

Università Carlo Cattaneo – LIUC

International Tax Law a.a.2017/2018

*Tax Residence of individuals and
Companies*

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Topics

- OECD Model Convention
- Domestic Legislation
- Main impact of Treaty Residence

OECD Model Convention (MC) Application

- Who can apply a tax treaty?
- Article 1 of the OECD Model Convention:

"This Convention shall apply to persons who are **residents** of one or both Contracting States."
- 'Resident' status is crucial for treaty application

Residence Definition Art. 4 OECD MC

Residence defined in Article 4(1) OECD MC

1. For the purposes of this Convention, the term "resident of a Contracting State" means any person who, ***under the laws of that State***, is ***liable to tax therein by reason of*** his domicile, residence, place of management or any other criterion of a similar nature

→ 4(1) OECD MC Refers to domestic legislation

→ Indirect reference to WW tax liability (Comprehensive Taxation - C4(8))

Residence Definition Art. 4 OECD MC

- Article 4 continues:

“But this term does not include any person who is liable to tax in that State in respect only of income from sources in that State or capital situated therein.”

Art. 4 (1) OECD MC

Art. 4(1), second sentence:

- Persons who are subject to tax only through the source of income or property (real or otherwise) do not have a right to access the treaty through their residence status (although they may obtain other treaty rights as 'non residents')
- Residents of countries with a territorial tax system: treaty access or not? See C4(8)

Domestic Criteria for Residence of Individuals

- Physical Presence
- Habitual Abode
- Family Connections
- Residential Property
- Centre of Vital Interests
- Nationality

Domestic Criteria for Individuals

- Physical Presence
 - Over 183 days
 - ‘Simple Majority’ of the time – France
 - Substantial Presence – US
- Nationality
 - Can create global liabilities (USA)
 - Difficult to give up

Domestic considerations - Individuals

- Habitual Abode
 - Presence over a number of years/usual presence
- Family Connections and Residential Property
 - Spouse and/or children remain in home location
 - Home retained while temporarily absent abroad
- Centre of Vital Interests

Country practices for Individuals

France

An individual with a home or principal place of residence in France will be a French tax resident. Home is defined as the place where the taxpayer and his family (spouse and children) normally live. A taxpayer with a spouse and children in France will generally be considered as tax resident even if forced to work abroad for extensive periods of time.

Country Practices for Individuals 2

USA

- Nationals
- Green Card Holders
- Individuals meeting the Substantial Presence test

Country Practices for Individuals 3

USA

- Substantial Presence Test

An expatriate who meets *both* of the following tests is considered a resident of the USA :

- He is physically present in the US for 31 days in the current year and,
- He is physically present in the US at least 183 days during the current calendar year and prior 2 years determined by counting each day of presence in the current year as 1 day, each day of presence in the first prior year as one third of a day, and each day of presence in the second prior year as one sixth of a day

Country Practices for Individuals 4

Ireland

- Two levels of residence – resident and ordinarily resident
- **Resident** if in Ireland for more than 183 days in a tax year; or more than 280 days in 2 consecutive tax years, but ignoring any tax year in which he is present for 30 days or less.
- **Ordinarily resident** if resident for 3 successive years. An individual leaving Ireland will not cease to be ordinarily resident until he has been non-resident for 3 continuous tax years.

Country Practices for Individuals 5

Belgium

Individuals are regarded as resident in Belgium if they have a permanent home there or if they manage their fortune and economic interests from Belgium. It is a matter of facts and circumstances, not relying on citizenship or the duration of stay

Country Practices for Individuals 6

Netherlands

Art. 4 General Taxes Act

- “determined by considering the circumstances”
- Concept developed through case law

Domestic Criteria for Residence of Companies

- Place of incorporation
- Place of management and control
- Statutory company seat
- Place of effective management
- Place of the main business purpose
- Other criteria

Country practices

UK

- Where the 'real' business of the company is carried on – designed to capture businesses which are incorporated overseas
 - Various tests applied by the UK authorities
- Also – if a company is incorporated in the UK, it will always be UK tax resident

Country practices 2

Italy

- Legal Seat – place indicated in the articles of incorporation
- Place of Effective Management – where the Directors manage the company (and “deemed” place of Effective Management for Companies controlling another Italian Company)
- Place of the Main Business Purpose – as indicated in the articles of incorporation

Country practices 3

Netherlands

- Companies incorporated under Netherlands law are deemed to be residents of the Netherlands
- Resident of the Netherlands for tax purposes if they are deemed to be "actually situated" there on the basis of "facts and circumstances". Case law helps determination:
 - Place of effective management
 - Residence of Directors/Supervisory Board
 - Place of shareholder meetings
 - Location of company assets etc.

Country practices 4

Germany

- Legal seat in Germany
- Place of Management – the place where the persons who have final authority make their decisions concerning the management of the business
- Also, all entities organized under German commercial law must have their legal seat and their place of management (*Verwaltungssitz*) in Germany

Art. 4 (2) and (3) OECD MC – Tiebreaker Rules

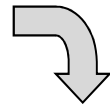
- Why are tie-breaker rules needed?
- Due to differences in domestic residence legislation dual residence is possible. For treaty purposes only one state in which the individual or company is resident

Art. 4(2) OECD MC Tiebreaker Rule for Individuals

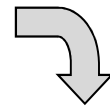
- Permanent Home
- Centre of Vital Interests (only if a permanent home is available in both States)
- Habitual Abode
- Nationality
- Mutual Agreement

Tie-breaker rules – Individuals Art. 4(2) OECD/UN Model

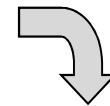
Permanent home



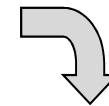
Personal and economic relations
(centre of vital interests)



Habitual abode



Nationality



Mutual agreement

OECD MC Tiebreaker Rule for Individuals

Permanent Home

- Often sufficient test
- Permanence is a key factor
- Any form of home can fall within the definition
- Should be available (when rented out not available)
- Ownership not required

OECD MC Tiebreaker Rule for Individuals

Centre of Vital Interests

- Otherwise known as ‘personal and economic relations’
- ‘Personal’ is a key consideration
- Family and social relations
- Occupations
- Political, cultural and other interests
- Circumstances must be examined as a whole
- ‘First Home’ retention a key concept

OECD MC Tiebreaker Rule for Individuals

Habitual Abode

- If a permanent home available in both jurisdictions, staying in one country more than the other generally 'tips the balance'.
- If a permanent home in neither, decided purely on a physical presence basis.
- In any case the residence in the State must be habitual
- Often difficult to determine

OECD MC Tiebreaker Rule for Individuals

Nationality

- Resolves most issues, except, of course, in the case of dual nationals

OECD MC Tiebreaker Rule for Individuals

Mutual Agreement

- Competent Authority
- Procedure outlined in Article 25
- Should apply to the competent authority in the 'resident' country (!) within 3 years

Impact of Residence Determination - Individuals

- Dependent Personal Service article
- Independent Personal Service / Business profits article
- Passive Income articles
- Elimination of double taxation

Impact of Residence Determination - Individuals

- Income from Employment (formerly the Dependent Personal Services)
- Key in deciding which jurisdiction has primary taxing rights
- Also an impact on the employer provisions of this article – both individual and company residence rules need to be considered.

Impact of Residence Determination – Individuals

- Independent Personal Services article
- Deleted from the OECD MC
- Now covered by Business Profits article

Impact of Residence Determination – Individuals

- Passive Income articles
- Dividends & interests: share vs. exclusive taxation
- Royalties: which State has an exclusive taxation right
- Immovable property: primary vs. exclusive taxation
- Capital gains: primary vs. exclusive taxation

Impact of Residence Determination - Individuals

Elimination of Double Taxation (Articles 23A and 23B OECD MC)

- Exemption Method and Credit Method
- Allocates taxing rights – when taxing rights accrue to the Source State, the Residence State must grant relief

Art. 4(3) OECD MC Tiebreaker Rule for Companies

“Where by reason of the provisions of paragraph 1 a person other than an individual is a resident of both Contracting States, then it shall be deemed to be a resident of the State in which its ***place of effective management*** is situated.”

Actual tax treaties may contain a different tiebreaker, e.g. Canada

Difference with the notion of place of management of Art. 4(1) OECD MC

Art. 4(3) OECD MC Tiebreaker Rule for Companies

- Changes to the Commentary introduced on April 4 2000 relevant to the individuation of the place of effective management (Par. 24 of the Commentary relevant to Art. 4 – board of directors)
- Observation of Italy to paragraphs 24 and 24.1 (place where the main and substantial activity of the entity is carried on)

OECD Multilateral Convention (MLC)

- Approved in November 2016
- Aimed at providing States a multilateral instrument to implement treaty related BEPS measures and amend bilateral tax treaties
- Not yet ratified by any jurisdiction
- If applicable, Article 4(1) MLC would replace the tie-breaker rule of Article 4(3) OECD MC

Art. 4(1) MLC – Dual Resident Entities

«Where by reason of the provisions of a Covered Tax Agreement a person other than an individual is a resident of more than one Contracting Jurisdiction, the competent authorities of the Contracting Jurisdictions shall endeavour to determine by mutual agreement the Contracting Jurisdiction of which such person shall be deemed to be a resident for the purposes of the Covered Tax Agreement, having regard to its place of effective management, the place where it is incorporated or otherwise constituted and any other relevant factors. In the absence of such agreement, such person shall not be entitled to any relief or exemption from tax provided by the Covered Tax Agreement except to the extent and in such manner as may be agreed upon by the competent authorities of the Contracting Jurisdictions»

Art. 4(1) MLC – Dual Resident Entities

- Similar to the alternative provision envisaged by par. 24.1 OECD Commentary (cfr. Action 6 - Final Report, par. 47)
- Treaty residence to be decided by competent authorities under MAP
- If disagreement, no “treaty relief or exemption” unless if and as agreed by competent authorities
 - ✓ Treaty benefits not limited to residents
 - *E.g.*: Art. 24(1) OECD MC (cfr. US Tech. Expl. Sub Art. 4(4))
 - ✓ Treaty provisions not granting relief or exemption
 - *E.g.*: Art. 15(2)(b) OECD MC or art. 10 OECD MC to dividends paid by the dual resident (cfr. Action 6 - Final Report, par. 48)

Case Study 1

- Company A:
 - Established under Dutch law in the Netherlands
 - A subsidiary of a US company
 - Has 6 Managers: 4 resident in the US, 2 in Ireland
 - One of the Irish Directors is the MD for day to day decisions and has the power to act on behalf of the company
 - Board Meetings are in Ireland
- Where is company A resident for treaty purposes?

Case Study 1 Solution

- For domestic law purposes, Company A is resident in
 - Ireland, due to the location of management and control
 - Netherlands, since the company was established under Dutch law
- We need to use the Irish/Netherlands treaty to resolve this issue

Case Study 1 Solution Pt. 2

Art. 2(1)

(f) the terms "resident of one of the States" and "resident of the other State" mean a resident of the Netherlands or a resident of Ireland, as the context requires; and the term

"resident of the Netherlands" means:

(1) any company whose business is managed and controlled in the Netherlands;

(2) any other person who is resident in the Netherlands for the purposes of Netherlands tax and not resident in Ireland for the purposes of Irish tax;

Case Study 1 Solution Pt. 3

Art. 2(1)

(f) the terms "resident of one of the States" and "resident of the other State" mean a resident of the Netherlands or a resident of Ireland, as the context requires; ...the term "resident of Ireland" means:

(1) any company whose business is managed and controlled in Ireland; provided that nothing in this paragraph shall affect any provisions of the law of Ireland regarding the imposition of corporation profits tax in the case of a company incorporated in Ireland and not managed and controlled in the Netherlands;

(2) any other person who is resident in Ireland for the purpose of Irish tax and not resident in the Netherlands for the purposes of Netherlands tax;

Case Study 2

- Pierre is *single* with French nationality.
- He works as a commercial representative in Germany between 1999 and 2002.
- He maintains a home in France
- He rents an Office in Germany
- From 2001, he rents an apartment in Germany for use during the week.
- Where is Pierre resident in the years 1999-2002?

Case Study 2 - Solution

- For 1999 and 2000: French Resident, as he has a permanent home in France
- From 2001, we need to use Article 4 in greater depth:
 - 'Permanent Home' in both states
 - Vital Interests arguably evenly divided
 - Place of habitual abode cannot be easily established
 - Nationality is the determining factor
- Therefore, most likely treaty resident of France.

Case Study 3

- Klaas is a 71 years old Dutch national
- He owns a large apartment in Netherlands and a villa in Spain
- He has spent 1 month per year in Netherlands and 11 months in Spain
- Klaas has a Spanish temporary residence permit
- His children from a prior marriage live in France; his new wife's children in the Netherlands
- The majority of his assets are in Netherlands; he is a retired managing director of a Dutch company

Case Study 4

- George is a UK national
- He has lived for 10 years in the Netherlands
- He is married to a Dutch woman and has two children
- He worked first in Belgium, then in Luxembourg
- He rented a house in Luxembourg, his family stayed in Netherlands
- He spent the weekends in Netherlands
- Where is George resident?

Case Study 5

- Wilhelm is a German national
- He was MD and owner of a German company
- He married a Danish woman in 1991
- Wilhelm moved to to Denmark in 1994
- He commuted to Germany daily, occasionally he was staying over at his workplace

- Where is Wilhelm resident?