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Helpsheet

The Foreign Loss Election

Why it matters

Non-UK domiciled taxpayers who have made a claim for the remittance basis need to make a decision about their foreign capital losses.

The default position if no election is made is that non-UK capital losses realised by the taxpayer are not allowed when calculating their net gains.

All the while the taxpayer claims the remittance basis (and doesn't remit non-UK gains to the UK) this is not significant. However, if the taxpayer might remit proceeds from capital disposals, or might file on the arising (i.e. worldwide) basis in their first 15 years of residence, then being able to offset non-UK losses could impact their overall UK tax liability. To take a simple example:

Example

Overseas gains / losses as follows in a year that the taxpayer is on the arising basis (ignoring annual exemption for simplicity):

- Company A - £100 gain
- Company B - £40 loss

If no foreign loss election has previously been made, the taxpayer would be taxed on the £100 gain.

If, however, the foreign loss election has previously been made, the taxpayer could reduce the gain by the loss and only pay tax on £60.

What is the election?

The election can be made on the taxpayer's tax return, and must be made within four years of the end of the tax year where the remittance basis was first claimed.

The election is irrevocable (although it lapses when the taxpayer becomes deemed domiciled in the UK after 15 years of residence, or becomes domiciled in the UK under general law).

Effects of making the claim

On the face of it, making an election seems like the obvious option to take. However, there are three main implications of the election which mean that it is not the right decision for all taxpayers:

1. Ordering rules

By making an election, strict rules must be followed for all applicable tax years whilst the taxpayer is not UK domiciled and not deemed UK domiciled for tax purposes. Both UK and foreign losses must be offset against gains in the following order:

1) Remitted offshore gains that arose during the tax year

2) Unremitted gains that arose during the tax year
3) Any UK gains arising during the tax year

Example

The following gains / losses were incurred in a tax year (ignoring annual exemption for simplicity):

- Unremitted foreign gains: £50
- UK Gains: £20
- UK Losses: £40

If a foreign loss election was in place when the above scenario occurred, then the taxpayer would be taxed on the £20 UK gain. This is because under the election, the UK losses are allocated to the unremitted foreign gains in priority to UK gains.

If no election was in place, then the losses could be allocated to the UK gains, resulting in no taxable gains in the year.

2. Annual exemption restriction

Where the foreign loss election has been made and an individual is taxable on the arising basis, the annual exemption is not available to offset against remitted gains realised in prior tax years.

It should be noted that this is only relevant where the taxpayer is taxed under the arising basis, since a remittance basis claim results in the full loss of the annual exemption.

Example

The following gains / losses were incurred and taxable in 2023/24:

- Foreign gains from 2023/24: £2,000
- Remitted foreign gains from prior years: £10,000
- Available 2023/24 annual exemption: £6,000

If a foreign loss election was in place when the above scenario occurred, then the taxpayer would be taxed on full £10,000 remitted gains from the prior tax years. This is because under the election the annual exemption is not allowable against remitted gains from prior tax years. Note that the £2,000 gains realised in the current tax year have been offset by the £6,000 annual exemption, the unused exemption of £4,000 is then lost.

If no election was in place, then the annual exemption would have been fully utilised in the tax year, resulting in £6,000 of taxable gains in 2023/24.

3. Carry back loss restriction

Remitted gains are generally treated as accruing in the year they are brought into the UK. These gains are taxable with or without the foreign loss election in place. If the election has been made, then foreign losses will be deducted from the foreign remitted gains first per the ordering rules above.

Where a foreign loss election is in place, then a capital loss can only be offset against gains realised in the same tax year. This means that any foreign gains realised in an earlier tax year and then remitted in a later tax year cannot have any losses deducted against them.

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Example

The following gains / losses were incurred in the 2023/24 tax year (ignoring annual exemption for simplicity):

- Remitted Foreign gains from 2023/24: £200
- Remitted foreign gains from prior tax years: £1,000
- UK current year losses: £500

If a foreign loss election was in place when the above scenario occurred, then the taxpayer would be taxed on the £1,000 of remitted gains from the prior tax years. This is because losses cannot be 'carried back' and used against prior year realised gains. The £200 remitted gains accruing in 2023/24 under the election would be covered by the £500 capital loss. The remaining unused loss of £300 would then be carried forward to utilise against future gains.

If no election was in place, then the loss would be fully utilised in 2023/24, leaving £700 of taxable gains in 2023/24 and no loss to carry forward.

Summary

Care and consideration should be taken prior to making a foreign loss election claim. The election will not be beneficial for all taxpayers and will depend on a number of factors, including their current investments likely gains / losses (both UK and overseas) and their future intentions. The election is irrevocable and so the final decision requires accurate crystal-ball gazing!

If a taxpayer has very few UK assets or expected UK losses and anticipates needing offshore gains / losses in the UK, then the foreign loss election could be very valuable and reduce taxable gains for the taxpayer. However, a taxpayer who has both UK and overseas investments may find an election to their detriment.

What next?

The default position for non-UK domiciled individuals who have or will claim the remittance basis is that foreign losses are not allowable. However, the foreign loss election is not necessarily the right thing for all taxpayers because of the potential downsides outlined above. The best thing to do is to discuss the position so that we can assist you in thinking through whether the election may be beneficial to you.

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We undertake to apply reasonable care and skill in the provision of advice. We do not guarantee that tax planning steps will in all circumstances achieve a certain legal effect.

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