

Tax Deduction Scheme for Interest

Guidance Notes for Diplomats

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1. Introduction

Diplomats who come to the UK are normally entitled to certain exemptions from tax in accordance with the Vienna Convention on Diplomatic Relations, 1961, as given effect in UK law by the Diplomatic Privileges Act 1964. These exemptions apply, in particular, to their official remuneration and to any other income arising outside the UK. The exemptions do not however apply to private income arising from sources in the UK, such as interest payable by a UK bank or building society.

If you are a member of a Diplomatic Mission and get interest from a UK bank or building society you may therefore be liable to pay UK income tax on your interest.

2. Deduction of tax from interest by banks and building societies

Banks and building societies must deduct income tax at the lower rate of 20% from interest before they pay it, but there are exceptions. In particular, interest is paid without tax taken off

- if the investor is not ordinarily resident in the UK and has made a declaration to that effect on declaration form R105

or

- if the investor is ordinarily resident in the UK but has registered, on form R85, to have interest paid without tax deducted because they are unlikely to be liable to income tax.

Members of Diplomatic Missions in the UK often fall into one of these categories and are therefore entitled to have their interest paid without tax taken off, but it is not automatic. You must first decide whether you ordinarily resident or not ordinarily resident in the UK (see paragraph 4).

3. The Vienna Convention on Diplomatic Relations, 1961

The exemptions due to diplomats can be found in The Vienna Convention on Diplomatic Relations, 1961 (full text at <http://www.un.org/law/ilc/texts/diplomat.htm>). Article 34 (d) of the Convention provides that the exemption due to diplomats does not extend to “taxes on

private income having its source in the receiving State”. Interest paid by UK bank and building societies is “income having its source in the receiving State” for this purpose.

The full text of Article 34 is as follows:

'A diplomatic agent shall be exempt from all dues and taxes, personal or real, national, regional or municipal, except:

- (a) indirect taxes of a kind which are normally incorporated in the price of goods or services;
- (b) dues and taxes on private immovable property situated in the territory of the receiving State, unless he holds it on behalf of the sending State for the purposes of the mission;
- (c) estate, succession or inheritance duties levied by the receiving State, subject to the provisions of paragraph 4 of Article 39;
- (d) dues and taxes on private income having its source in the receiving State and capital taxes on investments made in commercial undertakings in the receiving State;
- (e) charges levied for specific services rendered;
- (f) registration, court or record fees, mortgage dues and stamp duty, with respect to immovable property, subject to the provisions of Article 23.'

4. Am I ordinarily resident or not ordinarily resident in the UK?

The rules for determining your residence status apply to you as a member of a Diplomatic Mission in the same way as they apply to everyone else. They are explained in the Inland Revenue's booklet IR20 'Residents and non-residents – liability to tax in the United Kingdom'. It is available from any Inland Revenue Office or on the Internet at www.inlandrevenue.gov.uk

The basic position is that your ordinarily resident status is determined under UK domestic law and depends on your particular circumstances.

In general, you will be regarded as ordinarily resident in the UK if

- you come to the UK and intend to, or do, stay here for 3 years or more. (The date from which you are regarded as ordinarily resident will depend upon when your decision to stay here for 3 years or more was made)

or

- you come to, and remain in, the UK and buy, or acquire on a lease of 3 years or more, accommodation for your own use. (The date from which you are regarded as ordinarily resident will depend on when the accommodation was acquired).

Remember that if your circumstances change you could be treated as having become ordinarily resident in the UK for tax purposes.

For example, if you come here intending to stay for 2 years, you can complete form R105 (see paragraph 5) and have your interest paid to you without tax taken off. But if your circumstances change and you stay here for more than 3 years you will be treated as having become ordinarily resident in the UK for tax purposes from the beginning of the tax year (6 April) after the third anniversary of your arrival. You should tell your bank or building society to cancel the form R105 declaration.

5. I am not ordinarily resident in the UK - can I sign declaration form R105?

If you do not fall within one of the categories in paragraph 4 you are eligible to make a declaration that you are not ordinarily resident in the UK. This declaration is made on form R105.

You should first ask your bank or building society whether they accept declaration form R105 - there is no obligation for them to do so. If they do accept the form you should complete it in full and give it to the bank or building society. The address on the form must be your principal residential address (see paragraph 7).

Exceptionally, you may find tax is taken off your interest even though you have completed form R105. This is because banks and building societies are obliged to deduct tax if they have any information which indicates that you are, or may have become, ordinarily resident in the UK. If this happens, the bank or building society will continue to deduct tax

from any payments of interest it makes to you until it is able to confirm that you are entitled to have interest paid without tax taken off.

6. Where can I find a declaration form R105?

The declaration form R105 can be obtained from

- your bank or building society
- the Inland Revenue website at www.inlandrevenue.gov.uk

The form R105 is also available on the Inland Revenue website in the following languages.

French

German

Spanish

Arabic

7. Principal residential address

The address you give on form R105 **must** be your principal residential address. This will be the address where you usually live. It could be a foreign principal residential address, or a foreign PO Box address (but see paragraph 8), or an address in the UK if you are not maintaining a home abroad. You should only give your embassy address if it is your principal residential address and you actually live there.

8. PO Box addresses

A PO Box address can be given as a principal residential address **only** if that is an acceptable residential address for the country in question, and would allow the you to be traced. Your bank or building society will ask for confirmation that this is the case.

A PO Box address in the UK cannot be given.

9. What happens if my bank or building society will not accept declaration form R105?

The bank or building society will continue to deduct tax at the lower rate of 20% from all interest it pays to you. But you may be able to claim the tax back from the Inland Revenue. To find out whether you can do this contact Centre for Non-residents. Their telephone number is

08450 700 040 if calling from the UK, or

+ 44 151 210 2222 if calling from outside the UK

10. I am not ordinarily resident in the UK and have paid tax on my savings interest- can I claim a repayment?

If you are not ordinarily resident in the UK you may be able to claim back the tax which has been taken off your interest. To find out more contact the Inland Revenue Centre for Non-residents. Their telephone number is

08450 700 040 if calling from the UK, or

+ 44 151 210 2222 if calling from outside the UK

11. I am ordinarily resident in the UK - can I complete registration form R85?

Members of Diplomatic Missions who are resident in the UK for tax purposes are entitled to the same tax allowances as other UK residents.

Your salary and any income from overseas sources are exempt from UK income tax but interest you receive from UK banks and building societies is not exempt from UK income tax (see paragraph 3).

Investors who are unlikely to be liable to pay income tax for the tax year in which interest is paid may register their accounts for interest to be paid without tax taken off. This means you will not have to have tax taken off your interest if you expect that all of your income from UK sources will be less than your UK tax allowances. The registration form R85 is updated every year to show the personal allowances available for the current tax year. If your total UK income is less than your UK allowances you can register to receive interest

without tax taken off by completing registration form R85 and giving it to your bank or building society.

If you are unsure about whether you can complete form R85 to receive your interest without tax taken off, you can ring the Inland Revenue Helpline on 0845 980 0645.

Examples

Diplomat A has come to the UK for 4 years and under the residency rules he is ordinarily resident in the UK. He receives £3,000 a year in UK interest and his salary is exempt from UK tax. As his other UK income (his interest) is less than the tax allowance of £4615 (the personal allowance) he can complete a form R85. When the form is accepted by his bank or building society they will stop deducting tax from future payments of interest.

Diplomat B has come to the UK for 4 years and under the residency rules she is ordinarily resident in the UK. She receives £10,000 a year in UK interest from which £2000 is deducted as tax. Although her salary is exempt from UK tax her other UK income (her interest) is above the tax allowance of £4615 (the personal allowance) so she cannot complete a form R85 as she is liable to pay tax. Diplomat B has income of £5,385 (£10,000 less £4,615) which is taxable at 20%. Diplomat B is due to pay £1,077 tax but the bank has deducted more than this so she will need to claim a repayment. The Inland Revenue's booklet IR110 (see paragraph 12) explains how to get a repayment claim form and how to claim tax back.

12. Where can I find a registration form R85?

The registration form R85 is available from

- your bank or building society
- any Inland Revenue office
- the Inland Revenue website at www.inlandrevenue.gov.uk

You will also find a form R85 in the Inland Revenue's booklet IR110 'Bank and building society interest. A guide for savers' which is available from

- any Inland Revenue office
- the Inland Revenue website at www.inlandrevenue.gov.uk

13. I am ordinarily resident in the UK but not eligible to complete registration form R85 - can I claim back tax taken off my bank or building society interest?

If you are ordinarily resident in the UK, and the income you receive from UK sources is not covered by your UK tax allowances you cannot complete a form R85 and your bank or building society will pay you interest with tax taken off.

But because you are entitled to tax allowances you may be able to claim some of the tax back. You can do this if the tax taken off your interest is more than the tax you are due to pay (see example 2 in paragraph 11). The Inland Revenue's booklet IR110 (see paragraph 12) explains how to get a repayment claim form and how to claim tax back.

14. Joint accounts where all investors are not ordinarily resident in the UK

If you have a joint account and you and the other investors are all not ordinarily resident in the UK any one of you may sign a form R105 on behalf of all the other investors, but details of all investors must be given on the form. If the investor that has signed ceases to be a party to the account, for example, if he or she dies, a new declaration will be required.

Where a new party joins the account a new declaration on form R105 is required.

15. Joint accounts where all account holders are ordinarily resident in the UK

Joint accounts may be registered

- if each investor is entitled to register (see paragraph 11) and provides his or her own form R85, or
- one or more of the investors is entitled to register (see paragraph 16) and the bank or building society is willing to accept a partial registration.

For a joint account held by 2 people, partial registration means the bank or building society will only register one of the account holders so that the interest is paid half with tax taken off and half without tax taken off.

Example

Mr and Mrs Smith are both ordinarily resident in the UK and have 2 joint savings accounts in the UK. One of the accounts is with ABC Bank and the other is with XYZ Bank. ABC Bank pays them £1000 interest a year between them and XYZ Bank pays them £3000 interest a year between them.

Mr Smith is a diplomat and has no other income arising in the UK. Mr Smith's diplomatic salary is exempt from UK tax and his share of the interest is £2000 which is less than his personal allowance of £4615. Mr Smith is eligible to register for interest without tax taken off.

Mrs Smith has accompanied her husband on his diplomatic mission and works in the UK as a nurse. She receives a salary of £20,000 a year and her half share of the interest. Her total income is £22,000 which is more than the tax allowances she is due. Mrs Smith is not eligible to register for interest without tax taken off.

Mr Smith would like to register to receive interest without tax taken off and completes a form R85 for ABC Bank and a form R85 for XYZ Bank.

ABC Bank accepts the form R85 because they offer partial registration. Mr Smith's share of interest paid will be paid without tax taken off and Mrs Smith's will be paid with tax taken off. But XYZ Bank refuses to accept the form R85 from Mr Smith because they do not offer partial registration. So Mr Smith cannot have interest on this account paid without tax taken off but he can claim the tax back (see paragraph 13).

16. Joint accounts where one investor is ordinarily resident in the UK and one is not ordinarily resident in the UK

Banks and building societies can only pay interest on a joint account without tax taken off if the investors are eligible to receive interest without deduction of tax for the same reason. For example if one investor is entitled to register using form R85 and another investor is entitled to sign a declaration on form R105 interest cannot be paid without tax taken off. In other words, a mixture of a registration on form R85 and a declaration on form R105 is not allowed on the same joint account.