

BUSINESS ENGLISH

Subsidiaries, branches and tax

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Question 1

There are no taxes imposed on the formation of a **subsidiary** [\[1\]](#).

Question 2

A UK resident subsidiary would pay corporation tax on its worldwide income and gains, whereas a UK branch would be liable to corporation tax only on the items listed in question 3. The charge to UK **corporation tax** [\[2\]](#) imposed on a non-resident company only applies where the non-resident company is trading in the UK through a permanent establishment. This means that a **branch** [\[3\]](#) set up for investment purposes only, and not carrying on a trade, is not subject to UK corporation tax, though certain types of income arising in the UK ? notably rent and interest ? may be subject to income tax through **withholding** [\[4\]](#) (at 20%).

Question 3

Assuming that the local branch of a non-resident company is within the UK statutory definition of “**permanent establishment**” [\[5\]](#) (which is based on the wording of Article 5 of the OECD Model Convention), it will be treated as though it were a distinct and separate entity dealing wholly independently with the non-resident company. It will also be treated as having the equity and loan capital which it would have if it were a distinct entity, which means that the UK **thin capitalisation rules** [\[6\]](#) will apply to it.

Subject to any treaty provisions to the contrary, the taxable profits of a permanent establishment through which a non-resident company is trading in the UK would comprise:

- trading income arising directly or indirectly through, or from, the permanent establishment;
- income from property and rights used by, or held by or for, the permanent establishment (but not including exempt distributions); and
- capital gains accruing on the disposal of assets situated in the UK and effectively connected with the operations of the permanent establishment.

Question 4

There is no branch profits tax.

[\[1\]](#) Società controllata

[\[2\]](#) Imposta sulle società (p.es. IRES)

[\[3\]](#) Filiale

[\[4\]](#) Ritenuta d'acconto

[\[5\]](#) Stabile organizzazione

[\[6\]](#) La *thin capitalization* o capitalizzazione sottile consiste nella sottocapitalizzazione di una società rispetto all'attività d'impresa esercitata e nel contestuale finanziamento della stessa con apporto di capitale di credito da parte dei soci qualificati.

<http://www.iclg.co.uk/jurisdictions/united-kingdom> (last visited 1.10.13)

COMPREHENSION QUESTIONS

Exercise 1.

The text below contains the answers to four questions (a, b, c, d). Match the questions with the appropriate answers.

- a. How would the taxable profits of a local branch be determined in its jurisdiction?
- b. What taxes (e.g. capital duty) would be imposed upon the formation of a subsidiary?
- c. Are there any other significant taxes or fees that would be incurred by a locally formed subsidiary but not by a branch of a non-resident company?
- d. Would such a branch be subject to a branch profits tax (or other tax limited to branches of non-resident companies)?

Exercise 2.

Answer these questions:

- i When is UK corporation tax imposed on a branch?
- ii When is a branch treated as a distinct and separate entity?
- iii When a branch is considered a distinct and separate entity, there are consequences. What are they?

ANSWERS

Exercise 1

Q1/ b;

Q2/ c;

Q3/ a;

Q4/ d.

Exercise 2

i When the branch carries on a trade

ii When it is a 'permanent establishment'

iii A permanent establishment i.e. a distinct entity is considered to have (1) its own equity and loan capital so (2) it is subject to thin capitalisation rules.
