

Budget 2008



BN66

12 March 2008

DOUBLE TAXATION TREATY ABUSE

Who is likely to be affected?

1. UK residents who are participating in the avoidance scheme described below.

General description of the measure

2. UK residents are taxable on their income wherever it arises. A wholly artificial scheme seeks to avoid UK tax by artificially diverting income of a UK resident individual to a foreign partnership comprised of foreign trustees. The scheme is designed to ensure that the income nonetheless continues to belong to the UK resident as they will be a beneficiary of the foreign trust. Legislation will be introduced in Finance Bill 2008 to:
 - clarify, retrospectively, legislation introduced in 1987, which itself was retrospective, so that it has effect as intended. This will ensure that, notwithstanding the wording of any double taxation treaty, UK residents pay UK tax on their profits from foreign partnerships; and
 - prevent tax avoidance through the misuse of Double Taxation Treaties by UK residents.

Operative date

3. The first measure will be treated as having always had effect. The second will have effect for income arising on or after 12 March 2008.

Current law and proposed revisions

4. UK law taxes a UK resident beneficiary of certain trusts on the income to which they are entitled under the trust arrangement as it arises. This means that, in cases exploiting the above avoidance scheme, the UK resident should be taxable in the UK on his or her share of the profits of the partnership comprised of the foreign trustees.
5. But the users of the scheme claim that a provision, known as the Business Profits Article, common to most tax treaties, exempts the partnership profits from UK tax – not only in the hands of the foreign partners but also in the hands of the UK beneficiaries.

6. The first provision will make clear that (in line with retrospective legislation introduced in Finance (No2) Act 1987) tax treaties do not exempt UK residents from UK tax on any profits of a foreign partnership to which they are entitled.
7. The second measure will ensure that the Business Profits Article in the UK's tax treaties cannot be read as preventing income of a UK resident being chargeable to UK tax.
8. Draft legislation and explanatory notes have been published today on the HM Revenue & Customs website.

Further advice

9. If you have any questions about this change, please contact Martin Brooks on 020 7147 2651 (email: martin.brooks@hmrc.gsi.gov.uk) or Simon Davis on 020 7147 2666 (email: simon.davis@hmrc.gsi.gov.uk). Information about Budget measures is available on the HM Revenue & Customs website at www.hmrc.gov.uk