

FURTHER REVISION OF THE JULY 2007 MODERNISATION OF THE ARRANGEMENTS FOR THE SHARING OF COMMON DUTIES BETWEEN THE UK AND THE ISLE OF MAN

Introduction

1. The **1979 Agreement** between the Governments of the United Kingdom and the Isle of Man sets out the framework for UK/IOM relations in respect of customs and excise matters. The **1979 Isle of Man Act** gives effect to the Agreement and lays down the general basis for determining the Isle of Man's share of the common duties, including VAT.
2. The detailed revenue sharing arrangements, and formula and accounting procedures to be employed, are agreed between the two parties and formalised in a **HM Treasury Direction**.

Modernisation of UK/IOM Revenue Sharing Arrangements

3. In October 2009 the parties agreed a revised set of arrangements based on relative levels of national income, hereinafter called the 'Share of GNI Model'. The rest of this document is split into two areas: the first deals with the functioning of the Share of GNI Model; and the second with the in year payment methodologies and other issues where the intention is to enable appropriate funding flows between the two parties, avoiding the build up of significant over/under payments.

Description of the 'Share of GNI' model

4. With the 'Share of GNI' model revenues are shared on the basis of each jurisdiction's share of combined national income. Both jurisdictions' national incomes are calculated on the same basis to ensure fairness, consistency and equivalence. For the UK, national income is measured by Gross National Income (GNI) at current market prices (National Statistics identifier ABMX), adjusted to current basic prices (less taxes plus subsidies on products) (National Statistics identifier NQBU). For the IOM, national income is measured by Gross National Income (GNI) at current basic prices. Where data required by the model is not available, published real growth forecasts are used.

For UK growth the central point in the range of GDP forecasts published in the annual Financial Statement and Budget Report is used, and for IOM growth it is the national income forecast in the Central Planning Assumptions published on the Isle of Man Government web site.

Functioning of the 'Share of GNI' model

5. The 'Share of GNI' model operates as set out in steps 1 to 6 below. Steps 1 to 4 lead to the provisional IOM share for any given year. Steps 5 and 6 deal with adjustments to be made after the year end when actual/more up to date data is available.

Step 1: Obtain national income data

Obtain the latest published national income data for both the UK and IOM¹. Calculate focal year national income for both jurisdictions by applying the latest published growth forecasts.

Step 2: Calculate the IOM sharing fraction for the focal year

Divide the IOM's national income by the sum of both jurisdictions' national incomes to give the provisional IOM sharing fraction for the focal year.

Step 3: Apply the Provisional IOM Sharing Fraction to forecast VAT receipts

Apply the provisional IOM sharing fraction to the published forecast for UK VAT receipts² in the focal year to determine the provisional VAT revenue allocated to the IOM.

Step 4: Apply the Provisional IOM Sharing Fraction to forecasts of receipts from other common duties

Apply the provisional IOM sharing fraction to the published forecasts for UK receipts³ in the focal year from other common duties covered by the 1979 Agreement that are not shared on the basis of actual consumption (see paragraph 6) to determine the provisional duty revenue allocated to the IOM.

(Note – the sum of steps 3 and 4 give the provisional annual share of IOM joint revenues.)

Step 5: Annual adjustment to take account of certified joint revenues

Within three months of the end of the focal year (i.e. by 30 June) obtain certified joint VAT and all relevant shared common duty revenue figures.⁴ Apply the provisional IOM sharing fraction from the previous focal year to the difference between certified

¹ For the UK data for calendar years is converted to financial years by a simple $\frac{3}{4}$ plus $\frac{1}{4}$ conversion.

² IOM VAT receipts (for which there are no published forecasts) are included in Step 5

³ Pool Betting Duty and IOM other duty receipts (for which there are no published forecasts) are included in Step 5

⁴ The figures appear in the audited IOM Service Account and UK Trust Statement

revenues and the forecasts of revenues used in the Step 4 calculation for the previous focal year and make a single adjusting payment (see paragraph 8 Step 3). Prepare the IOM Account with the provisional sharing fraction applied to certified revenue.

Step 6: Annual adjustments to take account of the latest published national income data

Within three months of the end of the focal year (i.e. by 30 June) obtain published new and revised national income data. The provisional sharing fractions to the VAT and duty revenues allocated to the IOM will be adjusted accordingly. These revenue adjustments, which will be shown as 'previous year adjustments' in the IOM Account, are subject to a 5 year cap, so that, for example, no adjustment of the 2010/11 revenue allocation may be made in respect of changes to national income published after 31 March 2016 (see paragraph 10).

The Appendix contains an example, using illustrative data, of the Share of GNI model calculation.

Scope of the 'Share of GNI' model

6. The sharing fraction will be applied to the following common duties:
- VAT
 - Tobacco products duty
 - Beer end products duty
 - Spirits duty
 - Wine and made wine duty
 - Cider and Perry duty
 - Customs duty
 - Anti-dumping duty
 - Agricultural duties
 - Pool betting duty

Lottery duty and Hydrocarbon Oil duty will continue to be shared on the basis of actual consumption. Air Passenger Duty is outside the scope of the revenue sharing arrangements.

Transitional arrangements

7. To mitigate the fiscal impact of adjusting to the 'Share of GNI' model, the two parties agreed that in 2010/11, the IOM would receive a transitional payment of £50m. This transitional payment supersedes and replaces any previous transitional payment arrangements between the two parties.

In Year Revenue Transfers

8. To ensure that collected tax revenues are remitted to each jurisdiction's exchequer at the earliest practicable date, arrangements have been developed for making monthly in-year transfers. The arrangements will operate as follows.

Step 1 – Calculate net monthly transfers to or from the IOM before the start of the relevant year.

- i. Calculate the annual IOM share of common duties (Steps 3 and 4 in paragraph 5)
- ii. Deduct agreed forecast of IOM local collection of common duties for the year; and
- iii. Divide the result by 12 to determine the monthly transfers to the IOM (if the result is positive) or from the IOM to the UK (if the result is negative).

Monthly transfers will be paid by HMRC to the IOM or by IOM to HMRC on an agreed date⁵ each month in line with the calculation at iii).

Step 2 – Monitor level of actual common duties collected and make adjustments in-year on a quarterly basis.

- a. Compare on a monthly basis IOM profiled forecast of common duties (i.e. Step 1 ii) divided by 12) to actual common duties collected by IOM for that month;
- b. maintain cumulative record of plus and minus adjustments each month; and
- c. apply that compensating plus or minus adjustment to the calculation of the first monthly payment after each quarter end.

The direction of revenue transfer will be determined by whether funds are due to IOM or to HMRC at the end of each quarter and will be paid by HMRC or IOM as appropriate on the agreed date for months 4, 7, 10 and 1 of the new year. The quarterly adjustments will allow for fluctuating monthly revenue levels and avoid the potential for any material under/overpayment building up during the year.

⁵ Payment will be effected on the 21st of the month or₄closest working day

It is assumed that actual common duties receipts by IOM will follow forecasts. Where the trend indicated by actual receipts exceeds the results in Step 1 by more than 10% on the annual figures, then transfers to IOM will be suspended, Step 1 will be recalculated and the full amount of the overpaid advance will immediately become due to HMRC. Where the trend indicated by actual receipts is 10% (or more) beneath the results in Step 1 on the annual figures, then transfers to IOM will be suspended, Step 1 will be recalculated and the full amount of the underpaid arrears will immediately become due to IOM.

Step 3 – Make annual adjustments at year end

The annual adjustment calculations will use the revenue receipt and national income adjustments (Steps 5 and 6 in paragraph 5), calculated within the specified timeframe and any additional revenue amounts due to IOM will be paid as a single adjusting payment by HMRC in the first possible month (probably July) in the relevant year. The payment will be made with, or offset against, the monthly payment due for that month as appropriate. Any overpayment to IOM will be paid as a single adjusting payment by IOM in the first possible month (probably July) along with or offset against the monthly payments due for that month as appropriate.

Other related issues

9. Capacity to make repayments

Both IOM and HMRC will ensure that where an immediate repayment does become due then funds will have been deposited in a sufficiently flexible way to allow instant access.

10. In addition to agreeing modernised revenue sharing arrangements (as set out above), in March 2007 the two parties also agreed to the following:

- Any retrospective **adjustments to revenue allocations to be made within 5 years of the relevant year end**; and
- HMRC/IOM to undertake a **joint review of the ‘Cost of Collection’ arrangements** at the end of the financial year 2010/11

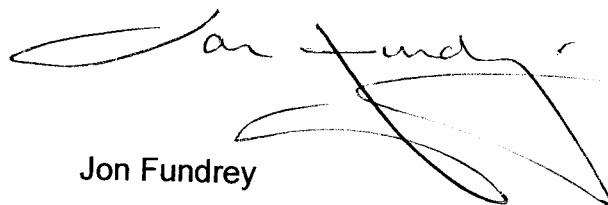
Date of adoption and implementation

11. The revised modernisation arrangements set out in this note, were approved by UK and IOM Treasury Ministers in October 2009 and the arrangements will apply from the start of the 2010/11 financial year.

Signed



Mark Shimmin
Chief Financial Officer
Isle of Man Government
15th October 2009



Jon Fundrey
Financial Controller
HM Revenue & Customs
15th October 2009

Appendix to HM Treasury Direction

Worked example of revenue allocations for 2009/10 using Share of GNI Model (using illustrative figures)

	Isle of Man	United Kingdom		
Step 1 Obtain latest published National income data				
	2006/07 national income (£ billion) (Last published for UK and IoM)	1.94491	1,203.18	
	2007/08 Obtain growth rates (%)	8.50%	2.50%	
	2008/09 Obtain growth rates (%)	4.50%	-0.25%	
	2009/10 Obtain growth rates (%)	2.50%	-2.25%	
A	Step 1 2009/10 National income forecast (£ billion) (See Note 1)	2.26031727	1202.497383	
Step 2 Calculate the provisional IOM sharing fraction (See Note 2)				
B		0.001876159	0.998123841	
Step 3 Apply provisional sharing fraction to forecast VAT receipts (B *C)				
C	Obtain forecasts of UK VAT and Other duties receipts for 2009/10 (£ bn) before April 09	VAT 63.7	Other duties 19.7	Total 83.4
D1	Step 3 Apply provisional sharing fraction to forecast VAT receipts (B *C)	119,511,342		
D2	Step 4 Apply provisional sharing fraction to forecast receipts of other duties (B*C)	36,960,337		
D	Total IoM revenue share for 2009/10 (D1 + D2) (See Note 3)	<u>156,471,679</u>		
Step 5 Annual adjustment to take account of certified joint revenues				
E	Obtain certified revenue receipts for 2009/10 (£ billion) before end of June 2010	VAT 65.2	Other duties 19.9	Total 85.1
Adjustment for certified revenue using provisional sharing fraction				
F1	(B * (E - C)) (See Note 4) VAT	2,814,239		
F2	(B * (E - C)) (See Note 4) Other Duties	375,232		
F	Total Step 5 Adjustment	<u>3,189,471</u>		
Step 6 Annual adjustments for national income data				
Obtain new and revised national income data, probably mid-2010				
G	2009/10 national income (£ billion) (2010 vintage) (compare with A)	2.290400000		
H	Step 6a) Revised sharing fractions (See Note 2)	0.001896356		
I1	Adjust for national income data ((H - B) *E) (See Note 5) VAT	1,316,799		
I2	Adjust for national income data ((H - B) *E) (See Note 5) Other Duties	401,906		
I	Total Step 6 Adjustment	<u>1,718,706</u>		

Note 1

Calculated by applying growth rates to 2006/07 data being the most recent published by the UK and IOM.

Note 2

The provisional and revised sharing fractions are calculated by dividing each jurisdiction's national income by the sum of both jurisdictions' national income.

Note 3

As per Para 8 Step 1 (ii), the forecast of IOM local collection will be deducted from the IOM revenue share to arrive at the annual payment due to either the IOM or the UK

Note 4

The calculation is the provisional sharing fraction applied to the difference between certified and forecast VAT and Other Duty receipts.

Note 5

The calculation is the difference between the revised and provisional sharing fractions applied to certified revenue receipts.