
PRACTICE NOTE

PN 102/04

Date: 31 March 2004

INCOME TAX (AMENDMENT) BILL 2004

Introduction

This Practice Note seeks to give detailed information regarding the proposals within the Income Tax (Amendment) Bill 2004, which has now received its third reading in the House of Keys. The Bill is arranged in five parts as follows:-

- PART 1 - Basis of Assessment and supplementary provisions
- PART 2 - Tax Returns and Civil Penalties
- PART 3 - Documents and Information
- PART 4 - Differential Tax Rates: Anti-avoidance
- PART 5 - Miscellaneous and General

This Practice Note follows that sequence for ease of reference, however detailed examples of the provisions of parts 1 and 2 covering the move to a current year basis of assessment are to be set out in a separate public guide which will be available shortly.

Consultation

This practice Note sets out proposals regarding the application of the legislation which may be subject to change. Three provisions in particular will be the subject of detailed guidance notes when the final format of the legislation is known. They are –

- The anti-avoidance legislation dealing with loans to participators;
- The powers to obtain information and
- The accounts basis of assessment for a trade.

Your comments are invited regarding the operational guidance of these subjects or any other matter within the Bill. It would be helpful if they could be submitted to Richard Carter at the address above by 13th April.

General

An important new term of non-corporate taxpayer, which is defined in the Bill, is used for the clients to whom the new basis of assessment and the other changes apply.

PART 1 - Basis of Assessment and supplementary provisions

This part changes the basis of assessment from a previous year basis to a current year basis which will achieve a major simplification. It also makes the necessary changes to the Income Tax Act in relation to non-corporate clients, therefore removing the need for adjustments to assessment in relation to commencement or cessation of a source, where income falls in the opening years or on a major change in personal circumstance. The transition will be achieved by applying a deemed cessation to all those sources of income which are presently assessed on a preceding year basis.

The payment date for Income tax for non-corporate taxpayers is changed to 6th January following the year of assessment and a system of payment on account which will be due on 6th January during the year of assessment is proposed. The payment on account will be based on the previous year's assessed liability, less any ITIP or sub-contractor deduction credited.

Importantly, where a client's circumstances have changed and they feel that the payment on account requested does not accurately reflect the tax they are likely to have to pay, they may request an amount to be held over. There are, in order to protect the revenue, proposed interest provisions which will apply where their actual liability transpires to be higher than their estimate.

Changes are also proposed to the repayment supplement provisions which will ensure that supplement is payable from an earlier date for all non-corporate taxpayers. For these purposes, income tax deducted at source, e.g. ITIP deducted, will be treated as though it were paid on 6th January during the assessment year.

The proposed change to the interest provisions within section 111A of the Income Tax Act 1970 includes a change to a relevant date, which will be the payment on account date or the date on which tax becomes due and payable. There is also a provision for a higher rate of interest to be called the surcharge rate, which will apply where a non-corporate taxpayer fails to make and deliver a return by the 5th April following the year to which it relates.

PART 2 -Tax Returns and Civil Penalties

It is proposed to extend the due date for submission of income tax return forms to 6th October, except where a notice is served, e.g. on cessation of residence, when the time limit will be changed from 21 days to 6 months.

The intention is, after a period of publicity and education, to reinforce the due dates with an automated penalty. The Division recognises that this may cause difficulties for practitioners, particularly when dealing with other jurisdictions or trading concerns. It is therefore proposed that the Division will participate in discussions to agree a system of provisional assessment request, thus preventing a penalty being levied. Broadly, this may work in a similar manner to the provisional assessment request system in operation prior to 1999; this would allow the return form and accounts where relevant to be submitted at a later date.

It is also proposed to increase the Assessor's powers to allow him to issue a notice to require a person to prepare and deliver accounts. The powers would only be used in exceptional cases and not exercised without the authority of the Assessor or a Deputy Assessor. The powers extend to allow the notice to require the accounts to be certified or audited by a suitably qualified person. The cost of this preparation will be born by the Treasury where the amount does not differ significantly from the original figure declared.

PART 3 - Documents and Information

The Bill proposes to insert new sections 105C to 105O into the 1970 Act. The effect of the sections will be to strengthen the Assessor's powers to call for documents, particulars and evidence of or in relation to any taxpayer, in relation to any liability to income tax, the amount of such liability or information relevant to the person's residence status.

The powers are necessary primarily to ensure that the Island is able to comply with its international obligations on exchange of information, such as Tax Information Exchange Agreements.

The powers within Schedule 2 105D may only be used where the Assessor has reasonable grounds for believing that the taxpayer may have failed or may fail to comply with any provision of the Income Tax Acts and that such a failure is likely to have led or to lead to serious prejudice to the proper assessment or collection of tax. Schedule 2 105F contains provisions which have particular regard to the information held by auditors and tax advisers and does not oblige such a person to deliver or make available particular documentation in certain circumstances.

There are also provisions for the High Court to make an order requiring the production of information where the Assessor gives information on oath that a notice to deliver documents or information has not been complied with or there are reasonable grounds for suspecting that the notice will not be complied with.

Where the Assessor provides information on oath that there are reasonable grounds for suspecting an offence involving fraud has been or is about to be committed, a Deemster may issue a warrant allowing the Assessor to enter and search the premises, and persons found on the premises where he has reasonable grounds for believing the person to be in possession of the information.

The powers to search will be used sparingly and only in the most serious cases. Unlike other enforcement agencies where search warrants may be subject to application to a Justice of the Peace or the Deputy or High Bailiff, as an additional safeguard, applications for a search warrant by the Income Tax Division must be to a Deemster. The execution of warrants will always be in conjunction with officers from the Isle of Man Constabulary. Further internal safeguards will also be put in place, for example any application for a warrant will be made by the Deputy Assessor Compliance who will also be directly responsible for its execution.

PART 4 - Differential Tax Rates: Anti-avoidance

The proposed move to a zero rate of tax for companies requires the introduction of certain anti-avoidance measures to deter the extraction of profits from companies by participators which result in the avoidance of tax or the reduction in liabilities.

It is proposed to levy a tax charge on the company which makes a loan or advance to an individual who is liable to income tax in the Isle of Man and who is a participator, an associate of a participator, an officer of the company or an associate of an officer. The charge will be assessed on the company in the year in which the loan or advance is made and will be charged at the higher rate prevailing at that time.

The provisions will not apply to a Director or employee of the company or an associate company, who works full time and does not have a material interest in the company or an associated company.

There are provisions where a loan is made through an intermediary, or a loan is waived or written off and there are also new reporting requirements on the company in relation to certain transactions regarding loans.

PART 5 - Miscellaneous and General

Personal Allowances to Non-residents

It is proposed to insert a new section 35B to the 1970 Act which will entitle a non-resident to a personal allowance. In order to claim the maximum allowance a return of world income will be required. The individual will then be entitled to a proportion of the single person's allowance (but not less than £2000) based on the ratio of their Manx source income to their total world income. Where a non-resident does not submit a return of their total world income they will be entitled to the fixed deduction of £2000. The computation for this purpose will exclude any source which is exempt from income tax in the Isle of Man.

Temporary Taxation Orders

Clause 13 of the Bill proposes a change to Section 15 of Income Tax Act 1995 to allow the temporary taxation order provisions to be extended to accommodate urgent requirements regarding international agreements.

Taxation of Mariners

Clause 14 proposes that the mariners exemption is changed to ensure that the specific deductions relating to the remuneration and the single persons allowance are both set off against the remuneration first.

Enactment

The Bill contains a number of proposals, which form only one part of the phased introduction of the modified Taxation Strategy which has been agreed by Tynwald.

When the Bill has completed its legislative passage a number of the provisions will require an appointed day order to enact the legislation. After a period of consultation, the relevant guidelines will be published and once they have been in operation for a period of 12 months, consideration will be given to whether any of the guidelines should have a more statutory form and be incorporated into primary or subordinate legislation.

I Q Kelly

Assessor of Income Tax

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

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