Chartered Institute of Taxation
Excellence in Taxation

THE ADVANCED DIPLOMA IN INTERNATIONAL TAXATION

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ADVANCED INTERNATIONAL TAXATION (JURISDICTION)

Suggested Solutions

Question 1

Part 1: Tax residence status of foreign incorporated companies

Raymond is the shareholder of certain foreign incorporated holding companies. Where Raymond is the main shareholder, there is a risk that he will be seen to make those companies UK tax resident unless he takes steps to ensure that they are managed and controlled abroad.

This risk is elevated in the case of companies incorporated in tax haven jurisdictions particularly in the absence of significant substance.

Importance of UK Residence

A UK resident company is subject to UK corporation tax on its worldwide income and gains.

Determination of Residence Status

A foreign incorporated company is UK resident where it's central management and control is located in the UK. Central management and control is the top level strategic management of the company. Examples of decisions that may demonstrate central management and control include:

- Major finance decisions, e.g. the making of loans or entering into funding or loan arrangements;
- Decisions concerning the acquisition and disposal of significant assets;
- Decisions concerning the payment of dividends;
- Decisions to acquire or dispose of businesses or subsidiaries.

Where key strategic decisions such as those outlined above are taken by the directors of the company at directors' meetings central management and control will reside at those meetings. Thus the company will be resident where those meetings are held. This old principle known as "the case law test of central management and control" was reconfirmed in the Court of Appeal in *Wood v Holden* heard in 2006.

However if Raymond makes the type of decisions set out above in the UK then HMRC may argue that the company has become UK resident, even if the directors rubberstamp these decisions at directors meetings held abroad.

HMRC Challenge

HMRC may decide to challenge residence in various circumstances particularly where the beneficial owners of the company are UK tax resident. This is even the case where the beneficial owners of the company are non-domiciled taxpayers. HMRC have begun to make more frequent challenges regarding the residence status of companies following their success in *Laerstate BV -v- HMRC*. This case involved a situation where a UK resident individual carried out amongst other activities the negotiation of key contracts in the UK.

Factors that may be used by HMRC to argue that an "offshore company" is UK tax resident include:

- UK directors or individuals actually make key decisions of the company in the UK;
- Major contract negotiations take place in the UK;
- The company lacks substance e.g. does not have an office in the location that it is incorporated in;
- The key protagonists reside in the UK;
- UK individuals control the company's bank account;
- The overseas directors receive only nominal remuneration;
- Board meetings take place in the UK.

It is unlikely that HMRC will argue that a trading company with substantial substance in its country of incorporation is UK tax resident. Therefore it is unlikely on the facts that HMRC will challenge the tax residence status of the French trading group, particularly as the directors regularly meet in Paris to make key decisions. This is notwithstanding the fact that Raymond may negotiate key contracts in the

UK, provided that the board makes the final decision as to whether to enter into the contract. (*Wood v Holden*)

In the unlikely event HMRC did challenge residence status, residence would be determined by reference to the “place of effective management” tiebreaker provisions of the French-UK treaty. Effective management is a concept closely analogous to the concept of central management and control and is likely to be held to be exercised in France.

From a pragmatic perspective HMRC would in any event gain little by challenging the residence status of a trading company in cases where the company is resident and subject to tax in a high tax jurisdiction, as it would have to give credit for the foreign tax suffered.

However, HMRC may well attempt to challenge the tax residence status of Raymond’s holding companies as they are located in low tax jurisdictions. The Guernsey company holding Raymond’s investments may be particularly susceptible since the directors will need to continually monitor their investments and it is likely Raymond will offer advice on this aspect. In contrast the board of the BVI company holding the French group may have a more passive role since not many decisions may be required if their intention is simply to retain the shares in the French group.

<u>Part 2: Residence protocol</u>

In order to reduce the risk that a foreign incorporated company inadvertently becomes UK resident it should ensure that it has substance e.g. staff and offices in the country of its incorporation. In addition it should create and implement a residence protocol. This protocol will provide guidelines as to how the company is to be managed and includes a communications policy.

- Raymond should not participate in board meetings from the UK;
- Raymond should resign his directorships;
- Raymond should not issue instructions to the directors;
- Raymond should appoint new directors who understand the business of the holding companies and make the key decisions;
- Negotiations should not take place in the UK;
- The boards of the holding companies should meet regularly and as required;
- No board meetings should be held in the UK.

The determination of the residence status of an offshore company requires a consideration of all the circumstances to determine where the key decisions of the company are made. Companies incorporated in tax haven jurisdictions are subject to particular scrutiny. HMRC are increasingly investigating the tax residence status of allegedly offshore companies.

<u>Part 3: Permanent establishment</u>

Although activities undertaken by Raymond for the French trading group are unlikely to make the group UK resident, nevertheless activities such as arranging the group’s refinancing and developing customers in the UK are likely to create significant value.
'Permanent establishment' is defined at CTA 2010, Pt 24 Ch 2 (s 1141 et seq). A company has a 'permanent establishment' in a territory where:

- it has a 'fixed place of business' there through which its business is wholly or partly carried on; or
- it has an agent acting on its behalf there and this agent has and habitually exercises there authority to do business on its behalf.

A 'fixed place of business' includes a place of management; a branch; an office, factory or workshop.
There are specific exclusions which include:

- where the business is carried on there through an agent of independent status acting in the ordinary course of his business; or
- where the activities being carried on through a fixed place of business or agent are only of a 'preparatory or auxiliary character'.

It is likely that Raymond’s activities will fall to be treated as creating a fixed place of business or alternatively a dependent agent. It is unlikely that his activities would qualify for the exception for activities being 'preparatory or auxiliary in character'. Raymond may therefore constitute a PE of the French group in the UK and HMRC may attempt to allocate significant value to that PE through transfer pricing rules.

Metrol would be recommended to establish a UK resident subsidiary, to employ Raymond. The subsidiary would provide management services to the French group and charge arm’s length fees for the advice and services it provides.

Question 3

A company's residence can be determined by the location of its central management and control or place of effective management (P.O.E.M.). If a company is UK incorporated, then to move residence it will need to find a location that will treat it as resident on another test (normally some form of management test), and has a double tax treaty with the UK. It is then possible for the company to become non-UK resident under the treaty tie breaker clause. In the case of a treaty based on the OECD Model, this will be achieved by ensuring that the P.O.E.M. is not in the UK. If a company is non-UK incorporated, it either needs to ensure that its central management and control is no longer in the UK so that it is not treated as UK resident under UK rules, or it needs to become non-resident under a treaty, as outlined above.

To protect the UK tax revenue, there are certain procedures that need to be followed when a company migrates. In addition, there is anti-avoidance legislation to consider.

TMA 1970, s.109B-F sets out the procedures that need to be followed prior to a company ceasing to be resident. These are:

- A company must give advance notice to the Board of the Inland Revenue of its intention to cease to be UK resident, specifying the time at which it will cease to be resident, together with a statement of the amount of tax that is or will be payable.
- The notice must provide particulars of the arrangements which it proposes to make for securing the payment of the tax. These arrangements may include a proposal to enter into an exit charge payment plan arrangements must include provision for the payment of any outstanding PAYE tax for which the company is liable, any income tax deducted from payments made by the company for which it is accountable, any tax deducted from payments made to non-resident entertainers or sportsmen or to subcontractors in the construction industry, and any tax which the company is liable to pay in respect of certain continental shelf profits of non-resident persons. For these purposes tax payable includes interest on overdue tax.

If HMRC approval is given on the basis of incomplete information, it is void.

SP 2/90 sets down guidance notes to help companies comply with these requirements. The Statement of Practice provides details of where the notice should be sent to, what information it should contain and recommends that the notice be given at least two months before the company intends to migrate. If a company becomes non-resident and does not notify the Revenue in advance making arrangements to pay its tax outstanding, it will be liable to a fine of up to the amount of the tax payable, which has not yet been paid.

If tax remains unpaid by the migrating company 6 months from the time it became payable, then the Revenue can, within 3 years of the relevant time, issue a notice on certain persons stating the amount of tax due and requiring that they pay it.

Where an exit charge payment plan has been entered into, the relevant time is the later of a year and a day after the end of the accounting period in which the company ceases to be UK resident, or the date on which the tax is payable under the plan.

When a company migrates, it will cease to be within the charge to corporation tax thus it will be treated as if it has ceased to carry on a trade.

The consequences of migration are as follows:

1. An accounting period will end; CTA 2009, s.10(1)(g).
2. Inventory will be treated as disposed of on a cessation; CTA 2009, s.162.
3. Balancing allowances and charges will arise on plant and machinery; CAA 2001, s.61.
4. Loan relationships are deemed to have been disposed of and immediately reacquired at fair value; CTA 2009, s.333.
5. Derivatives will be treated as assigned and immediately reacquired at fair value; CTA 2009, s.609.

6. Intangible fixed assets are treated as disposed of and reacquired at market value; CTA 2009, s.859.
7. Capital assets are deemed to have been disposed of and reacquired at market value. TCGA 2009, s.185.

The company is deemed to have disposed of and repurchased its chargeable assets at market value immediately before migration, except for any assets situated in the UK which are used for the purposes of a trade that continues to be carried on in the UK through a PE.

It is possible to postpone the charge arising in relation to foreign assets where the migrating company is a 75% subsidiary of a UK company, and a joint election is made by the companies within two years of the migration. Foreign assets are those assets situated outside the UK, and used in or for the purposes of a trade outside the UK (i.e. non-trading and UK situated assets not included).
The postponement operates as follows:

1. The net gains on foreign assets on migration are calculated. (There is no postponement should a net loss arise).
2. The disposal is treated as giving rise to a single chargeable gain which can be postponed.
3. The postponed amount on the foreign assets will be brought into charge on the parent company as follows:
   i. If within six years the migrating company disposes of any of the assets which contributed towards the chargeable gain postponed, a proportion of the gain postponed will be brought in. For subsequent disposals of assets you only include the gains on the assets still held by the subsidiary immediately before each disposal in the figure for "gains postponed and "gross gains postponed at migration".
   ii. If at any time the company ceases to be a 75% subsidiary of the UK parent by the disposal of shares, any remaining postponed gain will be charged. Similarly, if the company ceases to be a 75% subsidiary of the UK parent for any other reason, the postponed gain will become chargeable if the UK parent subsequently disposes of its shares.
   iii. If the UK parent ceases to be UK resident, any remaining gain will be charged.

In order to ensure that the UK rules on exit charges are compatible with EU law, FA 2013 introduced provisions which allow companies incorporated in the EEA, including UK companies, to defer payment of corporation tax on unrealised profits or gains which become chargeable when they cease to be resident in the UK and become resident for tax purposes in another Member State, or when they cease to trade through a permanent establishment in the UK. The amount which may be deferred is the difference between the corporation tax which the company is liable to pay for the accounting period, and the amount to which it would be liable if the various exit charge provisions mentioned above did not exist. An exit charge payment plan is an agreement between the company and HMRC.

The company agrees to pay the deferred liabilities in accordance with the plan, together with interest which runs from the normal due date for payment of the tax to the date it is actually paid. There are two methods of payment available.

The first method is the standard instalment method, whereby the tax due is paid in six equal annual instalments. The first instalment is due nine months and one day after the end of the accounting period in which the migration takes place. Subsequent instalments are due at 12 monthly intervals following that date. The alternative method is the realisation method. Under this method, the plan must specify all of the relevant assets and liabilities held by the company (capital assets, stock, loan relationships, derivatives and IFAs), together with the amount of the tax attributable to each of them under the plan.

The company is then required to provide an annual report to HMRC, detailing the realisation of any assets specified in the plan. The tax deferred on chargeable assets is payable on the earlier of the date the asset is disposed of or ten years after the end of the period in which the migration took place.

The gain that can be postponed is 520,000 – 95,000 = £425,000.

None of the postponed gain will become chargeable as Houston Ltd is still a 75% subsidiary.

None of the postponed gain will become chargeable as the asset sold gave rise to a deemed loss on migration.

A deemed gain will crystallise on Houston Ltd of 75,000 × 50,000/120,000 = £31,250.

None of the postponed gain will become chargeable as the asset was sold more than 6 years after migration.

The remaining postponed gain of £43,750 will be brought into charge as Houston Ltd ceases to be a 75% subsidiary.

The whole of the postponed gain has been brought into charge thus no further amounts can be brought in.

Question 4

Part 1: Peter's domicile

Peter's domicile status would have followed that of his father Charles as a domicile of origin at birth and then it would continue to follow any changes in his father's domicile as a domicile of dependency, until he attained the age of 16 on 1 January 1977.

Charles' domicile of origin was Swiss. This was replaced by a Dutch domicile of choice. To acquire a domicile of choice in a jurisdiction an individual must physically reside in a jurisdiction and have an intention to reside there permanently or indefinitely (*Bell v Kennedy [1868] LR 1 Sc & Div 307*).

Charles did spend a period in England between 1960 and 1964 and this was a period in which Peter was born.

Peter inherited his father's domicile as his domicile of origin at birth. (*Udny v Udny [1869] Lr 1 Sc & Div 441*). This is likely to have been Swiss.

As demonstrated Peter's father had acquired a domicile of choice in the Netherlands so that at 16 Peter would have had a Dutch domicile of dependency. Peter would therefore retain that domicile unless he acquired his domicile of choice in another jurisdiction. Although Peter has lived in the UK, his objective was to pursue his career in banking and not to live in the UK permanently or indefinitely.

Furthermore, his continuing ties to the Netherlands including owning a home in the Netherlands (*Re Flynn (No 1) [1968] 1 WLR 103*) demonstrate that Peter has not abandoned his Dutch domicile. Following his retirement from banking Peter's reasons for remaining in the UK are strictly temporary i.e. to remain in the UK until his children complete their education here and then he wishes to return to the Netherlands with his wife Nelie, (*Douglas v Douglas [1871] LR 12 Eq 617*) where he wishes to remain and be buried there in his wife's family's cemetery. Peter has not therefore acquired a domicile of choice in England and Wales and has retained his Dutch domicile.

Part 2: Key Income Tax and Capital Gains Tax features of non-domiciled tax regime

Remittance basis key features are as follows:

- Remittance basis: Foreign income and capital gains arising from Peter's foreign portfolio and bank accounts are only taxable when remitted to the UK.
- UK income does not qualify for the remittance basis and is taxable on the arising basis.
- An election for the remittance basis must be made on the tax return.
- In the first 7 years of residence an individual may elect for the remittance basis free of charge.
- Where an individual (wishing to avail of the remittance basis) has been in the UK for at least 7 out of the immediately preceding 9 years prior to the relevant year that individual must pay a remittance basis charge of £30,000. As Peter has been UK resident at 5 April 2015 for 9 of the previous 9 years he would be required to pay the £30,000 RBC if he wished to benefit from the remittance basis.
- Where an individual has been UK resident for at least 12 of the 14 years immediately prior to the relevant year the RBC is increased to £50,000.
- Where an individual subject to the RBC elects for the remittance basis he must nominate income or gains.
- Where an individual elects for the remittance basis he loses his personal income tax and capital gains tax annual allowances.
- Income and gains are subject to mixed fund rules.
- The mixed fund rules make it very important to carefully segregate income and gains, for example to preserve 'pure capital'.

Part 3: Peter's exposure to inheritance tax

Non-domiciled individuals are not subject to inheritance tax on their non-UK situs assets.

Peter owns properties in the UK, the Netherlands, France and Switzerland. In the case of land situs depends upon actual physical situation. Therefore only the UK property would be subject to UK inheritance tax.

He has bank accounts in these four countries. A debt owed by a bank (e.g. bank account) is situated at the branch where it is primarily recoverable. (*R v Lovitt*, *[1912] AC 212*). Thus only the UK bank account would be subject to inheritance tax.

Peter's foreign portfolio of publicly quoted shares are likely to be foreign property and hence not subject to inheritance tax. In particular: registered shares and securities are situated where they are registered unless transferable in more than one country in which case they are situated in the country in which they would be likely to be dealt with in the ordinary course of affairs. (Standard Chartered Bank Ltd v CIR Ch D, [1978] STC 272; Treasurer for Ontario v Aberdein PC 1946, [1947] AC 24; R v Williams and Another PC, [1942] 22 All ER 95.

In the case of chattels situs depends upon actual physical situation. Thus if Peter brings Art and Jewellery to the UK it will be subject to inheritance tax. Extra-statutory concession F7 'Foreign owned works of art' ensures that where a work of art is in the UK temporarily for cleaning or restoration or for a loan to a public exhibition by a non-UK domicile and a chargeable event arises there is no charge to tax.

Where an individual has been UK resident for 17 out of 20 years he becomes deemed domiciled for inheritance tax purposes.

An individual who is deemed domiciled is subject to UK inheritance tax on their worldwide assets.

Question 5

Part 1: UK holding company

The United Kingdom has several advantages as a holding company of other trading companies. In particular, CTA 2009, part 9A introduced a broad exemption applying to UK and foreign dividends. UK does not qualify as a "small company" under the terms of the legislation. Dividends received by companies other than small companies will not be chargeable to UK corporation tax if:

- The dividend falls into an exempt class;
- The distribution is not of a kind mentioned in para E or F in CTA 2010 section 1000(1); and
- No deduction is allowed to a resident of any country outside the UK under the laws of that country in respect of that distribution.

Distributions fall into the exempt class if they are:

- Distributions from controlled companies;
- Distributions in respect of non-redeemable ordinary shares;
- Distributions in respect of shareholdings less than 10% of issued share capital;
- Dividends from transactions not designed to reduce tax; or
- Dividends received for shares accounted for as liabilities.

Anti avoidance provisions apply to prevent some exemptions applying but otherwise it is expected that the exemptions will cover the vast majority of dividends received by UK companies. One of the classes of shares not covered by the exemption is preference shares. These should therefore be avoided when formulating the structure for the new Croftlea Inc Group.
The EU Parent / Subsidiary Directive, which has been implemented into the Domestic Law of each of the member states, allows for the payment of dividends free of the requirement to deduct withholding taxes. Conditions vary from member state to member state but at a minimum:

- The dividend must be paid by a company in one member state (A) to another company in another member state (B);
- B must hold at least 10% of the share capital of A.

As noted above, specific conditions vary from member state to member state and the conditions in Italy and Portugal should be reviewed in detail to ensure that the exemption applies to payments to the UK.

As a general rule, UK domestic law requires companies making payments of interest to withhold tax at 20%. However, there are a number of exceptions to this general rule. The key exclusions are:

- Payments of interest that qualify for exemption under the EU Interest and Royalties Directive.
- Payments of 'short' interest. This is, broadly speaking, interest on loans that will not be in place for more than a year. However, the definition can be contentious, and detailed advice should be taken on this if intending to utilise this exemption.
- Exemption under a Double Tax Treaty e.g. the US.

The EU Interest and Royalties Directive applies in much the same way as the Parent – Subsidiary directive and has been adopted into the domestic law of the UK and other member states. Again, specific conditions vary from state to state, but at a minimum are:

- The interest must be paid by a company in one member state (A) to another company in another member state (B);
- There must be a direct shareholding or 25% or more between these companies, or there is a common 25% shareholding for the two companies.

Under the terms of the US – UK Double Tax treaty, interest can be paid without deduction of withholding tax if certain conditions are met and clearance is obtained.

Part 2: Restriction on the tax deductibility of interest costs in the UK

The newly created Croftlea Group will be a large group for the purposes of the Worldwide Debt Cap rules which are contained within part 7 or TIOPA 2010. The provision of these rules will apply to UK for an accounting period where the net debt of UK exceeds 75% of the “worldwide gross debt” of Croftlea group. This is the so called “gateway test”.

In the absence of further information on the indebtedness of the Croftlea Group, the net debt of UK is £30m. The worldwide gross debt of the Croftlea Group is £25m. As a result, the net debt of the UK exceeds 75% of the worldwide gross debt of Croftlea Group under the proposed structure.

Having failed the Gateway Test, the interest costs and other finance expenses of UK will be subject to a cap equal to the consolidated total finance expenses (including interest) costs of the Croftlea Group. The Gateway Test is applied using the average of debt at the end of the previous period of account and the debt at the end of the current period of account. Therefore, if the funding structure is just a short term measure which does not straddle an accounting period end, then there may be no cap on the finance expenses of UK. Detailed financial projections including balance sheet models should be prepared to evaluate whether the WWDC will apply or not.

The transfer pricing provisions of UK tax legislation (TIOPA 2010, Part 4) will also apply to the loan from Croftlea to the UK. The UK tax authorities will seek to make a transfer pricing adjustment to the taxable profits of UK where they consider a UK tax advantage has been obtained. Consideration will be given to both the level of funding and the interest rate applied to the loan. Comparisons will be made with the level of funding and cost of that funding that would be available to UK if it were to apply for external funding as a standalone entity. Therefore if Croftlea were to lend UK funds in excess of what a bank would be willing to lend, the interest on those excess funds would be disallowable for tax purposes. Under the same principle, an excessive interest rate would also be disallowed for tax purposes.

Interest costs on the loan from Croftlea Inc may also be disallowed under the unallowable purpose test. Section 441 CTA 2009 would apply where UK’s purpose for entering into a loan relationship includes a purpose that is not amongst the business or other commercial purposes of the company. Section 443 applies where the sole or main benefit of a scheme is to obtain a deduction for the purposes of corporation tax. As the interest expense arises on loans which are all related to a commercial transaction and have a clear commercial purpose of funding the acquisition of I and P, the loans are not part of a scheme the main purpose, or one of the main purposes, of which was to secure a UK tax advantage.

The late interest rules in CTA 2009 apply in certain cases to defer a UK corporation tax deduction for interest expense until the interest is paid rather than on a normal accruals basis if the interest is not paid within twelve months of the period that it accrues. However, these rules only apply if the recipient of the interest is resident in a non-treaty country. As the UK and the US have treaty, the late interest rules should not apply to the transaction.

However, more broadly, it is not tax efficient to put the majority of the debt into the UK which has the lowest headline corporate income tax rate of the four counties under consideration. Subject to transfer pricing and other restrictions on the deductibility of interest costs, the most tax efficient territory in which to have debt financing is generally the one with the highest rate. In this case, Croftlea would look like the natural home for the debt financing.

Part 3: Implications of inter-company trading

The EU is a free trade zone and therefore no customs duties or import VAT is payable on the movement of goods between member states.

VAT applies on the sale of goods and services in the EU. This applies to inter-state sales as well as intra-state. However, where a company has obtained the VAT number of another company in an EU member state, it does not need to charge VAT on the sale of those goods but instead can apply a rate of zero. The purchasing company is obliged to operate what is called the reverse charge mechanism. The purchaser will apply the rate of VAT applicable in its own country to the purchase and treat this as acquisition VAT. This acquisition VAT is added to output VAT on sales to arrive at total output VAT. Where a company is trading company such that VAT on all of its purchases is fully recovered, the full amount of the acquisition VAT can be recovered as input VAT. This is all done through the VAT return and there is therefore a cash flow advantage.

Question 6

Part 1: Lindsay

Permanent Establishment in the UK

Article 5 of the OECD model treaty gives us the definition of a permanent establishment.

Under article 5(1), a permanent establishment means a fixed place of business through which the business of an enterprise is wholly or partly carried on and this implies a degree of permanence.

Article 5(2) states that a fixed place of business includes:

- A place of management;
- A branch;
- An office;
- A factory;
- A workshop; and
- A mine, oil or gas well, quarry or other place of extraction.

However under article 5(3), a permanent establishment is not created where the work carried on is of a preparatory or auxiliary nature.

On the basis of the above, it would appear unlikely that your proposed entry into the UK market will create a permanent establishment as she will have any permanent premises in the UK. Attendance at trade shows will not be considered in any way permanent.

The website, under the existing model treaty is also not considered to create a permanent establishment. The OECD commentary explains the position as follows:

1. A website cannot, in itself, constitute a permanent establishment;
2. Website hosting arrangements do not result in a permanent establishment for the enterprise that carries on a business through a hosted website.
3. Except in very exceptional circumstances, an internet service provider will not be deemed to constitute a permanent establishment for the enterprises to which it provides a service, and
4. A place where computer equipment, such as a server, is located, may in certain circumstances constitute a permanent establishment, but requires that the functions performed at that place go beyond what is preparatory or auxiliary.

Although you have engaged a UK internet service provider to host her website, the existence of the website should not create a permanent establishment under the terms of the above commentary.

However, recently, the OECD has looked again at the tax implications of a digital economy as part of its BEPS Action Plan.

The OECD released a discussion draft in March 2014 as part of this review which suggests certain modifications to the permanent establishment definition:

- The list of preparatory and auxiliary activities which are excluded should be removed.
- The creation of a new form of permanent establishment based on a "significant digital presence in another country's economy".
- Extending the current forms of permanent establishment to a "virtual fixed place of business", a virtual agency permanent establishment or an "on-site business presence permanent establishment".
- Not ring fencing the digital economy.

It is not yet clear how these proposals would be implemented in practice. However, I would have thought that a website targeted at customers in one particular country that makes significant sales in that country, may well fall within points 2 or 3 above. I note that you have requested a UK domain name for the website, which suggests that you are specifically targeting the UK market.

Consequently, it is possibly that under the definitions above, you may have a permanent establishment in the future on the basis of your proposed business model.

Obviously these proposals are still in draft form and are not yet incorporated in UK law. However, UK tax law on the definition of a permanent establishment makes direct reference to the OECD model. We will keep you updated of any developments in this area.

I conclude that on the basis of the above analysis, your business model proposal for the UK will not create a fixed place of business in the UK at the current time.

However, article 5 also provides that a permanent establishment will be created where a person, other an agent of an independent status is acting on behalf of an enterprise and has, and habitually exercises, in a Contracting State, an authority to conclude contracts in the name of that enterprise. (article 5(5)).

You have noted that you intend to attend several trade fairs and make trips to the UK for the conclusion of larger contracts. As the owner of your business, you cannot be considered to be an independent agent and it is likely that, depending on the number and significance of your trips to the UK, that your activities will fall squarely within the definition of article 5(5).

The attendance at trade fairs is unlikely in and of itself to create a permanent establishment unless you conclude contracts there. Visits to the UK for marketing and networking purposes are similarly unlikely to create a permanent establishment. The crucial element of article 5(5) is the authority to conclude contracts. Recent commentary on this article has also suggested that the ability to engage in detailed negotiations would also be a critical factor. May I suggest that you limit the activities of your visits to the UK to marketing and networking? Only in exceptional cases, should you engage in the negotiation and conclusion of contracts. That work would be better done by phone from Dublin if you wish to avoid a challenge from HMRC that you have created a permanent establishment in the UK.

Goods sold to UK customer from Ireland

The place of supply when goods leave Ireland is Ireland. If the UK customer is VAT registered in the UK and Lindsay obtains his VAT registration number, then Lindsay should zero rate the supply. This is often referred to as a dispatch.
If however the customer is not VAT registered in the UK, as is likely for many retail customers browsing on a website, Lindsay will need to charge Irish VAT at the rate that would be appropriate to the goods being sold.

When Lindsay’s cumulative annual UK turnover exceeds £70,000 she will be required to register for VAT in the UK under the Distance Selling Provisions (VATA 1994 schedule 2). The lever of turnover will be measured with reference to the calendar year. Once Lindsay is UK VAT registered, the place of supply for all UK sales will be the UK and they will therefore be subject to UK VAT whether the customer is UK VAT registered or not.

These Distance selling provisions were originally introduced to prevent businesses being able to take advantage of lower VAT rates in one member state over another by making sales from the lower tax territory. However, VAT rates in Ireland have historically been higher than those in the UK. All other things being equal, this would make the sales price to UK retail customers higher than they may be expecting. Lindsay may wish to register for VAT voluntarily even before she reaches the £70,000 threshold to allow her UK customers to benefit from the lower UK rate of VAT.

There are no port formalities within the European Union, so when Lindsay sends goods from the UK to Europe they are not held up at the port of entry into that European country. They go straight to the premises of the customer.

Returns

There are two returns of importance. The first return is called the Intrastat, or the supplementary Statistical Declaration (SSD). There is an acquisitions Intrastat and a dispatches Intrastat. These are required for dispatches if the total value within a year exceeds £250,000.The Intrastat must be completed and submitted electronically within 21 days of the end of the relevant month. Nil returns are not required. A failure to submit an Intrastat when required is a criminal offence.

The other return that has to be completed only applies to dispatches and is called the EC Sales List or ESL. It shows the value of supplies made to each customer, with each customer being identified by their VAT registration number in the appropriate Member State.

EC sales listings must be submitted quarterly (or monthly – see below) within 14 days of the end of the quarter for paper returns or within 21 days of the end of the quarter for electronic returns. It is possible to make an annual submission of an EC sales listing if turnover does not exceed £25,500 plus the current registration limit or, the sales to EU customers do not exceed £11,000. ESLs can be submitted quarterly provided that the VAT exclusive value of supplies of goods to other member states has not exceeded £35,000 in any one of the previous four quarters. Once the threshold is exceeded, monthly returns must be submitted. Most traders selling to EU member states will have to fill in an EC sales list and if it is wrong or if it is late, there are civil penalties to penalise the trader for his wrong doing.

There is one other return that has information on it in respect of sales to overseas customers and purchases from overseas suppliers and that is the VAT return itself. Lindsay will have to put an entry for the value of supplies in Boxes 6 and 8 of the VAT return. Box 6 is for total supplies made, excluding VAT i.e. the total sales figure, and this must include the Box 8 figure. Box 8 is the statistical box for supplies of goods and related services to the EU. Likewise the value of purchases has to be accounted for in Boxes 7 and 9 of the VAT return. Box 7 is for total purchases made, excluding VAT i.e. the net purchases figure, and this must include the Box 9 figure. Box 9 is the statistical box for acquisitions of goods and related services from the EU.

Question 7

Part 1: Maxine's residence status

In mid-2007 Maxine became UK resident but in March 2010 she left the UK, about the time her former partner left the UK to become tax resident in France. Under the case law test she was non-resident for 10/11 and 11/12, however she became UK resident again in 12/13. From 6 April 2013 residence is determined by reference to the Statutory Residence Test (SRT). Under that test she was non-resident for 13/14, but became UK resident again in 2014/15. Maxine's residence status is examined further in the following paragraphs.

Maxine is UK resident for 2012/13 under the case law test. From 6 April 2013 Maxine's residence is determined under the SRT. This test contains a set of objective criteria that determines an individual's tax residence position.

The legislation sets out automatic residence tests, which if satisfied determine residence. These are not met, in particular Maxine does not have a UK home for 30 days during that tax year.

Where these are not met the test determines residence by applying a series of connecting factors. Where a person has been UK tax resident in any of the previous 3 years the connecting factors to be taken into account are:

- Accommodation;
- Minor children/Spouse;
- Work;
- 90 days;
- Country tie (The country Maxine spends most time in).

The test is applied by determining the number of connecting factors a taxpayer has. The number of ties an individual has with the UK will determine the number of nights a person may spend in the UK in a tax year without becoming UK resident.

The tables are set out below. Table A applies in cases where the individual has been UK resident at any time in the previous 3 years. The second table applies where the individual has not previously been resident in the 3 immediately preceding tax years.

Table A: UK Ties needed if you were UK resident for one or more of the three tax years before the tax year under consideration *Days spent in the UK in the tax year under consideration*	*UK ties needed*
16 - 45	At least four
46 - 90	At least three
91 - 120	At least two
Over 120	At least one
Table B: UK Ties needed if you were UK resident in none of the three tax years before the tax year under consideration *Days spent in the UK in the tax year under consideration*	*UK ties needed*
46 - 90	All four
91 - 120	At least three
Over 120	At least two

Table A applies to Maxine, since as is explained below she was UK resident for the purposes of the SRT for 12/13. Each year is examined in further detail below.

Maxine's residence status position for 2014/15, 2013/14, 2012/13 is examined below:

Tax year	Days
2011/12	75
2012/13	140
2013/14	55
2014/15	95

2012/13
UK-Resident 140 Days (3 ties)

Leaving UK 11/12 –NR 10/11-NR 09/10 TR

Ties
- *Accommodation?*
  Yes.

- *Minor children/Spouse?*
  Yes Jack 18 yrs old August 2012.

- *Work?*
  Yes. Maxine works for more than 3 hours a day on more than 40 occasions.

- *Country tie?*
  No.

- *90 days?*
  No 10/11 No 11/12 (75)

Election
Although Maxine's residence period straddles the old case law rules and the new SRT Maxine may elect to determine her residence under the new SRT in respect of years before the new rules came into force (6 April 2013). This election is effective only from the perspective of applying the new rules, it does not affect the actual residence status for years prior to the introduction of the new rules**.**

2013/14
(2 ties) Non resident (55 days)

Leaving UK (Res 12/13)

Ties
- *Accommodation?*
  Yes

- *Minor children/Spouse?*
  No

- *Work?*
  No

- *Country tie?*
  No

- *90 days?*
  Yes (12/13 104)

2014/15
UK-Resident 95 Days (2 ties)

Leaving UK (13/14 NR –Res 12/13 11/12 -NR)

Ties (Two)

- *Accommodation*
  Yes

- *Minor children/Spouse*
  No

- *Work*
  No

- *Country tie*
  No

- *90 days*
  Yes

<u>Part 2: The effect of any applicable tax treaty</u>

Maxine is French resident for all tax years from 10/11-14/15. For 2012/13 and 2014/15 she is also dual resident being resident in the UK under UK domestic law. Maxine may seek relief under the French-UK treaty, so that her residence is awarded under that treaty to only one country, by reference to a tiebreaker test.
Where an individual is a resident of both states the OECD tiebreaker test provides as follows:

1. The person shall be deemed to be a resident only of the Contracting State in which they have a permanent home available to them; if they have a permanent home available to them in both States, they shall be deemed to be a resident only of the State with which their personal and economic relations are closer (centre of vital interests).
2. If the Contracting State in which the person has their centre of vital interests cannot be determined, or if they do not have a permanent home available in either State, they shall be deemed to be a resident only of the State in which they have an habitual abode.
3. If the person has an habitual abode in both Contracting States or in neither of them, that person shall be deemed to be a resident only of the State of which they are a national.
4. If they are a national of both Contracting States or of neither of them, the competent authorities of the Contracting States shall settle the question by mutual agreement.

Applying the above test for 2012/13 Maxine's residence is awarded to France, as she has a permanent home available to her in France, but not in the UK.

For most of 2014/15 Maxine only has a permanent home in France, so that the treaty will award residence to that state. From 15 March arguably Maxine also has a permanent home available in the UK, residence would then be determined by reference to 'centre of vital interests' There is insufficient information in the question to determine its location, however, as her child lives in the UK, the personal element of that test may be weighted towards the UK.

<u>Part 3: Overseas workday relief</u>

Where a non-domiciled individual becomes UK resident, a relief is available in respect of employment income for the first three years of UK residence, where that individual performs the duties of their employment at least partly abroad.

The conditions are:

- The individual must be not domiciled in the UK throughout the year; and
- Must be taxed on the remittance basis; and
- Must perform the duties of the employment wholly or partly outside the UK, and that year is either the first tax year immediately following three consecutive tax years for which they are not resident in the UK, or one of the next two tax years after such a year.

Where a remittance basis employee carries out both UK and non-UK duties under a single contract of employment, the total earnings from that employment are apportioned. The earnings relating to the UK duties will be assessed on an arising basis. The earnings qualifying for the relief are treated to be ‘foreign earnings’ and are not taxable in the UK unless remitted to the UK.

If the employee continues to pay the equivalent to national insurance in their former state of residence then they may be able to obtain a certificate of coverage which would exempt them from National Insurance in the UK. In particular where the employee is from a country in the European Economic Area (EEA) they will require a Portable Document A1, E101 or E102.