

EXECUTIVE COUNCIL

CONFIDENTIAL

Title of Report: Introduction of a liability for Payment on Account of Tax (POAT) and Medical Services Tax (MST) in Schedule 6, Taxes Ordinance 1997

Paper No: 280/10

Date: 25 November 2010

Report of: Taxation Officer / Commissioner of Taxation

1.0 Purpose

To present to Honourable Members an amendment to the Taxes Ordinance 1997 to introduce a liability to POAT and MST in Schedule 6.

2.0 Recommendation

It is recommended that Honourable Members:

- a. introduce a liability for POAT and MST in Schedule 6 (Territorial Extension of Charge to Tax) of the Taxes Ordinance so that where the subcontractor does not pay POAT after all attempts have been made the licensee becomes liable – i.e. bring POAT in line with income tax and corporation tax in Schedule 6;
- b. do not seek to implement the additional liability in advance of the other legislative drafting priorities due to the workload of the AG's office. However, if it is possible to be implemented by 1 January 2011.

3.0 Summary of Financial Implication

None

4.0 Background

- 4.1 Schedule 6 underpins the offshore oil contractors tax regime. It is the right, in the last instance, to collect the unpaid assessed tax relating to non-residents, who have carried out offshore activities in the controlled waters of the Falkland Islands, from Falkland Islands licensees. This procedure removes some of the risk of non-payment by non-resident contractors who have no presence in the Islands. This is a particular problem encountered by other countries, with offshore oil and gas exploration and production, which have not introduced a similar provision.

- 4.2** Schedule 6 can only collect Income Tax (IT) and Corporation Tax (CT), not POAT. It is based on the UK's Part 7A TMA 1970 (previously Schedule 15 Finance Act 1973) which also does not include Pay as Your Earn (PAYE). But UK is not in the same position in that the majority of the workforce on the North Sea rigs are UK or EU nationals, and are employed by companies already with a taxable presence in the UK because of their mainland base operations. There was no need to have PAYE collected from the licensee as the overall tax risk was perceived to be smaller given that the workforce is largely local. In addition the UK now has Mutual Assistance agreements with other mainly EU countries tax authorities to collect unpaid tax/PAYE and it has a system of assessing unpaid PAYE on the employer – neither of which the Falkland Islands (FI) has. In the FI oil industry the workforce is totally overseas, there are no agreements to collect tax from other countries and consequently the tax risk for non collection of POAT is much greater.
- 4.3** It would be far simpler and more cost effective (for all concerned) to have something in place which puts the onus on the employer to pay the POAT and to have the licensee ultimately responsible if their subcontractor fails to pay the POAT. This cuts down on resource cost as it is obviously less time consuming to chase one employer rather than all his individual employees, and cuts down resource required by the licensee if he only needs to deal with a claim from us for POAT from one employer rather than income taxes from all the employees. In addition the wages cost in the Profit & Loss account of the subcontractor (where we have accounts) can be used to arrive at an estimate of the wages paid in the designated area overall, to arrive at a 21% POAT deduction.
- 4.4** I would like to emphasise that this is a last resort measure. Where the licensee is aware that they can be liable to subcontractor's tax they put safeguards in place to protect themselves and they are more likely to chase up the subcontractor to pay FITO. The fact that IT and CT can be collected from the licensee has not had a detrimental affect on those wishing to carry out exploration in the FI, and I do not believe this will either. It will be a managed risk for the licensee.
- 4.5** During the 1998 campaign the majority of the resource in tax compliance was spent chasing a minority of employees where the subcontractor had not paid the tax, and I remember that this was still ongoing in 2003.
- 5.0 Other issues**
- 5.1** Section 5 of Schedule 6 allows for Exemption Certificates be granted to the licensee where the Commissioner is satisfied that the applicant will comply with the obligations imposed on them by the Taxes Ordinance in respect of tax payable. Thus the onus is on the applicant to pay any tax payable not the licensee. The exemption does not apply for POAT.
- 5.2** The affect of this will need to be considered for Retirement Pension Contributions (RPCs), which is not within taxes legislation.

6.0 Proposed amendment

6.1 Schedule 6 Territorial Extension of Charge to Tax

It is proposed to insert in Schedule 6 a subsection 3(1)(c) to include a liability to POAT and MSL.

6.2 It is proposed to amend section 5 of Schedule 6 for Exemptions Certificates to allow POAT and MSL to be exempt on the condition that the applicant will pay the POAT and MSL due on all workers, including sub-contractors, and those supplied by an agency, personal services companies and managed service companies.

7.0 Financial Implications

7.1 Without this amendment there is potential loss of income tax revenue where sub-contractors of the licensee do not pay the POAT due.

7.2 Currently we have a dedicated oil person so that collection of POAT during this oil campaign (2010) has been very successful. However, we are still attempting to collect POAT of approximately £150,000 from 2006 to 2009 that has not been paid and for which we have no recourse to the licensee.

8.0 Legal Implications

The Taxes Ordinance will need to be amended to give legal effect to this change. It was not possible to include this in the Taxes (Amendment) Bill being submitted for Executive Council's approval under ExCo paper 278/10, so it will need to be included in a future Taxes (Amendment) Bill. Unless Executive Council decides otherwise, this will not be given special priority but will be done as soon as possible, to the extent that competing priorities allow.

9.0 Human Resources Implications

None