EXPLANATORY MEMORANDUM TO

THE DRAFT DOUBLE TAXATION RELIEF (TAXES ON INCOME) (BOTSWANA) ORDER 2006

1. This explanatory memorandum has been prepared by HM Revenue & Customs and is laid before the House of Commons by Command of Her Majesty.

This memorandum contains information for the Select Committee on Statutory Instruments.

2. Description

The draft Order brings into effect those arrangements specified in the Convention set out in the attached Schedule.

3. Matters of special interest to the Select Committee on Statutory Instruments

3.1 Type of resolution

This draft Order is subject to the affirmative resolution procedure.

3.2 Details of the Convention

Further details of the Double Taxation Convention scheduled to the draft Order are annexed to this memorandum.

4. Legislative Background

4.1 General

This Order is made under section 788 of the Income and Corporation Taxes Act 1988 (c.1) which has been amended by section 277 of the Taxation of Chargeable Gains Act 1992 (c.12) and section 198 (1) and (2) of the Finance Act 2003 (c.14),

Section 788 provides the mechanism by which arrangements made with overseas territories for the purpose of affording relief from double taxation in relation to income tax, corporation tax and capital gains tax and taxes of a similar character in the other territory are given effect in the United Kingdom. The relevant Convention is scheduled to an Order under section 788 and thus given domestic legislative effect.

The arrangements contain provisions concerning the exchange of information between the territories and, in particular, provisions to deal with the prevention of fiscal evasion in relation to the taxes mentioned above and they are also given effect in the United Kingdom by means of an Order under section 788.

4.2 EU legislation

This instrument does not implement EU legislation.

5. Extent

This instrument applies to all of the United Kingdom.

6. European Convention on Human Rights

The Paymaster General (Dawn Primarolo) has made the following statement regarding Human Rights:

In my view the provisions of the draft Double Taxation Relief (Taxes on Income) (Botswana) Order 2006 are compatible with the Convention rights.

7. Policy background

Double Taxation Conventions aim to eliminate the double taxation of income or gains arising in one State and paid to residents of another State. They do this by dividing the taxing rights that each treaty partner has under its domestic law over the same income and gains. They provide additional protection for taxpayers by specific measures combating discrimination in tax treatment. More generally, Conventions benefit the taxpayer by ensuring certainty of treatment and, as far as possible, by reducing compliance burdens. Double Taxation Conventions also serve an Exchequer protection role by including provisions to combat avoidance and evasion — not least by measures providing for the exchange of information between Revenue authorities. They also encourage and maintain international consensus on the appropriate tax treatment of cross-border economic activity and thus promote international trade and investment.

8. Impact

8.1 A Regulatory Impact Assessment has not been prepared for this instrument as it has no impact on business, charities or voluntary bodies. However, taxpayers may in some cases have to make a claim to HM Revenue & Customs or the other country's fiscal authority in order to benefit from the Convention. However taxpayers will benefit from reduced compliance burdens and, in many cases, from having to deal with just one fiscal authority.

8.2 The impact on the public sector is that because of the nature of a Double Tax Convention, one or both of the Contracting States gives up all or part of their taxing rights so that a given source of income is taxed only once. Measured against a baseline of single taxation only, Conventions do not therefore generally have an exchequer cost; rather, by encouraging cross-border economic activity, they can lead to an increase in tax revenue. But where double taxation is unrelieved, the economic activity in question, and hence the higher tax revenue attributable to it, will often be only temporary.

9. Contact

Geoff Barnard at the HM Revenue & Customs Tel: 0207 147 2734 or e-mail: Geoff.Barnard@hmrc.gsi.gov.uk can answer any queries regarding the instrument.

ANNEXE

GENERAL

All the United Kingdom's recent Double Taxation Conventions largely follow the approach adopted in the OECD's Model Tax Convention on Income and on Capital. This Convention continues that approach. In addition, it reflects changes in policy and legislation in the United Kingdom and Botswana since the entry into force of the existing Convention between the two countries, which this new Convention replaces.

NOTES ON DETAILS

ARTICLE 1 – PERSONS COVERED

The Convention is to apply to persons who are residents of one or both of the Contracting States (the United Kingdom and Botswana).

ARTICLE 2 – TAXES COVERED

This Article lists the taxes to which the Convention is to apply.

The existing Botswana taxes to which the Convention applies are the income tax and the capital gains tax.

The existing United Kingdom taxes to which the Convention applies are the income tax, the corporation tax and the capital gains tax.

The Convention is to apply also to any identical or substantially similar taxes subsequently imposed by either country in addition to or in place of the taxes mentioned above. A provision on these lines is usually included in our Conventions.

ARTICLE 3 – GENERAL DEFINITIONS

This Article defines a number of terms used in the Convention and provides a rule for determining the meaning of terms not defined in the Convention.

ARTICLE 4 – RESIDENT

This Article establishes the meaning of "resident of" the United Kingdom or Botswana and lays down detailed rules for dealing with situations where individuals or other persons may be considered residents of both countries for tax purposes under their respective domestic law.

ARTICLE 5 – PERMANENT ESTABLISHMENT

This Article provides the definition of a “permanent establishment”. It defines when an enterprise will or will not be deemed to have a permanent establishment in the other country. It also provides that a building site, construction, assembly or installation project is considered a permanent establishment if it lasts for more than six months.

Taken with Article 7, this Article prescribes the circumstances and manner in which businesses of one country may be taxed on their profits in the other country.

ARTICLE 6 – INCOME FROM IMMOVABLE PROPERTY

This Article allows the country in which the property is situated to tax income from immovable property.

Paragraph (2) defines “immovable property”.

ARTICLE 7 – BUSINESS PROFITS

This Article provides that unless an enterprise of one country carries on business in the other through a permanent establishment situated there, its profits will be taxable only in its country of residence.

Where the enterprise has a permanent establishment in the other country, that country will be entitled to tax profits attributable to the permanent establishment.

ARTICLE 8 – SHIPPING AND AIR TRANSPORT

This Article provides that profits of an enterprise of one country from the operation of ships or aircraft in international traffic will be taxable only in that country. It also provides that a share of profits derived from participation in a pool, joint business or international operating agency shall be taxable on the same basis.

ARTICLE 9 – ASSOCIATED ENTERPRISES

This Article provides that appropriate adjustments may be made in determining the profits of an enterprise of one country where conditions made or imposed between the enterprise and an associated enterprise of the other country differ from those that would be made between independent enterprises.

Where such an adjustment is made to the profits of an enterprise by one country, the other country will make an appropriate 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 just one country.

ARTICLE 10 – DIVIDENDS

This Article contains the rules for the taxation of dividends paid by a company which is resident of one country to a resident of the other.

Paragraph (1) provides that dividends paid by a company resident in one country (the source country) to a resident of the other country may be taxed in that other country.

Paragraph (2)(a) provides that if the beneficial owner is a company resident in the other country that controls at least 25 per cent of the voting power in the company paying the dividends, the tax in the source country will not exceed 5 per cent of the gross amount of the dividends.

Paragraph (2)(b) provides that in all other cases the rate of tax in the source country is not to exceed 12 per cent of the gross amount of the dividends, provided the beneficial owner is a resident of the other country.

Paragraph (3) defines the term "dividends".

Paragraph (4) provides that where a resident of one country receives dividends from the other country and carries on business in that other country through a permanent establishment there, with which the holding from which the dividend arises is effectively connected, the provisions of paragraphs (1) and (2) shall not apply. The taxation of the dividends is then governed by Article 7 (Business Profits) or Article 15 (Independent Personal Services).

Paragraph (5) rules out the extra-territorial taxation by one country of dividends paid by a company that is a resident only of the other country. The first country may not tax the dividends unless they are paid to a resident of that country or connected with a permanent establishment or a fixed base there. Similar provision is made in respect of undistributed profits.

Paragraph (6), an anti-abuse provision, ensures that the provisions of the Article will not apply if the shares or other rights in respect of which the dividend is paid were created or assigned mainly to take advantage of the Article.

ARTICLE 11 – INTEREST

This Article contains the rules for the taxation of interest paid by a resident of one country to a resident of the other.

Paragraph (1) provides that interest arising in one country (the source country) and paid to a resident of the other country may be taxed in that other country.

Paragraph (2) provides that interest may also be taxed in the source country, but if the beneficial owner is a resident of the other country the tax in the source country will not exceed 10 per cent of the gross amount of the interest.

Paragraph (3) defines the term "interest".

Paragraph (4) provides that where a resident of one country receives interest from the other country and carries on business in that other country through a permanent establishment there, with which the debt claim in respect of which the interest is paid is effectively connected, the provisions of paragraphs (1) and (2) shall not apply. The taxation of interest is then governed by Article 7 (Business Profits) or Article 15 (Independent Personal Services).

Paragraph (5) provides rules for determining in which country interest arises.

Paragraph (6) provides that where, because of a special relationship between the payer and the recipient, the amount of interest paid is excessive, the relief under the Article will apply only to the interest that would be payable at "arm's length".

Paragraph (7), an anti-abuse provision, ensures that the provisions of the Article will not apply if the debt claim on which the interest is paid was created or assigned mainly to take advantage of the Article.

Paragraph (8) provides an exception to paragraph (2). Interest is exempted from tax in the country in which it arises if it is beneficially owned by the Government of the other country, by a government agency, a local authority or certain named development agencies.

Paragraph (9) provides an exception to paragraph (2) in the case of loans made, guaranteed or insured by certain named government agencies.

ARTICLE 12 – ROYALTIES

This Article contains the rules for the taxation of royalties arising in one country and derived by a resident of the other.

Paragraph (1) provides that royalties arising in one country (the source country) and paid to a resident of the other may be taxed in that other country.

Paragraph (2) provides that royalties may also be taxed in the source country, but if the beneficial owner is a resident of the other country the tax in the source country will not exceed 10 per cent of the gross amount of the royalties.

Paragraph (3) defines the term "royalties".

Paragraph (4) provides that where a resident of one country receives royalties from the other country and carries on business in that other country through a permanent establishment there, with which the right or property in respect of which the royalties are paid is effectively connected, the provisions of paragraphs (1) and (2) shall not apply. The taxation of royalties is then governed by Article 7 (Business Profits) or Article 15 (Independent Personal Services).

Paragraph (5) provides rules for determining in which country royalties arise.

Paragraph (6) provides that where, because of a special relationship between the payer and the recipient, the amount of royalty paid is excessive, the relief under the Article will apply only to the royalty that would be payable at "arm's length".

Paragraph (7), an anti-abuse provision, ensures that the provisions of the Article will not apply if the rights on which the royalties are paid were created or assigned mainly to take advantage of the Article.

ARTICLE 13 – TECHNICAL FEES

This Article contains the rules for the taxation of technical fees arising in one country and paid to a resident of the other.

Paragraph (1) provides that technical fees arising in one country (the source country) and paid to a resident of the other may be taxed in that other country.

Paragraph (2) provides that technical fees may also be taxed in the source country, but if the beneficial owner is a resident of the other country and subject to tax on them there, the tax in the source country will not exceed 7.5 per cent of the gross amount of the technical fees.

Paragraph (3) defines the term "technical fees".

Paragraph (4) provides that where a resident of one country receives technical fees from the other country and carries on business in that other country through a permanent establishment there, with which the obligation to pay the technical fees is effectively connected, the provisions of paragraphs (1) and (2) shall not apply. The taxation of technical fees is then governed by Article 7 (Business Profits) or Article 15 (Independent Personal Services).

Paragraph (5) provides rules for determining in which country technical fees arise.

Paragraph (6) provides that where, because of a special relationship between the payer and the recipient, the amount of technical fees paid are excessive, the relief under the Article will apply only to the technical fees that would be payable at "arm's length".

Paragraph (7), an anti-abuse provision, ensures that the provisions of the Article will not apply if the rights on which the technical fees are paid were created or assigned mainly to take advantage of the Article.

ARTICLE 14 – CAPITAL GAINS

This Article contains the rules for the taxation of gains deriving from the alienation of property situated in one country by a resident of the other.

Paragraph (1) provides that gains derived from the alienation of immovable property in one country by a resident of the other may be taxed in the country where the property is situated.

Paragraph (2) provides that gains by a resident of one country from the alienation of certain types of shares or interests in partnerships or trusts that derive their value principally from immovable property situated in the other country may be taxed in that other country.

Paragraph (3) provides that gains arising from the alienation of movable property relating to a permanent establishment maintained in the other country may be taxed in that other country.

Paragraph (4) provides that gains derived by a resident of one country from the alienation of ships or aircraft operated in international traffic shall be taxable only in the country where the taxpayer is resident.

Paragraph (5) provides for capital gains to be taxed only in the country of residence of the alienator in cases not covered by paragraphs (1) to (4).

Paragraph (6), an anti-abuse provision, preserves the right of a country to tax gains from the alienation of any property by a person (including an individual, company or trustee) who is or was a resident of that country at any time during the fiscal year in which the property is alienated, or at any time during the six preceding fiscal years.

ARTICLE 15 – INDEPENDENT PERSONAL SERVICES

Paragraph (1) provides that income derived by a resident of one country in respect of professional services or other activities of an independent nature shall be taxed only in the country in which they are resident, However, if there is a fixed base in the other country, they may be taxed there on the profits attributable to that fixed base.

Paragraph (2) defines the term "professional services".

ARTICLE 16 – DEPENDENT PERSONAL SERVICES

Paragraph (1) provides that, in general, employment income of a resident of one country can be taxed in the other country if the employment is exercised there.

Paragraph (2) provides an exception to the general rule where an employee is present in the other country for not more than 183 days in any twelve-month period beginning or ending in the fiscal year concerned, the remuneration is paid by or on behalf of an employer who is not a resident of the other country and the remuneration is not borne by a permanent establishment or a fixed base which the employer has in the other country. Where all three conditions are satisfied, the remuneration will be taxable only in the employee's country of residence.

Paragraph (3) provides that the remuneration of an individual working on a ship or aircraft operated in international traffic may be taxed in the country where the enterprise operating the ship or aircraft is resident.

ARTICLE 17 – DIRECTORS' FEES

This Article provides that directors' fees (and other similar payments) paid to a resident of one country who is a member of the board of directors of a company may be taxed in the country where the company is resident.

ARTICLE 18 – ENTERTAINERS AND SPORTSPERSONS

Paragraphs (1) and (2) provide that income in respect of the personal activities of entertainers and sportspersons can be taxed in the country in which those activities are exercised, whether it is paid directly to the entertainer or sportsperson or to some other person.

Paragraph (3) provides that income from the activities performed in the other country by an entertainer or sportsperson shall be taxed only in his country of residence, if the visit is wholly or substantially supported by public funds.

ARTICLE 19 – PENSIONS

Paragraph (1) provides that pensions (other than government service pensions), other similar remuneration paid in consideration of past employment and annuities, that are subject to tax in the country where the pensioner is resident, shall be taxable only in that country.

Paragraph (2) defines the term “annuity”.

ARTICLE 20 – GOVERNMENT SERVICE

Paragraph (1) provides that in general, remuneration paid to an individual in respect of services rendered to a country, or to a political sub-division or local authority of a country, will be taxable only in that country. If however the services are carried out in the other country by one of that country’s own nationals resident there or by a resident who, although not a national, did not become a resident solely to render the services, then that other country will have the sole taxing right.

Paragraph (2) provides that in general, a pension paid to an individual in respect of services rendered to a country, or to a political sub-division or local authority of a country, will be taxable only in that country. If however the individual is a resident and national of the other country then that other country will have the sole taxing right.

Paragraph (3) provides an exception to the rules in paragraph (1). In the case of remuneration or pensions arising in connection with a trade or business, the provisions of Article 16, 17, 18 or 19 are to apply.

ARTICLE 21 – STUDENTS

This Article provides that certain payments for the maintenance, education or training of a visiting student or business apprentice will not be taxed in the country visited, provided the payments are made from sources outside that country.

ARTICLE 22 - OTHER INCOME

Paragraph (1) provides that any item of income not specifically covered elsewhere in the Convention, will be taxable by the country of which the owner is a resident.

Paragraph (2) provides that the provisions of paragraph (1) will not apply, other than to income from immovable property, if the right or property in respect of which the income is paid is effectively connected with a permanent establishment maintained in the country of source. In that case, the income will be taxable in accordance with Article 7 (Business Profits) or Article 15 (Independent Personal Services).

Paragraph (3) provides that any item of income received by a resident of one country not specifically covered elsewhere in the Convention and arising in the other country, may also be taxed in that other country.

Paragraph (4) provides that where, because of a special relationship between the payer and the recipient, the amount of income paid is excessive, the relief under the Article will apply only to the income that would be payable at "arm's length".

Paragraph (5), an anti-abuse provision, ensures that the provisions of the Article will not apply if the rights on which the income is paid were created or assigned mainly to take advantage of the Article.

ARTICLE 23 – ELIMINATION OF DOUBLE TAXATION

This Article sets out the methods by which double taxation is to be eliminated.

Paragraph (1) provides the details of how United Kingdom tax will be allowed as a credit against Botswana tax on profits, income or chargeable gains. Such a credit shall not exceed the Botswana tax payable on that profits, income or chargeable gains in accordance with the laws of Botswana.

Paragraph (2) provides details of how Botswana tax shall be allowed as a credit against United Kingdom tax on profits, income or chargeable gains. In the case of a dividend paid by a company resident in Botswana to a company resident in the United Kingdom and controlling at least 10 per cent of the voting power in the paying company, the credit will take account of the Botswana tax payable by the Botswana company in respect of the profits out of which the dividend is paid.

Paragraphs (3), (4) and (5) give details of the circumstances in which "matching" credit will be allowed against UK tax for tax spared in accordance with development approval orders made under Section 52 or tax agreements made under Section 54 of the Income Tax Act of Botswana.

Paragraph (6) provides that, for the purposes of paragraphs (1) and (2), profits, income and capital gains owned by a resident of one country which may be taxed in the other country under the terms of the Convention, will be deemed to arise from sources in that other country.

ARTICLE 24 - LIMITATION OF RELIEF

Where tax on any income or gains is determined in one country by reference only to the amount actually remitted to or received in that country, relief given in the other country under the Convention will be restricted to that part of the income or gains that is taxed in the first-mentioned country.

ARTICLE 25 - NON-DISCRIMINATION

Subject to certain conditions, this Article provides that neither country shall impose discriminatory taxes (or requirements) on the nationals, permanent establishments and enterprises of the other. The Article only applies to the taxes that are the subject of the Convention.

ARTICLE 26 - MUTUAL AGREEMENT PROCEDURE

This Article permits a resident of one country who feels that the actions of one or both countries result, or will result, in taxation that is not in accordance with the terms of the Convention to present his case to the competent authority of the country of which he is a resident. If the case comes under paragraph (1) of Article 25, he may present his case to the competent authority of the country of which he is a national. It also provides that the competent authorities of the two countries may endeavour to resolve difficulties or doubts arising in the interpretation or application of the Convention.

ARTICLE 27 - EXCHANGE OF INFORMATION

This Article provides for the exchange of certain information between the competent authorities of the two countries. It confirms who such information may be disclosed to and for what purpose. Neither country is obliged to exchange information that would disclose any trade, business, industrial, commercial or professional secret or trade process or information the disclosure of which would be contrary to public policy.

ARTICLE 28 – MEMBERS OF DIPLOMATIC OR PERMANENT MISSIONS AND CONSULAR POSTS

This Article confirms that the provisions of the Convention are not to affect the tax privileges that diplomatic and consular officials are entitled to under international law or under the provisions of special agreements (such as the Vienna Convention on Diplomatic Relations).

ARTICLE 29 - ENTRY INTO FORCE

Paragraph (1) provides that both countries will notify each other through diplomatic channels of the completion of the relevant legislative procedures. The Convention will enter into force upon the date of the later of the notifications. It will take effect in Botswana in respect of income tax and capital gains tax on taxable income and gains derived on or after 1 July in the year next following that of entry into force. It will take effect in the United Kingdom in respect of income tax and capital gains tax for any year of assessment beginning on or after 6 April in the calendar year next following that of entry into force and in respect of corporation tax for any financial year beginning on or after 1 April in the calendar year next following that of entry into force.

Paragraph (2) provides that the United Kingdom/Botswana Double Taxation Convention signed in 1977 will be terminated on the entry into force of this Convention.

ARTICLE 30 – TERMINATION

This Article provides that the Convention may be terminated, subject to a minimum life of 5 years, by either country giving notice of termination through diplomatic channels at least six months before the end of a calendar year. The Article also details the dates from which such a termination will be effective.

EXCHANGE OF NOTES

The Exchange of Notes contained in Part 2 to the Schedule constitutes a formal agreement between the Governments of both countries. The Exchange clarifies the intended interpretation of Article 21 of the Convention. It also records the intention of the two Governments to consider further negotiations to amend the terms of the Convention should the Botswana Income Tax Act 1999 be amended in the way described at a future date.