

DEBIT, CREDIT AND CHARGE CARDS AND REMITTANCES

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This article considers whether the use of debit, credit and charge cards involves a remittance for the purposes of the remittance basis. The current HMRC investigation into offshore bank accounts makes this issue highly topical.

Background law

The starting point is to understand the legal nature of debit, credit and charge cards. The following analysis draws heavily on *The Law of Bank Payments*.²

On the use of a card, three contracts come into being. For present purposes the most important terms of the contracts are as follows:

(1) Cardholder and supplier

This is the contract for goods or services between the cardholder and the person from whom the cardholder purchases goods or services (“the supplier”). This contract is the same whether the cardholder pays by card or by cash.

(2) Card-issuer and supplier

The card-issuer undertakes to honour the card by paying the supplier.

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² Brindle and Cox, Sweet & Maxwell, 3rd ed. 2004, para. 4-013. In any particular case it is strictly necessary to review the specific terms governing the card concerned, but I expect that will not often make any difference in practice. Store issued cards are not discussed here.

(3) Card-issuer and cardholder

- (a) A *debit* card is only issued by a bank. The contract between the card-issuer bank and cardholder authorises the bank to debit the cardholder's account with the amount of the card transaction.
- (b) Charge and credit cards are different. Here the cardholder is required to make a payment to the card-issuer. A *charge* card requires the cardholder to repay the balance outstanding after a set period.³ A *credit* card allows the cardholder to take extended credit.

Distinctions

It is necessary to distinguish between use of cards to obtain (1) cash, and (2) goods or services. It is also necessary to consider separately whether there is a remittance under (1) ordinary remittance basis principles⁴ and (2) the deemed remittance rules.⁵ The Inspectors Manual distinguishes between "UK Cards" and "Overseas Cards" and it distinguishes between cards "used in the UK" and "used abroad". I consider the meaning of these expressions below.

Cards used to obtain cash

Debit card used to obtain cash

If a debit card is used to obtain cash in the UK from a foreign account which is in credit,⁶ and the card is used at a branch of the bank which issued the card, then there is clearly a remittance of the money on ordinary remittance basis principles. The same applies if the cash is withdrawn from a bank which is not the card issuing bank, because the third party bank acts as the agent for the card issuing bank.

3 In the case of a bank issued credit card, the issuer is normally authorised to debit the cardholder's bank account to meet a debt due on the card. But in practice this facility is not used unless needed (or the card effectively becomes a debit card).

4 See *Taxation of Foreign Domiciliaries* 4th ed Chapter 7 (the RFI remittance basis).

5 See *Taxation of Foreign Domiciliaries* 4th ed para. 7.36 (deemed remittances).

6 If the effect of use of the card is to put an account into debit, there is obviously no remittance on ordinary principles, though the deemed remittance rule will in principle apply when the overdrawn account is repaid.

Charge card used to obtain cash

It is considered that the use of a *charge* card to obtain cash in the UK from a foreign account is a remittance by one of the “agencies of commerce” and so is a remittance under ordinary principles.⁷ The time of the remittance is when the sum is debited from the account, not when the card is used.

Credit card used to obtain cash

What is the position if an individual uses a *credit* card to obtain cash in the UK? There is a remittance under ordinary remittance basis principles if the use is “merely a means of transmitting income”. By contrast, if the card is used not to transmit income but as a method of borrowing, then there is no remittance under ordinary principles, neither when the money is borrowed nor when the borrowing is repaid.

One might therefore contrast two different ways that a credit card can be used:

- (1) If the card is used to obtain credit, e.g. if the balance on the card is not repaid at the earliest opportunity, then there is clearly no remittance under ordinary principles.
- (2) If the balance is repaid at the earliest opportunity, the position seems less clear. Two views seem possible:
 - (a) It may be said there is a debt, even though a short-term one, and the position is as (1) above.
 - (b) HMRC might argue that in economic substance the charge card is simply a form of “plastic money”. The position is the same as a debit or charge card.

A modern Court may not view with favour a formal distinction between credit and charge card. However the tax planning possibilities which result are limited by the deemed remittance rules, and the decision to restrict the deemed remittance rules to persons who are ordinarily resident suggests that tax planning of this kind by non-ordinarily resident individuals is acceptable. Moreover, any distinction other than the formal distinction between debt and methods of transmitting money is difficult to apply in practice. So it is considered that there is no remittance on

⁷ See *Taxation of Foreign Domiciliaries* 4th ed para. 7.22.2 (method of remittance does not matter).

ordinary principles when a *credit* card is used to obtain cash, even if payment is made to the card issuer at the earliest opportunity.

Cards used to obtain cash: deemed remittance rules

I turn to consider the deemed remittance rules. These rules only apply to an individual who is ordinarily resident in the UK.

In the case of a debit card, there is no debt for money lent so the deemed remittance rules do not apply. Since use of a debit card involves a remittance on ordinary principles this does not matter.

Where a credit card is used to obtain cash there is a “debt for money lent”. Assuming the money is lent in the UK, or received in the UK, this is a UK-linked debt, and a subsequent payment from a foreign account to satisfy the debt is *prima facie* a deemed remittance under the deemed remittance rules. If the cash is withdrawn in the UK, then the sum is lent in the UK and both the debt and interest are within the deemed remittance rules.

Where a charge card is used to obtain cash, there is also a debt for money lent. What about the overlap with the ordinary remittance rules which arises when a charge card is used? Since the sum used to repay the debt is actually received here, it cannot be *treated* as remitted here: one cannot deem to be the case which is actually the case. But the deemed remittance rules can apply on repayment of the interest on a charge card.

Cards used to obtain goods or services

Debit card used to obtain goods or services

Where a debit card is used to obtain goods or services, money passes from the cardholder’s account to the supplier’s account. If the supplier’s account is in the UK, it is considered that there is a remittance of the money transferred to the UK, under ordinary principles, because the money is received in the UK by authority of the cardholder.⁸ Whether the card is a UK card or an overseas card is irrelevant.

UK Credit or charge card used to obtain goods or services

What is the position where a UK credit or charge card is used to obtain goods or services? HMRC focus on the payment which comes from the individual’s foreign

⁸ See *Taxation of Foreign Domiciliaries* 4th ed para. 7.26 (receipt by third party).

account to the card-issuer's account. The Inspectors Manual provides:

“1569. Remittance Basis: Use of credit cards Published: 9/95

If a taxpayer who is chargeable on the remittance basis uses a UK credit or charge card to pay for goods or services, either in the UK or elsewhere, and subsequently settles his credit⁹ card account out of overseas income chargeable under Case IV or V of Schedule D, then the payment sent to the UK to settle the [credit card] account constitutes a taxable remittance, even if it is made direct to the credit card company, since the remittance does not have to be received by the taxpayer personally, it merely being sufficient that it is received in the UK by some other person on his authority (see IM 1564(1)).”

This is correct. For this purpose, I think, by “UK card” the Manual means a card whose issuer has a UK bank account, into which the cardholder makes payments. For such cards there is a remittance under ordinary principles. The time of the remittance is when funds are paid to the card-issuer's account, not when the card is used.

Overseas credit or charge card used to obtain goods or services

The line of argument used against UK cards does not apply to a card where the card issuer has a foreign bank account into which the cardholder makes payment. This is what the Manual refers to as an “overseas credit card”.

The Manual continues:

“Where an overseas credit card is used in the UK instead of cash, the taxpayer is effectively authorising the credit card company to settle his account [with the supplier] in just the same way as if the taxpayer had instructed his foreign banker to send a remittance to the supplier. If, on that basis, the taxpayer's overseas income is ultimately the provider of sums received in the UK (by the supplier) then there is a taxable remittance.”

For this purpose, I think, a card is “used in the UK” if the supplier's bank account (which receives the money) is in the UK.¹⁰ If it is, HMRC here adopt an “economic substance” approach and regard the card as a method of transmitting

⁹ The Manual refers once to “a credit or charge card” and thereafter to “a credit card”. I assume that the Manual regards them as identical for tax purposes and all references to credit cards include debit cards.

¹⁰ It is irrelevant where the cardholder is physically present in the UK at the time of the credit card transaction.

money from the individual's foreign account to the supplier's account in the UK. Hence there is a remittance under ordinary principles. It is considered that this is correct for a charge card but not for a credit card (which is a method of obtaining credit, not of transmitting money; see above).

HMRC then turn to consider a fallback argument based on the deemed remittance rules:

"It is sometimes argued that any indebtedness created by the use of an overseas credit card lies between the cardholder and the card company, rather than between the cardholder and the supplier."

This "argument" is in fact absolutely correct. When a card is used, there is no indebtedness between cardholder and supplier and there is an indebtedness (i.e. a debt) between cardholder and card issuer. In these circumstances, HMRC contend that the deemed remittance rules apply:

"The debtor/creditor relationship thus established, however, amounts to a loan of money expended on purchase by the debtor by the use of his card, which would be caught by ICTA s.65(6)."

This is very doubtful. There is certainly a debt owed by the cardholder to the card issuing company. But is it a debt "for money lent"? Strictly the only possible answer is, no. There is no loan. But the debt is the commercial equivalent of a loan; would a modern Court apply a purposive construction? One difficulty in doing so is that the Court would then have to decide whether the money is lent in the UK or out of the UK. Since no money is actually lent, the question is unanswerable. The Inspectors Manual raises this question but does not answer it:

"The terms of the particular credit card agreement must be examined. If, under the terms of the agreement, the money is regarded as lent to the cardholder at the moment when his card is accepted as payment in lieu of cash, then the lending can be said to take place in the UK and any repayment of either the loan or any interest out of Case IV or V income is regarded as a taxable remittance."

If, on the other hand, the money is only regarded as being lent at the date the overseas card company settles the supplier's account on the cardholder's behalf, then the lending takes place outside the UK and ICTA, section 65(6)(b) operates to treat the repayment of the loan, but not any interest, as a taxable remittance."

However if any Inspector actually followed this instruction and examined the terms of the credit card agreements, he would, I expect, be disappointed. The agreement will not address the issue of where the money is lent, because as far as the cardholder/issuing company is concerned, this is not a question which arises or ever could arise. For this reason it is suggested that the deemed remittance rules will not apply when an overseas credit card is used to acquire goods or services.

Overseas card used abroad

The Inspectors Manual continues:

“If an overseas credit card is used abroad and the account is settled direct to the card company out of overseas income within Cases IV and V, no liability to UK tax will arise.”

This is correct; note for this purpose, I think, a card is “used abroad” if the supplier’s bank account which receives the money is outside the UK.

The Inspectors Manual concludes:

“But if an asset purchased using the card is brought to the UK and subsequently sold here, there will be a taxable remittance, at the date of disposal, up to the amount of any Case IV or V income used to settle the original account.”

It is considered that this is correct in the case of a debit or charge card but not for a credit card.

Credit cards: Conclusion

In summary, the position is as follows:

- (1) If a debit card is used to obtain cash in the UK from an account in credit, there is a remittance of the money received in the UK on general principles.
- (2) If a charge card is used to obtain cash in the UK from an account in credit, it is considered that there is a remittance of money received in the UK on general principles.
- (3) If a credit card is used to obtain cash in the UK, it is considered that there is no remittance either on ordinary principles or under the deemed remittance rules, though HMRC do not agree.

- (4) If a debit card is used to obtain goods or services, and the supplier receives the payment in an account in the UK, there is a remittance on ordinary principles.
- (5) If a UK credit or charge card is used to obtain goods or services, there is a remittance on ordinary principles.
- (6) If an overseas charge card is used in the UK, it is considered that there is a remittance on ordinary principles.
- (7) If an overseas credit card is used in the UK, it is considered that there is no remittance on ordinary principles, though HMRC do not agree.
- (8) If an overseas card is used abroad, there is in principle no remittance.

Planning implications

Clients should be advised to use overseas credit cards for transactions abroad.

Clients should be advised not to use overseas credit cards in the UK, because this is likely to lead to a dispute with HMRC, but if this course has been taken, any assessment should be firmly resisted.

James Kessler is the author of Taxation of Foreign Domiciliaries (4th ed. 2005), Key Haven Publications PLC.