Tax Residence for Companies Factsheet

It's important to know whether a company is UK tax resident or not. If it is, then it will be subject to UK corporation tax on all its profits, wherever they arise in the world. On the other hand, if a company is not UK resident, then it will (broadly) only be subject to tax in the UK on profits which are earned here or which relate to UK land and buildings.

Incorporation v Residence

Most countries have a central government agency which registers (or "incorporates") new companies.

In the UK this is Companies House. A company which is incorporated in the UK will by default be tax resident in the UK (although this can sometimes be overridden by a double tax treaty with another country – see later).

However there is another way in which a company, incorporated in another country, can be UK tax resident. This is if its "central management and control" is exercised in the UK.

There has been a lot of case law on what "central management and control" means, but it is generally accepted to mean the location where the highest level of decision-making in the company takes place.

This is often the place where the Board of Directors meets, but it need not be if, for instance, the real decision-making power rests elsewhere and the Board merely acts as a "rubber-stamp". This is one reason why it is important for UK-based groups to ensure that the governance processes of non-UK subsidiaries is fully respected.

If all decisions are taken in the UK and there is no evidence of proper board consideration of major decisions at the subsidiary level, there is a real risk of the subsidiaries inadvertently becoming UK tax resident.

Double Taxation Treaties

To complicate matters further, the basic rules outlined above can be overridden by double taxation treaties.

Other countries have their own rules regarding whether a company is resident in their territory or not. Predictably, these rules are not the same as the UK rules. This creates the risk that a company may potentially find itself tax resident, and subject to tax on its worldwide profits, in more than one country.

Double taxation treaties can sometimes (though not always, unfortunately) resolve these conflicts by providing tie-breaker rules which override the basic rules of the UK and the other country.

The UK has a very extensive network of such treaties, with most of the major countries of the world. These treaties are negotiated on a bilateral basis and so all differ slightly from each other, but where there is such a tie-breaker rule it should (in theory, at least) ensure that a company is tax resident in one country or the other only.

Such issues can sometimes take a very long time to resolve, though, as they require the tax authorities of the two countries to come to an agreement on the position.

Permanent establishments

Once a company's country of residence is established, this does not mean that it will only be subject to tax in that territory.

Most countries (including the UK) want to tax profits which arise from operations which are conducted, or assets which are situated, in their territories. This is irrespective of where the company which owns those operations or assets is resident.

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For trading operations, many countries have the concept of a "permanent establishment" (PE). In the UK we sometimes talk of a company having a "branch" rather than a PE, being an operation in another territory conducted by the company itself and not through a formal subsidiary.

If a company has a sufficient degree of presence in a country to have a PE, then any profits arising from the activity carried on through the PE are likely to be subject to tax in that country. The definition of PE varies from country to country, but having fixed premises, or staff who can conclude sales contracts on their own initiative, is often sufficient to constitute a PE.

Many countries, including the UK, also tax income from non-trading activity such as property rents and gains, where the property is located in the relevant country.

Double tax relief

As can be seen from the above, if a company is tax resident in Country A but has a permanent establishment in Country B, it will be taxable on the operations undertaken in Country B in both territories.

Fortunately, as long as there is a double tax treaty between the two countries (and even sometimes if there is not), the tax authority of Country A will usually allow a credit of the tax paid in Country B against the Country A tax liability, to ensure the same profits are not taxed twice.

As always, we hope this briefing note is helpful, but it should not be taken as constituting tax advice, and we accept no responsibility for any action taken or not taken as a result of this note.

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