



PROPOSALS FOR THE

MANX TAXATION STRATEGY

FOR THE PERIOD

2007 – 2012

TABLE OF CONTENTS

- 1. INTRODUCTION 3**
- 2. BACKGROUND 3**
 - 2.1 The 2000 Taxation Strategy 3
 - 2.2 The 2002 modified strategy..... 3
 - 2.3 Implementation to date 4
- 3. THE FUTURE OF THE TAXATION STRATEGY..... 4**
- 4. PROPOSED STRATEGY DEVELOPMENTS 5**
 - 4.1 Simplification of the income tax system..... 5
 - 4.2 Individuals 6
 - 4.3 International reputation 6
 - 4.4 Economic growth..... 6
 - 4.5 Improving tax compliance 7
- 5. FURTHER WORK 7**

1. Introduction

In his March 2007 Budget the Treasury Minister asked the Assessor to prepare a revised taxation strategy. The proposals presented here are principally an evolution of the aims of previous versions of the strategy, based on the over-riding objectives of:

1. continuing to simplify the Island's income tax system;
2. focusing on individual taxation and encouraging savings and investment through products provided on the Island;
3. continuing to build the Isle of Man's international reputation;
4. encouraging economic growth; and
5. improving tax compliance on the Island.

The Treasury and the Assessor would welcome comments on the proposals outlined in section 4 and suggestions that might further support the objectives listed above.

2. Background

The Isle of Man's taxation policies have played an important part in our economic success.

In 2000, Tynwald approved the Treasury's taxation strategy. The strategy was subsequently modified in 2002 to meet the twin challenges of the European Union's Code of Conduct for Business Taxation and its Directive on the Taxation of Savings Income (commonly known as the "EUSD") and it has continued to evolve in subsequent years. The legislative programme delivering the modified strategy has been completed.

2.1 The 2000 Taxation Strategy

The 2000 Taxation Strategy was based on the principles of acceptability, simplicity, competitiveness, high return and sustainability. Its components were:

For companies

- i) a reduction in the rate of income tax to 10% for trading companies and 15% for others;
- ii) simplification of the corporate tax system; and
- iii) addressing international concerns about aspects of our tax-exempt business system.

For individuals

- i) a reduction in the standard rate and higher rates of income tax;
- ii) simplification of the income tax system for individuals; and
- iii) measures to ensure fairness and equality.

It was intended that the above proposals would be phased in over a five year period.

2.2 The 2002 modified strategy

In 2002, the Taxation Strategy was modified but the objective of equipping the Island for the future in the best way possible remained. As stated by the Treasury at the time, "A taxation

strategy is a living document. In this global environment it has to be constantly reviewed to ensure it remains in step with the economic changes taking place both domestically and internationally."

The 2002 modifications were the introduction of the "0/10" system of corporate tax and a commitment to bring in measures equivalent to the EUSD in the Isle of Man.

2.3 Implementation to date

Five income tax acts have been passed in the seven years since the adoption of the 2000 Taxation Strategy, namely:

- Income Tax Act 2001
- Income Tax Act 2003
- Income Tax (Amendment) Act 2004
- Income Tax (Amendment) Act 2006
- Income Tax (Corporate Taxpayers) Act 2006.

Each act contributed to the delivery of the Taxation Strategy. Only three objectives have not been completed:

1. The standard rate of income tax for individuals was cut to 10%; although the aim of cutting the higher rate to 15% has not been achieved and it remains at 18%.
2. The strategy stated that, "*Deductions from income will be simplified to leave only those which either secure the elements that are essential to quality of life or encourage personal enterprise such as housing costs, child care costs and business start ups.*" The system of tax relief for individuals that we have today is as complex, and maybe more so, than it was in 2000. Public consultation in 2006 indicated little enthusiasm for simply abolishing tax reliefs.
3. The strategy also stated, "*...there is to be encouragement for self reliance through pensions and savings initiatives.*" This aim is still 'work in progress' and a taxation of pensions bill, which will be introduced in the House of Keys shortly, will bring in significant changes in April 2008.

3. The Future of the Taxation Strategy

The key principles of fiscal sovereignty, economic stability and adherence to international standards which underpinned the original Taxation Strategy remain just as relevant today, as does the need to ensure that the Isle of Man's income tax system is competitive, simple, sustainable and fair.

In preparing the 2000 Taxation Strategy, assumptions were made about the future. In preparing this document, we made the following assumptions:

- i) that the Island wishes to remain a competitive financial services centre with a diversified economy;
- ii) that the Isle of Man will continue to encourage wealthy individuals and business entrepreneurs to move here and manage their personal and business affairs from the Island;

- iii) that income tax continues to need to be considered in the wider context of the statutory requirement to budget for a surplus of income over expenditure.

4. Proposed Strategy Developments

4.1 Simplification of the income tax system

Simplification has been an aim of the Taxation Strategy since 2000 and it is proposed that this theme should continue; the Isle of Man's income tax system should be simple, easy to comply with and straightforward to administer.

A number of changes could further simplify our system.

- Simplify capital allowances - Our system of giving tax relief to businesses when they acquire certain types of asset such as machinery is based on capital allowances and not on the amount that would normally appear in their accounts, which is known as depreciation. In a global context, capital allowances are not the norm; in our local context they add complexity by obliging businesses to carry out additional calculations after their accounts have been prepared (the "tax computation"). The Assessor should work closely with the private sector to design an up to date replacement for the capital allowances regime.
- Simplified tax regime for small unincorporated businesses - The Island has approximately 7,900 self-employed individuals, with over 6,000 having taxable profits of £20,000 each year, or less. We should make the tax system simpler for these businesses.
- Consolidation of tax law - Manx income tax legislation should be reviewed and consolidated because at present our law is spread over a number of different Acts of Tynwald. This situation creates inefficiency and uncertainty for taxpayers, their advisers and the Assessor alike.
- Simplification or removal of the annual tax return cycle for individuals - Employed individuals have tax deducted from their pay via the ITIP regime. The Assessor is, therefore, in many cases aware of an individual's income from employment before the individual submits his or her tax return. If tax assessments could be pre-populated with this information, an individual's tax return may not need it to be included. Similarly, changes could be made to enable the income tax system to pre-populate assessments with information from local banks, e.g. mortgage interest payments and deposit interest receipts. This may enable many employed clients whose income tax affairs are straightforward to be assessed without any requirement to complete an annual income tax return.
- Simplification of some aspects of tax relief for individuals - Certain aspects of our tax relief system are complicated both for taxpayers and for the Income Tax Division and although those people currently benefiting from them may not wish to see changes, we ought to consider their impact on the tax system as a whole. Replacement of some forms of tax deduction could lead to lower tax rates or higher personal allowances and would make it easier to introduce a 'no tax return' system. For example:
 - life insurance tax relief is subject to complex rules;
 - private medical insurance tax relief is, again, subject to complex rules;

- where maintenance is paid, our system produces a tax-neutral position, in that the payer gets tax relief for maintenance payments and the recipient is taxed on that maintenance, but complicated checks have to be carried out before the relief is granted - we could consider removing the relief for maintenance paid and exempting maintenance received from tax;
- mariners' exemption involves a complex calculation.
- Deliver more services online - We should bring in more online tax services to give people and businesses customer-friendly and efficient options when dealing with the Income Tax Division.
- Banking business - At present, banks on the Island are taxed at 10% on income arising from the reinvestment or utilisation of client deposits, and at 0% on other income. The complex nature of the banks' businesses and structures makes determining exactly what income is taxed at what rate difficult and time consuming. We should introduce further changes to reduce the compliance burden on banks and to maintain their competitiveness.

4.2 Individuals

The following initiatives should be considered to encourage Manx resident individuals and those moving to the Island to hold their wealth here:

- clarifying the taxation of investment and insurance products;
- providing incentives for investing in locally-provided savings products e.g. a Manx Individual Savings Account with tax exemption on interest to a certain level; and
- providing up to date guidance on the taxation of share option schemes.

4.3 International reputation

The Isle of Man is part of the global economy and to maintain its position it must continue to build its international reputation. Having regulatory and other standards that conform to modern international benchmarks benefits our economy. The Taxation Strategy can help to build our international reputation by committing us to:

- ensure that our tax system complies with international standards;
- expand our network of international taxation agreements; and
- operate our existing network of international taxation agreements effectively.

4.4 Economic growth

The Taxation Strategy should continue to focus on economic growth by:

- encouraging new business and economic sectors to set up operations in the Isle of Man;
- making it attractive for business to retain profits for growth and re-investment on the Island;
- encouraging local production and supply; and
- providing income tax incentives to Manx graduates that will encourage them to return to the Island to work.

4.5 Improving tax compliance

Our income tax system must not only be competitive, simple and sustainable, it must also be fair and everybody should pay the correct amount of tax at the correct time.

Simplification of the system should reduce the occurrence of errors and mistakes. The Assessor will continue to assist those people and businesses that make genuine mistakes. However, the Assessor should rigorously pursue those who, through evasion or neglect, fail to declare income and pay their tax liabilities and should use the courts to seek appropriate sanctions in the most serious cases.

5. Further Work

The Treasury and the Assessor would be happy to hear from any person who has ideas that might further support the principles outlined in this document. If you have any suggestions or queries, please contact:

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