

Assessor
M Couch

Telephone: (01624) 685400

Fax: (01624) 685351

E-mail: incometax@itd.treasury.gov.im

Website: www.gov.im/incometax

PRACTICE NOTE

PN 141/07

Date: 8 March 2007

The Taxation of Trusts in the Isle of Man

1. This Practice Note covers the taxation of trusts in the Isle of Man.
2. Every person who has a liability to Manx income tax is required to make a return of income each year to the Assessor. This requirement applies to persons residing in the Isle of Man and to persons not residing in the Isle of Man but who derive income from sources in the Island (subject to certain exceptions).
3. Trusts, settlements, trustees and beneficiaries are not referred to in Manx income tax law (although it would be feasible to introduce trust-specific legislation in the future). Nevertheless, trustees and beneficiaries are 'persons' for the purposes of Isle of Man income tax and it is possible to determine the taxation position of trustees and beneficiaries on the basis of current law and practice, i.e. a combination of residence and source-based taxation, having particular regard to the residence of the beneficiaries of the trust rather than the residence of the settlor or the trustees.
4. A trust is a fiduciary relationship in which the trustee receives property from the settlor to hold for the use and benefit of the beneficiaries. Legal ownership of the property vests in the trustee and the beneficiaries have an equitable interest only. However, the Assessor acknowledges that as trust property is held for the use and benefit of the beneficiaries, the taxation of the trust should reflect the tax position of the beneficiaries. This means that the burden of tax imposed on the income of a trust should be the same as would have been levied on the beneficiaries had they received the income directly.
5. Trusts having at least one trustee resident in the Isle of Man, or where the administration of the trust is conducted in the Isle of Man, will be referred to for convenience as Manx trusts, and are within the scope of Manx income tax.
6. Where income is derived from property held by one person as nominee for another, or from property held by a trustee for another person who is absolutely entitled to that property as against the trustee, then the person or trustee, respectively, is not within the scope of Manx income tax in respect of that income.

7. A beneficiary may have an immediate entitlement to all or part of the income produced by trust property, net of income expenses, including trust management expenses, met by the trustees. In this situation the beneficiary is said to have an interest-in-possession (IIP). If the trustees have the power to prevent any right of present enjoyment (such as a power to accumulate income) then an IIP does not exist. The fact that trustees have a power to terminate an IIP does not prevent a beneficiary's income entitlement from being an IIP while it continues. For the purposes of this guidance, if a beneficiary of a trust does not have an IIP then they have a discretionary interest, meaning that the trustees have the power to determine how much income, if any, the beneficiary receives.
8. When an IIP exists in respect of only a part of a trust's income, the trust will be treated as two separate trusts, one being an IIP trust and the other a discretionary trust.
9. The Assessor will adopt the following approach to Manx trusts:

A) IIP trusts

Archer-Shee v Baker (1927, 11 TC 749) established that when a beneficiary has an absolute right to the income of a trust, that beneficiary will be taxable in respect of the trust income as and when it arises. The Assessor will apply this principle to treat a beneficiary of an IIP trust as though the trust income accrued directly to the beneficiary.

The trustees are not liable to tax in this case.

B) Discretionary trusts

If trust income is distributed, the beneficiaries will be taxed according to their residence status:

- a) beneficiaries who are not resident in the Isle of Man will be taxed on the income distributed to them as if the income accrued to them directly;
- b) beneficiaries who are resident in the Isle of Man will be subject to Manx tax in respect of any income distributed to them (to the extent that it has not already been taxed in the hands of the trustees as previously undistributed income).

The trustees will be taxed on income not distributed as follows:

- i) if all of the beneficiaries are not resident in the Isle of Man, undistributed income will be subject to the same amount of tax as would be charged where the same type and amount of income had been received by a non-resident individual;
- ii) if any of the beneficiaries is resident in the Isle of Man, undistributed income will be subject to Manx tax.

10. As mentioned in paragraphs 2 and 3, the Isle of Man has a combination of residence and source-based taxation. For the avoidance of doubt, income which is derived from business transactions outside the Isle of Man, or from dealings with persons resident outside the Isle of Man, or from the provision of services outside the Isle of Man, will not be considered as Manx-source income merely because the transaction is carried out by a Manx trust or a partnership which includes one or more Manx trusts.
11. Subject to paragraph 12 below, a trust will be regarded as having a Manx resident beneficiary if a person resident in the Isle of Man is identified in the trust deed either specifically by name or generally by virtue of being a member of a class of beneficiaries. To obviate the need for unnecessary enquiries, the Assessor will accept a declaration on an annual basis that no current Isle of Man resident did or could benefit from the income of a trust in that year of assessment.

12. A trust shall not be regarded as having an Isle of Man resident beneficiary solely because:
- a) a person resident in the Isle of Man may become a beneficiary; or,
 - b) there have been distributions in the past to a Manx resident beneficiary; or,
 - c) the trust deed does not have a Manx 'exclusion clause'.
13. The income derived from any property of any trust established for charitable purposes only is exempt from Manx income tax. Where the only Manx resident beneficiaries who can benefit from the income of a Manx trust are a charity or charities, or an arrangement or arrangements the objects of which are wholly charitable, then the Assessor will not treat the trust as having any Isle of Man resident beneficiaries solely because of the residence of the Manx charity or charities, as mentioned in paragraph 9 (B) (ii) above.
14. The Assessor will take appropriate action where it appears that any arrangement or arrangements, including those involving trusts, have been entered into with the intention of avoiding taxation in the Isle of Man.

M Couch
Assessor of Income Tax

This Practice Note is intended only as a general guide and must be read in conjunction with the appropriate legislation. It does not have any binding force and does not affect a person's right of appeal on points concerning their own liability to income tax.

Comments and suggestions for improvements of issued Practice Notes and suggestions for future Practice Notes are always welcome.