

**EXPLANATORY MEMORANDUM TO
THE DRAFT DOUBLE TAXATION RELIEF (TAXES ON INCOME)
(SWITZERLAND) ORDER 2007**

2007 No.

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 Protocol 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 Protocol

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

4. **Legislative Background**

- 4.1 General

The Protocol is scheduled to this draft Order, which is made under the powers contained in section 788(1) of Income and Corporation Taxes Act 1988 (c.1) (“ICTA 88”) as extended by section 277 of the Taxation of Chargeable Gains Act 1992 (c.12), and in section 173(1) of the Finance Act 2006 (c.25) (“FA 06”). It is thus given domestic legislative effect.

This draft Order is made under section 788(10) of ICTA 88 and section 173(7) of FA 06.

Section 788 of ICTA 88 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 06 provides the mechanism by which such arrangements may also include provisions about, among other things, the exchange of information

foreseeably relevant to the administration, enforcement or recovery of any tax or duty.

4.2 EU Legislation

This instrument does not implement EU legislation.

5. **Extent**

The draft Order applies to the whole of the United Kingdom.

6. **European Convention on Human Rights**

The Financial Secretary (Jane Kennedy) has made the following statement regarding Human Rights:

In my view the provisions of the draft Double Taxation Relief (Taxes on Income) (Switzerland) Order 2007 are compatible with the Convention rights.

7. **Policy background**

7.1 Double Taxation Conventions 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. 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.

7.2 The draft Order is intended to give effect, in accordance with the legislative powers, to a Protocol to the Double Taxation Convention that was concluded in 1978 between the Governments of the United Kingdom and Switzerland and amended by Protocols in 1982 and 1994.

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 Taxation Convention, one or both of the countries 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

Douglas Rankin at HM Revenue & Customs (Tel: 020 7147 2696 / Email: Douglas.Rankin@hmrc.gsi.gov.uk) can answer any queries regarding the instrument.

ANNEXE

NOTES ON DETAILS

ARTICLE I

Article 3 – General definitions

This Article adds a new sub-paragraph (1) to paragraph 1 of Article 3 of the Convention. The new sub-paragraph defines the term “conduit arrangement” as it is used in the Convention.

ARTICLE II

Article 4 – Residence

This Article deletes the existing paragraph 3 of Article 4 of the Convention and substitutes a replacement paragraph 3 which explains how the residence of dual resident persons other than individuals may be determined. In cases of doubt the competent authorities shall endeavour to determine the person’s place of effective management by mutual agreement.

Article III

Article 10 – Dividends

Paragraph A deletes paragraphs 1 to 3 of Article 10 and replaces them with new paragraphs 1 and 2.

New Paragraph 1 provides that the dividends paid by a company resident in one State to a resident of the other State may be taxed in that other State.

New Sub-paragraph 2(a) provides that such dividends shall be exempt from tax in the State of the company paying the dividend if the beneficial owner of the dividend is (i) a company resident in the other State controlling, directly or indirectly, at least 10 per cent of the capital of the company paying the dividends, or (ii) a pension scheme.

New Sub-paragraph 2(b) provides that, except for cases covered by sub-paragraph 2(a), the dividends may be taxed in the State in which the company paying them is resident and according to the laws of that State, but the tax rate shall not exceed 15 per cent of the gross amount of the dividends.

Paragraph B renumbers paragraphs 4 to 6 of the Article as paragraphs 3 to 5.

Paragraph C deletes the reference to paragraph 3 in the renumbered paragraph 4 (formerly paragraph 5).

Paragraph D provides that a new paragraph 6 shall be added to the Article to disapply this Article in respect of any dividend paid under, or as part of, a conduit arrangement.

Article IV

Article 11 – Interest

This Article introduces a new paragraph 7 to disapply this Article in respect of any interest paid under, or as part of, a conduit arrangement.

Article V

Article 12 – Royalties

Paragraph A replaces paragraph 2 of the convention with a new paragraph. The new paragraph defines the term “royalties” and the new definition does not include equipment leasing.

Paragraph B introduces a new paragraph 4 to disapply this Article in respect of any royalty paid under, or as part of, a conduit arrangement.

Article VI

Article 13 – Capital gains

This Article adds a paragraph 6 to the Article in the Convention which confirms the UK’s right to tax gains from the alienation of property arising to a person who is, or has been during the previous six fiscal years, a resident of the United Kingdom or who is a resident of the United Kingdom at any time during the fiscal year in which the property is alienated.

Article VII

Article 15 – Dependent personal services

This Article substitutes a new sub-paragraph (a) of paragraph 2 of Article 15 and explains that the fiscal year referred to is the fiscal year in the State in which the employment is exercised.

Article VIII

Article 18 – Pensions

This Article substitutes a new Article 18 in the Convention.

Paragraph 1 of the new Article provides that pensions and other similar remuneration paid to a resident of a Contracting State shall be taxable only in that State.

Paragraph 2 provides that, notwithstanding the provisions of paragraph 1, lump-sum payments from pension schemes shall be taxable only in the State in which the pension scheme is established.

Paragraph 3 provides that pension contributions to a pension scheme recognised for tax purposes in one State made by and on behalf of an individual working temporarily in the other State shall be treated in the same way as contributions made to a recognised pension scheme in the individual’s home State.

Paragraph 4 provides that paragraph 3 shall apply only under certain conditions.

Paragraph 5 defines the meaning of the term “pension scheme” as used in paragraphs 2 to 4 of this Article and explains what is meant by “recognised for tax purposes”.

Article IX

Article 21 – Other income

Paragraph A adds a new paragraph 3 to Article 21 of the Convention. The new paragraph is an anti-avoidance provision which provides that where, because of a special relationship between the payer and the recipient, the amount of the income referred to in paragraph 1 of the Article in the Convention exceeds the amount which the two parties would have agreed upon in the absence of that special relationship, the Article will apply only to the amount that would have been agreed upon by them in the absence of the special relationship. The “excess” part of the income shall remain taxable according to the laws of each State.

Paragraph B adds a new paragraph 4 to Article 21 of the Convention which provides that the provisions of this Article shall not apply if income covered by this Article of the Convention is paid under, or as part of, a conduit arrangement.

Article X

Article 22 – Elimination of double taxation

Paragraph A substitutes a new sub-paragraph (b) of paragraph 1 of Article 22 of the Convention. Where a United Kingdom company controls at least 10 per cent of the capital or voting power of a Swiss company from which a dividend is received the credit for United Kingdom tax purposes will take into account Swiss tax payable in respect of the profits out of which the dividend is paid.

Paragraph B substitutes a new paragraph 3 of Article 22 of the Convention which explains how Switzerland will give relief from Swiss tax when paragraph 2 of article 10 applies.

Article XI

Article 23 – Non-discrimination

This Article substitutes a new paragraph 4 of Article 23 to take account of additional provisions in previous articles.

Article XII

Article 25 – Exchange of information

This Article deletes existing Article 25 of the Convention and substitutes a replacement Article 25, which is closer to the standards recommended by the OECD. It provides new rules governing the exchange of certain information between the competent authorities of the two States. It requires the competent authorities to exchange information that is foreseeably relevant to the administration or enforcement of the provisions of the Convention or of the domestic laws of the two countries, insofar as the taxation is not contrary to the Convention. Each competent authority is to use its information gathering measures to obtain requested information even though it may not need the information for its own purposes, and may not decline a request solely because the information concerned is held by a bank or financial institution. No information containing trade, etc. secrets or information the disclosure of which would be contrary to public policy is to be exchanged.

Article XIII

Article 27 – Miscellaneous rules

Paragraph A deletes the words “or tax credit” in paragraph 8 of Article 27 of the Convention.

Paragraph B deletes paragraph 9 of Article 27 of the Convention.

Article XIV

This Article contains the provisions governing how and when the Protocol will enter into force and take effect.

Paragraph 1 provides that each State will notify the other of the completion of the necessary domestic legal procedures required to bring the Convention into force.

Paragraph 2 provides that the Protocol shall enter into force on the date of the later of the notifications

When the Protocol enters into force, the amendments in respect of the provisions relating to the exchange of information will have effect in both States from the date on which the Protocol enters into force. In the United Kingdom the other provisions will take effect from 1 April (for corporation tax purposes), and from 6 April (for income tax, capital gains tax and tax credit purposes) in the calendar year next following the date of entry into force. In Switzerland, the other provisions will take effect from 1 January following the date of entry into force.

EXCHANGE OF NOTES

The Exchange of Notes contained in Part II to the Schedule constitutes a formal agreement between the Governments of both countries, and clarifies the intended interpretation of the paragraphs of the Convention referred to in the Exchange of Notes.