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Introduction

The Corporate Services Panel has already presented two reports to the States on the Zero/ten Design proposal:

- Interim Report (S.R. 4/2006), presented to the States on 28th September 2006. This report was based on the initial consultation document, dated 5th May 2006.
- Second report (S.R.3/2007), presented to the States on 23rd January 2007. This report examined the Treasury and Resources Minister's revised proposals contained in R.80/2006 and the first part of the draft Zero/Ten legislation[1]

The Corporate Services Panel subsequently reconstituted the Sub Panel to conduct the next stage of the review which was to examine the shareholder legislation.

In particular, the Sub Panel wished to follow up one of the major concerns identified in its earlier reports, namely the fact that non-Jersey owned businesses would escape tax liability in Jersey. The Sub Panel believes that this could give non resident owners a competitive advantage over local firms, particularly if they are also avoiding or postponing tax in their own jurisdictions, and could encourage them to seek to buy out locally owned businesses.

The Sub Panel believes that a proposal from Jurat Peter Blampied (the 'Blampied proposal') for a tax on owner-occupied business property (in effect a re-introduction of Schedule A) is a workable solution to the problem of collecting a tax contribution from foreign-owned trading companies.

The Treasury and Resources Minister has acknowledged that this proposal is '*effectively the only solution I can see on the table which has anything going for it at all*'[2]. The Sub Panel was pleased to see that he has agreed to investigate the economic impact and the potential yield.

This interim report is presented to the States by the Sub Panel in advance of its further review of the draft shareholder legislation[3] in order to share with States members its analysis of this proposed solution.

Panel Membership

The Corporate Services Scrutiny Panel is constituted as follows –

Deputy P. J. D. Ryan, Chairman
Senator J. L. Perchard, Vice Chairman
Connétable J. Le Sueur Gallichan
Connétable D. J. Murphy
Deputy C. Egré

Officer support: Mr M. Haden and Miss S. Power

For the purposes of this review the Panel formed a Sub Panel, which was constituted as follows –

Senator J. L. Perchard, Sub Panel Chairman
Senator B. Shenton
Deputy P. J. D. Ryan

Independent Expert Advice

The Panel engaged the following advisers to assist it with the review –

Mr. Brian Curtis, FCIB, MSI (dip.), PFS, FInstD, has worked in Jersey's Finance Industry for some 35 years and is currently involved with a number of activities within the industry and the voluntary sector.

Mr. Richard Teather, BA, ICAEW, a senior lecturer in Tax Law at Bournemouth University; a Freelance Tax Consultant and a writer on Tax Law and Policy.

Terms of reference

The Corporate Services Scrutiny Panel approved the following terms of reference for the third phase of the review of the Zero/ten design proposals:

To review the second part of the Zero/Ten Draft Legislation, and any areas of concern raised by the Zero/Ten system as modified by that draft law, with a particular focus on the following areas –

1. *The provisions for taxing Jersey-resident shareholders;*
2. *The provisions (or lack thereof) for obtaining revenues from non-Jersey owned companies;*
3. *The distributional effects and equity of the proposed Zero/Ten system;*
4. *The effectiveness and fairness of any anti-avoidance measures and disclosure obligations;*
5. *The extent to which the proposed legislation meets the concerns raised in the Panel's first two reports on Zero/Ten; and*
6. *The extent to which the obligations under Jersey's agreement with the EU have been satisfied.*

Documentation

The following documents are available on the Scrutiny website http://www.scrutiny.gov.je/research.asp?reviewid=56

BDO Stoy Hayward LLP - Review of the 'Blampied proposal' from a United Kingdom tax perspective, 21 December 2006.

What is the economic and distributional impact of an owner-occupied immovable property tax? Note prepared for States of Jersey by Oxera, 22nd May 2007

Note prepared by Jurat P.G. Blampied on the Oxera Paper: What is the economic and distributional impact of an owner-occupied immovable property tax?

Hearings

The following witnesses attended hearings with the Sub Panel:

7th August 2007
Jurat P.G. Blampied

16th August 2007
Senator Terry Le Sueur, Treasury and Resources Minister
Mr. Malcolm Campbell, Comptroller of Income Tax

Verbatim transcripts are available on the Scrutiny website

Background: Previous Scrutiny reports

Unfair competition between local and foreign owned businesses

1. Under Zero/Ten the profits of Jersey-owned businesses would be taxed (as deemed distributions to the shareholders), but non-Jersey owned businesses (including many High Street operations) would escape any tax liability in Jersey. The Sub Panel believes that this would give non resident owners a competitive advantage over local firms, particularly if the owners are also avoiding (or postponing) tax in their home country.

2. Furthermore, the Sub Panel believes it is vital that the Island continues to receive some form of tax contribution from non-Jersey owned companies trading in the Island, and that it is equitable for them to continue to make some form of contribution to States revenues.

3. The Treasury recognised at an early stage in their design proposal that failing to tax foreign-owned businesses would cause problems for the Island. The initial Zero/Ten Design consultation document therefore contained a proposal which was aimed at ensuring that off-island owned businesses continued to make a contribution to the Island's tax revenues once the standard rate of corporate income tax was reduced to 0%. This became known as the '**RUDL' charge** as it was to be levied on all businesses registered under the Registration of Undertakings and Development (Jersey) Law 1973.

4. In RC 80/2006 it was stated:

   The charge would avoid unfair competition between local and foreign owned businesses and any tendency for locally owned businesses to sell out to foreign investors (16.2.3)

5. The charge would not have impacted on locally-owned companies as it was intended that it would be creditable against income tax paid by resident shareholders. The problem for foreign owners, however, was that the charge would not be a creditable tax in their home territory and would have been an additional cost of doing business in the Island.

6. The Sub Panel, while agreeing with the concerns that had prompted the RUDL charge, had strong concerns with this proposal itself, hearing from witnesses that it would be excessively complex, administratively expensive for both businesses and government, discourage new investment into the Island, and increase prices for consumers.[4]

The Sub Panel was therefore pleased to note that the Treasury removed the RUDL charge from the Revised Design Proposal as a result of the opposition which had been voiced during the consultation and Scrutiny period.

7.

Would Jersey-owned businesses be disadvantaged?

8. It has been said by the Treasury that non-Jersey owned businesses would not gain any advantage under 0/10, because their tax reduction in Jersey will be balanced by additional tax in their home country, leaving the total tax on their profits unchanged.

9. For example a Jersey business owned by a UK company currently should pay 20% tax in Jersey plus a further 10% in the UK (the UK's usual rate of 30% minus the credit given for the Jersey tax paid). Under 0/10 there should be no Jersey tax, but also no tax credit in the UK, so the full 30% tax will be due in the UK. The tax would be paid wholly to the UK Treasury, rather than some to Jersey and some to the UK, but the total amount remains unchanged.

10. The Panel was advised that this view is naïve, and that non-Jersey owned businesses would be able to avoid tax, or postpone it for many years[5]. Simple tax planning would therefore give them a significant advantage over Jersey-owned businesses, and amount to unfair competition.

11. Even those accountants who said that these businesses would pay tax in the UK implied that any payment would be postponed and uncertain - they would only say that "at some point they probably will" pay UK tax, and that "it is just a fact of commercial life that if you introduce a rule people are suddenly inspired to think around it"[6].

12. Indeed the Treasury's own approach to 0/10 suggests that many shareholders will seek to avoid tax once their companies become tax-free under 0/10, otherwise the deemed distribution provisions and the extended information powers given to the Comptroller would not be necessary.

13. In the case of a Jersey **branch** of a UK company, it is true that the full profits would be taxable in the UK (currently at 30%) as soon as they are earned. However in the case of a UK group with a Jersey **subsidiary**, under 0/10 that subsidiary will pay no tax in Jersey, and the group would only pay UK tax when its profits are paid to the UK parent company as a dividend.[7] Since a dividend would attract tax, there would be a strong incentive for UK groups to avoid receiving dividends from their Jersey subsidiaries. Instead profits could be reinvested tax-free, either in Jersey or elsewhere in the group, or extracted by way of a loan to the parent group.[8]

14. For businesses owned outside the UK, the treatment will vary. However it seems likely that a Guernsey company, for example, will be able to avoid, or at least postpone for a long time, any tax on its Jersey operations.

15. It therefore seems that off-Island owned trading operations in Jersey will pay no Jersey

tax, and will be able to avoid or delay paying tax elsewhere. Their costs will therefore decrease, giving them an advantage over locally-owned businesses.

16. This advantage also means that Jersey businesses will be more valuable to off-Island investors than they are to Jersey residents, who may therefore find themselves outbid. Although there are of course many reasons for making an investment, giving a tax advantage to off-Island investors can only accelerate the current trend for Jersey businesses to be bought by non-Jersey investors.

Alternatives to RUDL charge

17. The Sub Panel has remained convinced that the real problems of inequity between locally owned and non-locally owned non-finance businesses operating in the Island, which the RUDL charge was intended to solve, had to be addressed. In its first report the Sub Panel proposed two alternatives to the RUDL charge, a GST restriction and a proposal from Jurat P.G. Blampied to re-introduce Income Tax Schedule A whereby owner/occupiers of real property in Jersey were assessed to income tax (the 'Blampied' proposal).

18. It should be noted that prior to 1963 it was normal practice in both the United Kingdom and Jersey to tax the benefit in kind that owner occupiers enjoyed through occupying their own properties, and this was achieved through Schedule A assessments.

19. Subsequent to the Sub Panel's first report it became clear that the second proposal would be the more suitable of the two options. This proposal is discussed in more detail below (paragraph 23 onwards).

Creditable against United Kingdom tax

A key issue with regard to the proposal is whether the tax under Schedule A would be creditable against income tax so that the overall tax burden on company shareholders is not increased. If the tax is creditable then any Jersey tax paid should give an equal reduction in UK tax, so that the overall tax paid by the company and its shareholders remains the same. It is clear that in Jersey the Schedule A tax would be creditable for resident shareholders. The question is whether it could be structured so that UK-owned businesses would therefore be able to recover it against their UK tax.[9] Without this the tax would be an absolute cost of doing business in Jersey, and therefore (like RUDL) would risk reducing investment in the Island.

20.

21. However even if it is not creditable in the UK, the Schedule A tax would not be inflationary if UK-owned businesses can successfully avoid paying UK tax on their tax-free Jersey profits under 0/10 (see paragraphs 53-56 below).

22. The Sub Panel commissioned BDO Stoy Hayward LLP ("BDP") in London to provide definitive advice on this question.

23. The advice from BDO concluded that a tax on deemed rents for non-residential Jersey property would not be an admissible tax in the United Kingdom, either for United Kingdom companies with a Jersey branch or in relation to dividends paid by Jersey companies to a UK parent company. The basis for this advice was:

> Primarily that the UK only gives credit for taxes which "correspond" to UK income tax or corporation tax; since the Jersey tax would be on **deemed** (notional) rents whereas UK tax is charged on **actual** income, it would not "correspond" to UK tax.

> Secondly, in relation to a Jersey business which is a branch rather than a subsidiary of a UK company, the UK only gives credit for tax charged on "the same item of income" as the UK tax; since the Jersey tax would be on deemed rents whereas the UK tax would be on trading profits, the two taxes would therefore not be on the same income.

24. An alternative route was suggested by the Sub Panel, that a UK-owned operation which currently owns and occupies its own premises in Jersey could instead transfer the property to another group company, so that the property holding company would charge rent (at full value) to the trading company[10]. This would transfer part of the profits from the trading company to the rental company. Instead of the trading company paying Jersey tax on a *deemed* rent (which it appears might not be recoverable against UK tax) the property company would pay Jersey tax on its *actual* rental income.

25. The advice from BDO stated clearly that in this case the Jersey tax would be creditable against UK tax:

> "*The associated property ownership company will have creditable tax for UK purposes"*

26. .However, BDO stressed that the wider implications of such a move were beyond the scope of their advice.[11]

The only potential solution

27. The Treasury and Resources Minister agreed that the Blampied proposal might be a viable alternative and agreed to undertake further investigations to confirm that the parallel company structure would work and to assess whether setting up such a structure

might be too expensive.

28. The Minister told the Sub Panel in December 2006:

> ***Senator T.A. Le Sueur:***
> *"… My only potential solution at the moment as to dealing with the non-resident shareholder issue is something along the Blampied proposal… I do not know yet as to whether they work fully or not but I cannot think of anything that works better than that so it is, from my point of view, at the moment that or nothing. I am not looking at any other alternatives."*[12]

29. In a subsequent public hearing on 16th August 2007, the Minister confirmed that it was still the case that the Blampied proposal represented the only potential solution on the table and he was minded to explore the consequences still further with the Sub Panel. He said:

> *I am leaning much more towards the Blampied idea on the grounds of equity. But one has to be careful; if one generates greater equity in one area does one create inequity of imbalance elsewhere?*

Economic impact

30. In order to address potential commercial disadvantages, the Treasury and Resources Minister commissioned a note from Oxera on the economic and distributional impact of the Blampied proposal[13]. This note concludes:

> *For the business sector, the analysis show that such a tax is likely to have a negative impact on the international competitiveness of Jersey export sectors, and to distort the competitive balance between domestic and international firms in Jersey.*

31. The Sub Panel believes that the Oxera report is flawed because it assumes that credit will not be available to non resident owned trading companies against United Kingdom income tax, and so the tax would represent an additional cost to doing business in Jersey compared to their current position and that under 0/10. This is in contrast to the advice received by the Sub Panel in the BDO report referred to above which found that 100% credit should work provided the parallel company structure was used. Indeed even if the Schedule A tax were not creditable against UK tax, the Panel's advice still cast doubt on Oxera's claim that it would be inflationary. If UK-owned businesses can avoid UK tax on their Jersey profits under 0/10 then they will reduce their cost of doing business in Jersey, so the Schedule A tax would merely cancel out part of that advantage (See paragraphs 53 - 56 below).

32. The Sub Panel discussed this point with Jurat Blampied[14]. He said that Oxera had mistakenly looked at Schedule A as a stand-alone tax. He explained that Schedule A tax was payable on the net annual value:

That net annual value on which income tax was payable, that net annual value was deducted from the assessed profits. So if you had profits of £500,000 and you owned the building in which you traded, the net value, £100,000, would come off. You would pay tax under schedule D which lays out the rules on which trading profits are assessed, at £400,000 and you would pay schedule A, £100,000: £500,000. So you would in fact be paying 20 per cent tax on your total income. If the schedule A exceeded the profit there would be a loss and the loss would be set off against the schedule A, which would mean you would only still pay tax on your actual profits. So the effect disappears. This would be the same for the company owned by non-residents as it would be for the company owned by residents because a tax assessment would have to be calculated in order, so far as the Jersey resident is concerned, that can be imposed on the Jersey resident shareholder. So the same would happen for the schedule A for the company owned by the non-resident. If, by any chance, the schedule A exceeded the trading profit, there would be a theoretical loss and there would be no schedule A payable.

33. Jurat Blampied told the Sub Panel:

When 0/10 is introduced these companies will be in a significantly better position than Jersey owned trading limited liability companies and I have no doubt that it is this benefit which makes the acquisition of Jersey trading companies attractive to non residents.'

34. It is worth noting that the Economic Adviser to the British Chamber of Commerce, Mr. David Kern, gave the same warning in a recent public presentation[15]:

Non-local companies have effectively been given major tax advantages and are able to operate in Jersey without contributing to the local tax base. The consequences of this massive shift in Jersey's tax structure have not been given adequate weight in subsequent policy decisions, eg the retail sector. More generally, it is critically important to assess future policy decisions with regard to their impact on Jersey's wealth and tax base. The drastic changes in Jersey's tax structure alter fundamentally the cost-benefit analysis relating to the importing of non-resident firms into Jersey. But proposed policy changes seem to ignore this critical point while damaging a key domestic sector.

Taxing deemed rents on owner-occupied business property

The Proposal

35. Under this proposal, the annual value of all Jersey non-residential property would be subject to income tax at 20%, either:

    By taxing the landlord[16] on rents received
    (actual rents for properties let on legitimate arms-length terms, full market value rent for property owned by a related party); or

    By taxing the occupier on the notional (market value) rent, for owner-occupied property.

Advantages

Raises revenue, to help plug the 'Black Hole', by taxing use of a scarce resource;

Collects tax from off-Island owned businesses, which will otherwise escape Jersey tax under 0/10, whilst being creditable against UK corporate tax and therefore not increasing the cost of doing business in Jersey (see below).

Practicalities

36. From discussions with a rates assessor, it appears that the Rates data could be adapted to deal with this tax. Although Quarters are based on historic rather than current market values, the intention is that they will be revised on a rolling basis so that the Quarters reflect the *relative* current market rental value. It would therefore be simple to publish an annual multiplier that converts Quarters into market rent.

Compliance with EU Code of Conduct

37. Being based on Jersey land, this should be a non-distorting (i.e. permitted) exception to the general 0% rate. Indeed it is merely an extension to the existing, accepted proposal to tax actual Jersey rents at 20%. Being based on the arm's length price, the calculation of the tax base is in line with international standards.

Creditability against UK tax

38. Whether UK-owned businesses can offset this tax against their UK tax liability is a key issue; if they can, then the cost will be effectively nil for such companies. This is one of the main advantages of this proposal against the RUDL levy.

39. This point will have to be analysed further, and it appears that it may depend on whether the Jersey operation is a branch or subsidiary of the UK company. However as an initial appraisal it appears that even if the tax is not automatically creditable, a simple change in the group structure will ensure that it can be.

40. A company that owns its own premises (TradeCo) could transfer its property into another group company (PropCo) and pay an actual, market value rent. PropCo would receive real rent, and pay Jersey tax on that real rent. It would then (if UK resident) pay UK tax on that rent, and it is clear that Jersey tax on actual rent is creditable against UK tax on the same actual rent.

41. We suggested this structure to BDO when they advised the Panel last December, and their comment was that "t*he associated property company will have creditable tax for UK purposes*"

42. See appendix for **technical analysis.**

Effect on other businesses -

43. To comply with the EU Code, this tax would have to be levied on all businesses. The effect on owner-occupier businesses other than UK-owned ones would be:

a. Jersey sole traders & partnerships

44. This proposal would have no effect on the amount of tax payable. Tax would be charged on the deemed rent at 20%, but that same deemed rent would also be treated as a tax-deductible expense against trading profits, giving an equal 20% reduction.

Example:

A business has profits of £50,000, before taking account of the deemed rent on its premises.

The deemed rent is £20,000.

Deducting the deemed rent from the trading profit gives a trading profit of £30,000.

Tax is therefore due on £30,000 of trading profits plus £20,000 of deemed rent, a total of £50,000 – exactly the same amount as would have been taxable anyway.

45. If the business is making a loss, that loss can be offset against the deemed rent under normal principles. If the deemed rent is larger than the trading profit, when it is deducted from the trading profit it will create a loss which can be offset in the same way.

Example:

A business has profits of £50,000, before taking account of the deemed rent on its premises.

The deemed rent is £70,000.

Deducting the deemed rent from the trading profit gives a loss of £20,000.

This loss can be set against the deemed rent, giving a taxable deemed rent of £50,000 – exactly the same amount as would have been taxable anyway.

b. Jersey-owned companies

46. The tax-deductible expense would be valueless for a 0% company. The company will therefore be paying Jersey income tax on its deemed rent, whereas under 0/10 it would normally not be paying any tax.

47. However any Jersey income tax paid by the company will be creditable against Jersey tax paid by the shareholders on their actual or deemed dividends, so the overall amount of tax paid would remain the same.

48. As a beneficial side effect, this will ensure that Jersey-owned trading companies pay at least some tax in Jersey even if the Jersey ownership is hidden (e.g. through an offshore trust).

49. The only problem would be for loss-making companies, where there would be a tax on deemed rents but no overall profits to generate an actual or deemed distribution for the shareholders. It would be very unusual to allow such companies to offset their trading loss against their deemed rental income, because the trading profits would not be taxable. In this case the tax would have to be carried forward, and set off against the shareholder's tax on future dividends, giving a cashflow disadvantage. Alternatively the Limited Liability Partnership option could be resurrected, for this limited group of companies only.

c. Financial services companies

50. Tax would be charged on their deemed rent at 20% (for those companies that own their own premises). . However the corresponding deemed tax-deductible expense will only reduce profits charged at 10%, increasing the overall tax burden slightly[17].

51. For a UK-owned bank that can use double tax relief this will not be an additional expense, but it could be for some non-UK owned (and potentially for some UK-owned) banks.

52. If it is necessary to give the industry some compensation for this, then the GST flat rate charges could be reduced so that banks will pay slightly more income tax and slightly

less GST, keeping the overall burden the same as under the Design Proposal. This would actually benefit some banks, because the income tax is potentially available for double tax credit whereas the GST charges will not be.

d. Utilities companies -

53. The deemed rent would be taxed at 20% but would also attract 20% relief as a tax-deductible expense against trading profits, so the overall amount of tax paid would remain the same (just as for Jersey resident partnerships).

Is creditability against UK tax essential?

54. Creditability is clearly an advantage, since it makes the tax effectively free for companies that can use the credit. However it is not necessarily correct to say that the tax would be inflationary if it is not creditable.

55. In the case of a Jersey branch of a UK company, the tax would be an additional cost, because the full profits would be taxable in the UK as soon as they are earned.

56. However in the case of a UK group with a Jersey subsidiary, under 0/10 that subsidiary would pay no tax in Jersey, and the group would only pay UK tax when its profits are paid to the UK parent company as a dividend. UK anti-avoidance (CFC) rules would not apply in most cases, because the company has a genuine commercial reason for being in Jersey. Since a dividend would attract tax, there would be a strong incentive for UK groups to avoid receiving dividends from Jersey subsidiaries. Instead profits could be reinvested, either in Jersey or elsewhere in the group, or extracted by way of loan.

57. It therefore seems highly probable that UK-owned trading operations in Jersey will pay no Jersey tax, and will postpone paying UK tax for several years, perhaps indefinitely. Their costs will therefore decrease, and an alternative tax would therefore not be inflationary provided its impact was less than the other tax benefits of 0/10.

Tax base

58. What would be taxed? Currently landlords are taxed on their profit, i.e. rents less expenses (including mortgage interest). That could be used as the basis for this tax, but the primary purpose is to replace the tax on business profits, so it might be better to simply tax gross rents.

59. This might cause some problems for UK groups; if 20% Jersey tax on their gross rents is more than the UK tax on their net profits on the rent they might not be able to receive any

UK tax credit for the excess. However even that could probably be solved by moving debt around the group, so that the interest is borne by a different company.

Extension to domestic property

60. This report is examining ways of collecting tax from off-Island owned, Jersey-based businesses in order to ensure that they contribute to the Island's economy. However Jurat Blampied is also keen to extend the principle of taxing owner-occupiers to domestic property as well as commercial. This proposal is beyond the scope of the current review.

Potential yield

61. The total annual rental value of commercial property in Jersey is £190 million.[18] Tax at 20% on that would yield £38 million, but the yield would be substantially reduced by:

Rented property (rather than owner-occupied), which is taxed already;

Property owned by Jersey-owned businesses and utilities, which would obtain a full tax credit;

Property owned by finance businesses, which would obtain a half tax credit (10% against 20%);

Property owned by Parishes and Jersey-based charities, which would presumably be exempt;

States properties, for which no net tax would be received.

62. These are unknown factors, and therefore the yield is difficult for the Sub Panel to estimate. Provided the collection is cost effective the Sub Panel believes that this proposal will address the issue of inequity although the reduction of inequality will be small unless the tax the foreign-owned business pay under this proposal is a substantial proportion of the tax they escape under 0/10/.

63. It is important therefore that the Treasury estimates the expected yield of the tax, now that the Minister is “minded” to pursue it.

Related issue: exemption for Pension Funds

64. Taxing owner-occupied business premises in the way suggested above lends further weight to the argument for abandoning the current exemption for foreign pension funds from tax on Jersey property[21], otherwise UK-owned groups would simply transfer their Jersey property into their UK pension funds (this is already done in the UK, with a major UK group having been reported as carrying out this switch this year). That would mean

that the trading operation no longer owned its premises, so would not be taxed on any deemed rent, but the group body that did own the building would not be taxed on the rent it received.

65. The Minister told the Sub Panel that such a move would have to be carefully considered as there could be an impact on property prices, on rental yields and on competition. The Minister said that this could possibly devalue the capital value of some of the Waterfront land[22].

Appendix – credibility against UK corporation tax[23]

A) UK companies with a Jersey branch

66. The UK gives unilateral double tax relief, which in this case is more generous than that available under the UK-Jersey treaty. Section 790 (4), Income & Corporation Taxes Act 1988 (UK), states:

    Credit for tax paid under the law of the territory outside the United Kingdom and computed by reference to income arising or any chargeable gain accruing in that territory shall be allowed against any United Kingdom income tax or corporation tax computed by reference to that income or gain

67. Clearly what is being paid is “tax”. The two questions are:

    Is it computed by reference to “income arising” in Jersey?

    Jersey is exempt from this requirement (ICTA s790(5)(a)).

    Is there any UK tax “computed by reference to <u>that</u> income”?

    This is a potential problem, since the Jersey tax is on (deemed) *rental* income but the UK company would be seeking to offset this against UK tax on the *trading* profits of the branch.

68. There are two alternative potential solutions to this problem:

    1) Alter the group structure

    2) Tax Jersey businesses on their business profits, but compute those profits by reference to the deemed rental value of the premises they occupy

Altering the group structure

69. The simple answer to a UK company faced with Jersey tax on deemed rental income that is not creditable against the trading profits of (say) a Jersey shop, is to convert the deemed rent into an actual rent.

70. In other words, transfer the ownership of the premises to another group company,[24] which will charge rent to the trading company. This will reduce the profits of the trading company, and the property-owning company will be paying Jersey tax on actual rents which should be creditable against UK tax on those same actual rents.[25]

71. There are probably other mechanisms that could be devised, but the above is a simple

and practical solution which should enable double tax relief to be claimed. Consultation with relevant companies and their advisers should result in a Jersey tax system that gives maximum flexibility to UK-based companies seeking double tax relief.

Taxing Jersey businesses on their business profits, but computing those profits by reference to the deemed rental value of the premises they occupy

72. The proposed new tax could be re-drafted as a tax on business profits, but with the profits equal to the deemed rent. This could be seen as an over-elaborate system, although it may work to allow UK creditability[26] ().

73. However it seems likely to fall foul of the EU Code, particularly B4 whether the rules for profit determination in respect of activities within a multinational group of companies departs from internationally accepted principles

B) UK companies with a Jersey subsidiary

74. Under 0/10, this may well become the dominant structure, as UK groups take advantage of the 0% tax rate.

75. In the case of a subsidiary (provided the UK parent company owns at least 10% of the Jersey subsidiary), the conditions for UK unilateral double tax relief are less onerous than for a branch. Section 790 (6), Income & Corporation Taxes Act 1988 (UK), states:

> *Any tax in respect of its profits paid under the law of the territory by the company paying the dividend shall be taken into account in considering whether any, and if so what, credit is to be allowed in respect of the dividend.*

76. The same issue therefore arises as to whether tax on deemed rents is tax “in respect of profits. There are several areas where the UK tax authorities suggest that deemed and actual income are to be treated as the same, but there remains a strong risk that the proposed tax on deemed rents would not be permitted.”, However the same “parallel property company” structure could be used as for the branch.

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[1] Draft Income Tax (Amendment No.28)(Jersey) Law 200-

[2] Transcript of public hearing on 16th August 2007

[3] Draft Income Tax (Amendment No.29)(Jersey) Law 200-

[4] Corporate Services Scrutiny Panel Report, Review of the Zero/Ten Design Proposal (SR4/2006), Section 5.5

[5] Jurat P.G. Blampied: Notes on Oxera paper

[6] Transcript from public hearing dated 4th August 2006

[7] UK anti-avoidance (CFC) rules would not generally apply where the company has a genuine commercial operation in Jersey.

[8] Clearly there are limits to this process; if the profits retained in the Jersey company become too large then it risks being treated as an investment company rather than a trading operation, and so risks being caught by the UK's anti-avoidance rules. However it seems that it will be possible to avoid paying a dividend for many years, giving a substantial tax advantage.

[9] This is on the basis that under Zero/Ten UK-owned companies will still be paying the same amount of tax but to the UK Treasury rather than to Jersey. In the Sub Panel's Interim report some doubt was cast on this assumption by some witnesses **(Corporate Services Scrutiny Panel Report, Review of the Zero/Ten Design Proposal (SR4/2006), Section 5.5)**

[10] It is in fact already quite common amongst large UK retail chains for a separate group company to hold all the property.

[11] To view the BDO advice in full please refer to the Scrutiny website

[12] Transcript from public hearing, 15th December 2006, p.26

[13] To view the Oxera paper please refer to the Scrutiny website

[14] Notes by Jurat P.G. Blampied on the Oxera note dated 6th July 2007; transcript of hearing dated 8th August 2007

[15] The Jersey Economy: Prospects, Opportunities and Threats, 17th July 2007

[16] Possibly collected from the tenant, through a withholding tax on rent.

[17] Only very slightly, since banks would be expected to have a very high profitability per square foot, so the deemed rent would be a small proportion of the overall profits.

[18] Parish Rates data

[19] Parish Rates data

[20] Household Expenditure Survey; because the two figures are calculated in different ways, the net figure for owner-occupied property is unlikely to be accurate. However it gives a good indication of the potential yield.

[21] Through repeal of Article 115(a) of the Income Tax (Jersey) Law 1961. See Corporate Services Scrutiny Panel Report, Review of the Zero/Ten Design Proposal (SR3/2007), Section 7.6) for discussion of the issues.

[22] Transcript of public hearing on 16th August 2007

[23] This Report is prepared for the States of Jersey to explore the possible impact of a proposed tax reform. It is not intended as commercial advice, and businesses should seek their own advice before proceeding. Neither the Panel nor its advisers accept any responsibility for any loss or costs caused by following the theories expounded herein.

[24] It may be necessary to introduce a stamp duty relief to facilitate this

[25] Per BDO's advice to the Scrutiny Panel, see above.

[26] see *Yates v GCA International*, where a Venezualan tax charged on a highly artificial tax based was accepted for credit against UK tax on conventionally-calculated profits