Saint Christopher and Nevis

Inland Revenue Department

Guidance on tax residence and taxable presence in the Federation

Inland Revenue Department,
September 2020

1. Introduction

This guidance is based on current law as at September 2020. There are plans to modernise the Federation of St Kitts and Nevis'("Federation") tax laws. In particular, the Government plans to formalise the current common law test of residence into statutory law, and to introduce a definition of "permanent establishment" for non-residents conducting business in St. Kitts and Nevis ("SKN").

Although the law will be updated, it is likely that the concepts set out in this guidance will continue to be helpful to taxpayers in the future. In practice, the way the concepts apply to taxpayers are expected to remain much the same.

For the avoidance of doubt, this document is intended to guide taxpayers on concepts that arise under the laws of SKN and not to provide a conclusive decision/determination on factual scenarios of taxpayers. Further guidance on issues arising can be sought from the St Kitts and Nevis Inland Revenue Department ("SKNIRD") in the usual manner.

2. Background on existing law

The SKN system of tax is governed by the Income Tax Act ("ITA"), which establishes the taxation framework for companies that fall within the scope of taxation in the Federation.

SKN operates a worldwide system of corporate income tax, such that companies that are to be treated as tax resident in the Federation are taxable on a worldwide basis, whilst companies that are not tax resident in the Federation are solely taxable on their income that is sourced within SKN.

The worldwide system of tax is set out by Section 3 of the ITA, which states as follows:

> "*Income tax shall, subject to the provisions of this Act, be payable at the rate or rates specified hereafter … upon the income of any person accruing in or derived from the State or elsewhere and whether received in the State or not.*"

Whilst Section 3 provides an all-encompassing charge to tax for residents, the legislation establishes a more restrictive basis of tax for non-residents. More specifically, Section 3(2) of the ITA states:

> *"Provided that in the case of income arising outside of the State which is earned income and which arises to a person who is not ordinarily resident in the State, or not domiciled in the State, the tax shall be payable on the amount received in the State"* [Emphasis Added]

As a result, Section 3 collectively establishes not only the fundamental basis of taxation, but also that residents and non-residents are taxed differently, namely:

- SKN resident companies are taxed on a worldwide basis; or
- Non-resident companies are taxed on a source basis.

Given that taxability of companies in the Federation is linked to both residence and income being sourced in SKN, companies should consider whether they meet the criteria to be considered to have a taxable presence in the Federation. This Guidance seeks to enable companies to understand:

- When a company would be deemed to be tax resident in SKN; and
- If, under the laws of the Federation, the company is considered to be a non-resident, the circumstances that would suggest that the company has sufficient operational presence within the Federation to fall within scope of tax.

3. Tax residence

3.1. Existing law on the term "resident"

A company's tax status will be determined by whether or not it is "resident" in SKN.

Whilst the ITA has a specific definition of "resident" for companies engaged in a shipping business, the ITA does not prescribe a single definition of residence for companies engaged in other sectors.

As a commonwealth jurisdiction, in the absence of a legislated definition, the term resident is interpreted by reference to common law. Broadly, this identifies that a company will be deemed to be tax resident in the jurisdiction in which the management and control of the company reside.

3.2. The central management and control test

Under the common law test of corporate residence – established by the English case *De Beers Consolidated Mines v. Howe (Surveyor of Taxes) [1906] AC 455* ("*De Beers*") – a company will be resident in the jurisdiction where its "*central management and control*" is located. According to *De Beers*:

> "*In applying the conception of residence to a company, we ought, I think, to proceed as nearly as we can upon the analogy of an individual. A company cannot eat or sleep, but it can keep house and do business… a company resides for purposes of income tax where its real business is carried on. Those decisions have been acted upon ever since. I regard that as the true rule, and the real business is carried on where the central management and control actually abides.*"

De Beers (and subsequent cases) have established that the central management and control of a company is where its highest-level decision making is situated. This will generally be where the meetings of the board of directors (BoD) are physically held. There may be circumstances where this is not the case: for example, if the BoD merely "rubber-stamps" decisions made by key individuals, or other entities in a corporate group. It is necessary to consider, as a matter of fact, who is formulating the actual management decisions of the company and from where those decisions are being exercised.

Where a company's BoD meetings are held in SKN, this will usually indicate the company is resident in the Federation. This conclusion of fact would further be supported where:

- ► The key strategic decisions of the company (especially relating to its capital structure, business strategy, investments, and dividend policy) are actually made at the BoD meetings;
- ► The BoD is comprised of individuals suitably qualified and capable of managing the affairs of the company; and
- ► Documentation (e.g. minutes of the BoD meetings) clearly indicate such meetings are the medium through which the strategic decision-making of the company is carried out.

Equally, where the BoD meetings are held outside the Federation, this will usually indicate that the company is not tax resident in SKN.

3.3. Tax residence is determined in a distinct manner from legal seat

A company that is incorporated in SKN will have its legal "seat" in the Federation. Since its legal seat is in the Federation, any SKN-incorporated company will be governed by SKN corporate law. It will be required to meet filing deadlines and other obligations, in order to remain legally constituted in the Federation.

Where an entity has its legal seat is determined entirely separately to where it is tax resident. Under SKN tax law, an entity will be tax resident where it is centrally managed and controlled, which will usually be the place where its BoDs meet. The jurisdiction where an entity is incorporated has no bearing on whether or not it is tax resident in SKN. Consequently, companies incorporated outside of the Federation are capable of being deemed tax resident in the Federation if their central management and control is in the Federation. Conversely, companies incorporated inside the Federation will be deemed tax resident outside the Federation if their central management and control is located abroad.

Maintaining clear records as to where board meetings are held, which people (within the management of the company) play a key role in determining and directing the affairs of the company, and where that power and role is physically exercised (if not through board meetings), will help to demonstrate the location of the tax residence of the company.

3.4. Delegated corporate secretarial functions in most cases do not amount to central management and control

The common law test of central management control looks to the highest-level decision-making of the company. Central management and control means the strategic decision making in relation to how a company conducts its core business, as typically carried out by the BoD.

Company secretarial functions, including filing and ensuring the company meets its regulatory and legal requirements in the Federation, do not amount to central management and control. Therefore, a SKN-incorporated company should not be considered SKN tax resident where its sole activities in the Federation amount to the delegation of corporate secretarial functions to third-party corporate service providers.

3.5. Tax treaties

There are certain situations where an entity can be tax resident in the Federation and another jurisdiction. It arises in situations where jurisdictions apply different tests for tax residence. For example, an entity might be managed and controlled in SKN, but incorporated in another jurisdiction that applies an incorporation test of residence (i.e. in another jurisdiction that considers all companies incorporated under its laws to be tax resident there).

In such circumstances, double tax treaties (including the CARICOM Double Taxation Agreement) provide a "tie-breaker" test to determine in which of the two countries the entity should be deemed tax resident. The "tie-breaker" in the CARICOM and other SKN treaties impose a test that is substantively the same as "central management and

control" but worded slightly differently: this is the "place of management" or "place of effective management".

The IRD applies the "place of management" test in the same way as the "central management and control test". As such, where a company that is incorporated outside SKN is centrally managed and controlled in SKN, this should determine residence both under SKN domestic law and under SKN's tax treaties.

3.6. Tax Residence – Summary

Tax residence determines whether a company will be subject to worldwide taxation in the Federation.

In summary:

- ► Tax residence in the Federation is determined by the central management and control test, as established under common law.
- ► Where a company is tax resident is determined separately from where it has its legal seat. A company's incorporation in the Federation does not mean it will be tax resident in SKN. It is possible for a company to be incorporated outside of SKN and tax resident in SKN, if centrally managed and controlled in SKN, and vice versa.
- ► Normally, central management and control will be located in the jurisdiction where the BoD convene and make management decisions on behalf of the company.
- ► This will be further substantiated where:
    - The BoD is comprised of individuals suitably qualified and capable of managing the affairs of the company;
    - The key strategic decisions of the company (especially relating to its capital structure, business strategy, investments, and dividend policy) are made at the BoD meetings; and
    - Documentation (e.g. minutes of the BoD meetings) clearly indicate such meetings are the medium through which the strategic decision-making of the company is carried out.
- ► The delegation of corporate secretarial type functions to third parties in the Federation should not give rise to those companies having their central management and control in the Federation.

Where a company is not tax resident in the Federation, it would next need to consider whether it has sufficient operational presence in SKN (i.e. a Business Enterprise) to be considered taxable in the Federation.

4. Business Enterprise

4.1. Background

Where a company makes a factual determination that it is not tax resident in the Federation (on the basis of it not being centrally managed and controlled in the Federation), it would not, as result, be taxed in SKN on a worldwide basis. However, non-resident companies may still be subject to SKN taxation for SKN source income, being income from conducting business in the Federation.

For non-resident companies with SKN source income, it is crucial to determine whether they conduct sufficient business activities in SKN to meet the threshold of having a taxable presence in SKN.

4.2. What is the existing law?

Section 3(2) of the ITA sets limitations on the taxation of persons (including a company) not ordinarily resident in SKN:

> *"Provided that in the case of income arising outside of the State which is earned income and which arises to a person who is not ordinarily resident in the State, or not domiciled in the State, the tax shall be payable on the amount received in the State"*

It is implicit within this provision that a company that is not tax resident in SKN, but which has income arising to it within SKN, will be considered to have a taxable presence in the Federation.

Common law establishes that a non-resident company will have a taxable presence in a jurisdiction where that company carries on a business or trade. A business or trade will generally arise where a company establishes a physical and economic footprint in that jurisdiction.[1]

This is effectively a common law equivalent of the concept of a Permanent Establishment ("PE"), as set out in Article 5 of the Organisation for Economic Cooperation and Development's ("OECD") Model Tax Convention and often incorporated into domestic law. Since the Government of SKN has not, at the date of writing, specifically legislated for PE rules,[2] a non-resident company will have a taxable presence where it has a trade or business in the Federation, applying common law principles.

For ease of understanding, the IRD uses the terminology of a "Business Enterprise" to describe this taxable presence. This terminology is largely modelled on the concept of a Business Enterprise, as defined under the CARICOM Double Taxation Agreement. Whilst this is not a specific legislative provision under the ITA, the definition is used in this Guidance to provide clarity to taxpayers on when a non-resident company may be

[1] The following cases set out when a company is engaged in a trade or business: of *F L Smidth & Co v. Greenwood (1922) 8 TC 193; Inland Revenue Commissioner v. Hang Seng Bank Ltd [1991] 1 AC 306; and Commissioner of Inland Revenue v. HK-TVB International Ltd [1992] 2 AC 397*

[2] It is the intention of the Government of SKN to introduce the OECD definition of "Permanent Establishment" into the ITA.

considered to have a taxable presence in the Federation, but should not be treated as being a prescriptive and exclusive definition.

4.3. Criteria for "Business Enterprise"

The IRD uses the following definition of a Business Enterprise:

> "*business or trading operations that are physically located within the Federation, conducted along commercial lines for profit and shall be inclusive of (but not limited to) business or trading operations conducted through the following, to the extent they are located within the Federation:*
>
> *a) An office, branch, place of business or seat of management*
> *b) A factory, plant, industrial workshop or assembly shop*
> *c) A construction project in progress*
> *d) An agency or premises for the purchase and sale of goods*
> *e) An agent or representative"*

In common with the OECD concept of a "PE", a "Business Enterprise" requires business or trading operations to be "physically located" within the Federation. Physical location is most likely to be demonstrated through an office, shop or factory. In addition to real estate, the existence of employees and capital expenditure on the Federation are also likely to be indicators of whether a non-resident company has a Business Enterprise.

Unlike residence, the focus of the Business Enterprise test is on the actual business activities generating a company's profits, rather just than the highest-level decision making of the company (as is the case with the "central management and control" test).

4.4. Treatment of agents

The "Business Enterprise" definition also includes an "agent". This can be regarded as similar to the OECD MTC Article 5 concept of a "dependent agent" PE. To give rise to a taxable presence, an agent must be conducting "business or trading operations" on behalf of the non-resident company. A Business Enterprise will not arise simply because of the delegation of corporate secretarial, shareholder stewardship, or other administrative functions to corporate service providers in the Federation. Such providers are not "agents" within the definition of a "Business Enterprise", on the basis they are not carrying out the core functions of the company's business.

An employee of a non-resident that travels to SKN on business may be an "agent" within the definition of "Business Enterprise". Such business activities might be of a limited and short-term in nature. It might also be preparatory to some future business on the Federation. Unless that employee makes sales in the Federation and has the capacity and authority to legally bind the company on its behalf, it is unlikely that the employee will give rise to a Business Enterprise.

The following are examples of what would not, on their own, be considered to give rise to a Business Enterprise in the Federation:

1. Actions undertaken to ensure that the company complies with its corporate requirements in the Federation; and
2. Establishment of a bank account in SKN; and
3. Investment in equity holdings in the Federation.

4.5. Taxation of profits allocated to SKN

Once it is established that a non-resident has a “Business Establishment” within the Federation, a non-resident is taxed under the ITA. The non-resident company is therefore required to file Corporation CIT-100 returns and pay tax.

Consequently, where a non-resident company is deemed to have a Business Establishment in SKN, the company will be liable to tax at the prevailing tax rate on such proportion of the company’s profits that are attributable to the Business Establishment.

4.6. Business Enterprise – summary

A non-resident company should take a factual assessment of the business operations of the company to assess whether it has a Business Enterprise, and thus taxable presence in the Federation, and this should be assessed on a case by case basis.

In summary:

- A non-resident company will have a taxable presence in the Federation where it has a Business Enterprise in the Federation conducted along commercial lines for profit.
- To meet Business Enterprise Criteria, it would be necessary for there to be a physical conduct of business operations in SKN (e.g. through an office or branch located in the Federation).
- Actions undertaken to ensure that the company complies with its corporate requirements in the Federation, the establishment of a financial account in SKN, and investment in equity holdings in the Federation should not give rise to the non-resident having a Business Enterprise in the Federation.
- The delegation of corporate secretarial, shareholder stewardship, or other administrative functions to corporate service providers in the Federation should not lead to the creation of a Business Enterprise in SKN.

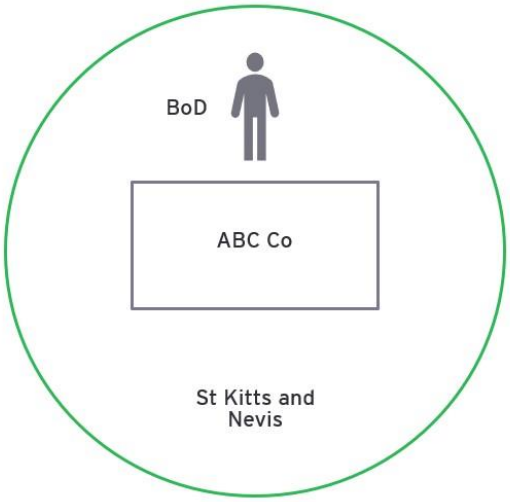
Where a company has a Business Enterprise in the Federation, it would be liable to tax on its income connected with operations carried out in the Federation.

Alternatively, where a company is not tax resident in the Federation and does not have a Business Enterprise in the Federation, it would fall outside the scope of tax and would not be taxable in the Federation.

Appendix 1 – Examples: residence test under SKN law

Example 1 – central management and control in SKN

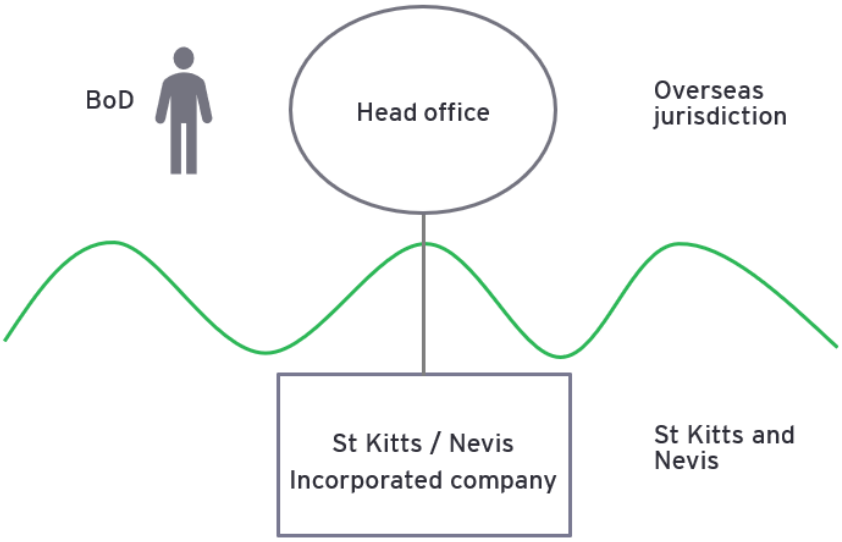
ABC Co is incorporated in SKN and the management of the company (i.e. the BoD) is located in SKN.



Since its central management and control is in SKN, ABC Co will be deemed tax resident in SKN and liable to tax on its worldwide income.

Example 2 – central management and control outside SKN

ABC Co is incorporated in SKN but has its head-office located in another country. The core strategic decision-making meetings of the company are conducted from outside of SKN; the company's directors' meetings occur outside of SKN.



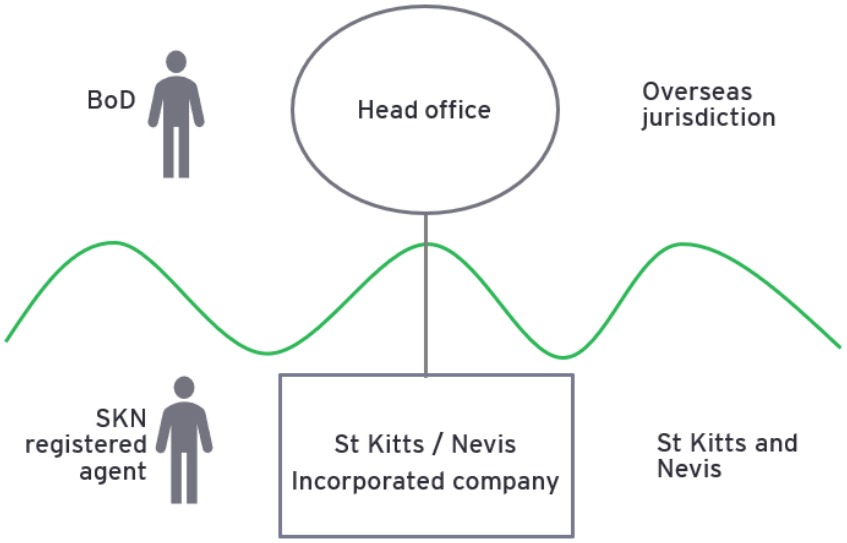
Despite the fact that the company is incorporated in SKN, it should not be deemed tax resident in SKN.

This is because the BoD meetings occur outside of SKN and the highest-level of decision-making of the company occurs outside of SKN.

Consequently, the company will be deemed to have its central management and control located outside of SKN and thus will not be deemed resident in SKN.

Example 3 – SKN registered agent

ABC Co is incorporated in SKN but has its head-office located in another country. The core strategic decision-making meetings of the company are conducted outside SKN; the company's directors' meetings occur outside of SKN. The company, however, has a registered agent in SKN that acts on its behalf and solely performs corporate roles in relation to the registration of the company and filing of documents.



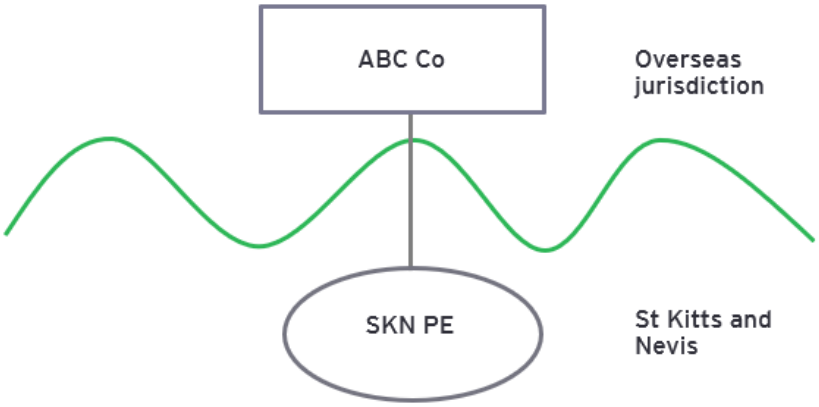
Despite the fact that the company was incorporated in SKN, it should not be deemed tax resident in SKN.

The registered agent is only providing general administrative obligations and his actions would not constitute him being involved in the strategic decision-making of the company.

Appendix 2 – Example: Business Establishment

Example – office in SKN

ABC Co, a company tax resident in another country, is engaged in the business of accounting services, and decides to commence business in SKN. It sets up an office in SKN, hires employees, and starts to provide accounting services to corporate clients in the Federation.



ABC Co would be liable to tax in SKN at the prevailing tax rate on its profits directly linked to its operations in SKN, subject to any allowances, exemptions, exclusions provided under the ITA.