to change its tax year end.
11. Firstly, the basis period rules, which unincorporated businesses with accounting dates other than 31 March or 5 April, used to determine what profits should be taxed each year, were abolished from 6 April 2024. From that date, those businesses must report their profits to 5 April (or 31 march) each year, regardless of their accounting date.
12. Secondly, Making Tax Digital for Income Tax (MTD IT), which is being phased in from 6 April 2026, is going to require self-employment and property rental income, including from overseas sources, to be reported to HMRC on a quarterly basis, using the four quarters to 5 July, 5 October, 5 January and 5 April. It is already problematic for taxpayers to work out their foreign profits using UK tax rules.
13. And finally, from 6 April 2025, the remittance basis rules for non-UK domiciled individuals are being replaced with a four-year FIG relief. In simple terms, this will mean that FIG received in the first four tax years of UK residency will not be taxed in the UK. Any legislation and guidance would need to be clear as to how the FIG rules would interact with any amounts that are taxed on a calendar year basis.

ANSWERS TO SPECIFIC QUESTIONS

SECTION 2 – BACKGROUND TO THE TIMING MISMATCH

Question 1 – do you agree with the issues caused by the mismatch as set out above?

14. While not technically correct, ICAEW is aware that some taxpayers and their advisers already report offshore income on a calendar year basis, whether through ignorance of the rules or because they consider that it would make little difference to the individual's aggregate tax liability over time.
15. ICAEW agrees that there is a mismatch between AEOI data and the figures reported by taxpayers. We generally support measures that aim to reduce one-to-many nudge letters and enquiries that arise from this mismatch, as well as measures that could reduce errors in tax returns, such as the need to apportion overseas income between tax years and make estimates where information has not been received from overseas by the 31 January filing deadline.
16. However, the data HMRC receives under AEOI does not include details of foreign taxes paid. Our members have reported that overseas banks also report items as interest under CRS, which are not classed as interest for UK tax purposes.
17. ICAEW has concerns about HMRC pre-populating returns with the data it holds, which is not always accurate. For example, the RTI (2013) and dynamic coding (2017) measures were meant to reduce the number of P800 year-end reconciliations that HMRC issues, but our members' experiences are that there has been no real reduction. A disagreement with HMRC shouldn't automatically lead to an enquiry being opened. There needs to be safeguards for taxpayers and we have received the following suggestions:
    - Pre-population should include a line-by-line breakdown of the entries.
    - The taxpayer should be able to attach the statements or summaries they have used and HMRC should be required to review this data, along with white space notes, before opening an enquiry.
18. Until such time as HMRC has details of foreign taxes and it can share the data it holds with the taxpayer and make better use of that data, ICAEW considers that HMRC should not use AEOI data to pre-populate tax returns or to collect tax through PAYE codes.

Question 2 – are there any other issues this mismatch causes?

19. It is unclear from the consultation if trusts and estates would be included in this measure. If they are not, trusts and estates would need to report overseas interest to 5 April, but the beneficiaries/heirs would need to report to 31 December. This would cause confusion and increase the chance of incorrect tax return entries being made inadvertently.

20. Consideration needs to be given as to how a calendar year basis of taxation would interact with:

    a. the new FIG regime that will replace the remittance basis from 6 April 2025.

    b. periods of non-residence.

    c. dates of arrival to the UK and dates of departure.

    d. the year of death.

    e. double tax agreements. A member has noted that there could be a conflict where a treaty states which country can tax interest, but the UK uses a non-UK tax year to work out what is taxable in the UK.

Question 3 – how would you mitigate these issues?

21. ICAEW considers that the £2,000 de minimis for claiming the remittance basis should be replicated in the legislation that is replacing the non-domicile and remittance basis rules from 6 April 2025. Currently there is a personal savings allowance of £1,000 for basic rate taxpayers and £500 for higher rate taxpayers. This would keep a large number of taxpayers out of self assessment who have little to no UK tax liability once double tax relief claims are taken into account.

22. ICAEW would also be in favour of an optional but irrevocable election that a taxpayer could make to report all of their foreign investment income to 31 December, or if the overseas territory has a different tax year end, to match that date. We would support a targeted anti-avoidance rule (TAAR) to prevent manipulation of the election, or altering the timing of receipts, to avoid UK tax. Provisions would also be required to deal with the cessation of a source of income from a country with a 31 December tax year end. Would the taxpayer revert automatically to a 5 April basis, or could they make a new election if they have other overseas investment income from a non-calendar year country? HMRC could consider whether such an election could be made on a country-by-country basis, although this would add to the complexity.

Question 4 – which changes could be prioritised to drive improvements in taxpayer experience?

23. ICAEW considers that it would be better to use a term such as ‘non-UK income’ or ‘overseas income’, rather than ‘offshore income’. Some taxpayers associate the word ‘offshore’ with people who are involved with ‘tax avoidance’ or ‘tax evasion’ and they do not recognise that their income fits into that category. People may not realise that their overseas income is taxable in the UK, especially if they have suffered tax in the country where the income originated and do not have a UK tax agent.

24. ICAEW would also like HMRC to use the data it holds to improve the contents of the nudge/one-to-many letters or discovery assessments it sends to taxpayers that relate to overseas income. ICAEW responded (ICAEW REP 02/25), to HMRC’s tax administration framework review, which proposed that nudge letters should be put on a statutory footing. At present, taxpayers who respond to nudge letters are left with no certainty, as they receive no acknowledgement of receipt of their response and no notification as to whether HMRC will take any further action. This is contrary to our ten tenets, in particular tenet two (see Appendix 1) that “… in virtually all circumstances the application of the tax rules should be certain”. ICAEW would like to see the following improvements to these letters:

    i. Any letter about a potential under-declaration of offshore income should include a detailed breakdown of the amounts of income that were notified to HMRC and the source country (or countries), plus any additional relevant details that HMRC is able to provide such as a commencement or cessation date. A taxpayer cannot respond properly if they don't know what HMRC's specific concerns are. An agent representing a taxpayer would probably contact HMRC to request this information anyway. If HMRC can provide the information upfront, it would mean that agents would not need to contact HMRC, which takes up agent and HMRC time.

ii. Letters should be clear that income and gains usually need to be declared in the UK, even if foreign tax has been deducted, and that claims for double tax relief must be made to offset overseas tax suffered against UK tax liabilities.

iii. There should be an online system where taxpayers and their advisers can respond to these letters and attach any relevant information.

iv. In cases where HMRC is satisfied with the response received, follow-up letters should be issued to taxpayers and their agents confirming that HMRC does not intend to take any further action (subject to any necessary caveats about fraud, etc).

v. HMRC's systems also need to be able to track and take account of previous responses from a taxpayer or their agent and factor these into its risk assessment and issue of letters. For example, some taxpayers have received the same letter multiple times for different tax years, suggesting they had underdeclared their offshore income, even after they had previously provided evidence to HMRC to demonstrate that they are the bare trustee of an account and that someone else is taxable on it as the beneficial owner.

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?

25. In principle, switching the taxation of overseas interest to a calendar year basis appears to be the easiest area to implement and the most easily understood, particularly for those who have recently arrived in the UK.

26. However, it actually adds complexity, because it creates a two-tier system where all other overseas investment income sources remain taxable to 5 April. Simplification must deliver benefits for taxpayers and not just be implemented to make things easier for HMRC. An individual whose overseas investment income all arises on a calendar year basis would benefit from simplification. However, anyone with investment income from a non-calendar year country would still need to make apportionments.

27. Changing the taxation of offshore interest to 31 December does not work for countries that do not have a 31 December year end as an apportionment calculation would still be needed. Therefore, ICAEW considers that an irrevocable election, as noted at paragraph 21, would be the best solution for taxpayers.

28. In summary, ICAEW considers that either a 5 April basis (as at present) or a calendar year basis should apply to all offshore investment income and not just interest. ICAEW is not in favour of making it compulsory for all overseas interest to be taxed on a calendar year basis.

29. ICAEW would also be open to considering the wider solution, namely the pros and cons of changing the UK tax year to 31 December, as noted at paragraphs 6-12.

SECTION 3 – ALIGNING THE TAXATION OF OFFSHORE INTEREST WITH THE CALENDAR YEAR

Question 6 – do you think the idea of aligning taxation of offshore interest to a calendar year has merit?

30. Please see our response to Question 5.

Question 7 – do you agree the issues identified with this solution are the right ones?

31. Please see our responses to Questions 3 and 5.

Question 8 – are there other issues that have not been covered?

32. Our members expressed concern as to how any change to the taxation of offshore income would interact with the new FIG regime that is to replace the non-domicile and remittance basis rules from 6 April 2025, particularly for years one and five and periods of non-residency. The FIG rules, as drafted, deny the taxpayer the opportunity to make amendments (consequential claims) after more than 12 months after they file their tax return, for example if they inadvertently make an under-declaration (see our Finance Bill comments ICAEW REP 091/24), which unfortunately means that taxpayers are likely to over-declare their FIG.

33. These are the comments we received from one member:

> "One thing that needs to be considered and made clear is the interaction between these rules and the new four year-FIG regime/periods of non-residence. My understanding is that this would change the tax year in which income was taxable, not whether it is in fact taxable/relievable.
>
> This would mean, for example, an individual who became UK resident on 6 April 2025 would report their foreign income of the calendar year 2025 on their 2025/26 tax return, three months of which would not be taxable at all, nine months of which they would claim relief for under the FIG regime.
>
> Then on their tax return for the 2029/30 tax year (ie, fifth tax year of residence), they would report their foreign income for the 2029 calendar year, three months of which they would claim relief under the FIG regime, and nine months of which would be taxable.
>
> For claiming relief under the FIG regime, I can see that this would be simpler for the middle three years but would be more complicated in the first and fifth tax years. Would this be based on when income was received or a pro-rata basis?
>
> If the rules were extended beyond interest, the position gets more complicated. For dividends from close companies, the latter may give taxpayers an unfair position compared to existing rules. For foreign rental income, would the year be split into two accounting periods or would it be a pro-rata approach?"

34. It should be clear what sources of income are able to be reported on a calendar year basis. For example, amounts arising under anti-avoidance provisions, such as the accrued income scheme and transfers of income stream rules.

Question 9 – how would you deal with the transitional year?

35. If the decision was made to switch to a calendar year basis from 31 December 2025, ICAEW recommends that this is dealt with as follows:

> 2024/25 tax year – declare overseas income from 6 April 2024 to 5 April 2025 as normal.
>
> 2025/26 tax year – declare income from 6 April 2025 to 31 December 2025, approximately 9/12ths.
>
> 2026/27 tax year – declare income from 1 January 2026 to 31 December 2026.

36. ICAEW appreciates that there would be a deferral of HM Treasury's receipts for the 2025/26 tax year, as they would reduce by 3/12ths, but we consider that the longer-term benefits of fewer errors, estimates and amendments to returns would outweigh this.

Question 10 – do you receive tax information from your Financial Institute on a calendar basis?

37. Some taxpayers do, but not all. It depends on the country concerned and what the investment adviser can provide.

Question 11 – how often is tax deducted at source on payments of offshore interest?

38. It depends on the country concerned.

Question 12 – should the proposed solution be mandatory if it did go ahead?

39. No, as mentioned at paragraph 21 above, ICAEW considers that an irrevocable election would be the best option.

Question 13 – do you think this measure could cause issues for financial institutions, agents and taxpayers when considered alongside basis period reform?

40. As we have already mentioned, there is not just basis period reform, but also MTD from 2026 (paragraph 11) and the FIG regime coming in from 6 April 2025 (paragraph 12).

SECTION 4 – REPORTING REQUIREMENTS FOR INDIVIDUALS WITH OFFSHORE INCOME

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

41. Please see our earlier responses.

Question 15 – are there any other challenges you have with reporting requirements for offshore income?

42. Please see our earlier comments, particularly in relation to the new FIG regime.

APPENDIX 1

ICAEW TAX FACULTY'S TEN TENETS FOR A BETTER TAX SYSTEM

The tax system should be:

1. Statutory: tax legislation should be enacted by statute and subject to proper democratic scrutiny by Parliament.
2. Certain: in virtually all circumstances the application of the tax rules should be certain. It should not normally be necessary for anyone to resort to the courts in order to resolve how the rules operate in relation to his or her tax affairs.
3. Simple: the tax rules should aim to be simple, understandable and clear in their objectives.
4. Easy to collect and to calculate: a person's tax liability should be easy to calculate and straightforward and cheap to collect.
5. Properly targeted: when anti-avoidance legislation is passed, due regard should be had to maintaining the simplicity and certainty of the tax system by targeting it to close specific loopholes.
6. Constant: Changes to the underlying rules should be kept to a minimum. There should be a justifiable economic and/or social basis for any change to the tax rules and this justification should be made public and the underlying policy made clear.
7. Subject to proper consultation: other than in exceptional circumstances, the Government should allow adequate time for both the drafting of tax legislation and full consultation on it.
8. Regularly reviewed: the tax rules should be subject to a regular public review to determine their continuing relevance and whether their original justification has been realised. If a tax rule is no longer relevant, then it should be repealed.
9. Fair and reasonable: the revenue authorities have a duty to exercise their powers reasonably. There should be a right of appeal to an independent tribunal against all their decisions.
10. Competitive: tax rules and rates should be framed so as to encourage investment, capital and trade in and with the UK.

These are explained in more detail in our discussion document published in October 1999 as TAXGUIDE 4/99 (see https://goo.gl/x6UjJ5).