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The Meaning of “Enterprise”, “Business” and “Business profits” in the UK’s Double Taxation Conventions

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THE MEANING OF "ENTERPRISE", "BUSINESS" AND "BUSINESS PROFITS" IN THE UK's DOUBLE TAXATION CONVENTIONS

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ABSTRACT

The terms "enterprise" "business" and "business profits" are used extensively in the OECD Model, which is the basis for the majority of the UK's double tax conventions, and are central to the accepted rationale for attributing the right to exercise jurisdiction to tax on a source basis. However, none of these concepts is exhaustively defined.

This paper focuses on the difficulties faced by the UK Courts and tax authorities in interpreting these terms in the context of permanent establishment provisions contained in UK tax treaties, and pays particular attention to the interaction between treaty law and the UK's domestic law, including comparative law and public international law.

It also highlights the problems which may arise where a differing interpretation of these terms are applied by reference to different countries' domestic tax systems.

It is based on a wider study that took place in connection with a seminar organised by the University of Piacenza, the OECD and the Italian Council of Ministers in Milan on 22 November 2010 entitled "The meaning of "Enterprise", "Business" and "Business Profits" under Tax Treaties and EU Tax Law" (referred to in this paper as the "Study").

TABLE OF CONTENTS

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LIST OF ABBREVIATIONS

Art.	Article
Ch.	Chapter
Commentary	OECD Income and Capital Model Convention and Commentary (2008)
CTA 2009	Corporation Taxes Act 2009
CTA 2010	Corporation Taxes Act 2010
HMRC	HM Revenue & Customs or UK tax authorities
ICTA	Income and Corporation Taxes Act 1998
IHT	Inheritance Tax
IHTA	Inheritance Tax Act 1984
ITA	Income Tax Act 2007
ITEPA	Income Tax (Earnings and Pensions) Act 2003
ITTOIA	Income Tax (Trading and Other Income) Act 2005
MAP	Mutual Agreement Procedure
MoU	Memorandum of Understanding (MoU)
OECD	Organisation for Economic Co-operation and Development
OECD MC	OECD Model Tax Convention on Income and Capital (2008)
PE	Permanent establishment
Pt.	Part
Sch.	Schedule
Sec.	Section
TCGA	Taxation of Chargeable Gains Act 1992
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TIOPA	Taxation (International and Other Provisions) Act 2010
UK	United Kingdom
US	United States
VATA	Value Added Tax Act 1994
Vienna Convention	Vienna Convention on the Law of Treaties 1969

One of the very first points preliminary to making international conventions or agreements on double taxation is to define the terms so that there will be no possibility of misinterpretation.[1]

Bruins, Einaudi, Seligman and Stamp

1. Sassville J.,Ch.4 the Study p.41 which refers to the Report on Double Taxation (League of Nations, 1923, at 25) Reprinted in, Legislative History of United States Conventions, Vol.4: Model Tax Conventions, Washington DC: US Government Printing Office, 1962 (LHUSTC) at 4003-4055.

CHAPTER 1

1. INTRODUCTION AND SCOPE

By far the largest portion of income derived from cross border economic activities is categorised as "business profits"[2] under the UK's double tax conventions, which are generally patterned on the OECD Model. Since the "permanent establishment" concept, which is the basic nexus for the source taxation of such profits, is defined by reference to the terms "enterprise" and "business", it is crucial that the English Courts interpret the terms "business",[3] "enterprise" and "business profits" correctly, in order to ensure the correct field of application of UK treaties.

Since the terms "enterprise", "business" and "business profits", which are contained in Arts.3, 5 and 7 of the OECD MC,[4] are not exhaustively defined, the UK Courts must look to other sources of interpretation to deduce their meaning. Amongst the interpretative rules which apply, Art.3(2) indicates that a domestic law meaning may be adopted to the extent meaning cannot be derived from the context of the Convention. However, as will be seen, the words "enterprise", "business" and "business profits" are not used in the United Kingdom's domestic tax law and therefore in that regard, at first blush, no help is to be found.

How much weight then, should be given to the UK domestic tax law meaning of these terms, to the extent such a meaning exists? And if there is no domestic tax law meaning, how persuasive should the meaning of these terms be in domestic non-tax law? Where the meaning of the term in the treaty is

2. Art.7 OECD MC, which is the basis for the majority of the UK's tax treaties, is headed "Business Profits" although the term "profits" is referred to in Art.7.

3. Although the term "business" is mainly used in connection with the PE concept, the terms "enterprise" and "profits" appear frequently in other articles of the Model.

4. Organisation for Economic Co-operation and Development, Model Tax Convention on Income and on Capital: Condensed Version (Paris: OECD, July 2008). The OECD MC referred to will be the 2008 draft, although a subsequent draft Model was published on 22 July 2010, reworking Art.7.

ambiguous, should an autonomous meaning nevertheless prevail? Finally, what solution should be reached where the apparent treaty meaning and the domestic tax law meaning conflict?

This paper, which is in five parts, examines the difficulties faced by the Courts in interpreting the terms “enterprise”, “business” and “business profits” in UK tax treaties, in light of the UK’s domestic tax law. It also explains how the design of the Model solves the majority of the qualification conflicts that arise where differing domestic law meanings of these terms are applied by each contracting state.

After setting the scope of this paper in Chapter 1, Chapter 2 sets out the approach of the UK courts to interpreting treaty terms and explores the relationship between tax treaties and domestic law. Chapter 3 summarises the use of the terms “enterprise”, “business” and “business profits” in UK domestic tax and non-tax law, and summarises the application and scope of equivalent domestic tax law concepts. Chapter 4 attempts to find a contextual meaning of these terms in the UK’s tax treaties in the light of UK tax treaty practice, and considers the application of the equivalent UK domestic law concepts to the contextual treaty meaning of these terms. Chapter 4 goes on to illustrate how the current OECD Model deals with the conflicts of qualification which may arise where the application of terms “enterprise” “business” and “business profits” results in differing tax treatment under the domestic law of source and residence states. Finally, Chapter 5 sets out the conclusion that may be reached from the above analysis.

CHAPTER 2

2. TAX TREATY INTERPRETATION AND ARTICLE 3(2)

Under constitutional rules, tax treaties concluded by the UK are given effect in domestic law by virtue of Sec.2 TIOPA, via the issue of an Order in Council. However, this does not mean that UK treaties are to be interpreted by the Courts in the same way as UK domestic law.[5]

In fact, the UK is mandated pursuant to Art.31(1) of the Vienna Convention on the Law of Treaties 1969 ("Vienna Convention")[6], to give an "ordinary meaning" to "terms of the treaty in their context and in the light of its object and purpose", which requires it to seek a common treaty interpretation i.e. an interpretation that is acceptable to it and the other Contracting State.[7]

There are various cases in which UK courts have discussed the interpretation of tax treaties in light of this objective, including *Padmore v. IRC*[8], where the wording of the treaty was central to the decision, the non-tax case *Fothergill v. Monarch Airlines Limited*[9], in which the Court discussed the relevance of the Vienna Convention on the Law of Treaties, and *IRC v. Commerzbank AG*[10], in which Mummery J. adopted the approach in *Fothergill*, and set out a number of principles that should be used in interpretation. In summary, Mummery J. stated that a clear meaning of the words used in the

5. In any event, treaties are not drafted in the same manner as domestic tax legislation. See Goulding J. in *I.R.C. v Exxon Corporation* [1982] S.T.C. 356 at 369 and Baker, P., E.06.

6. Strictly speaking the Vienna Convention only applies to parties to the Convention, and to treaties concluded after it came into force in 1980. However, it is seen as a codification of existing customary international law.

7. See *R v. Secretary of State for the Home Department ex.p Adam* [2001] 2 WLR 143 where it was said of the Geneva Convention on the Status of Refugees that "…the Refugee Convention must be given an independent meaning derivable from the sources mentioned in articles 31 and 32 [of the Vienna Convention] and without taking colour from distinctive features of the legal system of any individual contracting state. In principle therefore there can only be one true interpretation of a treaty."

8. [1989] BTC 221; [1989] STC493

9. [1981] AC 251, HL.

10. [1990] BTC 172; [1990] STC285.

relevant article of the treaty should be sought, but if the meaning lead to ambiguity, a purposive construction may be given to the treaty looked at as a whole. Regard should also be had to Art.31(1) of the Vienna Convention. However, if the adoption of this approach leaves the meaning of the relevant provisions unclear or ambiguous, recourse may be had to supplementary means of interpretation including the decisions of foreign courts, the Commentary and the writing of scholars.

Special problems arise in interpreting treaty terms such as "enterprise", "business" and "business profits" where those terms are also used in the domestic laws of Contracting States, since this may give rise to a qualification conflict.

Since these terms are not expressly defined in the treaty (either in Art.3(1) or elsewhere) the problem of qualification may be resolved by resorting to the "general renvoi clause" in Art.3(2) which states that:

> "As regards the application of the Convention at any time by a Contracting State, any term not defined therein shall, unless the context otherwise requires, have the meaning that it has at that time under the law of that State for the purposes of the taxes to which the Convention applies, any meaning under the applicable tax laws of that State prevailing over a meaning given to the term under other laws of that State."

Art.3(2) is one of the most controversial provisions of the OECD MC and a comprehensive discussion of its application is outside the scope of this paper.[11] However, in summary the rule provides that each state may interpret treaty terms in accordance with its own domestic law, with a treaty interpretation

11. The Commentary states that Art.3(2) is a general rule of interpretation. The relationship between Art.3(2) and other rules of interpretation is unclear, but the prevailing view seems to be Art.3(2) is a special rule and therefore takes precedence over the general rules in the Vienna Convention (Vogel at 209), although other commentators consider it to be a rule of last resort. Heinrich J. and Moritz H., "*Interpretation of Tax Treaties*" (2000) vol. 40, no. 4 at 149.

permissible if the context of the treaty requires. The advantage of this approach is that the "qualification conflict" no longer exists since courts and taxpayers can rely on familiar terms that promote legal certainty. This is particularly the case where an autonomous meaning of an undefined term is not possible due to insufficient criteria for developing the qualification.

However, the application of Art.3(2) raises several issues, for instance when is a domestic law definition permitted, and which states' laws are to apply?

Art3(2) states that a domestic law interpretation may only be applied to the extent that the context of the treat does not otherwise require. An explanation of "context" has been inserted into the Commentary, which suggests that it should be broadly interpreted[12] to include any extrinsic evidence taken into account by states in clarifying the intention of treaty negotiators.[13] However, a domestic tax law meaning may only be disregarded if the context "*requires* otherwise" [italics added], which suggests any contextual argument must have some force and that "not every apparently convincing interpretation from the context should give rise to a divergence from the rule of Art.3(2), but only those based on relatively strong arguments."[14]

In relation to the branch of domestic law which should be applied, Art.3(2) has a broad scope, referring to the meaning of the term in question according to the branch of the domestic law of the Contracting State applying the treaty, whether or not a provision of tax law. Although it may be argued that a non-tax law meaning of the treaty term is not relevant and only a meaning that is specific to domestic tax law or a non-tax meaning that is used in domestic tax law is relevant, Art.3(2)

12. Vogel K., 'Klaus Vogel on Double Taxation Conventions' (Third edition) Kluwer Law International 1996at 215.

13. The Commentary to Art(3), Para.12 states "The context is determined in particular by the intention of the Contracting states when signing the Convention as well as the meaning given to the term in question in the legislation of the other Contracting State (an implicit reference to the principle of reciprocity on which the Convention is based)."

14. Vogel, ibid.fn.12 at 214.

states that "….any meaning under the applicable tax laws of that State prevailing over a meaning given to the term under other laws of that State" which suggests that it should be possible to ascertain the domestic law meaning of an undefined treaty term by reference to the meaning that it has for the purposes of the non-tax law of the state applying the treaty, as long as that meaning is used in domestic tax law and the tax law meaning is given priority.[15] This also suggests that if the term is used in tax laws not covered by the treaty (i.e. VAT) or in another branch of domestic law i.e. commercial law, then Art.3(2) does not apply and general interpretative rules would be applicable.

In relation the question of which Contracting State's domestic law should be applied (i.e. the UK or its treaty partner), Vogel has stated there are three possibilities[16] (i) both states applying the treaty qualify the terms according to the requirements of their own domestic law (ii) both states qualify treaty terms consistently according to the law of the state in which income arises i.e. the source state or (iii) both states seek to establish a consistent qualification from the context of the treaty i.e. an autonomous qualification. Assuming an autonomous interpretation of the treaty term in option (iii) is not possible, and the application of both state's domestic laws in option (i) results in conflict, the general view is that the law of the state of source should prevail.[17]

Assuming this is the case, to the extent the UK and its treaty partner cannot agree on an autonomous meaning of the terms "enterprise" "business" and "business profits" from the *context* of the treaty because the autonomous contextual meaning is unclear, it will be necessary to ascertain the meaning of the terms by reference to each Contracting States' domestic tax laws and compare the domestic tax law meanings with the contextual treaty meaning, to the extent one can be derived, to see whether the

15. In 2000, Commentary Para.32, Arts.23A and B put beyond doubt that the source state's categorization should prevail.

16. See Vogel ibid.fn12 at p210.

17. The residence state may also apply its interpretation. However given the OECD approach, this has not been considered further.

context otherwise requires. If there is still a qualification conflict caused by the differing application of each states' domestic laws, the source state qualification should prevail.

To this end, Chapter 3 will set out the meaning of each of the terms in the UK's domestic tax laws, which, to the extent an autonomous definition of the terms cannot be deduced, may be relevant in interpreting the meaning of treaty terms in the context of Art.7.

CHAPTER 3

3. THE MEANING OF "ENTERPRISE" "BUSINESS" AND "BUSINESS PROFITS" IN UK DOMESTIC TAX LAW

3.1 The meaning of "Enterprise"

There are few references to the word "enterprise" in UK domestic tax law,[18] a term which is thought to be derived from economics and originate in the legal systems of civil law countries,[19]although with the influence of Europe, the term has crept into various tax statutes. [20] Consequently, where the term "enterprise" is used in UK law, it is generally defined by reference to the term "business".[21]

3.2 The meaning of "Business"

3.2.1 Direct tax

Similarly, UK direct tax law does not generally use the term "business" to define taxing jurisdiction, and it is not defined in UK taxing statutes. Instead, the primary charging provisions[22] are concerned with whether a company is "trading", or in the case of an individual, carrying on "a trade, profession or vocation", and whether a business is carried on is relevant only in a narrow set of circumstances (e.g. in the context of whether a company is carrying on a property business).[23] This follows the

18. In *Ostime v. Australian Mutual Provident Society* 38TC492, 517 the Court held that "Enterprise … [has] no exact counterpart in the taxing code of the United Kingdom".

19. The meaning of the term "enterprise" is not clear in any common law jurisdiction. See Avery Jones, J.et al., "The origins of concepts and expressions used in the OECD Model and their adoption by states" [2006] British Tax Review at 223.

20. Including Enterprise Management Incentives Part 1, Sch.5 ITEPA, Enterprise Investment Scheme Pt.5 ITA, so-called enterprise zones for capital allowances purposes Sec.298(2) Capital Allowances Act 2001 (repealed by Finance Act 2008) and transfer pricing provisions in Part 4 TIOPA.

21. Sec.129(1), 130 Enterprise Act 2002 define the term "enterprise" as "activities, or part of the activities, of a business."

22. For income tax purposes these are charged under Pt.2 ITTOIA and for corporation tax purposes computed under Pt.3 CTA 2009.

23. See Pt.3 ITTOIA for income tax purposes and Pt.4 Ch.2 CTA 2009 corporation tax purposes. In

practice in UK commercial law, where it is often necessary to establish whether a "trade" is being carried on as opposed to a "business".[24] In fact the word "business" is more commonly used in UK commercial, consumer and insolvency law,[25] it is typically accompanied by the word "trade" under statute.[26] However, the two expressions are not necessarily synonymous with one another,[27] and the concept of "business" is generally considered to encompass that of "trade."[28] Therefore, where it is necessary to establish that a business is being carried on, it is not generally necessary to establish whether a person is also trading, although whether a trade is being carried on is an important factor in determining whether a business exists.

Where the UK courts have sought to define the term "business" in the context of direct tax law, they have typically given the term a wide meaning; for instance, in *CIR v. Marine Steam Turbine Co Ltd*[29] "business" was defined as "any particular matter or affair of serious importance...."

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addition, the concept of "business" is relevant in the context of partnerships (since the definition of partnership requires the carrying on of a business), and Sec.13 ICTA (which allocates the small companies' rate of corporation tax to groups).

24. Under statute, the existence of a "business" may either (i) entitle the person carrying on the business to certain rights, i.e. compensation or (ii) make the person carrying on a business liable under statute for civil or criminal sanction.

25. The Sale of Goods Act 1979 and Supply of Goods and Services Act 1982 both confer rights on the consumer to sue for damages where a person has supplied goods (or in the case of the SGSA, services) in the course of a business which are defective and Sec.265 Insolvency Act 1986 provides that: "A bankruptcy petition may not be presented to the court by one of the individual's creditors…. unless the debtor … has carried on business in England and Wales."

26. *Halsbury's Laws of England* states at Vol. 18 (Competition) Para. 370 that the term "business" is wider than the term "trade" and not synonymous with it, and means anything which is an occupation as distinguished from a pleasure.

27. *Re Sarflax Ltd* [1979] Ch 592, [1979] 1 All ER 529.

28. See Lord Denman CJ in *Harris v. Amery* LR. 1 CP148 who held that "every trade is a business, but every business is not a trade; to answer that description it must be conducted by buying and selling." See also *Smith v. Anderson* where Jessel M.R. held: "It is unnecessary to refer to authorities to show that 'business' has a more extensive signification than 'trade."

29. 12TC174.

In *Torkington v. Revenue and Customs Commissioners*,[30] in assessing the business activities of a company, the First Tier Tribunal took into account "the wide interpretation often given to the term business", rejecting the United Kingdom tax authority's assertion that the term "trade" had the same meaning as "business" in the context of rules set out in Sec.392-Sec.395 ITA, which provide that an individual is entitled to deduct interest costs on a loan for acquiring shares or lending money to a close company.

As discussed, "trading income" is the main taxing category in UK direct tax law. However, despite this, there is no exhaustive statutory definition of the word of "trade".[31] Whether a trade is carried on is primarily a question of fact for the Courts to decide,[32] and therefore the meaning of the term must be ascertained from common law.

As in other jurisdictions, UK cases in this area evolve around three common themes (i) trade vs. expensive pastimes/hobbies, where the taxpayer has sought to deduct related expenses (ii) trade vs. isolated or speculative transactions or (iii) trade v. passive investment. In cases concerning (ii) and (iii), the taxpayer generally argues that the resulting gain is capital (either subject to lower rates of tax or no tax at all prior to 1965) rather than trading income.[33]

In these cases, UK Courts have generally given the term "trade" a wide meaning, as including "any venture in the nature of trade" and it has been held to "usually denote operations of a 'commercial' character by which the trader provides customers for reward some kind of goods or services."[34]

30. [2010] WL 3975673.

31. Sec.1119 (1) CTA 2010 and Sec.989 ITA 2007 state that "'trade' includes any venture in the nature of trade."

32. HMRC guidance note BIM20070.

33. De Broe L.,The Study, Chapter 3 p.33.

34. *Ransom v. Higgs* [1974] 50TC1.

In addition to case law, the 1955 Final Report of the Royal Commission on the Taxation of Profits and Income set out an "all facts and circumstances" test referred to as the "badges of trade", which may be applied in order to indicate whether a trade is being carried on, which are as follows: (i) subject matter of the transaction: the nature of property that is subject of the transaction may indicate whether a transaction is in the nature of trading[35] i.e. certain types of property are less likely to be in the nature of trade; (ii) length of ownership: acquiring property with a view to disposing of it shortly afterwards suggests trading rather than investment, although this may not be conclusive;[36] (iii) frequency of transactions: if transactions of the same type are carried out in relation to the same property the activity is more likely to be trading in that property.[37] However, while it is clear that repeated transactions may support the inference of a trade, an isolated transaction may nonetheless constitute trading activity;[38] (iv) work on the property: if property is improved in order to make it more marketable,[39] or the property is broken down into smaller lots to facilitate sale, the activity is more likely to be trading;[40] (v) circumstances responsible for realisation: if property is sold due to some emergency, then it is less[41]likely that the disposal will be made as part of a trade and (vi) profit motive:[42] although profit motive is not determinative in deciding whether a person is trading, if other facts and circumstances are ambiguous, the intention of the person might be persuasive in determining whether they are trading.[43]

35. *Rutledge v. IRC* (1929) 14 TC490.
36. *Marson v. Morton* supra note 76.
37. *Pickford v. Quirke* (1927) 13 TC251.
38. HMRC guidance note BIM20230.
39. *IRC v. Livingston* (1926) 11 TC 538
40. *Edwards v. Barstow & Harrison* (1955) 36 TC 207.
41. *Cohan's Executors v. IRC* (1924) 12 TC 602.
42. This is similar to the position in English commercial law. *Rolls v. Miller (1884) 27 Ch.D. 71, 88*.
43. *F.A. and A.B. Ltd v. Lupton* [1971] 3 All ER 948, 47TC580 and *Ensign Tankers (Leasing) Ltd v. Stokes* (1992) 1 WLR1222.

Although no one of the "badges of trade"[44] is decisive, they are nevertheless persuasive in determining whether a trade is being carried on. However in the recent case of *Azam v. Revenue and Customs Commissioners*[45] the First Tier Tribunal commented that the badges of trade "must be approached with caution" and referred to *Marson v. Morton* where it was stated that the badges "are in no sense a comprehensive list of all relevant matters."

In order to determine whether the non-resident company is "trading" by or through a PE[46] for corporation tax purposes,[47] and therefore subject to tax on all its chargeable profits,[48] HMRC have stated that it is necessary to determine where the operations take place from which in substance the profits of the company arise.[49] The conclusion of contracts in the UK is an important but not a deciding factor.[50] More important is to establish whether the company is carrying out a profit-making activity.[51]

44. Subsequently, nine badges of trade were identified in *Marson v Morton* [1986] STC 463.

45. [2011] UKFTT 50 (TC) (FTT Tax).

46. Sec.5(2) CTA 2009.

47. Sec.19 CTA 2009.

48. Chargeable profits including trading income, income from property or rights, i.e. royalties, chargeable gains on assets used for the purposes of the trade.

49. HMRC consider the following comment made by Lord Atkin in *Smidth & Co v Greenwood* [8TC193] are important "…the question is, where do the operations take place from which the profits in substance arise?"

50. Parties may easily manipulate the contract's location to suit their convenience and therefore courts have looked more recently at the location of the operations from which the profits of the company are derived to determine whether an activity amounts to trading in the UK. *Firestone Tyre v. Lewellin* (1957) 37TC111.

51. For instance, a representative office supplying information will not give rise to tax. Nor will the mere purchase of goods for export and resale abroad. *Sulley v. A-G* (1860) 5 H&N 711, (1860) 2TC149. However, in *Taxation Commrs v. Kirk* [1900] AC 588, PC goods were manufactured in the UK for export and not simply bought. A trade was therefore held to have been carried on.

Taxation of individuals

In relation to individuals, [52]the position is more complicated, since they may carry on a "trade", or where the individual is an independent service provider ("ISP"), a "profession" or "vocation" depending on the context.

The terms "profession" and "vocation", are not defined in UK legislation.[53] However, under common law, a profession[54] has been defined as an occupation in which the only or dominant skill employed is intellectual skill,[55] i.e. law or manual skill controlled by the intellectual skill of the operator, for instance, painting or surgery. Meanwhile, the courts have stated that the term "vocation" is hard to define, although it has been stated that a vocation is "the way in which a man passes his life".[56]

It is difficult to distinguish between these two taxing categories although the significance of whether a profession or vocation is being carried on causes few differences in tax treatment or calculating taxable profit.[57] Whether an individual is carrying on a "profession" or "vocation" is assessed by reference to similar criteria to those that apply to "trading" for UK tax purposes. However, there is no

52. In commercial law, individuals may be deemed to be carrying on a "business". The difference between trade, profession and business were examined in insolvency law in *Re a Debtor* (No 3 of 1926) [1927] 1Ch 97.

53. HMRC guidance note BIM14090 states that the terms "profession" and "vocation" take their ordinary meanings. A "profession" normally involves some substantial exercise of intellectual skill whilst a vocation indicates a "calling", with a bookmaker, jockey, dramatists and professional singers all being treated by the courts as carrying on vocations.

54. *IRC v. Maxse* (1919) 12TC41.

55. This is consist with commercial law, where the courts are more likely to hold that a profession is being carried on rather than a trade, where an individual's goodwill 'adhere[s] to [his] personal qualities' as opposed to the business premises itself. *Stuchbery & Son v. General Accident Fire and Life Assurance Corporation Ltd* [1949] 1 All ER 1026.

56. *Partridge v. Mallandaine* (1886) 2TC179.

57. There are few practical differences in computation, although some allowances and exemptions are only allowable for traders. HMRC guidance note BIM14090.

concept equivalent to "venture in the nature of trade"[58] in professions and vocations, and therefore they necessarily involve an element of continuity.

The UK courts have held that business activities for the purposes of UK tax law encompass the carrying on of trades, professions and vocations.[59]

3.2.2 Indirect tax and other taxes

In contrast to the position in UK direct tax law, the term "business" is commonly used in UK indirect tax law, since the concept of "economic activity" in Art.4(1) VAT Directive[60] was translated into the Value Added Tax Act 1994 as a "supply in the course of furtherance of a business." In their comprehensive guidance note V1-6 Business/non-Business, HMRC state that the term "business" is superficially different from "economic activity." However since "domestic legislation must be interpreted so it agrees with Directive "business" and "economic activity" must be seen as having the same meaning."

Since the meaning of the term "business" is not defined in VAT legislation, the indicia derived from the decision in *Lord Fisher's Case*[61] are generally used[62] to determine whether a business exists for VAT purposes. It should be noted that these indicia are similar to the "badges of trade" referred to above, although generally require continuity to apply.

58. Even if an activity is insufficient to amount to a trade, it may still be a venture in the nature of trade. HMRC BIM200065.

59. Park J in *Jowett (HMIT) v. O'Neill & Brennan Construction Ltd* [1998] BTC133 at 139.

60. EC Directive 2006/112/EC.

61. QB [1981] STC238; [1981] 2 All ER 147. *CC&E v. Morrison's Academy Boarding Houses Association* [1978] STC1.

62. *William John Terry (in business as Wealden Properties) v. HMRC* [2009] FTT 202 (TC).

3.3 Meaning of "business profits"

Following on from the analysis in 3.2 above, there is no taxing category of "business profits"[63] in UK tax law and therefore the primary charging provisions are concerned with whether an entity is earning "trading profits", and in the case of individuals, whether they are earning profits from a "trade", "profession" or "vocation".

Where a company holds shares[64] or lets out property in return for rent[65] it may, in certain circumstances, be considered to be carrying on an investment business and earn business income,[66] although as with the position in non-tax law,[67] the mere holding of property in the UK, i.e. shares, immoveable property or cash,[68] may not constitute the carrying on of a business for tax purposes.[69]In

63. However, the corporate law case of *Re The Spanish Prospecting Company, Limited* [1911] 2 Ch. 92 at 98 defined "profits as implying "a comparison between the state of a business at two specific dates usually separated by an interval of a year. The fundamental meaning is the amount of gain made by the business during the year."

64. *Land Management Ltd v. Fox* (2002) Sp C306 where the company did not carry on a trade but owned shares and a freehold property. Since it was held to carry on a business of the managing and letting of property and the making and holding of investments, and its memorandum of association showed it was incorporated for activities of an investment nature, it was held to be carrying on a business.

65. *Fry v. Salisbury House Estate Ltd* [1930] AC432 where the House of Lords held that rents received by a company were profits arising from the ownership of land chargeable as property income and therefore could not be included in the assessment as trade receipts of the company.

66. If the holder is not trading, any gain arising on sale will be chargeable to capital gains tax or corporation tax on chargeable gains as appropriate and any income derived from the exploitation of the property, i.e. rental income will be property income rather than trading income. *Webb v. Conelee Properties Ltd* [1982] STC913.

67. The mere holding of investments will not be a business, but the active management of them will be. The "carrying on" of business is not merely a question of whether there is business involved in what people are doing; the word "business" means an active occupation or profession continually carried on. *Pamment v. Sutton* (1998), *Times*, 15 December.

68. *John M Harris (Design Partnership) Ltd v. Lee.*

69. A distinction should be made between a company carrying on an investment business and where it has withdrawn from a previous trade or business and is merely 'gainfully employing assets while keeping itself in existence pending any trading opportunity which might arise…." by keeping money on a deposit account. *EYL Trading Co Ltd v. IR Commrs* (1962) 49 TC 386.

fact the Courts have held that not every isolated act of a kind that is authorized by a company's memorandum necessarily constitutes the carrying on of a business,[70] although the fact that a company is carrying out one of the principal objects stated in its Memorandum may be relevant.

In light of this distinction, the UK broadly categorizes companies in three ways for tax purposes: (i) trading companies, which are companies whose business consists wholly or mainly of the carrying on of a trade or trades (discussed above); (ii) investment companies, which are defined in Sec. 1218 Corporation Tax Act 2009 (CTA 2009) as companies whose business consists wholly or mainly of the making of investments; and (iii) companies which hold investments but do not carry on any business.[71]

In contrast with the categorisation of some companies as holding companies, a partnership will only exist under UK law where a business is carried on.[72]

3.4 Conclusion

As can be seen, the term "enterprise" is not used, other than colloquially, in UK direct tax law or in UK non-tax law. Furthermore, the term "business" is not the main charging provision in UK direct tax law, which is instead concerned with whether companies are "trading" for corporation tax purposes and whether individuals are carrying on a "trade", "profession" or "vocation" for income tax

70. See*American Leaf Blending Co Sdn Bhd v. Director-General of Inland Revenue* [1979] AC 676, a Privy Council decision on appeal from the Federal Court of Malaysia, where Lord Diplock made a distinction between receipt of rents by a private individual where there would be no presumption that a business was being carried on, and by a company where there was a presumption that it might be. *RCC v. Salaried Persons Postal Loans Limited* [2006] EWHC 736(Ch).

71. *Jowett (HMIT) v. O'Neill & Brennan Construction Ltd* [1998] BTC.

72. As a consequence, partnerships and limited partnerships were not used much as investment vehicles due to the uncertainty of whether the holding of investments constituted business activity, until 26 May 1987, when the British Venture Capital Association reached agreement by way of a Memorandum of Understanding (MoU) (superseded by the MOU agreed between the BVCA and the Inland Revenue on 25 July 2003) with the UK tax authorities and Department for Trade and Industry that such entities were carrying on a business.

purposes. However, the term “business” has been defined by the Courts a few limited contexts for income and corporation tax purposes. Although the terms “trade”, “profession” or “vocations” are not synonymous with the term “business”, according to tax and non-tax case law they are encompassed by the term “business”, which is generally given a wider meaning.

The term “business” is more widely used in the UK’s commercial, consumer and insolvency laws, in conjunction with the term “trade”, and is also significant in the application of other taxes e.g. VAT. However, the term “business profits” is not used in direct tax law other than in relation to investment income, although the term “profits” has a meaning in UK commercial law.

In Chapter 4, this paper will examine the meaning of the terms “enterprise”, “business” and “business profits” in the context of the UK’s tax treaties, and to the extent a contextual treaty meaning can be ascertained, compare that meaning with the UK domestic law meaning summarised above.

CHAPTER 4

4. THE MEANING OF "ENTERPRISE" "BUSINESS" AND "BUSINESS PROFITS" IN THE PERMANENT ESTABLISHMENT PROVISIONS OF THE UK'S DOUBLE TAXATION CONVENTIONS

4.1 Treaty usage of the terms "enterprise", "business" and "business profits"

Since Art.31(1) of the Vienna Convention states that an ordinary meaning should be given to the terms of the treaty in their context, it follows that the meaning of the terms "enterprise", "business" and "business profits" will vary, according to their use in the relevant treaty.

In modern UK treaties that follow the OCED MC, the terms "enterprise", "business" and "business profits" are used in the PE provisions as follows:

Art. 5(1) of the US treaty, concluded in 2001 states that:

> "For the purposes of this Convention, the term 'permanent establishment' means a fixed place of business through which the *business* of an *enterprise* is wholly or partly carried on." [Italics added]

Meanwhile, Art. 7(1) of the same treaty, being the corollary to Art.5, refers to "profits"[73] stating that:

> "The profits of an *enterprise* of a Contracting State shall be taxable only in that State unless the *enterprise* carries on *business* in the other Contracting State through a permanent establishment' situated therein. If the *enterprise* carries on or has carried on *business* as aforesaid, the profits of the enterprise may be taxed in the other State but only so much of them as is attributable to that permanent establishment'." [Italics added]

73. The current approach to Art.7(1) dates from OEEC Third Report (1960).

The majority of the tax treaties concluded by the UK, follow the OECD MC in use of the terms "business" and "enterprise" and "business profits", but of course, the referenced Model depends on the date on which the treaty was negotiated, and therefore the terminology may deviate from that set out above. A small number of treaties constitute double taxation "arrangements" with former crown colonies and dependencies and follow a slightly different "colonial model".[74] Finally there are a few early treaties concluded before 1963, which depart significantly from what subsequently became the OECD Model.[75]

The scope of the term "profits" in Art.7 may also vary depending on the treaty partner i.e. in some treaties the term may be defined so that income which is attributable to a PE that has ceased to exist may still be taxed (US 2001) or in others, where a PE takes an active and substantial part in the negotiation and conclusion of contracts entered into by the enterprise, a proportion of profits may be attributable to it, notwithstanding the fact that other parts of the enterprise also participated in those transactions (India 1993) and (Mexico 1994). The treaty with Egypt (1977) provides an extensive but not exhaustive definition of "profits", whereas the term "profits" in treaty with Bangladesh (1979) is expressed not to include income from the operation of ships.

Given these variations, in practice it is necessary to interpret treaty terms in each agreement separately. However, for the purposes of this Chapter, it is assumed that UK treaties follow the wording of the Model, unless otherwise stated.

74. Antigua, Montserrat, St Kitts and Sierra Leone (all 1947), Grenada (1949), (all 1950), Guernsey and Jersey (1952), and Isle of Man and Malawi (1955).

75. Greece (1953), Israel (1962) and South Africa (1962). *Cleave B., The Impact of the OECD and the UN Model Conventions on Bilateral Tax Treaties Concluded by the United Kingdom.*

4.2 Historical development of the terms "enterprise", "business" and "business profits" in the OECD Model

As above, Art.31 of the Vienna Convention requires treaty terms to be interpreted in light of their context. Since the context of a treaty is considered to include its historical background,[76] the evolution of treaty terms in older models may shed light on their modern meaning.

The precursor to the term "enterprise" in Art.7 in most early treaties concluded prior to 1940, which were patterned after the three alternative models included in the 1928 Report of the League of Nations[77] was the term "undertaking" which was accompanied by the phrase "and other trades and professions".[78] No attempt was made to define "undertaking." However, the Commentary stated that the term "undertaking" must be "understood in its widest sense, without making any distinction between natural and legal persons."

Tax treaties concluded by the UK after 1940, e.g. the treaty with the US (1945), replaced the term "undertaking" with "United Kingdom enterprise", which is defined as "an industrial or commercial enterprise or undertaking carried on by a resident of the United Kingdom". The context of the term "enterprise" in this treaty suggests it could either refer to a business organisation or an entity belonging to a person or body, although in some contexts, the term "enterprise" appears to refer to the person itself rather than a business organisation carried on by the person.[79]

76. Edwardes –Ker, M. at p.234 quoting Willis J., "Statute Interpretation in a Nutshell" 1938 Canadian Bar Review 1.

77. Double Taxation and Tax Evasion: Report Presented by the General Meeting of Government Experts on Double Taxation and Tax Evasion, Document C.562.M.178.1928.II., Geneva, 31 October 1928.

78. Art.5 Draft Convention 1a) of the League of Nations Draft.

79. III(1) US treaty 1945 which refers to "an enterprise…engaged in trade or business in the territory through a permanent establishment'."

An expanded version of the definition of "enterprise" can be found in the UK treaty concluded with Mauritius[80] where "enterprise" means "an industrial, mining, commercial, plantation or agricultural enterprise or similar undertaking." Meanwhile, the Bosnia and Herzegovina treaty[81] defines the term "enterprise" in relation to Bosnia-Herzegovina as "an organisation of associated labour, a self-managed organisation or community, working people who individually perform activities independently and an enterprise established in accordance with the laws of Yugoslavia." Since the term "enterprise" in older treaties is used to refer to a person, business organisation or activity and is therefore ambiguous, the historical background of the term "enterprise" does not appear shed further light on its meaning in modern treaties.

Rather than use the concept of "business profits", earlier treaties, particularly those based on the colonial model, refer to "income from any industrial, commercial or agricultural undertakings and from any other trades or profession."[82] Later drafts based on the London model, refer to "income from any industrial, commercial or agricultural business and from any other gainful occupation…" This definition is thought to be widely drawn and does not expressly exclude income from asset management whereas, colonial model treaties and some other earlier treaties simply refer to "industrial or commercial profits" which is thought to be generally equated with trading, as opposed to investment income (although this may not always be the case in relation to banking and insurance income). Again, the predecessors to Art.7, do not provide much guidance as to the scope of the term "business profits" in modern treaties.

80. (1981).

81. (1967).

82. Art.3(1) Antigua and Barbuda (1947).

4.3 Meaning of "enterprise" in the OECD MC

4.3.1 Contextual meaning

The term "enterprise" is used extensively throughout the OECD MC.[83]

Before 2000, there was no definition of the term "enterprise"[84] and its meaning was deduced from the definition in Art. 3(1)(d), which stated that "enterprise of a Contracting State" was an "enterprise carried on by a resident of a Contracting State". However in 2000, a partial definition was inserted in Art. 3(1)(c) OECD MC, which provides that the term "enterprise" applies to the "carrying on of any business". Although some commentators have stated that on basis of this partial definition, the term "enterprise" has been held as likely to equate to the term "business," it has been explained[85] that the addition in Art.3(1)(c) was made in order to ensure that what was previously covered by Art.14 was now covered by Art.7.[86]

If an attempt is made to give an "ordinary meaning" to the term "enterprise" on reading the Model, the resulting meaning is at best ambiguous and may not be identical in all parts of a treaty.[87] For example, the definitions in Art.3 suggest that the term "enterprise" refers to an activity, but the wording in Art.5(1) appears to refer to an entity. In fact, commentators[88] have observed that the term

83. For an inventory of where the term "enterprise" is used in the OECD MC, seethe Study, Van Raad K., Ch.5, p.62.

84. The 1963 OECD MC states that "no definition…of the term "enterprise" has been attempted.

85. Sassville J., The Study p50.

86. This provision was included with Art.3(1)(h) stating that the term "business" includes "the performance of professional services and other activities of an independent character" as a result of the deletion in 2000 of the IPS Art.14.

87. E.g. in *Boake Allen Ltd & Ors (including NEC Semi-Conductors Ltd) v. Revenue and Customs Commissioners* [2007] BTC 414 [2007] UKHL 25, reference to "enterprise" in Art.25(5) (non-discrimination on the basis of ownership) and in similar treaties was taken to refer to the companies that were the subject of the alleged discrimination and not the business they undertook. SeeLord Hoffmann at Para. 7.

88. The Study, Van Raad K., Chapter 5 p.62.

"enterprise" is broadly used in three ways in the Model (i) where an "enterprise" is a person or entity (ii) where an "enterprise" is a business or (iii) where "enterprise" can mean both business and person.

Since the ordinary meaning of the term "enterprise" results in an ambiguous and unclear result, according to the principles applied by Mummery J. in *Commerzbank*, recourse may be had to supplementary means of interpretation.

Unfortunately, the wording in Para. 4(4) of the Commentary to Art.3 does not clarify the position, stating that "The question of whether an activity is performed within an enterprise or is deemed to constitute in itself an enterprise has always been interpreted according to domestic law" which suggests that the term "enterprise" may either refer to an entity or an activity[89] although it is not inconsistent with the "ordinary meaning" referred to above.

Meanwhile, the High Court of Australia in *Thiel v FCT*[90] which is the leading foreign court decision on the meaning of "enterprise", held that a treaty meaning should be given to the term, without reference to domestic law. The Court had to consider the application of the treaty between Switzerland and Australia, which contained undefined the terms "enterprise" and "profits. It reversed the decision of the Federal Court and held that question of interpretation was to be "resolved by reference to the Agreement itself and any extrinsic materials which may properly be considered", since the words "have no particular or established meaning in domestic law of Australian income tax which is relevant to the outcome of the question for decision."

89. In "Does 'Enterprise' in the OECD Model mean 'Business'?" Avery Jones et al note the difference in the French expression *entreprise*, which is defined to include "*l'exercice de tout activité ou affaire*", whereas in English enterprise is defined in terms of business and business is expanded to include professions.

90. 21ATR 1990, p.531. The case concerned a Swiss resident taxpayer who sold shares, which resulted in gains that were taxable in Australia. He sought to rely on the Switzerland–Australia treaty, arguing that since the profit made on sale constituted "business profits" within Art.7, and since there was no PE in Australia, he was not subject to Australian tax.

Scholars take differing views on whether the term "enterprise should be given an autonomous or domestic law meaning. According to Van Raad, "enterprise" in the OECD MC means "business" or "business organisation".[91] However, Vogel believes[92] that an autonomous international meaning of the term "enterprise" may be deduced from the treaty context in line with the High Court of Australia's decision in *Thiel,* with the following characteristics (i) the enterprise's activity may be a one-time activity (ii) it has to be an activity with a lucrative intent, excluding passive holding of assets (iii) it must be carried out independently (iv) it must not qualify as agricultural or forestry activities.

4.3.2 UK Treaty practice

Case law indicates that the term "enterprise" has generally been given an autonomous meaning by UK Courts, without an attempted reference to domestic law. In *Padmore v. Inland Revenue Commissioners,*[93] the Court of Appeal was concerned with whether the taxpayer, a UK resident partner in a Jersey partnership, could benefit from the exemption in the Jersey tax agreement on the basis that the partnership was resident in Jersey. Art.2 of the agreement defined "Jersey enterprise" as "an industrial or commercial enterprise or undertaking carried on by a resident of Jersey" and a "Resident of Jersey" as "any person who is resident in Jersey for the purposes of Jersey tax and not resident in the UK for the purposes of United Kingdom tax". The term "Person" was defined as "any body of persons, corporate or not corporate". The Court decided that the partnership was a "body of persons" resident in Jersey for the purposes of the Jersey tax agreement. This was despite the fact that the definition of "body of persons" in the UK income tax rules did not include a partnership. The domestic law definition of "body of persons" was disregarded since the addition of the words "corporate or not corporate" indicated that the reference to "person" in the agreement was autonomous and not defined under the equivalent of Art.3(2) (i.e. by reference to UK domestic law).

91. Van Raad K., "The term enterprise in the Model Double Taxation Convention – Seventy years of confusion", [1994] *Intertax,* p.491.

92. Vogel in Vogel and Lehner Deoppelbesteuerungsabkommen–Kommentar, Munich: C.H. Beck, 2008, 5th edn., Marg.Note41a referred to in the Study, German Report p335.

93. [1989] STC493.

Therefore, "person" did include a partnership in this context and the partnership was a "Jersey enterprise" for the purposes of the treaty. Similarly, in *Sun Life Assurance Co. of Canada v. Pearson*,[94] a company was held to be a "Canadian enterprise" for the purposes of the treaty in relation to the attribution of profits to a UK PE.

From a practical point of view, HMRC look to see whether a company is deemed to be an "enterprise" for treaty purposes in the same way as any other taxpayer, by looking to see if the company carries on a "trade" or has a "business" of making investments. A foreign company must be carrying on a trade in the UK through a PE before the income of a branch is chargeable to corporation tax.[95] Therefore, if a PE is deemed to be trading for UK tax purposes, it should constitute an "enterprise" for treaty purposes, since the concept of "business", which has been equated to that of "enterprise" in Art.3(1)(d), is wider than "trade". It follows that a company that is exclusively earning investment income will only be considered to be carrying on an enterprise in the UK, if it is carrying on a financial trade i.e. a bank.

In practice, the ambiguous contextual treaty interpretation of "enterprise" as a business organization or business activity does not appear to create many practical difficulties. The main complication in applying the contextual treaty meaning in UK domestic law, is that it appears to use three concepts, a resident carrying on an enterprise, and a business activity which is carried on by the enterprise, with the concept of "enterprise" interposed between the two concepts that are understood in domestic law[96] i.e. a taxpayer and a business.[97] However, the interposition of an enterprise between tax object and tax subject, may be crucial to the application of the treaty. For instance, if a fiscally transparent

94. 59TC250.

95. See Sec.6(2)ITTOIA and Sec.19 CTA 2009.

96. The Study, Australia Report p.154.

97. Avery Jones et al contrast this with the French translation, where the enterprise is synonymous with either the taxpayer or the business ibid 92.

partnership is considered to be an "enterprise"[98] carried on by several partners which are residents of a contracting state, provided the conditions in Art.5(5) are met, an agent acting on behalf of the partnership will be considered to be a dependent agent, resulting in a PE in the source state. This analysis may not follow if the enterprise in this example is considered to be the partners themselves, rather than the partnership (on the basis that the partnership is transparent and therefore disregarded). In those circumstances, it could be argued that the agent was acting on behalf of several principals, and therefore, on that basis the agent may be considered to be acting independently.[99] Therefore, although some commentators have argued that deletion of the term "enterprise" from the OECD MC would not alter its application, this is not true in every case.

4.3.3 Meaning of "enterprise" applying Art.3(2)

The contextual meaning of the term "enterprise" appears to imply that it may either refer to a person or an activity, although the use of the term in some contexts is not entirely clear. Therefore, in light of Art.3(2), the question may arise as to how strong the indications from the context must be before the non-application of the domestic law meaning is required.[100] On the other hand, since meaning of the term "enterprise" is being sought by reference to UK tax law[101] where the term is not used, it is arguable that even in light of an ambiguous contextual meaning, it would be difficult for the UK courts to argue that a domestic law meaning of the term should be applied. Since the reference to UK domestic tax law in Art. 3(2) gives no result, it is not possible to consider whether "the context

98. The Commentary to Art.5, Para 19.1 confirms this is the correct approach, stating that "in the case of a fiscally transparent partnership, the twelve month test is applied at the level of the partnership as concerns its own activities. If the period of time spent on the site by the partners and the employees of the partnership will therefore be considered have a permanent establishment."

99. See Canada *Swiss Bank Corp. et al. v. Minister of National Revenue*, [1974]S.C.R.1144. Even if the partnership was disregarded, the same result may be reached if all of the partners are "acting together" in giving instruction to the agent, which in those circumstances, would not be considered independent.

100. Baker P., Double Taxation Conventions at E-21.

101. The Commentary to Art.3, Para. 4(4) states that recourse should be had to domestic law in order to interpret whether an activity is "performed within an enterprise or is deemed to constitute in itself an enterprise."

otherwise requires" by reference to UK law, and therefore the term "enterprise" in UK treaties is left to be interpreted in accordance with public international law.

4.4 Meaning of "business" in the OECD MC

4.4.1 Contextual meaning

The term "business" is not defined in the OECD MC, although Art.3(1)(h) does provide a partial definition, stating that it includes "the performance of professional services and other activities of an independent character".

However, this clarification is not exhaustive and was included as a result of the deletion in 2000 of the IPS Art.14 in order to ensure that income, which used to fall within the ambit of Art.14 was covered by Art.7 after the deletion. These changes have not been included all UK treaties concluded since they were included in 2000.[102]

Since there is no definition of "business" in the OECD MC, further clarity on the contextual meaning may be sought by reference to supplementary means of interpretation.

The Commentary to Art.3 at para 10.2 states clearly that the term "business" should take its meaning from domestic law, stating:

> The Convention does not contain an exhaustive definition of the term "business", which, under paragraph 2, should generally have the meaning, which it has under the domestic law of the State that applies the Convention.

102. Since the deletion was made in the OECD MC, the UK concluded 27 treaties with other states, which are still in force, and of those, six include an ISP Art.14.

If it is accepted that a domestic law meaning of the term "business" should be applied, the question is, to what extent should the contextual meaning of "business" in the treaty (to the extent one can be deduced) restrict the domestic tax law meaning, if at all?

There are no reported UK cases in which the definition of "business" in the context of Art. 7 has been discussed. However, the decisions of foreign courts may be persuasive.

In *Transvaal Associated Hide and Skin Merchants v. The Collector of Income Tax Botswana*,[103] the taxpayer company, which was resident in South Africa, rented out a shed in Botswana from an abattoir, which was used to cure and store raw hides purchased from the abattoir there. The company employed between 20 and 30 labourers to perform the curing of the hides, although payment and negotiation of contracts for sale were concluded in South Africa. The Court held that income from the contracts was attributable to a PE in Botswana on the basis that (i) the curing process carried on in the shed was the characteristic feature and the most important essential element of the taxpayer's business and thus dominant over the selling activities in South Africa and (ii) use of the shed was not temporary or occasional, but permanent. Therefore the activities went beyond mere purchase or storage of goods and constituted the carrying on of a business.

Meanwhile, in *Rutenberg v Her Majesty the Queen*,[104] the Federal Court of Appeal held that a US resident investing in Canadian real estate did not constitute the carrying on of a business by a US enterprise. In assessing whether the activities carried out by the taxpayer in the US constituted an enterprise, the Court made a distinction between the taxpayer's main business of as a jeweller and diamond broker, his other real estate investments in the US and Israel and his investment in Canadian real estate, concluding that the activities did not constitute a single enterprise. The Canadian real estate investment had a distinct and separate character, and on the basis that the initiative in the

103. (1967) S.A.T.C.97.

104. (1979) A-415-75.

development and management of the enterprise in connection with that investment was carried on in Montreal by the taxpayer's broker, the activities carried on by the taxpayer in the US, which included telephone calls, having meetings concerning the business and concluding contracts, were not sufficient to constitute an "enterprise" "carried on"[105] there.

The leading case in this area *Thiel,*[106] illustrates the extent to which the courts are prepared to restrict the domestic law concepts in establishing whether a business is being "carried on" "in order to establish whether a PE exists." The question before the High Court of Australia was whether the sale of a number of shares, which the taxpayer had received in consideration for units he had originally acquired in an Australian trust, and subsequently listed, constituted an "enterprise" "carried on". Even though Australian domestic law did not regard an isolated activity of acquiring shares with a view to sale at a profit as constituting a "business" for tax purposes, which required some continuity,[107] it nevertheless held that the sale of shares amounted to "an adventure in the nature of trade" and could constitute an "enterprise carried on" provided the activity or activities are entered into for business or commercial purposes. It dismissed the judgment of Franklyn J. Sheppard L.J. and Lee L.J. of the lower court in which they had distinguished the phrase "carried on" from the phrase "carried out", and held that the words "carried on" only indicated that the enterprise should be undertaken by a resident of a Contracting State. The approach of the Australian Court suggests that an autonomous interpretation of "business" should be applied in interpreting the term in the tax treaties, and there is also doctrine to suggest that this may be the correct approach.[108]

105. The treaty referred to an "enterprise" carried on rather than a "business" carried on, using the alternative meaning of the term "enterprise" to refer to a business activity.

106. *Thiel v. Federal Commissioner of Taxation*, (1990) 21 ATR531.

107. The Court held that the words "carried on" did not impose a requirement of continuity due to the Commentary which stated "The question whether an activity is performed within the framework of an enterprise or is deemed to constitute in itself an enterprise has always been interpreted according to the provisions of the domestic laws of the Contracting States."

108. Rust, A., Chapter 6, the Study p.85 fn.5.

4.4.2 UK Tax treaty practice

HMRC consider that "business" has a broader meaning than "trade." Therefore to the extent a "trade" is being carried on in UK domestic law, HMRC consider that a "business" should also be carried on although they take the view that the definition of "business" in a treaty context should involve some element of activity, with the passive holding of investments not being sufficient.[109]

4.4.3 Meaning of "business" applying Art.3(2)

It appears that the meaning of the term "business" in a treaty context, whilst having a broad scope, principally derives its meaning from domestic tax law, as indicated in the Commentary. The foreign court decisions set out above indicate that the term "business" should be given a broad meaning, holding that the meaning of "business" in a treaty context includes "anything which occupies the time attention and labour of a man for the purposes of profit is business"[110] and "isolated activities".[111] Although the courts also held that there must nevertheless be some active involvement in profit making activity to constitute a business, and the mere holding of property is not sufficient,[112] there is nothing in the first two cases per se, to indicate that a contextual meaning of the term "business" was applied in preference to domestic law. However, in *Thiel*, the Court clearly found it necessary to restrict the Australian domestic law meaning of "business".

It is difficult to reconcile the decision in *Thiel,* which restricts the application of domestic law, with the clear statement in the Commentary, which suggests that a domestic law meaning of the term "business" should be applied. Although, strictly speaking, *Thiel* concerned the interpretation of the words "enterprise" "carried on", it nevertheless dealt with the question of whether an activity had a business purpose for treaty purposes. In that case, the Australian Court decided that the context of the Convention "otherwise required" that the domestic law meaning be restricted to a certain degree, and

109. This view was given based on discussions with David Price, Doug Jones and Mike Hogan from HMRC.

110. Maisels J.A. in *Transvaal* quoting the dictum of Jessel M.R. in *Smith v. Anderson*.

111. *Thiel* and also Canada: *MNR v. Tara Exploration and Development Co. Ltd* (1972) 28DLR 135.

112. *Rutenberg*. See also *Sogetra S.A.C. Etat Belge* (1974) Pas. Belge 1124 referred to in Baker P., at 7B.05.

an autonomous approach taken. Therefore, in light of the Commentary and case law, one must conclude that although a domestic tax law meaning of the term "business" it may be applied, it may be necessary to restrict the meaning according to the context of the convention.

On attempting to apply a UK domestic tax law meaning, one comes up against the initial hurdle that the term "business" is not used in UK to define tax jurisdiction. However, there is doctrine to suggest that Art.3(2) should cover not only words and expressions but also treaty concepts. This is on the basis that a "term" may also express a concept[113], and therefore, analogy may be made to synonymous terms in domestic tax law.[114]

The terms "trade", "profession" and "vocation" which are commonly used in the UK's income tax law have been held to constitute the carrying on of a "business" in case law, with Park J. holding in *Jowett (HMIT) v. O'Neill & Brennan Construction Ltd*[115] that business activities for the purposes of UK tax law encompass the carrying on of trades, professions, vocations and investment." Therefore although "trade", "profession" and "vocation" are not entirely synonymous with 'business", the concepts overlap, with the concept of "business" given a wider meaning.[116]

Therefore, although a meaning of the term "business" may be derived in other tax laws (i.e. VAT) and in UK commercial law, it is logical to apply the UK domestic tax law meaning of "trade" (or "trade", "profession" and "vocation" in relation to individuals) for the purposes of interpreting "business" in Art.7, to the extent the treaty context allows. There is a question of whether the domestic law meaning

113. *Burghardt, Estate of v. Commissioner*, 80 T.C. 705 (1983).

114. See *Gladden Estate v. The Queen*, 85 DTC 5188, at 5191 where the Canadian Court considered the term "disposition" in Canadian domestic law was synonymous with the term "alienation" in Art.13 OECD MC. Edwardes-Ker, Tax Treaty Interpretation, at p83. Kandev M., "*Tax Treaty Interpretation: Determining Domestic Meaning Under Article 3(2) of the OECD Model*" Canadian Tax Foundation website referring to Ward D., Ward's Tax Treaties 1996-1997, at 48.

115. [1998] BTC 133 at139.

116. LR. 1.CP148. See also *Torkington v Revenue and Customs Commissioners, Harris v. Amery, Smith v. Anderson* and *Re A Debtor ibid.* pp.19 and 21.

of “trade”, “profession” and “vocation” may be restricted according to the context of the Convention. Since UK domestic tax law recognises that a “venture in the nature of trade” may constitute trading for UK tax purposes, the incompatibility between the treaty meaning and domestic tax law meaning that applied in *Thiel* should not be relevant. However this may not be the case in relation to “professions” and “vocations”, which require an element of continuity in order to be treated as a business activity, and therefore in attempting to apply those terms, the wider treaty meaning of “business” may apply.

4.5 Meaning of “business profits” in the OECD MC

4.5.1 Contextual meaning

Once it has been established that an “enterprise” is carrying on a “business” in the UK, it is necessary to determine whether any resulting income from business activities carried on by the enterprise constitutes “business profits” for treaty purposes.[117] It follows that most of the practical difficulties that have arisen from interpreting the term “business profits” are related to the different meanings of “business” in domestic law, and difficulties related to the application of Art.7.

The term "business profits" is not defined in the Model and is often only used in the heading to Art.7, and the Article itself refers to "profits of an enterprise." That the term is undefined, is confirmed in para.71 of the Commentary to Art.7, which states that:

> “Although it has not been found necessary in the Convention to define the term “profits”, it should nevertheless be understood that the term when used in this Article and elsewhere in the Convention, has a broad meaning including all income derived in carrying on the enterprise.

117. In *Thiel*, 4720, Dawson J. argued that once it was established that a single activity could constitute an enterprise, it was arguable whether the categorization of income as “business profits” imposed any additional restriction, as any profit of a business nature or commercial character would constitute business profits. However, see the differing approaches of civil and common law countries companies at 4.6 below.

> Such a broad meaning corresponds to the use of the term made in the tax laws of most OECD member countries."

It is hard to reconcile the Commentary above, which states that the term "profits" should be given a wide meaning including any income derived from an "enterprise", with the approach in para 10.2 of the Commentary to Art.3, which indicates that a domestic law meaning of "business" should apply, since it suggests that all income from the carrying on of an enterprise will be business profits, irrespective of the actual treatment of that income under domestic law.

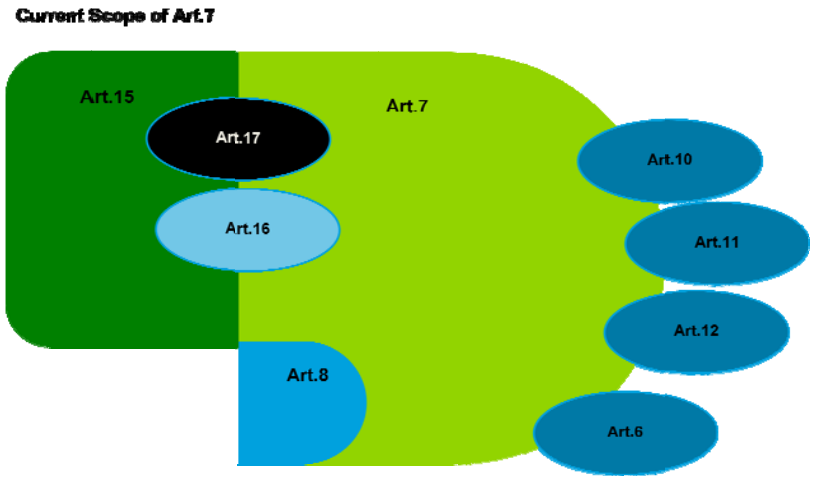
Since the Commentary indicates that the term "business profits" should be given a wide meaning, there is a question of how the term interacts with other distributive rules in the treaty. This is particularly the case in the light of Art.7(7), which states that "items of income which are dealt with separately in other Articles of this Convention…shall not be affected by the provisions of this Article." Applying this rule, the scope of the term "business profits" may be clarified further by analysing the interaction of Art.7 with other distributive rules.

Although a comprehensive discussion of the interaction of Art.7 with other articles in the Model, is outside the scope of this paper, it may be deduced that after the deletion of Art.14 in 2000,[118] and the inclusion of "independent personal services" in Art.7, that Art.15 which applies to income from employment, limits the application of Art.7 to income derived from independent activities.[119] This

118. UK treaties used to distinguish between business profits in Art.7 and "professional services and other activities of an independent character" referred to in Art.14. The concept of a "fixed base" in Art.14(1), which was equivalent to a "fixed place of business" in Art.5(1), was deleted from the OECD Model on 29 April 2000 because there was no intended difference between these two concepts.

119. In fact the Commentary to Art.15 states that a country's domestic law cannot go "too far" by arguing that someone who provides services to a large number of clients does not have a business and is an employee of each client.

exercise may also be undertaken by reference to other distributive rules, resulting in the following graphical description:[120]



As can be seen, it is broadly the case that some treaty provisions are *leges speciales* to Art.7 (i.e. Art.8, which broadly applies to income from the operation of ships or aircrafts and boats) whereas others are *leges speciales* to Art.15 (e.g. Arts.18 and 19 which apply respectively to (i) income from pensions and other similar remuneration from past employment and (ii) income from remuneration paid by the government). Arts.16 and 17 deal with the provision of services (by directors and artistes and sportsmen), which can be exercised dependently or independently and can therefore overlap within either Article (i.e. Arts. 7 or 15). There is also partial overlap between Art.7 and the "passive income" articles, Arts. 6,10,11 and 12, which apply to income from immoveable property, dividends, interest and royalties. These special "passive income" articles take priority by virtue of the effect of Art 7(7), to the extent that (i) the activity producing such income amounts to mere holding activities and no business activity is deemed to be carried on, (ii) the income is not effectively connected to a PE in the source state by virtue of the deeming rules in Arts.10(4), 11(4) and 12(2). See 4.6 below for an illustration of the application of these provisions.

120. This diagram is reproduced from Rust A., the Study, Chapter 6 p102. Vogel also discusses the relationship between Art.7 and other distributive rules. Vogel K., ibid.fn12.at pp.406-407.

4.5.2 UK Tax treaty practice

Case law suggests that the UK Courts are prepared to give the term "business profits" a wide meaning, and that treaty provisions will override domestic law provisions where necessary. This is despite the fact that most of the cases involve the interpretation of earlier treaties, which use the phrase "commercial and industrial profits"[121] which in the courts' view[122] may not be coextensive with the term "profits" used in later treaties.[123]

In *Ostime (HM Inspector of Taxes) v. Australian Mutual Provident Society*,[124] the House of Lords held that where there was a clear conflict between the provisions of the Double Taxation Relief (Taxes on Income) (Australia) Order, 1947 and domestic law, the treaty provisions overrode domestic law[125] such that a notional sum of investment income based on a deemed proportion of income from investment of a life assurance fund, constituted "industrial or commercial profits"[126] for the purposes of the Australian treaty. Therefore, the attribution rules in that treaty applied and the House of Lords rejected the Crown's contention that "industrial or commercial profits" only referred to trading

121. See Art.3(1) Antigua and Barbuda (1947).

122. See Vinnelot J in *Sun Life Assurance*. This definition led to problems, especially with regard to interest received by banks. *ES & A Bank Ltd v. F.C.T.* (1969) 69 A.T.C.4069. David Price, Doug Jones and Mike Hogan from HMRC express the view that property and royalty income are not included in this definition and may therefore deny credit on that basis.

123. Vogel K., ibid.fn.12 at 418 states that the term "industrial and commercial profits" as used in German treaties should be interpreted according to domestic law, but that it was suggested that the term includes "income from letting and leasing or any other way of using the enterprise and furthermore gains from the sale of the business as a whole or in part."

124. (Ch.D) [1958] Ch. 774; All E.R.305.

125. See Roxan, I., "United Kingdom" in G. Maisto (ed.), *Tax treaties and domestic law*, Amsterdam: IBFD Publications BV, Vol. 2 EC and International Tax Law Series, p. 340 in which the author explains this concept in more detail.

126. This was despite the definition in Art.II(1)(i) of the treaty, which stated that "industrial or commercial profits includes profits from such activities or business but does not include income in the form of dividends, interest, rents, royalties…."

profit.[127] Similarly, in *Sun Life Assurance Company of Canada v. Pearson*,[128] the Court of Appeal found that "profits" for the purposes of the Double Taxation Relief (Taxes on Income) (Canada) Order 1967 referred to a Canadian enterprise's investment income, not its income less expenses. The Court held that while the term "profits" commonly referred to "receipts less expenses", that interpretation was by no means easily applicable to all businesses and that a wider interpretation of "profits" may be required.[129] Finally, in *General Reinsurance Co. Ltd. v. Tomlinson, H.M. Inspector of Taxes*,[130] the High Court held that enhanced values obtained from sale or conversion of securities from underwriting activities which arose on capital account, may be charged as trading profits of the London branch, where what was done was not merely a realization or change of investment, but an act done in what was the carrying on or carrying out of a business.[131]

Meanwhile, *Padmore*, is an example of an conflict between the provisions of a treaty and UK domestic law, which was not accepted by the UK. In response, UK Parliament enacted legislation[132] with retrospective effect to intentionally override the effect of Art.7 and ensure that business profits attributable to a person resident in the UK were nevertheless chargeable to tax.[133]

127. Lord Denning dissented on the basis that the treaty made a distinction between business profits and investment income and under UK domestic tax principles, a mutual assurance company would be making investment, rather than trading income.

128. [1986] BTC 282.

129. Art.7(7) stated that "where profits include items of income which are dealt with separately in other Articles of this Convention…", which indicated that profit were simply another item of income.

130. 48 TC 81.

131. See also *Northern Assurance Co v. Russell* 2 TC.

132. Sec.58 Finance Act 2008.

133. The legality of the retrospective effect of this legislation has recently been challenged unsuccessfully under the Human Rights Act 2008 in *Huitson v. HMRC* [2010] EWHC 97 (Admin).

4.5.3 Meaning of “business profits” applying Art.3(2)

From a practical point of view, whether income is considered to be “business profits” according to a treaty, will depend on whether the activity generating the income is considered to be a “business” for treaty purposes. Since the meaning of “business” (according to the Commentary) is to be decided by reference to domestic law (albeit within the contextual restraints on the treaty), it is difficult to see how this approach should be reconciled with the Commentary to Art.7 at para.71, which suggests that an autonomous treaty meaning of “business profits” should be applied.

This approach should not be problematic in civil law countries where all income of a commercial company will be classified as business profits. However it may cause problems in the UK and other common law countries, where the difference in the way income is categorized is more significant.[134]

In order to reconcile the two approaches it is inevitable that recourse will need to be had to domestic law to ascertain a meaning of “business profits”, and following the analysis in 4.4, it is logical that the profits from a “trade” “profession” or “vocation” are used as an equivalent income category in the UK. However, the analysis above also demonstrates that any domestic law meaning will be restricted by contextual considerations, particularly the interaction of Art.7 with other distributive rules.

134. See Avery Jones, J.et al., “Treaty conflicts in categorizing income as business profits caused by differences in approach between common law and civil law”, B.F.I.T June 2003.

4.6 Qualification conflicts

4.6.1 Differing approaches to income categorisation in civil and common countries

Where both countries to a treaty interpret the meaning of "business" and "business profits" in light of different domestic laws, different distributive rules may be applied to the same income, leading to a qualification conflict. [135]

As discussed, from a source-state perspective, the UK does not automatically treat all profits earned by a foreign company as "business profits" (which are treated as "trading profits" for UK domestic tax purposes). Instead, the UK, will start by establishing whether a trade is carried on in the UK through a PE, and then examine the type of income attributable to the PE, in order to determine whether that income constitutes "business profits".[136]

However in contrast to the UK and other common law jurisdictions, there is an irrebutable presumption (or fiction) in most civil law jurisdictions that every resident commercial company carries on an "enterprise" with all of its assets, with the result that all income received by such companies is "business profits".[137]

4.6.2 Qualification conflicts

Most qualification conflicts in the interpreting the terms "enterprise", "business" and "business profits" arise as a result of the different treatment of companies by civil and common law countries, since categorization of income is either made by reference to the nature of the income itself (the

135. In contrast with civil law countries, which generally treat commercial companies as enterprises with all income of such companies deemed to be business profits. See p. 238 of Avery Jones, J.et al., ibid.p46.

136. Avery Jones, J.et al., ibid.

137. E.g., in Germany under § 8 Abs.2 of the KstG a company's entire income qualifies as business income. See the Study German Report p.338.

approach of common law countries, including the UK) or by reference to the taxpayer deriving the income (the approach of civil law countries).

However, these differences in approach rarely lead to the application of different distributive rules because of the effect of two provisions in the OECD MC (i) Art.7(7) which addresses the conflict that would otherwise arise from the broad definition of "business profits" and provides that to the extent that income is dealt with separately under another Article of the convention dealing with specific income categories, the provisions of that article should apply and (ii) the deeming provisions in Arts.10(4), 11(4), 12(3) and 13(2) which deem income or gains to be taxed in accordance with Art.7, to the extent that they are effectively connected with a PE in the source state.

In practice, these provisions mean that common law countries will apply the relevant special article (i.e. Arts10,11 or 12) if they determine the activity is not a business activity, whereas civil law countries will start with Art.7, but Art.7(7) will then require the application of the other relevant distributive rule.

4.6.3 OECD Approach

Despite the design of the Model, there are circumstances in which source and residence states may nevertheless apply different distributive rules. However these situations are generally resolved by applying the "new" OECD approach, which was introduced in the Commentary in 2000,[138] and gives priority to the source state's categorization of the income.

An example of the circumstances in which the application of different distributive rules may occur is where a company resident in a civil law residence state, manages a portfolio of shares through an office in the UK. Although the company is not carrying on a genuine business activity, the residence state is a civil law country and regards all income received by a company as business profits, whereas

138. See Commentary Para.32, Arts.23A and B.

the UK, as source state looks at the type income earned by the company in order to decide whether it constitutes business profits. The residence state will apply Art.7 and then applies Art.10, which then applies Art.7 via Art.10 (4). This is because the residence state considers that the company is carrying on a business of asset management at the office in the source state, which is a PE for tax purposes. However for the UK there is no PE since it does not apply an "enterprise" fiction, and mere asset management does not constitute a business. Therefore Art.10 will apply and there will be no return to Art.7 via 10(4).

The second example, is where the source state is a civil law country and considers all income earned by a company is business income and the UK, as the residence state treats all income according to its nature i.e. dividend income. In this case, the UK will apply Art.10 and the source state will apply Art.7.

In both these cases where different distributive rules are applied, the new OECD approach will avoid double non-taxation (or low taxation) and double taxation.[139] In the first case, whereas the residence state would normally exempt all income attributable to the PE (assuming it is an exemption state), since the UK is not entitled to a full taxing right (it will be applying a reduced withholding tax under Art.10) the residence state will instead apply a credit. In the second example, since the source state is exerting a full taxing right, the UK will be obliged to grant exemption.[140]

139. It is suggested that such a dispute is solely one of "qualification" of the income, even though the question whether there is a PE (or the connection of the income to the PE) is also involved, which might be taken to be a dispute about the interpretation of the treaty.

140. The application of the OECD approach may lead to some countries manipulating their domestic law to ensure that either (i) the definition of "business" in their domestic law is as wide as possible to ensure that income constitutes business profits falling within Art.7, or (ii) where a tax treaty contains a provision equivalent to Art.21(3) of the UN Model (which allows the source country to tax without a PE), to ensure that income from certain sources (e.g. technical fees) does not constitute business profits under domestic law and therefore falls within the "other income" article.

There may be circumstances in which the differing domestic laws of contracting states may lead to double taxation. This may occur where a bank receives interest on the only loan made to a resident of a particular state. Since there is only one loan, there will be no PE. The source state will treat the income as interest income resulting in a withholding tax being charged on the gross interest. However, if the residence state is a civil law country, it will treat the interest as business profits, and in the absence of a PE will assume full taxing rights over the income. However, the tax deducted in the source state may be too high to be fully credited against the residence country's tax on net profits.[141]

4.6.4 Mutual Agreement Procedure

To the extent that the UK cannot agree on a correct qualification of income with its treaty partner, and the new OECD approach does not resolve the conflict,[142]UK treaties (other than those following the colonial model) generally provide for mutual agreement articles to allow contracting states "to resolve by mutual agreement any difficulties or doubts arising as to the interpretation or application of the Convention."[143] However, the process can take many years and does not guarantee final resolution of the dispute.

As at October 2010, the UK tax authorities confirmed that there have been no cases in the preceding 12 months, where individuals have sought to rely on MAP in the UK in relation to conflict of qualification issues and, in practice, very few cases are settled in this way.[144]

141. See Avery Jones J., ibid p.48.

142. The Commentary to Art.23, Para.32.5 makes it clear that the "new approach" does not force the residence state to eliminate double taxation if it does not agree with the interpretation given by the other state. Sassville J., "*Klaus Vogel Lecture – Tax Treaties and Schrödinger's Cat"* B.F.I.T. February 2009.

143. See Art.25(3) Faroe Islands.

144. David Price, Doug Jones and Mike Hogan from HMRC expressed this view, although it was acknowledged that if conflicts are not resolved within MAP, there is generally no recourse since few treaties contain arbitration clauses.

CHAPTER 5

5. CONCLUSION

In summary, the meaning of the terms “enterprise”, “business” and “business profits” in the OECD MC is not entirely clear from the text of the Model alone. However a consensus may be reached on the likely scope of these terms in UK treaties patterned on the Model, by applying the interpretative rules described in Chapter 2.

The contextual meaning of the term “enterprise”, in light of the Commentary, case law and the writing of scholars suggests it may refer to (i) a business organisation, which may either be synonymous with the taxpayer (i.e. a company) or an intermediate entity such as a fiscally transparent partnership (ii) a business activity, or (iii) both business organisation and business activity. Although this resulting meaning is not entirely clear, and therefore arguably, may not have sufficient force to restrict the application of domestic law, since the UK does not use the term “enterprise” at all in its domestic tax law, the application of Art.3(2) has no practical effect and therefore there are good grounds to take the view that a treaty meaning of the term “enterprise” (as set out in cases law and doctrine) should be applied in UK tax treaties.[145]

Meanwhile, in light of the clear language of the Commentary to Art.7, there are good reasons to conclude that the term “business” should generally take its meaning from domestic law. This approach is not straightforward in the context of UK tax treaties, since the UK uses “trade” “profession” and “vocation” to express tax jurisdiction, rather than the term “business.” However, following doctrine and case law, which suggest that Art.3(2) applies to treaty concepts as well as treaty terms, there are good grounds to argue that the treaty concept of “business” may take its meaning from the equivalent concepts of “trade” “profession” and “vocation” in UK domestic tax

145. This approach is confirmed in *Thiel*.

law. However regard should also be had to the decision in *Thiel*, which suggests that a domestic law meaning of "business" may be restricted by a common treaty meaning in certain circumstances. The language of the Commentary also indicates that a domestic law meaning of "business" may be qualified in certain circumstances, since it states that "business" "should *generally* [italics added] have the meaning which it has under domestic law…". Although the application of a common treaty meaning should not affect the meaning of "trade" since scope of the term "trade" in UK domestic tax law appears to be consistent with the scope of "business" as applied in *Thiel* for treaty purposes, this may not be the case in relation to the terms "profession" and "vocation", which have a narrower scope than the apparent treaty meaning of "business".

Meanwhile, the position in relation to "business profits" is less clear. On the basis that the meaning of the term "business" should be determined by reference to UK domestic tax law, it should logically follow that the term "business profits" which refers to income arising from a "business" should also take its meaning from domestic law.

However, the Commentary to Art.7 suggests that the term "business profits" should have a wide meaning and include any income from an "enterprise." This suggests that an international treaty meaning may be appropriate. There are two arguments in favour of this approach. Firstly, a wide meaning would seem to fit well with Art.7(7), which has the effect of designating "business profits" as a general category of source state income that does not fall within special distributive rules (although Art.21 may apply to limited categories of income not falling within other rules). Secondly, an international treaty meaning would ensure that both states always apply the same distributive rule, which would be consistent with the objective in the Vienna Convention to construe the treaty in the "light of its objective and purpose" i.e. mitigating international double taxation. However, from a practical point of view, an international treaty meaning may be difficult to achieve in practice, given the differing meaning of "business" in various contracting states and in order to define the term,

undefined words will be needed which may open up new problems and questions of interpretation.[146] In order to reconcile the approach taken with regard to the term "business", it is inevitable that recourse will need to be had to domestic tax law to interpret the term "business profits", so that the term in UK treaties has the meaning of profits derived from a "trade" "profession" and "vocation". However, any meaning of the term "business profits" derived from UK domestic tax law will be restricted by contextual considerations, most particularly the interaction of Art.7 with other distributive rules.

146. An autonomous approach may lead to double non-taxation if the term "business profits" is broader in the tax treaty than in the domestic law of the source, which may not be able to make use of its taxing right. Meanwhile, a narrower definition of "business profits" than its domestic law meaning may create problems for civil law countries, which will have to apply a treaty categorization that differs from its own domestic law classification. Neither the new approach, nor Art.23A(4) would solve these problems, as there is no disagreement as to the interpretation of the treaty. See Avery Jones J.et al, Treaty conflicts in categorizing income as business profits caused by differences in approach between common law and civil law.

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