HMRC Trustee Residence Guidance

Introduction

The following guidance gives HMRC's view on the application of the residence tests in section 69 (2D) Taxation of Chargeable Gains Act 1992 and section 475 (6) Income Tax Act 2007 in relation to overseas trust companies particularly those owned by UK-based groups.

The guidance has the following sections:

PART 1 Background

1. There have been longstanding tests to determine the residence of trustees to establish whether the trust of which they are a trustee is subject to UK tax. However, these rules were different for income tax and capital gains tax with the result that trustees could be UK-resident for income tax purposes but non-UK resident for capital gains tax, or vice versa. Therefore in Finance Act 2006, as part of the Trust Modernisation programme, the Government made some changes to the trustee residence test and introduced a common test for both income tax and capital gains tax. One of the objectives of the Trust Modernisation programme was to provide greater consistency of approach between income tax and capital gains tax in relation to the taxation of trusts so reducing the administrative burden especially on smaller trusts.

2. The new legislation, Section 69 Taxation of Chargeable Gains Act 1992 (and for income tax section 685E Income and Corporation Taxes Act 1988, now replaced by sections 475 and 476 Income Tax Act 2007) took effect from 6 April 2007.

3. The rules that came into force on 6 April 2007 treat the trustees of a settlement as a single person, as distinct from the persons who may be of trustees from time to time. The residence status of that single person (referred to below as the "body of trustees") at any given time is determined in the first instance by the residence status of the persons who are trustees at that time:

   - If all the trustees are either resident in the UK or not resident in the UK, the residence status of the body of trustees follows that outcome.
   - If at any time at least one trustee is resident in the UK and at least one is not, the body of trustees is resident in the UK only if any settlor of the trust was resident, ordinarily resident or domiciled in the UK at any time when he or she introduced property into the trust.

Branch, Agency or Permanent Establishment

4. The rules include the provision (section 69(2D) TCGA 1992 and section 475(6) ITA) that a trustee will be treated as UK resident (and therefore, if he is the sole trustee, the trust will be taxed as a UK trust) when the trustee acts as trustee in the course of a business which he carries on through a '*branch, agency or permanent establishment*' in the UK.

5. HMRC accept that for trustees the '*branch*' and '*agency*' tests apply to non-corporate trustees and the '*permanent establishment*' test to corporate trustees. Non-UK resident companies that are trustees therefore need only be concerned about being treated as UK resident if they carry on a business through a permanent establishment in the UK. This is in line with section 10B Taxation of Chargeable Gains Act 1992 which has the effect that an overseas company is not taxed on the gains made by a UK branch or agency, but only on those made by a permanent establishment here.

6. The Commentary to the OECD Tax Model Convention provides further guidance on the meaning of "permanent establishment". The Convention is used by OECD and other countries as a basis for the negotiation, application and interpretation of bilateral tax treaties. Further information on the OECD Tax Model Convention is given in Annex A.

7. As the legislation refers to a business carried on in the UK through a '*branch, agency or permanent establishment*' the same principles outlined in A-C and the examples below apply in the case of non-corporate trustees (a branch or agent) as they apply in the case of corporate trustees (permanent establishment). Because most cases will in practice involve non-UK resident trust companies the examples refer only to them. However, where particular concepts that are peculiar to permanent establishment are concerned, eg the independent agent exemption, then they affect only corporate trustees, and the language used reflects that.

8. When considering the applicability of the tests in section 475(6) Income Tax Act 2007 and section 69(2D) Taxation of Chargeable Gains Act 1992 the following three questions are relevant:

A. Is the trustee carrying on a business in the UK?

By business we mean the business of providing professional trustee services for a fee. This question does not relate to the business of a particular trust that might be conducted by the trustee. It enquires whether the person who is a trustee carries out business activities (as a professional or businessman, not as trustee of a particular trust) in the UK.

B. If the trustee is carrying on a business in the UK is it carrying on that business through a branch, agent, or permanent establishment in the UK?

Again this means that the trustee is carrying on through the branch, agency or permanent establishment the sort of activities from which it substantially derives its worldwide profits - providing professional services for a fee - and not what it is doing in relation to an individual trust. In the case of a corporate trustee it might be the case that activities are carried out in the UK on its behalf by a dependent agent with the result that the trustee is treated as having a PE in the UK (see paragraph 3 of Part 2 of this guidance).

C. If so is the trustee carrying on the activity of being a trustee of that particular trust in the course of its business through the branch, agent or permanent establishment?

For example, a corporate trustee could have a permanent establishment in the UK but it is only when it is acting as a trustee through that place that the deemed residence rules apply in relation to the particular trust for which the company acts as trustee. The test is on a trust by trust basis. So while a corporate trustee might be acting as a trustee in relation to one trust through a fixed place of business in the UK, other trusts must be considered separately according to their facts and circumstances.

The same principle applies in the case of a non-corporate trustee: the test is on a trust by trust basis.

Core activities

9. In connection with Question C and in line with the Commentary to the OECD Tax Model Convention, "carrying on the function of being a trustee" means in this context activities which are the core activities of a trustee and not those activities which are auxiliary or preparatory. This applies equally to non-corporate trustees.

10. A trustee is the person who has a legal duty to manage the assets of that trust in the best interests of the beneficiary or beneficiaries. The trustee manages, employs and disposes of the trust assets in accordance with both the terms of the trust and the duties and responsibilities which the law places upon trustees. The core activities of a trustee would therefore be regarded as including:

10.1 the general administration of the trusts

10.2 the over-arching investment strategy.

10.3 monitoring the performance of those investments.

10.4 decisions on how trust income will be dealt with and whether distributions should be made.

11. There are other activities which trustees carry out which are not core activities central to their conduct and management of the trust, but are instead preparatory or auxiliary activities. These generally can include information gathering meetings, including meetings with independent agents or with beneficiaries but, as mentioned below, each case will have to be considered individually.

12. In deciding whether the conduct and management of a particular trust is being carried on in the course of the corporate trustee's business through a permanent establishment, HMRC's approach will be to look at where the core activities are physically being carried out. If these core activities are being carried on in the UK through the corporate trustee's permanent establishment, the trustee would be treated as UK resident for the purposes of the particular trust. However as well as the nature or significance of the individual activities and meetings and whether they are core activities, we would also consider the

issue of frequency. So where there is, in relation to a particular trust, evidence of considerable administrative work – such as meetings with investment managers or beneficiaries - being carried on in the UK through a permanent establishment, so that such meetings have become a major element of the trustee's activities in relation to that trust, and no longer preparatory or auxiliary, we would need to consider carefully whether as a matter of fact the non-UK resident corporate trustee was acting as a trustee through that permanent establishment.

13. The guidance that follows sets out examples of when a corporate trustee may or may not be regarded as UK resident. This guidance is based on the law as it stood on the day of publication. HMRC will publish amended or supplementary guidance if there is a change in the law or in the Department's interpretation of it. Whilst the guidance is intended to be as extensive and helpful as possible, it should not be assumed that it will provide a definitive answer in every case. That will depend upon the facts of each individual case. You can of course take your own advice on this issue and where HMRC's view is that there is a liability to UK tax on the basis that it regards a trust as UK resident because of how these rules apply to the trustees then the trustees can appeal to an independent tribunal.

PART 2 Examples and Scenarios

The following examples run through various activities which could be carried out in the UK in connection with a trust by offshore trust companies and cover the following areas:

1. Preparatory work prior to the creation of any trust.
2. Trustee carrying out duties for the administration of any trust.
3. Activities carried on for the trust other than by the non-UK resident corporate trustee
4. UK resident directors or other employees of a non-UK resident corporate trustee.

The examples all relate to non-UK resident companies that are trustees. The same principles would apply for other non-UK resident persons who are trustees (and for whom the relevant UK-based entity would be a branch or agency rather than a permanent establishment).

1. Preparatory work prior to the creation of any trust

1.1 A non-UK resident trust company that is to be a trustee of a settlement may carry out a number of activities in the UK before the trust is created. This might, for example, include discussions with clients such as potential settlors or beneficiaries over the appropriate terms of any trust. It could also include research with specialist professionals about possible trust investments and assets. These discussions may take place even before the beneficiaries are chosen.

Example 1

Before the January Trust is established, February Ltd, a non-UK resident trust company holds several meetings in the UK at its Manchester office with the potential settlor Mr January. The meetings are to discuss the possible terms of the trust and suitable investments.

HMRC view: The January trust does not yet exist, so there is no need to consider the tests in section 69(2D) TCGA 1992 and section 475(6) ITA. In any case, introductory meetings and discussions of this type would generally be regarded as preparatory or auxiliary activities and not core activities.

2. Trustee carrying out duties for the administration of any trust

As mentioned in paragraphs 9 to 11 of the Background section of this guidance, a range of activities may be carried out by a trustee once a trust

has been set up including meetings. When considering whether the corporate trustee is carrying on the administration of a particular trust in the course of their business through the permanent establishment, the frequency of the meetings will be looked at as well as their significance and quality.

Example 2

March Ltd, a non-UK resident trust company that is trustee of the April Trust, holds quarterly meetings in the UK at its London offices with investment advisers. The purpose of these meetings is for March Ltd to collect purely factual information about potential assets to inform future investment strategy for the April trust. The actual decisions about the investment strategy are taken by March Ltd at their home office outside the UK. No other activities or meetings relating to the April Trust are carried on in the UK.

HMRC view: March Ltd has a permanent establishment in the UK. However, the significance of the meetings with the investment advisers is not sufficient for March Ltd to be regarded as acting as a trustee in respect of April Trust through that permanent establishment. They will not, therefore, be regarded as UK resident for the purposes of the April Trust.

Example 2a

May Ltd, a non-UK resident trust company, is sole trustee of the June Trust. May Ltd carries out all the work for the trust through its UK offices, including preparatory work, general administration, meetings with investment managers, accountants, beneficiaries etc.. The investment and distribution policies are also all determined in the UK office. Formal ratification of those strategies, including signature of documents, is made by May Ltd at very brief meetings outside the UK, with little or no further discussion of the proposals before

approval is given.

HMRC view: Although the strategic decisions are core activities, all the administration of the June Trust has been carried out in May Ltd's UK office. The formal meetings outside the UK although prima facie core activities are in reality merely "rubber stamping" all the UK work. May Ltd has acted as a trustee in respect of the June Trust through its UK permanent establishment and so will be treated as UK resident for the purposes of the June Trust.

Example 2b

July Ltd, a non-UK resident trust company is trustee of the August Trust. It always carries out the core activities of the August Trust at its office overseas. The beneficiary of the trust has a single one-off meeting with July Ltd at July's Manchester office to discuss the potential release of capital from the August trust. The discussion involves the imposition of certain conditions on the beneficiary before such a release.

HMRC view: On the face of it July Ltd by discussing the release of capital and the imposition of conditions with the beneficiary has engaged in a core activity and this has taken place at what is July's permanent establishment in the UK. So prima facie July Ltd is acting as trustee of the August Trust through a permanent establishment However the whole context has to be looked at - i.e. where the decision making on the trust is being carried on and if the meeting in the UK was a one-off. If the trustee took the information from the meetings out of the UK with them and then discussed and made the decisions outside the UK, they would not be UK resident. If there was any doubt as to where the decision making is taking place we would as part of our considerations consider the frequency of any meetings both within and outside the UK.

3. Activities carried on for the trust other than by the non-UK resident trust company

3.1 Whilst a non-UK resident trust company acting as a trustee may not carry out trust business at a fixed place of business permanent establishment in the UK, it is also necessary to consider whether activities are carried out in the UK on that non-UK resident trust company's behalf by a dependent agent. If this is the case the trustee may be treated as having a permanent establishment in the UK. Annex A provides further information on dependent agents.

3.2 The activity of providing services to a non-UK resident trustee, whether by a connected person or not, does not of itself create a dependent agency permanent establishment (see paragraph 5 in the Annex). It is necessary to consider the capacity in which the person provides the services to the trust on behalf of the non-UK resident trustee. Where the services that are provided to the trust are only those that the person is contractually obliged to provide under their agreement with the non-UK resident trustee and are remunerated at arm's length, then this is unlikely to create a dependent agency permanent establishment.

3.3 Whether there is a dependent agency permanent establishment will depend on the facts of the case; the position is the same whether it is an unconnected third party or a UK subsidiary or other connected person that carries out the work for the trust. Where, say, a UK subsidiary of a non-UK resident trust company is providing services to a trust, then unless the powers granted to it by the non-UK resident trust company are such that it becomes a '*dependent agent with authority to do business on behalf of the non-resident trustee*' (see paragraph 5 of Annex A) we will not contend that the UK subsidiary's actions cause the non-UK resident trustee company to have a permanent establishment.

Example 3

September Ltd, a non-UK resident trust company contracts with October Ltd which is a UK company within the same group. The services to be provided by October Ltd are for investment advice for the November Trust. The contract between September Ltd and October Ltd is on an arm's length basis and October Ltd has no powers granted to it by September Ltd

HMRC view: October Ltd is providing a service for September Ltd and has contracted to do so on arm's length terms. They have no authority to do business on behalf of September Ltd so are not their dependent agent. Therefore, September Ltd will not be treated as having a permanent establishment through the work carried out by October Ltd in the UK. So September Ltd will not be treated as UK resident for the purposes of the November Trust.

Other examples which would be treated in the same way where there was an arm's length relationship are:

- Preparing trust accounts for the trustees' review and approval
- Preparing trust tax returns for the trustees' review and approval and filing the return on their behalf with HMRC
- Obtaining quotes for necessary repair work on trust property
- Having contact with workmen to ensure that those repairs are carried out
- Day to day management of let property (such as dealing with tenants etc)
- Signing small cheques such as paying for minor repairs

Example 3a

As above but October Ltd also has authority to buy and sell commodities with a view to realising profits for the trust subject to trading limits set by September Ltd. It receives an arm's length fee for this activity.

HMRC view: The investment manager is appointed by the trustee, and so is its agent. If it receives an arm's length fee for the investment management services, it will not ordinarily constitute a dependent agent of the non-UK resident trustee. If, however October Ltd was providing investment management services to the trustees other than on arm's length terms i.e. was acting as their dependent agent, rather than simply providing a service to them, in that case the trustees would be likely to have a dependent agent permanent establishment. (This is in line with the Investment Manager Exemption provisions – in particular that the provision of services at less than a customary rate can indicate that the investment manager is not an independent agent of the non-UK resident trustee.)

4. UK resident directors or other employees of a non-UK resident trust company.

4.1 First, it is necessary to consider the role of the UK resident director or employee of the non-UK resident trustee.

4.2 If the UK resident employee is not carrying out activities that would be regarded as core trustee activities in relation to a particular trust then the presence in the UK of an employee of a non-UK resident trust company could not by itself cause a non-UK resident trustee to have a permanent establishment in the UK.

4.3 Where in relation to a particular trust the UK resident employee does carry out trustee activities in the UK then it is likely that the non-UK resident trustee will have a permanent establishment in the UK. This will be the case if the employee operates from a fixed base, or does not have a fixed base but habitually acts on behalf of the non-UK resident trustee for the particular trust, i.e. is a dependent agent permanent establishment of the non-UK resident trustee. The crucial point in relation to a dependent agent permanent establishment is whether the non-UK resident trustee company has in the UK-resident employee a dependent agent with authority to conduct business on behalf of the non-UK resident trustee. If this UK resident employee of a non-UK resident trustee does have the authority to make decisions then s/he is likely to constitute a dependent agent permanent establishment of the non-UK resident trust company.

Example 4

December Ltd, a non-UK resident trustee has a director or other employee Mr. Monday who is resident in the UK. (This individual may also be an employee or director of UK resident group members.) The group provides office accommodation in the UK to Mr. Monday. His role is to market the business of the non-UK resident trust company in the UK which includes meeting with prospective settlors and other business contacts for this purpose.

HMRC view: In this case, Mr Monday's role is only meeting with prospective settlors and other business contacts for the purpose of marketing the business of December Ltd. Although these activities are carried out at the same place, they are not activities as a trustee that are carried out at a fixed place of business. They would generally be preparatory or auxiliary activities. This would not cause December Ltd to be treated as carrying on trustee business through a permanent establishment in the UK.

Example 4a

As in example 4, but Mr. Monday's role also extends to meeting beneficiaries of existing trusts.

HMRC view: In this case, the importance of the subject matters discussed and the decisions taken at those meetings, and the frequency of the meetings held, will need to be analysed in relation to each trust in order to reach a conclusion as to whether December Ltd is carrying on a business through a permanent establishment in the UK for that trust through Mr Monday

If no office accommodation is at his disposal Mr Monday could still constitute a dependent agent permanent establishment of the non-UK resident trustee if he has authority to enter into contracts or otherwise do business on behalf of the trustee of the trusts i.e. more than simply meeting the beneficiaries and he habitually exercises that authority on behalf of his employer for the trust.

Example 4b

As in example 4a but the significance of the meetings Mr. Monday has in the UK with the beneficiaries of the Tuesday Trust is sufficient for December Ltd to have a permanent establishment in the UK in respect of that trust. However December Ltd has a co-trustee Mr. Wednesday who is a non-UK resident trustee.

HMRC view: As there is a co-trustee who is non-UK resident and as the settlor of the Tuesday Trust was not resident or domiciled in the UK when he introduced property into the trust that means that the trustees of the Tuesday Trust as a body will not be UK resident.

Annex A

OECD Tax Model Convention

1. Under the OECD Tax Model Convention of January 2003, Article 5 defines 'permanent establishment' as a fixed place of business; a dependent agent of the non-resident is a deemed permanent establishment.

Fixed place of business

2. The OECD Commentaries on this Article state that for a fixed place of business to be a permanent establishment three conditions have to be met:

a) The existence of a "place of business" i.e. a facility such as premises, or in certain instances machinery or equipment;

b) This place of business must be "fixed", i.e. it must be established at a distinct place with a certain degree of permanence;

c) The carrying on of the business of the enterprise is through this fixed place of business. This means, usually, that persons who, in one way or another, are in a paid relationship with the enterprise (usually the personnel of the business) conduct the business of the enterprise in the State in which the fixed place is situated.

3. The Commentaries also state that in connection with conditions a) and b) above a place of business of one enterprise could be situated in the business premises of a second enterprise, including possibly an affiliated company, if some space were put at the disposal of the first enterprise. In considering whether a place of business is "at the disposal of" an enterprise it makes no difference whether that enterprise's use is exclusive or shared, whether the enterprise owns, rents or even occupies a place illegally. According to paragraph 6.1 of the Commentaries temporary interruptions of activities do not cause a permanent establishment to cease to exist. Similarly where a particular place of business is used only for very short periods of time

but such usages take place regularly over long periods of time, the place of the business should not be considered to be of a purely temporary nature.

4. The OECD commentary on article 5 at paragraph 42 discusses the applicability of the permanent establishment test in the situation where one subsidiary company (Company A) of a company or a group of companies provides services to another subsidiary company (Company B). These services are provided by Company A on its own premises and using its own personnel so neither premises or personnel are those of Company B. In this situation, because the place where these services are provided is not at the disposal of Company B and as it is not Company B's business that is carried on through that place, Company A's premises will not be considered as constituting a permanent establishment for Company B.

Dependent agent

5. If a non-resident company does not have a physical presence in the UK it can however still have a permanent establishment if it acts through an agent (other than an independent agent) and that agent has and habitually exercises authority to do business on behalf of a non-resident company. If a double taxation agreement is in place it is likely that there will be a slightly narrower requirement that the agent has and habitually exercises authority to conclude contracts on behalf of the non-resident company (depending on the precise wording used in the agreement). The habitual element is the equivalent of having a presence of not less than 6 months and limiting the charge to those who can conclude contracts again ensures that there is economic activity of some significance in the UK.