

Reflecting Gibraltar's strong and continuing economic growth, this year's Budget, presented to Parliament by the Government at the end of June, provides a time-table for the long-awaited introduction of a low corporate tax regime. And while an immediate 2 per cent reduction in the tax paid by tax resident companies – from 35 to 33 per cent – has disappointed the local business community, they and investors will take some consolation from the fact that the Government committed to a timetable to achieve an across-the-board corporate tax of 10 to 12 per cent by 2010.

While the financial services sector had hoped for a bolder approach to the corporate tax question, the Government clearly has felt constrained by the pressures to phase out tax exempt companies by 2010 and the imminent ruling from the European Court on Gibraltar's appeal against the European Commission's ruling on "regionality" in relation to Gibraltar's broader tax proposals. With a general election expected later this year, the Budget also contained a basket of fiscal measures for local consumption - clearly a populist Budget with appeal to the average person in the street. However, Gibraltar's financial and commercial communities were less enthusiastic – disappointed that the Government had not delivered the bold new reduced flat rate in corporate tax that had been widely anticipated. Instead, as indicated above, corporate taxes for 2007/08 are to be reduced by a mere 2 per cent – from 35 per cent to 33 per cent and in the following tax year by a further 3 per cent to 30 per cent – and, finally in the 2009/10 tax year there will be another 3 per cent cut to 27 per cent.

The new low flat corporate rate – which the Government anticipates will be between 10 and 12 per cent – is expected to come into effect in 2010. The Government's claim, that Gibraltar's economy "has never been better" would justify swifter corporate tax cuts; and with the European Court ruling only a few weeks away, the new low flat rate could have been brought forward to take effect from next year critics argue. They are concerned that unless there are alternate provisions to off-set the paucity of the proposed tax reduction it will deter newcomers – particularly to the booming insurance sector. "Grandfathered" companies will, of course, enjoy their tax exemptions for three more years before tax exempt companies are phased out in 2010 to comply with EU legislation. It should also be noted that the Gibraltar tax system is based on the territorial principle. Therefore only Gibraltar sourced income, i.e. income which is accrued or derived in Gibraltar, is subject to Gibraltar taxes. Furthermore, there is no capital gains tax in Gibraltar.

In dealing with corporate taxes in his Budget speech, the Chief Minister stressed that to sustain a successful economic model Gibraltar would have to retain its commitment to a very competitive tax model. And because it was no longer acceptable to have one set of taxes for local companies and another, different one for "foreign" companies, a low tax system for all companies was vital... "otherwise overseas companies will leave and the economy will suffer hugely".

The across-the-board low, flat tax rate which the Government would introduce by 2010 will most probably be set at 10 per cent, but in any event not higher than 12 per cent. This would be similar to the arrangements that already exist in Ireland, Malta, Cyprus and other EU countries. Between now and then, it is expected that the Government will consult extensively with the different economic sectors with a view to further mitigate the consequences of a relatively high rate of corporate tax to companies having a bricks and mortar presence in Gibraltar.

The Budget also heralded modest changes to taxes imposed on High Net Worth Individuals (HNWI) and Category 2 status individuals, while abolishing both category 3 and category 4 status for new entrants. From July 1 this year the minimum tax payable by HNWIs is increased from GBP14,000 to GBP18,000 while the taxable income level increases by GBP10,000 to GBP60,000. Existing Category 3 status individuals will retain that status until June 2009 – unless their certificates lapse sooner – but will also face a GBP5,000 a year hike in taxes to GBP15,000,

while similar time constraints will apply to Category 4 individuals, whose taxes will also increase by 50 per cent – from GBP5,000 to GBP7,500.

Meanwhile, in a year in which Gibraltar's Chief Minister will seek a record fourth term in office, it is no surprise that the 2007 Budget contained a raft of vote-catching measures. And, as Gibraltar's economy continues its strong and robust expansion, these are measures that the Government can afford – with a record over-all Budget surplus of GBP24.8 million and capital reserves that stand at a new all-time record of GBP100 million.

The Budget announcements have provided much needed clarity from the Government in relation to corporate tax rates over the medium term. Hopefully, this will be further enhanced when the European Court's long awaited ruling on regionality is issued in Gibraltar's favour.

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