Business and individuals to benefit from new tax law

A new Tax Act has signaled the end of Gibraltar as a jurisdiction that relied on administrative and statutory ring fencing and secretive tax exempt companies and trusts to attract inward investment, as former Advisor to the Income Tax Commissioner, *Chris White*, explains.

In creating a level playing field for both local and inward investors, Gibraltar has swept away the obstacles to it taking full membership of the company of respectable jurisdictions which no other jurisdiction has grounds to black list or censure.

As *Gibraltar International* went to press in October, the new Act was set to become law.

Although the European Court of Justice had not denied Gibraltar the opportunity to implement a 0-8 per cent regime, the Government took a more responsible approach, more consistent with modern requirements for the acceptability of Offshore Finance Centres.

It retained the principles of the current Tax Act, modernised it and reduced the rate for corporate entities from 22 to 10 per cent.

The only exception to this low rate of tax will be a surcharge of an additional 10 per cent on utility companies (electricity, telecommunications, water, petroleum and sewage) and any company which has a dominant market position and abuses it.

The territorial basis of taxation has been retained and only tax income ‘accrued in’ or ‘deriving from’ Gibraltar is covered.

The government has amplified the definitions based on case law and ensured that companies operating under a licence granted by Gibraltar, or ‘passporting’ into Gibraltar under a licence issued elsewhere (e.g. insurance companies), are entitled to take advantage of the 10 per cent tax rate while not suffering tax on the activities they undertake through a branch or permanent establishment outside Gibraltar.

It is interesting and re-assuring to note that the UK Government has recently launched a consultation paper exploring the possibility of moving parts of its own tax system to a territorial basis.

Sustainable

That the 10 per cent tax rate is sustainable over the long term was demonstrated by the details of the state of the economy announced in the June budget.

At a time when most of the economies of the Western World are in dire straits, the economy of Gibraltar is alive and well!

In the year to 31 March 2010, economic growth was 5.4 per cent and the budget showed a surplus of £29.4m on a Gross Domestic Product (GDP) of £848m. Public debt represented 15.2 per cent of GDP.

By comparison, the UK and much of the rest of the developed world are struggling with huge deficits; UK debt is about 70 per cent of GDP and in many countries, approaching 100 per cent.

The jurisdiction’s state of economic health has enabled not only the reduction of the corporate tax rate to 10 per cent, but also has several subsidiary effects.

Savings gains

The programme of reducing taxation of savings and passive income has been advanced by exempting all interest on investments (i.e. interest other than interest earned by banks and moneylenders as part of their trading income), royalties, and the part of a dividend paid by a company which relates to its non taxable profits.

That is not only an incentive for local people to invest for their future, but also when combined with the lack of Capital Gains Tax or any sort of Estate/Wealth tax, it is a powerful attraction for those with savings income who wish to relocate from a high tax jurisdiction to a more economically friendly jurisdiction.

The top rate of tax has also been reduced to 29 per cent for those earning up to £353,000; above that level, tax rates begin to fall.

The effective rate of tax on earnings of, say, £1m is 20 per cent, with anything above that charged at 5 per cent.

Trusts tax limited

The quid pro quo for these significant reductions in corporate and personal taxation is a new system of self assessment, legislation to modernise tax collection and extensive measures to counter avoidance or evasion of tax.

Although taxation of trusts and beneficiaries of trusts has been introduced where the beneficiaries of a trust are outside Gibraltar, the taxation position remains much the same as it was before.

Taxation on trust income is limited to trusts with Gibraltar resident beneficiaries and taxation on beneficiaries is restricted to distributions which can be matched with the taxable income of the trust reduced by offsetting of any underlying tax which has been paid by the trust.

For this purpose, those High Net Worth Individuals who have Category 2 status and their spouse and children are treated as not resident.

If neither the trust nor the beneficiaries are subject to tax, a licensed trustee will have no need to make returns for the trust or to make the trust known to the Commissioner of Income Tax.

The principle of reducing taxation of savings and passive income is carried on into funds and their investors.

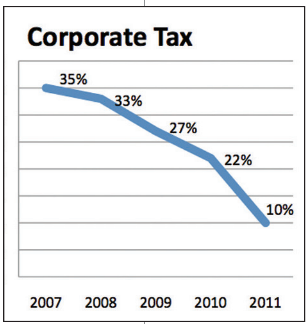
Funds exclusions

The position of the fund itself is unchanged by the new Act and the same exemptions apply as before, strengthened by the further exclusion of categories of savings and passive income from taxation.

In the case of the investor into a fund there are changes which make the trust regime even more attractive.

Income from a fund which is available to the general public is no longer taxable regardless of how the income arose in the fund.

If a fund is not available to the general public, a 'look through' basis is used and tax is limited to whatever it would have been if the recipient had received the income from the entity underlying the fund.



Tax on interest limited

Again the entity will have the advantage of the absence of tax on savings and passive income which means that with very few exceptions - e.g. a fund investing in Gibraltar real estate - there will be no tax payable by the investor.

Taxation on interest is limited to that interest received by banks or moneylenders as trading receipts. In the case of both, trading receipts are defined to exclude the interest which would arise from a Treasury function.

This gives banks and moneylenders the same advantages as all other companies where the possibility of using Gibraltar as a Treasury base arises.

Effectively a non-Gibraltar group company can borrow money from the Gibraltar Treasury company, receiving a deduction in accordance with the laws of its jurisdiction, and the Treasury company will not be taxed on the receipt of the interest.

The changes made in the new Act are also beneficial for companies receiving dividends from subsidiaries.

Gibraltar already does not tax the receipt of dividends from EU subsidiary companies, and has now removed the taxing right to any part of a dividend received from a company which carries out its profit making activities elsewhere.

With neither liability to tax nor withholding of dividends paid to non-residents, group profits can flow through or be invested in Gibraltar without taxation.

Increasing attraction

There is a lot more detail to the legislation but, overall its aim is to create a corporate low tax environment and lay the foundations for, not only the security of the corporate environment, but also the continued reduction in the tax burden on individuals.

The environment created by the new legislation not only places Gibraltar amongst those jurisdictions who comply with all international codes of conduct relating to tax behaviour, but also leaves it as an attractive and tax efficient location for individuals and businesses who wish to locate either in whole or in part to a pleasant, tax efficient, new home.

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