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Time of Request: Tuesday, November 23, 2010 00:11:11 EST
Client ID/Project Name:
Number of Lines: 152
Job Number: 1823:254830590

Research Information

Service: Terms and Connectors Search
Print Request: Current Document: 1
Source: Doing Business in the United Kingdom
Search Terms: § 24.05 International Element

Doing Business in the United Kingdom

PART VI TAXATION
CHAPTER 24 Introduction to the UK Tax System

2-24 Doing Business in the United Kingdom § 24.05

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§ 24.05 International Element

[1] Introduction

For tax purposes, the UK comprises England and Wales, Scotland, Northern Ireland and (for certain taxes) the territorial waters of those countries and the Continental Shelf; the Channel Islands and the Isle of Man are not included. In theory, the UK Parliament could impose a tax liability on any person in the world in respect of his activities anywhere in the world. But as a practical matter, for a charge to tax to be effective (that is, for there to be more than a remote chance of recovering the tax charged) either the person sought to be taxed must have some personal contact (by residence, ordinary residence or domicile) with the UK or the activity giving rise to a charge to tax must take place within the UK (that is, have a UK source).

Consistent with general rules of private international law, the UK courts will not enforce the taxation laws of other countriesn1 but European Union law does provide for mutual assistance in the collection of Value Added Tax in other Member States in appropriate cases.

[2] Connecting Factors

[a] Residence and Ordinary Residence of Individuals.

Tax in the UK is founded mainly on the concept of residence.n2 Residence is determined by physical presence in the UK in a year of assessment. Accordingly, a person who is present in the UK for 183 daysn3 or more during a tax year is always treated as UK resident for that year. Similarly, an individual is treated as having become resident in the UK when his visits to the UK have averaged three months a year in four consecutive tax years (although if a person intends to make visits averaging such periods, he is treated as being UK resident from the time of his first visit).

Previously, where a person had accommodation available in the UK for his use (which excludes, for example, property which has been commercially let), he was treated as UK resident for any tax year in which he was present in the UK however short his stay might be and whether or not he used the accommodation. This is no longer the case, with effect from 1993-94.n4

Although "ordinary residence" does not normally determine liability to UK tax, it often determines the extent of any liability. The place of a person's ordinary residence is where he is usually resident as established by examining his pattern of residence over several tax years. It is therefore possible for an individual to be ordinarily resident in the UK during a particular tax year, even though he is not present in the UK at any time in that year.

Where during the course of a tax year an individual becomes a new permanent resident or leaves the UK to take up permanent residence (or in certain cases fulltime employment) abroad HMRC will, by concession,n5 split the tax year. The concession (ESC 11) applies only to those coming to live in the UK permanently or who intend to stay for at least two years (for whatever purpose) and to those leaving the UK to live permanently abroad or for a period of at least three years. With effect from 19 March 1998, the split year concession does not apply for capital gains tax purposes. Persons returning to the UK after a period of non-residence lasting less than 5 years of assessment ("Temporary Non-Residents") are subject to capital gains tax on asset disposals made during these intervening years. For departures from the UK in the year 2005/06 onwards use of the tie-breaker clause of a double tax treaty will no longer be effective in avoiding the charge to tax.n6 Prior to that it was possible to be UK resident but to be treated as non-resident under the terms of certain double tax treaties.n7

From 1996/97 onwards the liability of non-residents who do not trade in the UK, is limited to tax deducted at source, if any.

[b] Residence of Trusts.

A trust is resident where the majority of the trustees are resident.n7.1 Finance (No.2) Act 2005 introduced measures to counter the avoidance of capital gains tax by trustees under the relieving terms of certain double tax treaties, where the trustees are UK resident at some point in the tax year and make a disposal when non-resident.n8

[c] Residence of Companies.

The test of company residence was radically revised by the Finance Act 1988.n9 Formerly, a company was resident for UK tax purposes where its central management and control was exercised. With effect from 15 March 1988, a company which is incorporated in the UK is regarded as resident here, irrespective of other factors. For other companies the central management and control test remains the principal factor in determining the residence of a company.

Company residence is considered in greater detail below.n10

[d] Residence of Partnerships.

A partnership is resident in the UK if the partners are resident in the UK, notwithstanding that the partnership business may be carried on outside the UK. However, where the partnership business is controlled and managed outside the UK, the partnership is deemed to be non-resident, notwithstanding that some of the partners are resident in the UK and that some of the business operations of the partnership are connected with the UK. However under the UK self-assessment legislation, UK partners must include their share of such income in their calculation of liability to UK tax.n11

[e] Dual Residence.

A person may be resident for UK tax purposes in more than one country, so that the fact that someone is already considered to be resident in a country other than the UK does not of itself preclude the Inland Revenue from treating him as also being resident in the UK. For example, a US corporation whose central management and control is in the UK is regarded as resident in the UK by UK law and as resident in the USA by US law. But see *"Treaty residence"* section below for tiebreaker rules.

[f] Treaty Residence.

Where the UK and another tax jurisdiction could each claim to tax a person in respect of the same taxable activity and have entered into a double tax treaty,n12 the terms of that treaty may determine in which of the two jurisdictions that person is considered to be resident for the purposes of applying the treaty,n13 or which jurisdiction should have first claim to tax in respect of that income or activity, and such provisions would modify the normal domestic law of one of the jurisdictions. The most recent double tax treaty between the UK and the USn14 contains a "tie-breaker clause"n15 setting out the rules for determining the extent of liability in each country. For individuals, these follow the OECD Model Tax Convention; for companies the competent authorities of the UK and the US will endeavour to determine by mutual agreement how the treaty will apply to dual resident companies.

Some capital gains tax aspects of the tie-breaker clause of double tax treaties are discussed above.n16

[g] Domicile.

The concept of domicile in the UK differs from that of residence or ordinary residence and is different from that of "domicil" used in other jurisdictions, particularly continental ones.

Every individual is born with a domicile of origin which is generally the domicile of his father at the time of birth.n17 The domicile of origin remains unless and until it is displaced by the individual acquiring a domicile of choice.n18

A domicile of choice is acquired by anyone over the age of sixteenn19 becoming resident in another jurisdiction with the intention, formed independently of external pressures, of remaining in that jurisdiction permanently, or at least indefinitely.n20 Special rules apply to women who married before 1st January 1974.n21

Domicile is not dependent upon citizenship.

If an individual abandons his domicile of choice in any particular jurisdiction by ceasing to reside there with the intention of doing so permanently, his domicile of origin will revive unless, and until, a domicile of choice is acquired elsewhere.

Following a lengthy period of consultation beginning in October 1991, the Government announced in *Hansard* on 16 January 1996 that it had decided not to change the existing law on domicile. However, proposals to change the tax treatment of non-UK domiciled were set out following the pre-Budget in 2007 and may become law during 2008.

A company's domicile is the place of its incorporation.n22

[h] Deemed Domicile.

Domicile is construed in an extended sense for the purposes of inheritance tax, so that, in general, three years domicile outside the UK is needed for an individual with a UK domicile to acquire a foreign domicile. An individual who is resident in the UK for 17 out of the 20 years ending with the year in which the tax liability arises is also usually deemed to be domiciled in the UK.n23 From 6 April 1996, no account is to be taken of a person's retention of an entry in the UK electoral role as an overseas voter, in determining whether or not he is domiciled or deemed to be domiciled in the UK for income tax, capital gains tax or inheritance tax purposes.n24

[i] Citizenship.

Citizenship is not normally relevant for tax purposes. However, although the acquisition of citizenship does not necessarily imply a change of domicile, it may be a factor to be taken into account in determining whether or not there

has been such a change.n25

[j] International Exchange of Information.

The Inland Revenue has the power to gather information for, and to enter into agreements with, other countries to exchange information with the tax authorities in the other country on matters concerning liability to income tax, capital gains tax, inheritance tax and corporation tax.n26 The UK also applies the EU Mutual Assistance Directiven27 under which exchange of information takes place between EU countries and documents may be served on a UK resident in relation to a tax liability in another Member State. However, the extended powers enacted under FA 2006 now include the enforcement and recovery of taxes levied in other Member States.n28 International co-operation against tax avoidance took another step forward in 2004 with the Revenue authorities of Australia, Canada, the UK and the USA meeting together and entering into closer working arrangements.

Further provisions have been introduced to deal with the UK's obligations, in common with other Member States of the EU, to report the payment of cross-border interest payments to the authorities of the Member State in which the recipient of the payment resides.n29 This implements the EU Savings Tax Directive which took effect from 1 July 2005. In addition to the arrangements with the EU Member States under this directive, separate information exchange agreements have been entered into involving the UK and Jersey, Guernsey and the Isle of Man - S.I. Nos. 2005/ 1261, 1262 and 1263.

FOOTNOTES:
(n1)Footnote 1. Gov't of India v. Taylor [1955] AC 491.

(n2)Footnote 2. HMRC's practice is set out in detail in its leaflet IR20.

(n3)Footnote 3. Days of arrival and departure are, as a matter of practice, ignored but not for taxpayers to whom the split tax year concession applies, when both dates are counted as days present in the United Kingdom.

(n4)Footnote 4. FA 1993 s.208, inserting TA 1988 s.336(1), TCGA 1992 s.9(4) and IHTA 1984 s.267(4).

(n5)Footnote 5. Extra-statutory concessions All (1992), as amended 29 January 1996 in regard to temporary visitors to the UK, and D2 (1992).

(n6)Footnote 6. TCGA 1992 s.10A, introduced by FA 1998 s.127; and s.10A(9)-(9C), effected by F(No.2)A 2005 s.32.

(n7)Footnote 7. TCGA 1992 s.10A(10)), repealed by F(No.2)A 2005 s.32(6).

(n8)Footnote 7.1. ITA 2007 s.475, formerly ICTA 1988 s.685E.

(n9)Footnote 8. TCGA 1992 s.83A, introduced by F(No.2)A 2005 s.33.

(n10)Footnote 9. FA 1988 s.66.

(n11)Footnote 10. *See § 25.01[2] infra*.

(n12)Footnote 11. ITTOIA 2005 ss.857-858, replacing TA 1988 s.112, as amended by FA 1995 s.125; TCGA 1992 s.59.

(n13)Footnote 12. *See § 24.02[3] supra*.

(n14)Footnote 13. *See, e.g.* Article 4 of the 1977 OECD Model Double Taxation Convention on Income and Capital (*see Section 38.02 infra*).

(n15)Footnote 14. Concluded in July 2001 and effective from March 2003.

(n16)Footnote 15. Article 4 para. 5. *See also Inland Revenue Tax Bulletin* April 2003 (special edition).

(n17)Footnote 16. *See § 24.05[2][a] supra*.

(n18)Footnote 17. In the case of an illegitimate child it is the domicile of the mother.

(n19)Footnote 18. Udny v. Udny (1869) LR 1 SC & Div 441.

(n20)Footnote 19. Domicile and Matrimonial Proceedings Act 1973 s.3.

(n21)Footnote 20. *Buswell v. Inland Revenue Comm'rs (1974) 49 TC 334,* CA; *Inland Revenue Comm'rs v. Duchess of Portland [1982] 1 All ER 784.*

(n22)Footnote 21. *See* Domicile and Matrimonial Proceedings Act 1973 s.1. The effect of the Act for certain tax purposes is varied for US citizens by the UK/US double taxation treaty.

(n23)Footnote 22. *Crasque v. IRC 23 TC 210.*

(n24)Footnote 23. Inheritance Tax Act 1984 s.267(1)-(3) and (4).

(n25)Footnote 24. FA 1996 s.200.

(n26)Footnote 25. Wahl v. Attorney-General [1932] All ER Rep 922 HL.

(n27)Footnote 26. FA 2006 ss.173-174, replacing ICTA 1988 s.815C inserted by FA 2000 s.146 and IHTA 1984 s.220A inserted by FA 2000 s.147.

(n28)Footnote 27. Directive 77/799 EEC as amended by Directive 2004/56/EC from April 2004

(n29)Footnote 28. F(No.2)A 2005 s68, Mutual Assistance Provisions Order - SI 2004/3207 & FA 2006 s.173(2).

(n30)Footnote 29. FA 2003 s.197.