4.2.3 Treaty articles for British expats

If a British expat is potentially liable to UK tax on a UK source of income or gain, one of the first steps is therefore to look and see if there is a relevant double tax treaty (see **Appendix 3**) and, if so, whether treaty exemption or relief is available in respect of the UK tax potentially due.

Some of the more common articles used for British expats overseas are in respect of:

- the residence tie-breaker (see below);
- income from immovable property – rental income – see **5.10**;
- dividends – see **5.9**;
- interest – see **5.7**;
- employment income – see **5.2-5.6**;
- pensions – see **5.11**; and
- double tax relief – see below.

One of the first steps is to establish which country the individual is resident in for the purposes of the tax treaty. For non-residents this is straightforward as an individual will be resident for treaty purposes ("treaty resident") in the country he or she is living in and not in the UK, assuming the individual is regarded as a resident in that country under its domestic tax legislation and has broken UK tax residence under the statutory residence test.

Tie-breaker clauses

However, there are often situations when this is not the case. One example is a person who is resident in both the UK and the country he or she has moved to under the domestic tax law of both countries, i.e. a dual resident, which can very often be the case for the UK tax year when leaving or arriving in the UK. In this case, it will be necessary to look at the tie-breaker clause in the treaty (art. 4(2) of the OECD model treaty) to establish which country the individual is resident in for the purposes of the treaty *only*.

The tie-breaker clause will vary between different treaties, but following the OECD model treaty, the first test to be looked at is that of where the individual's permanent home is. In many cases this will determine where the individual is treaty resident. However, what about the scenario where an individual (Tom) is working and living overseas, say, in the Middle East, but his family have remained living in the family home in the UK which Tom visits often (and which may be why he has remained resident in the UK)?

Centre of vital interests

There is an argument to say, in this situation, that Tom has a permanent home in both countries, in which case he will then need to identify his centre of vital interests (i.e. where his personal and economic ties are closest). Again, this may not be so clear cut if his family and social activities are in the UK and he is performing work there, but his employment – where the majority of his work is performed – is overseas.

The OECD commentary can help in these scenarios, but if it still cannot be established in which country Tom's centre of vital interests is, or he does not have a permanent home in either country, then it is necessary to establish where his habitual abode is (but not in all treaties, e.g. the agreement with Australia does not include the habitual abode test). Again, the OECD commentary helps with trying to establish where a person's habitual abode is, and highlights that it is not necessarily where the individual visits the most frequently, as other factors (such as the regularity and length of visits) also need to be considered.

Nationality

If a person's treaty residence still can't be established, then nationality will be considered and the individual will be treaty resident in the country of nationality. If the person is not a national of either country, or is a national of both, then the two countries' tax authorities will need to agree where he or she will be regarded as treaty resident.

Overseas adviser

Usually the tie-breaker clause will establish where the individual will be regarded as resident for the purposes of the treaty. It is advisable to liaise with the individual's overseas tax adviser to agree the country in which he or she will be treaty resident (especially if it is not clear cut and so is open to different interpretations). Treaty residence is fundamental in using the treaty, and in determining which country has primary taxing rights and which country has to give exemption or relief. Substantial amounts of tax can often be at stake, so paying it in the right country is important. An individual will often question, though, the importance of which country tax has been paid in, so long as tax has been paid in one of the countries (see **4.2.5**, including **Example 2**).

Some very old treaties, still in existence, have not been updated and do not include a tie-breaker clause to establish which country the individual is resident in for the purposes of the treaty. This results in the individual not being able to obtain relief under the treaty if he or she is a dual resident. An example is the treaty with Malawi.

In the recent *Oppenheimer* case, HMRC argued the taxpayer was treaty resident in the UK, whereas the taxpayer contended he was treaty resident in South Africa. The FTT found in favour of the taxpayer on the basis of his habitual abode and shows how treaties should be interpreted – in accordance with the *Vienna Convention on the Law of Treaties 1969*.

Case: *Oppenheimer v HMRC* [2022] UKFTT 112 (TC)

Other considerations

Individuals who are not resident in both countries that are party to a treaty are unable to use the treaty.

If treaty relief or exemption is available under the treaty, this needs to be claimed via the individual's self-assessment tax return using forms HS302 (if treaty relief is claimed by a dual resident) or HS304 (if a non-resident with double taxed income/gain is claiming treaty relief). For both forms a certificate of residence is required from the tax authority of the residence state, i.e. the country the individual is regarded as being resident in for treaty purposes, except where the residence state is the US, in which case HMRC accept that a residence certificate from the US IRS is not required.

This certificate should cover the UK tax year concerned and confirm that the individual was resident in that country for the purposes of the double tax treaty. In practice, it can take some tax authorities months to produce this certificate, if indeed they do it at all(!), which can very often mean that the individual's self-assessment tax return needs to be filed without the relevant certificate if the online filing deadline of 31 January is to be met. In this situation, it is advisable to have a note on the tax return stating that the certificate has been applied for and will be forwarded to HMRC once received.

Treaty relief or exemption can be obtained at source by completing form DT-Individual, although this is just in respect of pension, interest and royalty income.

If treaty exemption or relief is not available for a particular type of income or gain, then double tax relief should be available. Under the treaty, it is usually the residence state (the country in which the individual is regarded as treaty resident) that must give relief for any double tax, thereby giving the source state what are known as primary taxing rights.

Care needs to be taken with regards to the UK/US double tax treaty, which contains a savings clause at Article 1(4):

> "(4) Notwithstanding any provision of this Convention except paragraph 5 of this Article, a Contracting State may tax its residents (as determined under Article 4 (Residence), and by reason of citizenship may tax its citizens, as if this Convention had not come into effect.
>
> (5) The provisions of paragraph 4 of this Article shall not affect—
>
>> (a) the benefits conferred by a Contracting State under paragraph 2 of Article 9 (Associated Enterprises), sub-paragraph (b) of paragraph 1 and paragraphs 3 and 5 of Article 17 (Pensions, Social Security, Annuities, Alimony, and Child Support), paragraphs 1 and 5 of Article 18 (Pension Schemes) and Articles 24 (Relief From Double Taxation), 25 (Non-discrimination), and 26 (Mutual Agreement Procedure) of this Convention; and
>>
>> (b) the benefits conferred by a Contracting State under paragraph 2 of Article 18 (Pension Schemes) and Articles 19 (Government Service), 20 (Students), 20A (Teachers), and 28 (Diplomatic Agents and Consular Officers) of this Convention, upon individuals who are neither citizens of, nor have been admitted for permanent residence in, that State."

This means that relief under the treaty may not be available on certain income.

4.2.4 How relief is given

Double tax relief is usually given by three methods:

- exemption;
- credit; or
- deduction.

The method used depends on the country concerned.

Exemption method

Under this method, there are two ways this is achieved:

- full exemption, where the income is treated as being completely exempt from tax in the residence state and is not included when establishing the person's tax rate for other income; or
- exemption with progression, where the income is exempt from tax but is included with other income to establish which rates of tax are to be used to tax the individual's other income.

The second of these is by far the more common, especially in European countries.