

LETTER TO THE EDITOR

Dear Mr Grundy

I was most interested in your article in the latest issue of the Grays Inn Tax Chambers Review on the *Smallwood* case.

I wonder if I can comment on another anomaly arising from the construction put on Article 4 of the former Double Taxation Agreement with Mauritius.

Article 4(1) defines the term ‘resident of a Contracting State’ as meaning any person who, under the law of that State, is liable to taxation therein by reason of his domicile, residence, place of management or any other criterion of a similar nature.’

We have here a situation where a trust only had UK trustees for a few days at the end of the year in which the Mauritian trustees had realised a substantial capital gain. It is said that the fact that the trust had UK trustees for part of the tax year means that it is to be regarded as UK resident for the whole of the tax year.

However, an anomaly arises here in that the UK trustees were not themselves liable for capital gains tax, the liability fell on the settlor under section 77 TCGA 1992. Furthermore, because the settlor was a beneficiary, the whole of the trustees’ income was treated as the settlor’s income rather than the trustees’ income. It might therefore be argued that the trustees were not liable for tax by reason of their residence in the UK and were only liable for tax in Mauritius. Put another way, whilst they might be UK resident according to our domestic law, they were not a resident of the UK as defined in Article 4.

.....in which case, the tie-breaker provisions which relate to the place of management may not be relevant?

Tony Foreman

PKF (UK) LLP

MG comments – I suppose the opposite view is that a distinction is to be made between “liable to tax” and “liable to taxation”, and by using the abstract noun, the treaty draftsman is describing not a person but a class of persons, those who are, so to speak, in the line of fire – on account of residence etc. On this analysis, it does not matter whether or not the person in question has any actual tax liability in that year: his income may be too small, say, or he may have carry-forward losses. It is enough that his residence etc is such that he would have a liability in other circumstances. “Other circumstances” in the *Smallwood* case could have been the death of the settlor or the failure of the settlor to pay his income tax.

Of course, the debate only becomes relevant if you accept (which I do not) that a trust has a residence. In my view, only persons can be resident and a trust is not a person. The Commissioners may have been (unconsciously) influenced by the concept of deemed trustee in the CGT legislation: that is only a domestic fiction and has no place in the interpretation of a tax treaty.