EXPLANATORY MEMORANDUM

THE DOUBLE TAXATION RELIEF AND INTERNATIONAL TAX ENFORCEMENT (TAXES ON INCOME AND CAPITAL) (ISLE OF MAN) ORDER 2008

2008 No. [DRAFT]

1. This explanatory memorandum has been prepared by the Commissioners for Her Majesty's Revenue and Customs (HMRC) 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 gives domestic legislative effect to an amending Arrangement to the 1955 Arrangement between the Governments of the UK and IOM relating to the avoidance of double taxation and the prevention of fiscal evasion with respect to taxes on income; and to a Tax Information Exchange Agreement between the two Governments, both set out in the Schedule to the draft Order and summarised in the attached Annex.

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

3.1 Type of resolution

The draft Order is subject to the affirmative resolution procedure.

3.2 Details of the Agreement

Further details of the Agreement and Arrangement scheduled to the draft Order are annexed to this memorandum.

4. Legislative Background

4.1 General

The Order is made under section 788(1) of the Income and Corporation Taxes Act ("ICTA")1988 (c. 1) and section 173(1) of the Finance Act ("FA") 2006 (c. 25). Section 788 was amended by section 88(1) of the Finance Act 2002 (c. 23) and extended by section 277 of the Taxation of Chargeable Gains Act 1992 (c. 12).

Section 788 of ICTA 1988 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.

Section 173 of FA 2006 provides the mechanism by which arrangements may include provisions about, among other things, the exchange of information foreseeably relevant to the administration, enforcement or recovery of any tax or duty.

The relevant arrangements are scheduled to the Order. They are thus given domestic legislative effect.

In accordance with section 788(10) of ICTA 1988 and section 173(7) of FA 2006, a draft of this Order is required to be laid before and approved by a resolution of the House of Commons prior to submission to Her Majesty in Council. Section 788(10) of ICTA was substituted by section 176 of FA 2006.

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 Financial Secretary, Stephen Timms, has made the following statement regarding Human Rights:

In my view the provisions of the draft Double Taxation Relief and International Enforcement (Taxes on Income and Capital) (Isle of Man) Order 2008 are compatible with the Convention rights.

7. Policy background

7.1 Tax Information Exchange Agreements facilitate the exchange of information between tax authorities for direct tax purposes. They assist Her Majesty's Revenue and Customs (HMRC) to carry out tax compliance activities by allowing them to receive information from and disclose information to other countries or territories which helps to ensure that taxpayers pay the right amount of tax at the right time in the right country or territory. Tax Information Exchange Agreements include safeguards to ensure that the information exchanged remains confidential and is used for tax purposes only. The UK and the Isle of Man are committed to the elimination of harmful tax practices and this includes a commitment to the effective exchange of information on tax matters.

7.2 Double Taxation arrangements aim to eliminate the double taxation of income or gains arising in one country and paid to residents of another country. They do this by dividing the taxing rights that each treaty partner has under its domestic law over the same income and gains. More generally, such arrangements benefit the taxpayer by ensuring certainty of treatment and, as far as possible, by reducing compliance burdens. They also encourage and maintain international consensus on the appropriate tax treatment of cross-border economic activity and thus promote international trade and investment.

7.3 The competent authorities of the UK and the Isle of Man have also concluded a Memorandum of Understanding (MoU) concerning the liability for costs of obtaining and providing information under the Tax Information Exchange Agreement. The text of the MoU is included in the attached Annex.

8. Impact

8.1 On business, charities, etc.

There is no significant Regulatory Impact on businesses, charities, voluntary bodies or individuals arising from this Agreement. Taxpayers may have to make a claim to HMRC or the Isle of Man taxation authority in order to benefit from the Double Taxation Arrangement. However, taxpayers will benefit from reduced compliance burdens and, in many cases, from having to deal with just one authority. There is no impact on the UK public sector.

8.2 On the Exchequer

Tax Information Exchange Agreements enable countries to obtain information to assist them to properly enforce their domestic tax laws. Such Agreements do not have an exchequer cost; rather, they improve HMRC's ability to assess and collect the correct amount of tax owed by UK taxpayers and should therefore lead to an increase in revenue.

The exchequer effects of the amendment to the Double Taxation Arrangement are estimated to be negligible. Under such an Arrangement one or both of the territories 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, by encouraging cross-border economic activity such an Arrangement 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

Jeff Worrell at HM Revenue and Customs, Tel: 020 7147 2723 or e-mail: jeff.worrell@hmrc.gsi.gov.uk can answer any queries regarding the instrument.

ANNEX

TAX INFORMATION EXCHANGE AGREEMENT

GENERAL

Part 2 of the Schedule to the draft Order contains the text of a comprehensive Tax Information Exchange Agreement (TIEA) between the UK and the Isle of Man. This is the second such TIEA to be signed by the UK; in December 2007 the UK concluded a TIEA with the Overseas Territory of Bermuda. The Isle of Man already has TIEAs in force with the United States and the Netherlands and has signed TIEAs with Denmark, the Faroe Islands, Finland, Greenland, Iceland, Norway, Sweden and the Republic of Ireland. The Agreement, which broadly follows the OECD Model Agreement on Exchange of Information on Tax Matters, extends the current scope of information exchange between the territories provided for under the UK's Double Taxation Arrangement with the Isle of Man. Notably it allows the UK, for the first time and in particular cases, to obtain banking and other third party information held by persons within the jurisdiction of the Isle of Man. The Agreement will enter into force once both the UK and the Isle of Man have completed the domestic legislative procedures necessary to give it effect.

NOTES ON DETAILS OF THE AGREEMENT

ARTICLE 1 – OBJECT AND SCOPE OF THE AGREEMENT

This Article states that the competent authorities of the UK and the Isle of Man ("the Territories") will provide assistance through the exchange of information relevant to administering or enforcing the domestic laws of the Territories in respect of the taxes covered by this Agreement.

ARTICLE 2 – JURISDICTION

This Article limits the obligation on a Territory to provide information held by its authorities or in the possession or power of persons within its territorial jurisdiction.

ARTICLE 3 – TAXES COVERED

This Article stipulates the taxes covered by the Agreement currently imposed by the UK and the Isle of Man. It further states that the Agreement will also apply to any identical or substantially similar taxes imposed after the date of its signature. The competent authorities of the Territories will notify each other of any major changes to their domestic taxation and related information gathering laws.

ARTICLE 4 – DEFINITIONS

This Article defines the terms used in the Agreement.

Paragraph 1 lists the definitions alphabetically.

Paragraph 2 states that any term not defined in the Agreement will be construed by a Territory in accordance with its domestic law.

ARTICLE 5 – EXCHANGE OF INFORMATION UPON REQUEST

This Article describes the specific elements, constraints and requirements for the effective exchange of information between the Territories.

Paragraph 1 provides that that the competent authority of the requested Territory will provide, upon request, information irrespective of whether conduct being investigated would constitute a crime under the laws of the requested Territory.

Paragraph 2 provides that if the competent authority in the requested Territory does not already hold the information requested, it will use all relevant information gathering powers to obtain the information regardless of whether it requires that information for its own tax purposes.

Paragraph 3 states that information may be provided in the form of depositions of witnesses and authenticated copies of original records to the extent this is permitted under its domestic laws.

Paragraph 4 provides that each Territory must ensure that its competent authority has the authority to obtain and provide information held by banks, other financial institutions or by any person (including a nominee or trustee) acting in an agency or fiduciary capacity and information on the ownership of companies, partnerships, etc.

Paragraph 5 provides that requests for information should give specific details such as the identity of the person, the nature of the information and the purpose for which it is sought, etc.

Paragraph 6 provides that the competent authority of the requested Party shall acknowledge receipt of the request to the competent authority of the requesting Party and advise if there are any unexpected delays.

ARTICLE 6 – TAX EXAMINATIONS ABROAD

This Article provides that officials from one Territory may, under certain conditions, visit the other Territory to pursue tax investigations.

Paragraph 1 provides that representatives from one Territory may enter the other to interview individuals and examine records.

Paragraph 2 provides that representatives from one Territory may attend tax examinations undertaken by the authorities in the other.

Paragraph 3 prescribes the procedures applicable to examinations referred to in paragraph 2.

ARTICLE 7 – POSSIBILITY OF DECLINING A REQUEST

This Article describes various circumstances in which the competent authority of the requested Territory may (and may not) decline a request for information.

Paragraph 1 provides that a Territory may decline to assist where the request is not valid (e.g. is outside the scope of the Agreement or does not conform to the requirements of Article 5), on public policy grounds, or where the requesting Territory's domestic laws would prevent it obtaining the same information from a person within its jurisdiction.

Paragraph 2 additionally states that a Territory is not obliged to supply information that would disclose trade, industrial or commercial secrets.

Paragraph 3 states that a Territory is not obliged to obtain or provide, in certain circumstances, information that is subject to legal privilege.

Paragraph 4 states that a request for information may not be refused simply because a tax claim to which it relates is disputed by the taxpayer.

ARTICLE 8 – CONFIDENTIALITY

This Article provides that any information received by a Territory under this Agreement will be treated as confidential, indicates to whom the information may be disclosed (broadly, only persons concerned with the assessment or enforcement of tax) and describes the conditions attached to any wider disclosure.

ARTICLE 9 – COSTS

This Article provides that the incidence of any costs incurred in providing assistance will be agreed by the Territories' competent authorities. A Memorandum of Understanding between the competent authorities of the UK and the Isle of Man, signed on 9th October 2008 (text reproduced below), provides details of the initial cost-sharing arrangements.

ARTICLE 10 – IMPLEMENTATION LEGISLATION

This Article states that the Parties shall enact any legislation necessary to comply with, and give effect to, the terms of the Agreement.

ARTICLE 11 – MUTUAL AGREEMENT PROCEDURE

This Article states that the Territories' competent authorities will jointly endeavour to resolve any difficulties in interpreting or applying this Agreement and to this end may mutually determine the procedures to be used and communicate with each other directly.

ARTICLE 12 – ENTRY INTO FORCE

This Article provides for mutual notification by the Territories of completion of the procedures required for the bringing this Agreement into force and stipulates the date of its entry into force and coming into effect as the date of the later notification.

ARTICLE 13 – TERMINATION

This Article provides for termination of the Agreement by either Territory and stipulates the date termination becomes effective and the conditions attached to it.

Text of the Understanding reached between HMRC and the Isle of Man taxation authority, pursuant to Article 9 of the TIEA and signed on 9th October 2008:

MEMORANDUM OF UNDERSTANDING
between
THE COMPETENT AUTHORITY OF THE UNITED KINGDOM
and
THE COMPETENT AUTHORITY OF THE ISLE OF MAN

concerning the liability for costs of obtaining and providing information in response to a request under the Agreement between the Government of the United Kingdom and the Government of the Isle of Man for the exchange of information relating to tax matters.

The Competent Authorities of the United Kingdom and the Isle of Man, desiring to facilitate the exchange of information relating to tax matters, have reached the following understanding in relation to the costs of obtaining and providing information in response to a request:

1. Pursuant to Article 9 of the Agreement, it is mutually agreed that ordinary costs in providing assistance shall be borne by the requested Party. Such ordinary costs would normally include the costs of international communication and any minor external costs.

2. All other reasonable costs that are not ordinary are considered extraordinary costs and will be borne by the requesting Party. Examples of extraordinary costs include, but are not limited to, the following:

   (a) fees charged by third parties for carrying out research;
   (b) fees charged by third parties for copying documents;
   (c) costs of engaging experts, interpreters or translators;
   (d) costs of conveying documents to the requesting Party;
   (e) litigation costs of the requested Party in relation to a specific request for information, including costs of engaging external counsel and advisers in connection with litigation, and;
   (f) costs for obtaining depositions or testimony.

3. The Competent Authorities will consult each other in advance if the costs of providing information with respect to a specific request are expected to be extraordinary.

ARRANGEMENT FOR THE AVOIDANCE OF DOUBLE TAXATION

Part 3 of the Schedule to the draft Order contains an Arrangement amending the 1955 Double Taxation Arrangement, which notably adds a new provision on the taxation of pensions and a mutual agreement procedure.

NOTES ON DETAILS OF THE ARRANGEMENT

Paragraph 1 makes clear that the term "1955 Arrangement" means that Arrangement as previously amended.

Paragraph 2 provides a new definition of the term "taxation authority" in both the United Kingdom and the Isle of Man for the purposes of the 1955 Arrangement and **Paragraph 6** deletes the existing definition.

Paragraph 3 amends the provisions of the 1955 Arrangement relating to associated enterprises. This provision governs the evaluation for tax purposes of transfers of goods, services, finance and intangible property between associated enterprises. It requires such transfers to be evaluated as if they had taken place between independent enterprises. The existing associated enterprises provision in the 1955 Arrangement is deleted and replaced with the latest OECD Model Tax Convention wording. The effect of the change is that where such an adjustment is made to the profits of an enterprise by one territory, the other territory will make an appropriate adjustment to the amount of tax charged on those profits, in order to relieve any double taxation which might otherwise arise.

Paragraph 4 adds a new provision to the 1955 Arrangement stating that pensions and similar remuneration (with the exception of government service pensions) paid to someone who is a resident of one of the territories shall be taxable only in that territory.

Paragraph 5 adds a new provision to the 1955 Arrangement that authorises the competent authorities of the two countries to endeavour to resolve, by mutual agreement, cases of taxation not in accordance with the Arrangement and to settle points of doubt or difficulty in the application or interpretation of the Arrangement. In particular:

Sub-paragraph (1) provides that, where a person considers that the actions of one or both territories will result in taxation not in accordance with the Arrangement, he may present a case to the competent authority of the country of which he is a resident. This right applies irrespective of any remedies provided by domestic law. The paragraph also sets out time limits for the presentation of a case.

Sub-paragraph (2) requires the competent authority to which the case is presented to endeavour, if it considers the objection justified and if it is unable to deal with the matter unilaterally, to resolve the case by mutual agreement with the competent authority of the other country.

Sub-paragraph (3) provides that the competent authorities shall endeavour to resolve by mutual agreement any difficulties or doubts arising over the interpretation or application of

the Arrangement. They may consult also on cases not provided for in this Arrangement, for the purposes of eliminating double taxation.

Sub-paragraph (4) permits the competent authorities to communicate directly with one another for the purposes of reaching agreement under this Paragraph.

Paragraph 7 concerns to the completion of procedures required by law for entry into force of the Arrangement and the effective dates thereof in respect of income tax and corporation tax in the UK and of income tax in the Isle of Man.