Statutory residence test: the exceptional circumstances rule

Personal tax

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The Upper Tribunal has considered the exceptional circumstances rule in the statutory residence test.

Key Points

What is the issue?

The First-tier Tribunal decision of *A Taxpayer v HMRC* [2022] UKFTT 133 (TC) concerned the UK residence status of an individual who had spent 50 days in the UK, which would make her liable to pay tax in the UK. She argued successfully that six days could be excluded under the 'exceptional circumstances' let out.

What does it mean to me?

The Upper Tribunal set aside the First-tier Tribunal's decision, concluding that the taxpayer was not entitled to exclude the six days under the exceptional circumstances rule.

What can I take away?

If a significant tax liability is a likely outcome of being found UK resident for a particular year, then plan any return visits with at least a few days as a safety buffer, just in case an unexpected visit to the UK occurs.

In the July 2022 issue of *Tax Adviser*, I wrote about the anonymised First-tier Tribunal decision of *A Taxpayer v HMRC* [2022] UKFTT 133 (TC) concerning the UK residence status of an individual otherwise based in Ireland. With three UK ties and her being classified as a 'leaver', the taxpayer would be treated as non-resident provided that her day count was 45 or below for the year in question. However, the taxpayer had spent 50 days in the UK.

Nevertheless, she argued successfully that six of her days could be excluded under the 'exceptional circumstances' let out (Finance Act 2013 Sch 45 para 22(4)). That meant that she could be treated as having spent only 44 days in the UK and therefore non-resident for the year.

In my previous article, I commented that an HMRC appeal was not off the cards and the case has indeed proceeded to the Upper Tribunal, whose decision is reported as *HMRC v A Taxpayer* [2023] UKUT 182 (TCC).

The facts of the case

Some of the background facts are set out in my earlier article. I shall repeat only those that are critical for the purposes of the present article.

The taxpayer had originally lived in the Manchester area but moved to Ireland on 4 April 2015 with her younger daughter. In the 2015/16 tax year, a family company paid her a dividend of £8 million, by reference to shares that had been transferred to her by her husband earlier in the year (or, per the First-tier Tribunal's decision, in September 2014). The husband had remained resident in the UK but was planning to move to Ireland when he retired.

In relation to the 2015/16 tax year, the taxpayer was not covered by the automatic tests for non-residence or residence and therefore her residence status had to be determined by looking at her statutory ties to the UK and the number of days spent in the UK.

It was common ground that the taxpayer had three such ties:

- the family tie: through her husband's continued residence in the UK;
- the accommodation tie: through the family home which continued to be available to her; and
- the 90-day tie: by reference to the number of days spent in the UK in the two previous tax years.

It was also common ground that the taxpayer had been resident in the UK during at least one of (in fact, all three of) the previous tax years. As a result, it was common ground that the taxpayer would be treated as UK resident in 2015/16 if her day count for that year exceeded 45.

The actual days spent in the UK in the were 50. However, the taxpayer argued that the last six of those (spread across a two-day and a four-day visit) should be excluded due to exceptional circumstances. Under para 22(4) and (6), it is possible to exclude up to 60 days if:

a) P (the person whose residence is being considered) would not be present in the UK at the end of that day but for exceptional circumstances beyond P's control that prevent P from leaving the UK; and

b) P intends to leave the UK as soon as those circumstances permit.

The essence of the taxpayer's argument was that she had to attend to the needs of her twin sister who suffered from depression and alcoholism and was a suicide risk and that she had an urgent and unexpected need to provide care for the sister's own children.

The First-tier Tribunal did not accept all of the taxpayer's arguments so far as the sister's condition was concerned. However, the tribunal concluded that the risk of neglect likely to be suffered by the children did constitute exceptional circumstances that temporarily prevented the taxpayer from leaving the UK. Thus, the six days were to be excluded, keeping the taxpayer's total below 46.

HMRC considered the First-tier Tribunal's decision to be tainted by errors of law and it appealed to the Upper Tribunal.

The Upper Tribunal's decision

The case came before Mr Justice Michael Green and Judge Anne Redston.

The Upper Tribunal identified the centrality of the day-counting rules in the statutory residence test. It noted that a day is generally counted if an individual is present in the UK at midnight at the end of that day – thus, the taxpayer in the present case was physically present in the UK for 50 midnights. However, para 22(4) provides one of the limited exceptions to this midnight rule, permitting some days (or midnights) to be excluded.

The Upper Tribunal also remarked upon the vagueness of the evidence that had been before the First-tier Tribunal. For example, the taxpayer was aware of the 45-day limit and that, prior to the two visits in question, she had reached a count of 44; therefore, she knew that she was going to have to rely on the exceptional circumstances test. Despite this, the taxpayer had very little recall of how she spent those days or even which nights she spent at her sister's home and which at her own home with her husband.

The Upper Tribunal further commented on what it considered to be a gap in the First-tier Tribunal's reasoning. In particular, it had accepted that, during her two visits, the taxpayer had put in place measures to ensure that the

sister's home was professionally cleaned and that the sister and her children were adequately supervised. However, this was in a case where the First-tier Tribunal disbelieved other aspects of the taxpayer's evidence (in particular in relation to the twin being a suicide risk).

The Upper Tribunal felt the First-tier Tribunal should have made clear why different parts of the taxpayer's factual case fared so differently. Furthermore, the Upper Tribunal was unclear why the taxpayer's involvement was so critical, given that the two sisters' brother (who lived only 20 miles away) was keeping a close eye on the taxpayer's twin, and that the twin also had two friends who visited several times daily.

The Upper Tribunal also remarked upon the lack of explanation as to why the taxpayer did not put in place ongoing arrangements to care for the twin and the twin's children after the first visit.

Moving onto HMRC's grounds of appeal, the Upper Tribunal then considered the 'exceptional circumstances' test. In contrast to the First-tier Tribunal, it decided that the test was entirely objective and did not permit a tribunal to consider any particular attributes of the taxpayer.

Furthermore, the Upper Tribunal emphasised that there must not only be an exceptional circumstance but it must also be one that prevents the individual from leaving the UK on each day for which the relief is being sought. Prevention was held to amount to stopping the individual from leaving the UK, making departure impossible. Referring to Supreme Court authority, the Upper Tribunal said that a 'mere hindrance' would not be sufficient.

The First-tier Tribunal had commented:

> 'It could hardly have been Parliament's intention to have required the "exceptional circumstances" test to be failed if, for example, a taxpayer thought it necessary to be present because of serious illness or at the death bed of a close relative.'

On the basis of the Upper Tribunal's interpretation, however, that is precisely what Parliament intended. As the Upper Tribunal explained, serious illness and death are not exceptional. Furthermore, the Upper Tribunal considered it not to be out of the ordinary for a person to have a sense of moral obligation towards a relative in such a position. In any event, continued the Upper Tribunal, it would not be the failing health of a relative that would be preventing the individual from leaving the UK but the individual's sense of moral obligation.

Similarly, the Upper Tribunal confirmed that an individual who has used up his or her allocation of days, who then finds that a relative is on their deathbed in the UK, must make the choice:

- visit (or remain in) the UK, satisfy his or her moral obligation and become UK resident; or
- remain outside (or leave) the UK, and maintain non-resident status for the year.

For these reasons, the Upper Tribunal concluded that the First-tier Tribunal had erred in law when making its decision. The Upper Tribunal further accepted HMRC's other three grounds of appeal.

It therefore set aside the First-tier Tribunal's decision. On the basis of its understanding of the law, it remade the decision and concluded that the taxpayer was not entitled to exclude the six days under the exceptional circumstances rule. Accordingly, the taxpayer must be treated as having been present in the UK on 50 days in the 2015/16 tax year. As an individual with three ties and who had been resident in at least one of the previous three tax years, she fell within the definition of resident for the 2015/16 tax year. As a result, the dividend paid to her was subject to UK tax.

Commentary

In my previous article, I explained that this case was not one whose facts looked the most compelling for an argument that the visits to the UK should be excluded on the basis of exceptional circumstances. However, I did feel that the First-tier Tribunal's approach to the exceptional circumstances test was reasonable and I am somewhat disappointed by the Upper Tribunal's undoing of that part of the decision.

However, it might be of some comfort that the interpretation put forward by HMRC in the First-tier Tribunal was not repeated in such strident terms in the Upper Tribunal. Care must now be taken to ensure that HMRC's arguments in future are based on the version that was endorsed by the Upper Tribunal and that HMRC does not revert to its previous formulation.

The case also illustrates how the phrase 'intention of Parliament' can be so easily misunderstood. This phrase is often used when describing the role of the courts when interpreting statutes; the courts' role being to ascertain Parliament's intention.

I doubt that many of the MPs who voted for the Finance Act 2013 would have intended an emergency visit to the UK to attend to a dying relative not to count as an exceptional circumstance for the purposes of this relaxation to the statutory residence test. However, the subjective intentions of MPs are of no relevance to statutory interpretation; instead, the intention of Parliament is discerned from an objective interpretation of the words Parliament used (although this exercise does not preclude the purpose of the legislation being considered).

According to the Upper Tribunal, Parliament did not intend to give any relief to individuals who were exceptionally discharging such a moral obligation.

The Upper Tribunal reached its view on the word 'prevents' from a Supreme Court decision which turned on the construction of insurance policies which covered 'loss … resulting from … Prevention of access to the Premises due to the actions or advice of a government or local authority due to an emergency'. It is immediately obvious that the context of that clause was very different from the rule in para 22 and I wonder whether the taxpayer will be tempted to appeal against the Upper Tribunal's decision to the Court of Appeal.

Indeed, the Upper Tribunal had reached its decision on the express basis that serious illness is not exceptional. However, Parliament had expressly provided, as examples of what might count, 'a sudden or life-threatening illness or injury'. This is also in a context where Parliament had permitted up to 60 days (i.e. approximately two months) in aggregate to be excluded from the day count. That in itself suggests a less extreme interpretation than that supported by the Upper Tribunal.

One possible response to the above reasoning is that the statutory words were not considering sudden illness or injury *per se* but only if suffered by the taxpayer him or herself. In other words, the taxpayer's falling into a coma *might* count as an exceptional circumstance preventing him or her from leaving the country but the taxpayer's spouse's similar predicament would not count. However, even that argument is likely to fail the Upper Tribunal's reading of the legislation because, applying the Upper Tribunal's own logic, it would not be the coma that prevents the individual from leaving the country; instead, it would be the medical advice and/or the good sense of relatives who follow that advice which ensures that the individual remains in the UK.

It should also be remembered that the statutory residence test was largely enacted to codify the more nebulous concept of 'residence'. Although pre-2013, an individual's day count was one of the factors used to determine

whether or not they were resident in any particular tax year, it was always accepted that a one-off spike because of exceptional circumstances would not convert non?residence into residence. Ultimately, any additional days in any particular year would be viewed in the light of the full facts of the case.

It is fully accepted that the new rules now adopt a more mechanistic approach, with their stronger emphasis on day counts. However, in my view, the fact that the statutory test has included a similar exceptional circumstances rule suggests that, as did the First-tier Tribunal, the rule should not be interpreted by reference only to wholly objective criteria but should instead take account of the individual taxpayer's personal circumstances.

With several millions at stake and a new area of law under consideration, an appeal to the Court of Appeal should not be ruled out. If the Court of Appeal rejects the Upper Tribunal's view of the exceptional circumstances test, it is similarly possible that it will forgive the other complaints that the Upper Tribunal had about the First-tier Tribunal's decision. There again, it remains my view that the taxpayer was lucky in the First-tier Tribunal on the particular facts of her case. This is not the set of facts I would want to put forward to prick the Court of Appeal's conscience.

What to do next

Subject to any further appeal, there is a simple lesson to be learned from this case: do not rely on the exceptional circumstances rule. Indeed, that advice would be worth following whatever the courts finally conclude about the exceptional circumstances rule. As a result, if a significant tax liability is a likely outcome of being found UK resident for a particular year, then plan any return visits with at least a few days as a safety buffer, just in case an unexpected visit to the UK occurs.