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Jersey's new corporate tax regime: zero/ten

Significant changes have been made to the system of corporate taxation in Jersey. These changes include the introduction of a standard rate of corporate income tax of 0% and the phasing out of exempt company status. The new regime is simply referred to in Jersey as "zero/ten". The "zero/ten" regime is intended to comply with the EU Code of Conduct for Business Taxation and the new regime promotes equal tax treatment between companies.

"Under the new "zero/ten" regime and subject to certain exceptions, a company which is resident in Jersey or which has a permanent establishment in Jersey will be charged income tax at a rate of 0%."

The end of exempt company status

Previously, exempt company status was available to any company (whether or not incorporated in Jersey) which did not have any Jersey resident beneficial owners.

Broadly, in order to obtain exempt company status, the ultimate non-Jersey beneficial ownership of the company had to be disclosed to the Jersey Financial Services Commission (the "JFSC") and an annual fee of £600 paid.

The key advantage in obtaining exempt company status was that the company was deemed for the purposes of Jersey taxation not to be resident in Jersey (even if the company was incorporated in Jersey and/or managed and controlled in Jersey).

Consequently, a company with exempt company status would not be liable to pay Jersey income tax on any profits (other than in respect of Jersey source income excluding bank interest).

In addition, a company with exempt company status would not be obliged to make any withholding on account of tax from any interest payments made by the exempt company to any person.

Under the new "zero/ten" regime, however, exempt company status will no longer exist.

Since 3 June 2008, it has not been possible for companies incorporating in Jersey to apply for exempt company status and such "newly" incorporated companies have been made immediately subject to the new "zero/ten" regime. As of 1 January 2009, all companies are subject to the new corporate tax regime, so that companies which previously had exempt company status are no longer able to apply for this status going forward.

The standard rate of 0%

Under the new "zero/ten" regime and subject to certain exceptions, a company which is resident in Jersey or which has a permanent establishment in Jersey will be charged income tax at a rate of 0%.

A company is regarded as being resident in Jersey if it is incorporated in Jersey or if its business is managed and controlled in Jersey. However, a company incorporated in Jersey will not be tax resident in Jersey if it is managed and controlled in another country, is tax resident in that country and the highest rate at which the company may be taxed in that country is at least 20%.

Permanent establishment is defined in the Income Tax (Jersey) Law 1961, as amended (the "Income Tax Law") to include a branch of the company, a factory, shop, workshop, quarry or a building site and a place of management of the company but the

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definition expressly states that "the fact that the directors of a company regularly meet in Jersey shall not, of itself, make their meeting place a permanent establishment."

The exceptions to the 0% standard rate concern: (a) certain financial services companies with a permanent establishment in Jersey, (b) certain Jersey utility companies, and (c) profits derived from Jersey rental income and Jersey property development. These exceptions are considered below.

Jersey financial services companies

Certain "financial services companies" which have a permanent establishment in Jersey will not pay income tax at the 0% rate but instead will have to pay income tax at a rate of 10%.

This distinction between the 0% rate and the 10% rate is the reason why the new regime is commonly referred to as "zero/ten".

A "financial services company" is defined in the Income Tax Law to mean a company that:

- is registered under the Financial Services (Jersey) Law 1998 to carry out investment business;
- is registered under the Financial Services (Jersey) Law 1998 to carry out trust company business;
- is registered under the Financial Services (Jersey) Law 1998 to carry out fund services business as an administrator or custodian in relation to an unclassified fund or an unregulated fund;
- is registered under the Banking Business (Jersey) Law 1991; or
- holds a permit under the Collective Investment Funds (Jersey) Law 1988 by virtue of being a functionary which is an administrator or custodian.

It is worth noting that not all regulated companies will be subject to the 10% rate. For example, it does not apply to insurance companies or companies which act as fund managers.

Jersey utility companies

Although the new tax regime is commonly referred to as "zero/ten", certain Jersey utility companies will be taxed at a rate of 20%.

The Jersey utility companies which will have to pay income tax at the rate of 20% are as follows:

- The Jersey New Waterworks Company Limited;
- Jersey Gas Company Limited;
- The Jersey Electricity Company Limited;
- any person licensed to run a public telecommunications system under the Telecommunications (Jersey) Law 2002; and
- any person authorized to convey letters by a licence granted under the Postal Services (Jersey) Law 2004.

Jersey rentals and property development

Despite the name "zero/ten", profits derived from any rental income of Jersey land and any profits derived from any commercial property development of Jersey land will be taxed at a rate of 20%.

Jersey resident individuals: personal tax on deemed dividends

Jersey resident individuals remain liable to pay income tax at the rate of 20%.
The introduction of "zero/ten" will cause a significant reduction in tax revenues collected by the States of Jersey.

To mitigate this shortfall and also to ensure that Jersey individuals cannot use the "zero/ten" regime to shelter profits from taxation, tax will be charged to Jersey resident individuals on the profits of companies in which they hold shares where the companies are taxed at 0% or 10% under the new "zero/ten" regime.

The Jersey resident individual shareholder will have to pay tax irrespective of whether the profits of the company are actually distributed to him. In other words, the shareholder has to pay tax on a "deemed" dividend rather than on an "actual" dividend.

These "deemed" dividend provisions are complex and a full analysis of these provisions is outside the scope of this briefing. However, in broad terms only, the following observations are made:

- Where a Jersey trading company (which is defined in the Income Tax Law to exclude a collective investment fund) is taxed at 0%, it will be deemed to have distributed, by way of interim dividend, 60% of its taxable profits for each accounting period. Any Jersey resident individual who holds more than 2% of the ordinary shares in such a company will have to pay personal income tax at a rate of 20% on his or her share of this "deemed" interim dividend.
- Where a Jersey trading company (which, as noted above, excludes a collective investment fund) is taxed at 0%, it will be deemed to have paid a final dividend representing its accumulated taxable profits

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since the company became subject to the new "zero/ten" regime on certain trigger events. Any Jersey resident individual who holds more than 2% of the ordinary shares in such a company will have to pay personal income tax at a rate of 20% on his or her share of this "deemed" final dividend. The trigger events include the Jersey individual ceasing to own more than 2% of the ordinary share capital of the company; the winding-up of the company; the death of the Jersey individual; and the Jersey individual ceasing to be resident in Jersey.
– Where a company is taxed at 0% and it is not a Jersey trading company or a collective investment fund (for example, a non-trading holding company), all of the company's profits will be attributed to the shareholders of the company for each accounting period. Any Jersey resident individual who holds more than 2% of the shares in such a company will have to pay personal income tax at a rate of 20% on his or her share of these profits as if the profits were those of the individual.
– Where a Jersey financial services company is taxed at 10%, a "deemed" dividend regime will also apply. However, the "deemed" dividends will not apply on an interim basis for each accounting period. Instead, there is only a final "deemed" dividend on the occurrence of certain trigger events. Any Jersey resident individual who holds more than 2% of the ordinary shares in such a company will have to pay personal income tax on his or her share of this "deemed" final dividend. The trigger events are the same as those which apply to the final "deemed" dividend of a Jersey trading company (which are described above). A financial services company will already have been taxed at 10% on its profits. So, a Jersey resident individual shareholder will be given a tax credit equal to the tax paid by the company on the profits out of which the "deemed" final dividend is treated as having been paid. In effect, therefore, the Jersey resident individual will only have to fund a 10% tax charge (and not a 20% tax charge) due to the benefit of the tax credit.

No additional tax is payable by Jersey individual shareholders on company profits that have already been taxed at 20%. Thus, the deemed taxation regime does not apply to Jersey utility companies as these companies have already paid tax on their profits at the rate of 20%.

It is worth noting that the deemed dividend provisions only relate to ordinary shares and will not apply to preference shares. It is also worth noting that the deemed dividend provisions do not apply to collective investment funds.

Individuals who have paid tax on a deemed dividend and who subsequently receive an actual dividend will obtain a tax credit in relation to the tax payable on the actual dividend.

Jersey withholding tax

Under the new regime, no Jersey company will be obliged to make any deduction on account of any Jersey tax from any interest payments made by the Jersey company.

As of 1 January 2009, Article 87 of the Income Tax Law, which potentially imposed a withholding tax on certain interest payments, has been amended such that it only applies to interest payments made by an individual resident in Jersey.

Conclusion

Companies that had exempt company status (or which could have applied for exempt company status) should not be prejudiced by the new "zero/ten" regime. For these companies, the tax neutrality of Jersey as a jurisdiction should continue to be respected since these companies will only be taxed at the rate of 0%. Only certain companies will actually have to pay income tax (being certain financial services companies, certain Jersey utility companies and companies in receipt of Jersey rental and/or property development profits). Indeed, there are advantages under the new "zero/ten" regime for companies that had exempt company status (or which could have applied for exempt company status). First, no annual fee will need to be paid in order to secure tax neutrality (whereas, as noted above, under the old exempt company regime an annual fee of £600 was payable in order to maintain exempt company status). Secondly, exempt company status could be threatened if the company had a Jersey resident shareholder. The existence of a Jersey resident shareholder will not affect the standard 0% tax rate applicable to companies (although that Jersey resident shareholder may be taxed on "deemed" dividends as outlined above).

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