EXPLANATORY MEMORANDUM TO

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

2025 No. 1302

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 James Murray MP, Exchequer Secretary to the 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 Jo Hammersley at HMRC Telephone: 03000 563904 or email: taxtreaty.team@hmrc.gov.uk can be contacted with any queries regarding the instrument.

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 and Protocol (the "2025 Arrangements") agreed by the United Kingdom and Romania. The 2025 Arrangements replace the existing arrangements (the "1977 Arrangements") between the two Governments for the Avoidance of Double Taxation with respect to Taxes on Income and Capital Gains which will cease to have effect.

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 Double Taxation Conventions (DTCs) is to prevent double taxation where income or gains are otherwise taxable both in the territory in which they arise and the territory in which the recipient is resident. They do this either by allocating to one of the territories an exclusive right to tax the income or gain, 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). 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 1977 and 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. The 1977 arrangements had been previously amended to incorporate these minimum standards as a result of the multilateral Convention to Implement Treaty Related Measures to Prevent Base Erosion and Profit Shifting (BEPS MLI).

What was the previous policy, how is this different?

5.5 The previous DTC between the United Kingdom and Romania entered into force in 1977. This instrument gives effect in the United Kingdom to the provisions of the new DTC. The 2025 Arrangements make changes to taxing rights on dividends, interest and royalties and eliminate withholding taxes on these in some situations where the relevant criteria are met. The 2025 Arrangements also include provisions which ensure that the United Kingdom can tax gains made by residents of Romania on indirect holdings of immovable property situated in the United Kingdom.

5.6 The following paragraphs in this section explain the provisions of the 2025 Arrangements including the main differences from the 1977 Arrangements and 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. The 1977 Arrangements had been amended to include this provision under the BEPS MLI.

5.9 The second provision clarifies that the 2025 Arrangements do not prevent a territory from taxing its own residents except where the provision 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 Romania taxes to which the Arrangements will apply are tax on income and tax on profits.

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. For the most part, changes from the 1977 Arrangements reflect changes in the OECD Model. In particular, the 2025 Arrangements include a definition of a "recognised pension fund", relevant to Articles 4, 10 and 11, to ensure that schemes 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 Romania.

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 change was incorporated into the 1977 Arrangements (which previously had place of effective management as the tiebreaker) as a result of the BEPS MLI, and uses the wording introduced to the OECD Model following the BEPS project to prevent 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. Compared to the 1977 Arrangements the new Article slightly expands the list of activities not to be considered a PE. The new Article also 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. This is consistent with the 2017 OECD Model which contains this rule at paragraph 4.1.

5.16 Consistent with the position adopted by the United Kingdom, under the Multilateral Convention to Implement Treaty Related Measures to Prevent Base Erosion and Profit Shifting (BEPS MLI), the United Kingdom and Romania agreed not to adopt the other amendments to the definition of PE recommended by the BEPS project.

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 materially replicates the equivalent provisions of the OECD Model and there are no material changes from the equivalent provision in the 1977 Arrangements.

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 in the 2025 Arrangements follow the latest OECD Model provisions first adopted in 2010 which ensure that the attribution of profits to PEs is more closely aligned with the "arm's length" principle used to allocate profits between associated enterprises under Article 9.

5.19 In line with the OECD Model, income from commissions, professional services or similar activities previously falling under Articles 13 and 15 of the 1977 Arrangements will now be dealt with under Article 7 of the 2025 Arrangements.

Article 8 (Shipping and air transport)

5.20 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)

5.21 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.

5.22 The Article replicates the OECD Model and includes a paragraph 2 which determines that 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. Paragraph 2 was introduced into the 1977 Arrangements through the BEPS MLI.

Article 10 (Dividends)

5.23 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. It allows the territory where the company paying the dividend is resident to tax the dividend but where the beneficial owner of the dividend is resident in the other territory the rate of tax is limited depending on the circumstances. No withholding taxes will be applied where the recipient of the dividend holds 10% or more of the shares in the company paying

the dividend or is a recognised pension fund. The rate is 5% in all other cases except for dividends paid by Real Estate Investment Trusts where, in line with the United Kingdom's preferences, a 15% withholding tax rate applies. The 1977 Arrangements permitted Romania to tax dividends paid to United Kingdom residents at 10% or 15%.

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. Paragraph 2 contains the general rule which allows the territory where the payer of the interest is resident to tax the interest at 3%. Paragraph 2 is restricted by paragraph 3 which provides that the interest will only be taxable in the territory in which the beneficial owner is resident where certain conditions are met, including where paid between intra-group companies. The 1977 Arrangements permitted the territory in which the interest arises to tax the interest at 10%.

Article 12 (Royalties)

5.25 Article 12 contains the rules for the taxation of royalties paid by a resident of one territory to a resident of the other territory. The Article differs from the OECD Model in that it allows the territory in which the royalties arise to tax the royalties. Paragraph 2 restricts the tax that can be deducted to a rate of 3%. Paragraph 3 provides for an exception to paragraph 2 and allows for the royalties to be taxed only by the territory in which the beneficial owner of the income is resident in certain intra-group transactions. The 1977 Arrangements permitted the territory in which the royalties arise to tax the royalties at 10% or 15%.

Article 13 (Capital gains)

5.26 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. The 2025 Arrangements include a paragraph 4 which allows for non-residents to be taxed on gains arising from the sale of shares in property rich companies. Paragraph 4 differs from the OECD Model in that it follows the United Kingdom's preference not to extend the taxing rights to shares in companies which have derived more than 50% of their value from property in the previous 12 months.

Article 14 (Income from employment)

5.27 Article 14 contains the rules for the taxation of employment income and follows the OECD Model. In line with the OECD model, remuneration paid to visiting professors, teachers and research workers, dealt with under Article 22 of the 1977 Arrangements will now be dealt with under Article 14 of the 2025 Arrangements. Transitional rules for those entitled to the benefits of Article 22 under the 1977 Arrangements when the 2025 Arrangements enter into force are contained at Article 22 Entry into Force.

Article 15 (Directors' fees)

5.28 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)

5.29 Article 16 contains the rules for the taxation of income derived from personal activities as an entertainer or sportsperson. The first two paragraphs are materially the same as the OECD Model. The Article has an additional third paragraph, taken from paragraph 14 of the OECD Commentary on Article 17, which allows for income to be

taxed only in the territory in which the entertainer or sportsperson is resident where the visit has been paid wholly or mainly by public funds provided by that territory.

Article 17 (Pensions)

5.30 Article 17 contains the rules for the taxation of pensions. It provides that all pensions, other than those in respect of government service or paid under social security legislation, are taxable only in the territory where the recipient is resident. The treatment of pensions paid in respect of past employment is in line with the OECD Model and follows the 1977 Arrangements. The 2025 Arrangements introduce a separate provision that grants sole taxing rights to the territory paying pensions under social security legislation to tax those pensions. This was a Romanian preference, although the UK has accepted it in other Conventions, and will have minimal effect since the UK State pension is below the Personal Allowance.

Article 18 (Government service)

5.31 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 income is subject to tax there. The effect of the Article is broadly the same as the 1977 Arrangements.

Article 19 (Students and business apprentices)

5.32 Article 19 contains the rules which govern the taxation of visiting students and business apprentices. Its provisions follow the OECD Model. The Article differs slightly from the 1977 Arrangements in that it no longer provides for a small, annual tax-free amount to be earned in the territory in which the student is studying.

Article 20 (Other income)

5.33 Article 20 contains the rules for the taxation of income not dealt with elsewhere in the 2025 Arrangements. The Article follows the OECD Model and 1977 Arrangements in that it determines that income falling within the Article shall be taxable only in the territory in which the recipient is a resident. In line with the United Kingdom preferences, 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 the equivalent condition in Articles 10, 11 and 12. Paragraph 2 clarifies the treatment of income derived through trusts and estates and confirms that it will be taxed in accordance with the rules applying to the underlying source of the income. Paragraph 4 includes a ‘special relationship’ provision equivalent to those found in Articles 11 and 12.

Article 21 (Elimination of double taxation)

5.34 Article 21 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 Romania and provides for relief by way of credit. Paragraph 2 details the corresponding provisions that apply in the United Kingdom. The United Kingdom will generally provide for relief by way of credit, but paragraph 2 also includes provisions that exempt dividends and the profits of PEs from tax in line with domestic law.

Article 22 (Non-discrimination)

5.35 Article 22 provides that, subject to certain conditions, neither territory shall impose discriminatory taxes or connected requirements on the nationals, PEs and enterprises of the other. In line with United Kingdom preferences, paragraph 5 deals separately with personal allowances granted to United Kingdom residents and nationals confirming that the Article does not require them to be granted to persons not resident in the United Kingdom. The 2025 Arrangement omits paragraph 6 of the OECD Model which extends the Article to taxes of every kind and description. This is in line with the United Kingdom's preference to limit the non-discrimination Article to those taxes covered by the convention.

Article 23 (Mutual agreement procedure)

5.36 Article 23 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, which was introduced into the 1977 Arrangements through the BEPS MLI. The Article differs from the OECD Model in that it omits paragraph 5 of the OECD Model which allows for mandatory binding arbitration.

Article 24 (Exchange of information)

5.37 Article 24 provides for the exchange of certain information between the competent authorities of the two territories in compliance with international standards. The Article differs from the OECD Model in that it excludes VAT and customs duty from the scope of the Article, with these taxes and duties being covered by the Trade and Cooperation Agreement between the UK and EU.

Article 25 (Assistance in the collection of taxes)

5.38 Article 25 provides for the mutual assistance in the collection of tax debts between the United Kingdom and Romania. The Article differs from the OECD Model in that it excludes VAT, customs duties and excise duties from the scope of the Article, with these taxes and duties being covered by the Trade and Cooperation Agreement between the UK and EU.

Article 26 (Members of diplomatic missions and consular posts)

5.39 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)

5.40 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 and was introduced into the 1977 Arrangements through the BEPS MLI.

Article 28 (Entry into force)

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

5.42 Paragraph 3 of Article 28 introduces a legacy provision which allows individuals who were entitled to benefit from Article 22 (Professors, teachers and research workers) of the 1977 Arrangements to retain an entitlement to such benefits until such time as the entitlement under the 1977 Arrangements would have ceased.

Article 29 (Termination)

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

Protocol

5.44 The Protocol contains clarificatory and additional material relating to the Articles above and forms an integral part of the 2025 Arrangements.

5.45 Paragraph 1 of the protocol makes clear the meaning of the words 'may be taxed'. This clarification was included at the request of Romania.

5.46 Paragraph 2 defines VAT, customs duties and excise duties for the purposes of Articles 24 and 25.

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 13 November 2024 and a written ministerial statement to that effect was made on 18 November 2024. A consultation on the 2025 Arrangements was not undertaken as they were the product of bilateral negotiations with Romania 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 both the UK and Romania have completed their 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 Romania 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 (Romania) 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").