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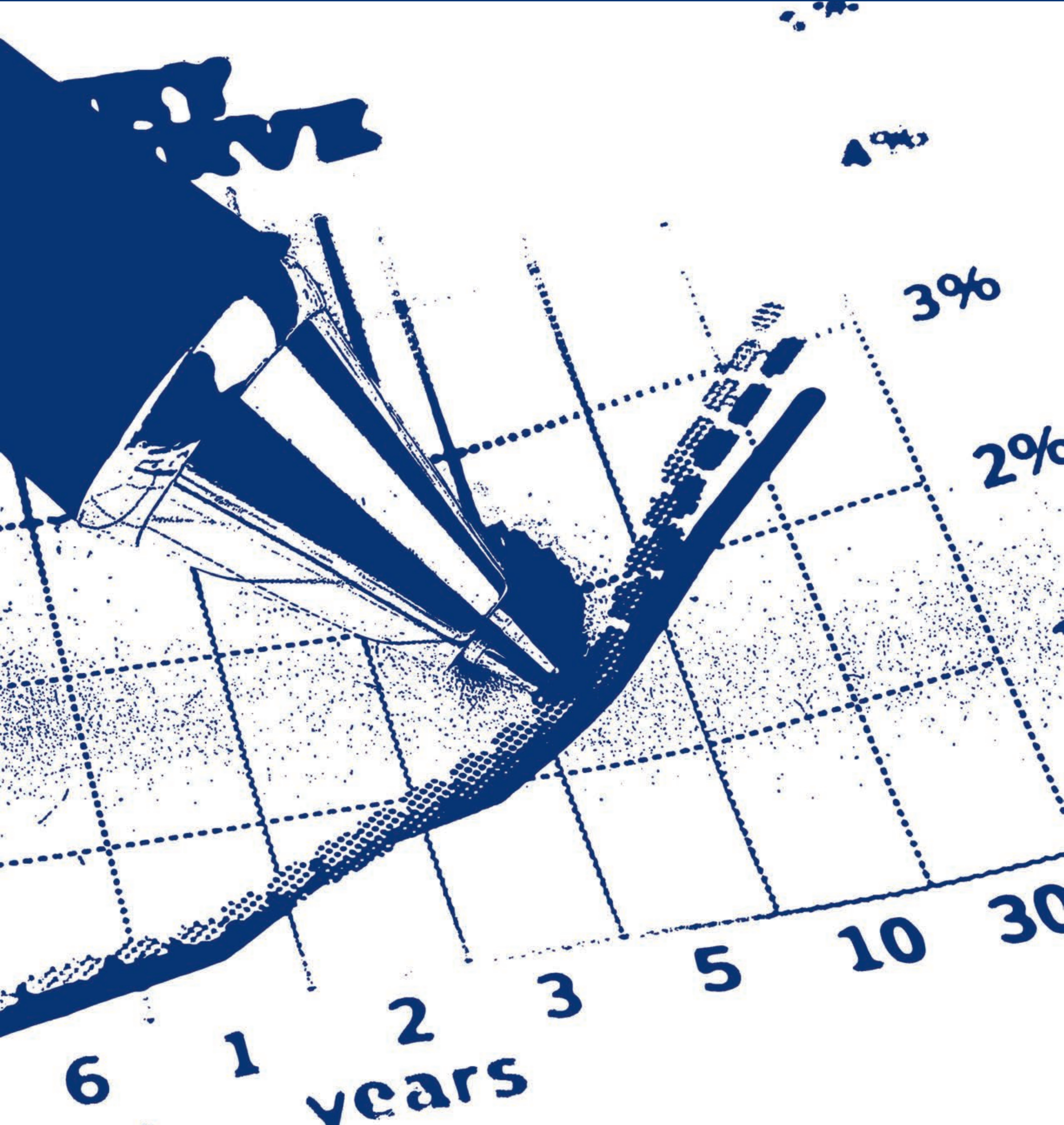

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Tax residency: coming or going – do you know where you are?

9 October 2013

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Introduction

This panel reviewed where companies and other entities are treated as being resident for tax purposes, a question which has become more important due to globalisation, executive mobility and the growth of online business. Passing or failing the test for corporate residence has significant implications for the tax position under both domestic law and international treaties. The panel also considered some technical and practical aspects of corporate redomiciliation and migration.

The Netherlands

The main question is how tax residency is determined. Based on Dutch law, any company that is incorporated in the Netherlands is considered a Dutch tax resident unless another country with which the Netherlands has concluded a tax treaty successfully claims its tax residency. The place of effective management is decisive to determine the tax residency. It is therefore relevant to look at where important meetings take place and where the majority of the board of the directors is present. It was noted that it does not consist of finding 'flyouts' for meetings; the decision-making should be effectively made in the Netherlands. As an exception to the tie-breaker rule, there are tax treaties (eg, the Dutch-UK tax treaty) where the tax residency is determined by way of a mutual agreement procedure.

Canada

With reference to the Canada-Hong Kong tax treaty, from a Canadian tax perspective, residency of a party is straightforward because it is based on enumerated grounds; moreover, in Hong Kong, the concept of residency has a different meaning. Therefore, if a company is incorporated in Hong Kong but centrally managed and controlled in Canada or vice versa, the question regarding residency is raised and to the extent that this corporation is resident in both countries, it could be useful to consult the competent authorities. The anti-treaty shopping paragraphs basically provide that the benefits of the reduced withholding rates are not applicable if a main purpose test is met. However, this main purpose test is extremely broad.

Hong Kong

First, it is to be stressed that tax residency is not a concept under Hong Kong domestic law. When Hong Kong was entering – very recently – into its first double tax agreements with various countries, it needed to adopt a concept of residency for treaty purposes that is foreign to domestic law. Under Hong Kong treaties, being incorporated in Hong Kong is sufficient to claim tax treaty benefits.

Under Hong Kong domestic law, the fact that a permanent establishment is established in Hong Kong does not automatically make it liable to tax. In order to be liable to tax, the profits must arise in or be derived from Hong Kong and, moreover, in respect to certain kinds of income, the tax authorities have historically taken an 'all or nothing' approach. Therefore, the permanent establishment could be either wholly taxable or wholly non-taxable. With some kinds of income, like services income, an apportionment could be made.

Israel

Under Israeli law, an individual is considered an Israeli resident if the centre of their life is in Israel. The question arises whether a married couple can have different residency. For a long period of time, the tax authorities thought that a married couple should reside in one place.

UK

From a UK tax perspective, an elective regime has been introduced regarding profits of UK foreign permanent establishments. Such regime leads to equal tax treatment between profits being repatriated in the UK from a foreign subsidiary and profits being repatriated in the UK from a foreign permanent establishment. As with controlled foreign company rules, these rules have some anti-diversion, anti-avoidance provisions.

Guatemala

Guatemala had a comprehensive tax reform that finished in January 2013. Several provisions, that are already in place in other jurisdictions, were implemented in Guatemala, such as permanent establishments, the concept of residency – which Guatemala did not have – and transfer pricing rules. This represents an effort to try to bring Guatemala up to speed in international tax law.

Mozambique

The source and residency criteria apply to taxation in Mozambique, with residents being taxed on all income generated on a worldwide basis, whereas non-residents and permanent establishments of non-resident entities are taxed only on income derived from Mozambique. Non-resident entities are usually required to register ventures or subsidiaries in Mozambique or they have to appoint a legal, local representative to comply with their tax obligations.

The concept of beneficial ownership

UK

In the UK the main principles of beneficial ownership income were developed in the Indofood case, according to which in order to be the beneficial owner of income for UK purposes, a full privilege to directly benefit from the income has to be demonstrated.

Hong Kong

Hong Kong holding companies are commonly used, particularly for investments into China. In this respect, the PRC tax authorities issued guidance on the beneficial owner of income.

Corporate residency

UK

In the UK, corporate residency is still very much a hot topic in which the HM Revenue & Customs are interested because, obviously, they are interested in getting all the UK tax of any of these entities which are actually resident of the UK under UK rules and, equally, they are interested in terms of denying claims for treaty benefits if they cannot take the benefit of the treaties when they are not actually UK tax residents. There are two tests in the UK: (i) an incorporation test and (ii) a test which is a case law, factual test based on central management and control of a company. This looks at the strategic highest level of control – where strategic decisions in terms of the business itself are taken – rather than day-to-day control.

The Netherlands

As discussed above, any company that is incorporated under Dutch law is considered a Dutch tax resident; we call that the 'deeming provision' which applies to those entities. Now that it is possible that foreign companies can be converted into a Dutch entity and the

Dutch entity can be converted into a foreign legal entity, the question arises whether these deeming provisions still apply to those entities.

Uruguay

Up until the entry into force of the 2006 tax reform, Uruguay had no corporate tax residency definition. The tax reform introduced the concept of tax residency which, for domestic purposes, is basically relevant in order to determine which kind of income tax the company will be subject to and the way in which these taxes have to be paid. The test for corporate tax residency essentially reads that all legal entities and other entities incorporated under Uruguayan law shall be considered to be tax residents, that is, there are no central management or control tests.

Portugal

If the head office or the place of effective management of the company is located in Portugal, then the company would be considered to be tax resident in Portugal. Therefore, you just need to have one of those located in Portugal for the company to be considered tax resident in Portugal. There is no legal definition of what is considered to be the head office or the place of effective management under Portuguese tax laws so each time you need to interpret the terms. For the definition of head office, reference to the corporate law meaning states that it will be the corporate and legal seat of the company.

In general, Portuguese companies, instead of migrating, normally incorporate another company in another jurisdiction in order to avoid the attention of the authorities and the public.

Italy

The Italian exit taxation regime has been recently amended by the Italian legislator, with the specific goal of making this regime consistent with the European Court of Justice's very recent jurisprudence. The general rule is that the transfer of a company's tax residency abroad is considered to be a taxable event, unless the assets of the company are located in a permanent establishment located in Italy. The rule for determining when a company is considered to be tax resident in Italy is quite strong; it is not easy not to be considered tax resident in Italy for a company. The rule is that a company is considered to be tax resident in Italy if for the greater part of the fiscal year (183 days per year) the company has had its legal seat, the place of effective management or 'its main business purpose' in Italy. Italy is one of the few countries in the world that uses this kind of prerequisite for establishing the tax residency in Italy.

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Cutting your losses: where did all my NOLs go?

Thursday 10 October 2013

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