EXPLANATORY MEMORANDUM TO

THE DOUBLE TAXATION RELIEF AND INTERNATIONAL TAX ENFORCEMENT (ANDORRA) ORDER 2025

2025 No. 1301

1. Introduction

1.1 This Explanatory Memorandum has been prepared by His Majesty's Revenue and Customs (HMRC) and is laid before the House of Commons by Command of His Majesty.

2. Declaration

2.1 Dan Tomlinson MP, Exchequer Secretary to the Treasury, at His Majesty's Treasury confirms that this Explanatory Memorandum meets the required standard.

2.2 James Dunstan, Deputy Director for Business, Assets & International at HMRC confirms that this Explanatory Memorandum meets the required standard.

3. Contact

3.1 Scott McCartney at HMRC can be contacted by email at the following address with any queries regarding the instrument: taxtreaty.team@hmrc.gov.uk. Alternatively, the department can be contacted by telephone: 03000 515978.

Part One: Explanation, and context, of the Instrument

4. Overview of the Instrument

What does the legislation do?

4.1 The instrument brings into effect a Convention (the "2025 Arrangements") agreed by the United Kingdom and Andorra. The 2025 Arrangements are a Double Taxation Convention (DTC) for the avoidance of double taxation on income and gains from cross-border activity.

Where does the legislation extend to, and apply?

4.2 The extent of this instrument (that is, the jurisdiction(s) which the instrument forms part of the law of) is the United Kingdom.

4.3 The territorial application of this instrument (that is, where the instrument produces a practical effect) is the United Kingdom.

5. Policy Context

What is being done and why?

5.1 The purpose of DTCs is to prevent income or gains being taxed both in the territory in which they arise and the territory in which the recipient is resident. They do this either by allocating an exclusive right to tax the income or gain to one of the territories, or by providing that one territory must give relief for the tax charged in the other territory in respect of the same income or gain. DTCs also provide additional protection for taxpayers by including specific measures that combat discriminatory tax treatment. More generally, DTCs benefit taxpayers by ensuring certainty of treatment and, as far as possible, by reducing compliance burdens.

5.2 Like all of the United Kingdom's more recent DTCs, the 2025 Arrangements largely follow the Organisation for Economic Cooperation and Development's (OECD) latest Model Tax Convention on Income and on Capital (OECD Model), with any necessary departures explained below. In doing so, they encourage and maintain international consensus on the appropriate tax treatment of cross-border economic activity, promoting international trade and investment.

5.3 DTCs also protect the Exchequer by including provisions to combat tax avoidance. For example, measures providing for the exchange of information between revenue authorities make it more difficult for residents of both territories to evade taxation by concealing assets offshore.

5.4 The 2025 Arrangements include the minimum standards recommended by the OECD/G20 Base Erosion and Profit Shifting (BEPS) project. The BEPS project created a single set of consensus-based international tax rules to protect against tax avoidance while offering increased certainty and predictability to taxpayers. These provisions are now included in the 2017 version of the OECD Model.

What was the previous policy, how is this different?

5.5 There was not previously a DTC between the United Kingdom and Andorra. This instrument gives effect in the United Kingdom to the provisions of the new DTC.

5.6 The following paragraphs in this section explain the provisions of the 2025 Arrangements including the reasons for material departures from the OECD Model.

Title and preamble

5.7 The title and preamble of the 2025 Arrangements follow the latest OECD Model. The change to the OECD Model arose from the BEPS Action 6 Report on preventing the granting of treaty benefits in inappropriate circumstances. The statement in the preamble that the territories intend to avoid creating opportunities for non-taxation or reduced taxation through tax evasion or avoidance, including through treaty shopping arrangements, is one of the elements of the minimum standard on preventing treaty abuse agreed under the BEPS project.

Article 1 (Persons covered)

5.8 Article 1 sets out the general scope of the 2025 Arrangements. The 2025 Arrangements include two provisions from the OECD Model that were introduced following the BEPS project. The first concerns the treatment of income or gains derived through fiscally transparent persons such as partnerships. This provision confirms that the benefits of the 2025 Arrangements are only due where such income is effectively taxed in the hands of a resident of one of the territories.

5.9 The second provision clarifies that the 2025 Arrangements do not prevent a territory from taxing its own residents except where it explicitly provides otherwise. This puts beyond doubt that the provisions of a DTC cannot be used to circumvent anti-avoidance rules in a territory's domestic tax law.

Article 2 (Taxes covered)

5.10 Article 2 lists the taxes to which the 2025 Arrangements are to apply. The existing United Kingdom taxes to which the 2025 Arrangements will apply are income tax, corporation tax and capital gains tax. The existing Andorra taxes to which the Arrangements will apply are corporate income tax (*impost sobre societats*), personal income tax (*impost sobre la renda de les persones fisiques*), tax on income for fiscal non-residents (*impost sobre la renda dels no residents fiscals*) and tax payable on the

increase in value in immovable property (*impost sobre les plusválues en les transmissions patrimonials immobiliáries*).

Article 3 (General Definitions)

5.11 Article 3 defines a number of terms used in the 2025 Arrangements and provides a rule for determining the meaning of terms not defined. In particular, the 2025 Arrangements include a definition of a "recognised pension fund", relevant to Article 4, to ensure that pension funds not treated as a separate person fall within the definition. The United Kingdom also uses a definition of "national" that differs from the OECD Model in order to reflect more accurately the provisions of its domestic law.

Article 4 (Resident)

5.12 Article 4 establishes the meaning of "resident of a Contracting State" and lays down detailed rules for resolving cases where individuals or other persons may be considered residents of both territories for tax purposes under their domestic laws. Unlike the OECD Model, the provisions of paragraph 1 include reference to "place of incorporation" as this condition establishes company residence under the domestic laws of the United Kingdom and Andorra.

5.13 Paragraph 2(a) also confirms that a recognised pension fund that is established in either territory will be considered to be a resident. Paragraph 2(b) does not have an equivalent in the OECD Model but reflects the United Kingdom's preference for confirming that certain non-profit organisations will enjoy the benefits of the 2025 Arrangements even if they are generally exempt from taxation.

5.14 Paragraph 4 provides a tiebreaker for persons other than individuals which are resident in both territories under paragraph 1 of the Article. Under the 2025 Arrangements the competent authorities will determine the residence status of such persons by mutual agreement. This uses the wording introduced to the OECD Model following the BEPS project and prevents companies manipulating their tax residence for tax avoidance purposes.

Article 5 (Permanent establishment)

5.15 Article 5 defines the term "permanent establishment" (PE) for the purposes of the 2025 Arrangements. Taken together with Article 7, it describes the circumstances and manner in which enterprises of one territory may be taxed on their business profits arising in the other.

5.16 The Article includes in paragraph 5 a rule recommended by the BEPS project that prevents companies from fragmenting their activities in order to avoid the PE threshold.

Article 6 (Income from immovable property)

5.17 Article 6 allows the territory in which the property is situated to tax income from immovable property. It also defines immovable property. The Article replicates the equivalent provisions of the OECD Model.

Article 7 (Business profits)

5.18 Article 7 provides that unless an enterprise of one territory carries on business in the other through a PE situated there, its profits will be taxable only in its territory of residence. Where the enterprise has a PE in the other territory, that territory will be entitled to tax profits attributable to the PE. The provisions of this Article replicate the 2017 OECD Model.

Article 8 (International shipping and air transport)

5.19 Article 8 governs the taxation of shipping and air transport operated in international traffic. It follows the OECD Model in providing that profits of an enterprise of one territory from the operation of ships or aircraft in international traffic shall be taxable only in that territory. In line with United Kingdom preferences, the provision also clarifies that certain incidental income will be included in profits from the operation of ships and aircraft in international traffic.

Article 9 (Associated enterprises)

5.20 Article 9 governs the evaluation for tax purposes of transfers of goods, services, finance and intangible property between associated enterprises. It is based on the "arm's length" principle, which requires such transfers to be evaluated as if they had taken place between independent enterprises.

5.21 Where an adjustment is made to the profits of an enterprise by one territory, the other territory will make an appropriate corresponding adjustment to the amount of tax charged on those profits, in order to relieve the double taxation which might otherwise arise as a result of an adjustment by only one territory.

Article 10 (Dividends)

5.22 Article 10 contains the rules for the taxation of dividends paid by a company that is a resident of one territory to a resident of the other territory. Sub-paragraph 2(a) ensures that only the territory where the recipient is resident may tax the dividend.

5.23 However, where the dividend is paid by a company which derives most of its income from immovable property as defined in Article 6, and where such a company distributes most of its income annually, Sub-paragraph 2(b) overrides Sub-paragraph 2(a) and allows the territory of residence of the company to tax the dividend at a maximum rate of 15%. This protects the United Kingdom's 'Real Estate Investment Trust' regime, which allows investors to collectively invest in real estate.

Article 11 (Interest)

5.24 Article 11 contains the rules for the taxation of interest arising in one territory and paid to a resident of the other territory. It provides that interest will only be taxed in the territory where the recipient is resident.

5.25 The definition of interest departs from the OECD Model to reflect the United Kingdom's preference for clarifying that the Article does not apply to amounts that are within the definition of a dividend in Article 10.

5.26 Unlike the OECD Model, the "special relationship" provision at paragraph 6 applies where the amount of interest paid is excessive "for whatever reason". This permits the territories to take into account both the rate of the interest and the amount of the debt in determining whether interest paid is excessive.

Article 12 (Royalties)

5.27 Article 12 contains the rules for the taxation of royalties paid by a resident of one territory to a resident of the other territory. In line with the OECD model, the royalties will only be taxed by the territory of residence of the recipient beneficial owner.

5.28 Paragraph 4 deviates from the OECD Model; this provides the source rule for the article and clarifies that if a royalty is paid by a permanent establishment situated within a territory, then that royalty is deemed to arise in that territory for the purposes

of this Article. The United Kingdom does not require this to be included when there is residence state only taxation, however this was Andorra's preference.

Article 13 (Capital gains)

5.29 Article 13 contains the rules for the taxation of gains deriving from the alienation of property situated in one territory by a resident of the other. It materially replicates the equivalent provisions of the OECD Model.

Article 14 (Income from employment)

5.30 Article 14 contains the rules for the taxation of employment income and follows the OECD Model.

Article 15 (Directors' fees)

5.31 Article 15 follows the OECD Model and provides that directors' fees may be taxed in the territory of which the company paying them is a resident.

Article 16 (Entertainers and sportspersons)

5.32 Article 16 contains the rules for the taxation of income derived from personal activities as an entertainer or sportsperson. It follows the OECD Model.

Article 17 (Pensions)

5.33 Article 17 contains the rules for the taxation of pensions. It provides that all pensions, other than those in respect of government service, are taxable only in the territory where the recipient is resident.

Article 18 (Government service)

5.34 Article 18 contains rules for the taxation of remuneration paid to an individual in respect of government service, including pensions. The general rule is that the remuneration is only taxable in the territory to which the services are rendered, in line with the OECD Model. However, there is an exception for remuneration, other than pensions and other similar remuneration, paid to locally engaged staff. Such remuneration is taxable only in the territory where the individual is resident, provided that the individual is subject to tax there. There is also an exception for pensions and other similar remuneration paid to someone who is a resident and national of the other state, in which case the state of residence has the sole taxing right.

Article 19 (Students)

5.35 Article 19 contains the rules which govern the taxation of visiting students and business apprentices. Its provisions follow the OECD Model.

Article 20 (Other income)

5.36 Article 20 contains the rules for the taxation of income not dealt with elsewhere in the 2025 Arrangements. There are some deviations from the OECD Model. Paragraph 1 confirms that the benefits of the Article are only due where the recipient of the income is the beneficial owner. This is in line with similar conditions in Articles 10, 11 and 12. Paragraph 2 contains a United Kingdom preference rule that ensures that income paid out of a trust arrangement maintains the same character it had on payment to the trust. It also deems that tax paid by the trustees on behalf of the beneficiary is treated as having been paid by the beneficiary. Paragraph 4 includes a "special relationship" provision similar to that found in Articles 11 and 12.

Article 21 (Capital)

5.37 Article 21 contains the rules for the taxation of capital and follows the OECD model. This was a preference of Andorra, as at the time of signing the United Kingdom does not levy any taxes on capital.

Article 22 (Elimination of double taxation)

5.38 Article 22 sets out the methods by which each territory will relieve double taxation and is broadly based on the equivalent article in the OECD Model, modified to reflect each territory's domestic double taxation relief rules. Paragraph 1 sets out the provision applying to Andorra and provides for relief by way of deduction. Paragraph 2 details the corresponding provisions that apply in the United Kingdom, which generally provide for relief by way of credit, but also include provisions that exempt dividends and the profits of PEs from tax in line with domestic law.

5.39 Paragraphs 3 and 4 determine which territory is obliged to provide credit relief in the unusual situation where both territories can tax a resident on the income, profits or gains. Paragraph 3 removes the obligation for Andorra to provide relief for United Kingdom tax where the income in question is taxable in the United Kingdom solely because it is income of a resident of the United Kingdom and paragraph 4 is an equivalent provision relating to relief for Andorran tax.

Article 23 (Non-discrimination)

5.40 Article 23 provides that, subject to certain conditions, neither territory shall impose discriminatory taxes or connected requirements on the nationals, permanent establishments and enterprises of the other. In line with United Kingdom preferences, paragraph 5 deals separately with personal allowances granted to residents and nationals, confirming that the Article does not require these to be granted to such persons where they are not resident in the territory in question. Paragraph 6 confirms that the provisions of the Article only apply to the taxes covered by the 2025 Arrangements.

Article 24 (Mutual agreement procedure)

5.41 Article 24 establishes a procedure for resolving difficulties arising from the interpretation or application of the 2025 Arrangements and meets the minimum standard on improving dispute resolution agreed under Action 14 of the BEPS project. This follows the OECD Model.

Article 25 (Exchange of information)

5.42 Article 25 follows the latest OECD Model and provides for the exchange of certain information between the competent authorities of the two territories in compliance with international standards.

Article 26 (Members of the diplomatic missions and consular posts)

5.43 Article 26 ensures that diplomatic or consular officials shall not receive less favourable treatment under the 2025 Arrangements than they are entitled to under international law or under the provisions of special agreements (such as the Vienna Convention on Diplomatic Relations). The Article follows the OECD Model.

Article 27 (Entitlement to benefits)

5.44 Article 27 is an anti-abuse rule. It includes "the principal purpose test" (PPT) which denies treaty benefits to a person who seeks to take advantage of the provisions of the 2025 Arrangements to secure a result which is contrary to their object and purpose. The PPT is one of the elements of the minimum standard on preventing treaty abuse agreed under Action 6 of the BEPS project.

Article 28 (Entry into force)

5.45 Article 28 contains the provisions governing how and when the 2025 Arrangements will enter into force and take effect.

Article 29 (Termination)

5.46 Article 29 contains the provisions that govern how the 2025 Arrangements can be terminated and how that termination has effect.

Correction via Notes Verbale

5.47 The Convention signed on 20 February 2025 had a small clerical error in the English version of the text. This error was corrected by way of Note No: 03/2025 to the Ministry of Foreign Affairs of the Principality of Andorra, dated 11 June 2025, in which His Britannic Majesty's Embassy proposes the correction of the Convention; and by way of the replying Note Verbale from the Ministry of Foreign Affairs of the Principality of Andorra, dated 12 June 2025 (the Notes). The Notes are published in the Schedule to the Order, and taken together constitute an agreement to correct the clerical error in the Convention signed on 20 February 2025. The text of the Convention appended to the Order has been corrected in line with the Notes.

6. Legislative and Legal Context

How has the law changed?

6.1 This instrument brings into effect the provisions of the 2025 Arrangements.

Why was this approach taken to change the law?

6.2 This is the only possible approach to make the necessary changes.

7. Consultation

Summary of consultation outcome and methodology

7.1 The 2025 Arrangements were published on the gov.uk website on 21 February 2025 and a written ministerial statement to that effect was made on 26 February 2025. A consultation on the 2025 Arrangements was not undertaken as they were the product of bilateral negotiations with Andorra that dealt with a wide range of complex issues not suitable for open negotiation. However, HMRC regularly consults with external interested parties, including business representatives, about the United Kingdom's network of DTCs.

8. Applicable Guidance

8.1 General guidance on the operation of the United Kingdom's double taxation conventions can be found on the HMRC pages of the gov.uk website[1] and in the Double Taxation Relief Manual[2].

8.2 This Manual will be updated once the 2025 Arrangements enter into force, which will be after Andorra also completes its ratification of the 2025 Arrangements.

[1]Guidance on the operation of the UK's DTAs: https://www.gov.uk/hmrc-internal-manuals/international-manual/intm150000

[2] Double Taxation Relief Manual: https://www.gov.uk/hmrc-internal-manuals/double-taxation-relief

Part Two: Impact and the Better Regulation Framework

9. Impact Assessment

9.1 A Tax Information and Impact Note has not been prepared for this instrument because it gives effect to a DTC.

9.2 As with all DTCs, this DTC does not introduce new tax burdens. Rather, it provides relief from tax. Taxpayers may have to make a claim to HMRC or the fiscal authority of Andorra in order to benefit from the Arrangements.

Impact on businesses, charities and voluntary bodies

9.3 There is no, or no significant, impact on business, charities or voluntary bodies because apart from one-off costs of familiarisation with the benefits of the DTC there are not expected to be further costs.

9.4 The legislation does impact small or micro businesses but as with other businesses, the impact is negligible and no special approach for small or micro businesses is necessary.

9.5 There is no, or no significant, impact on the public sector because apart from one-off costs of introducing the DTC any further costs of administration would be minimal.

10. Monitoring and review

What is the approach to monitoring and reviewing this legislation?

10.1 The approach to monitoring this legislation is that DTCs are kept under regular informal review through communication with affected taxpayer groups and other stakeholders, and this measure will be monitored as part of that process.

10.2 The instrument does not include a statutory review clause.

Part Three: Statements and Matters of Particular Interest to Parliament

11. Matters of special interest to Parliament

11.1 None

12. European Convention on Human Rights

12.1 The Exchequer Secretary to the Treasury has made the following statement regarding Human Rights:

"In my view the provisions of the Double Taxation Relief and International Tax Enforcement (Andorra) Order 2025 are compatible with the Convention rights."

13. The Relevant European Union Acts

13.1 This instrument is not made under the European Union (Withdrawal) Act 2018, the European Union (Future Relationship) Act 2020 or the Retained EU Law (Revocation and Reform) Act 2023 ("relevant European Union Acts").