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A REVIEW OF THE GOVERNMENT GAZETTE AND NEW DEVELOPMENTS IN LAW

Tax havens should be playing ball

Low tax rates only become a problem when information exchange is refused

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TAX havens have recently had some bad publicity. After the G-20 meeting in London in April, the Organisation for Economic Co-operation and Development (OECD) identified and blacklisted various tax havens.

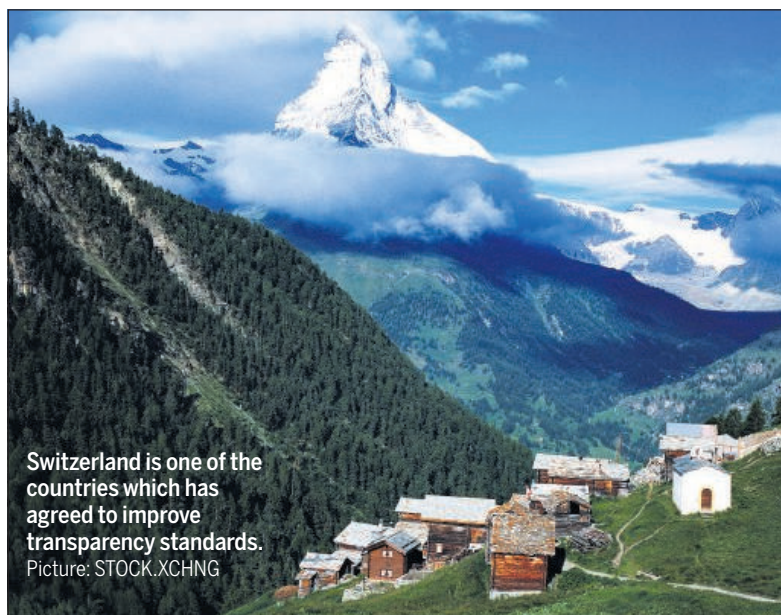
Within a few days of such identification, various of these identified tax havens were removed from the OECD's blacklist of unco-operative tax jurisdictions. This was a consequence of such jurisdictions making a commitment to exchange information at the levels required by the OECD.

The OECD report published around the time of the G-20 meeting included a separate grey list of coun-

tries that agreed to improve transparency standards. This list includes Belgium, the Cayman Islands and Switzerland. The grey list includes jurisdictions that have not yet agreed to exchange tax information at the required levels.

In this regard, one needs to identify the mischief which is being addressed by, among others, the G-20 and the OECD. Unquestionably there is no issue with a country exercising its sovereign right to elect a low national tax rate. Or even with a jurisdiction which offers low tax rates not to its own nationals, but to certain qualifying foreign investors.

Surely an issue only arises when tax havens refuse to co-operate with other nations seeking information about companies or individuals in which they



Switzerland is one of the countries which has agreed to improve transparency standards.
Picture: STOCK.XCHNG

have an interest from a tax perspective.

Tax havens typically offer low tax rates to foreign investors setting up companies in order to attract such investments. But for the low tax rate offered by the tax havens they may not attract these investors. Foreign investors set up operations and move

people to the tax haven thereby creating alternative sources of revenue for the tax haven other than tax revenues.

This has become a competitive market with many jurisdictions offering such tax incentives or exemptions to qualifying foreign investors. In order to be competitive, some tax havens have given the assurance that they will not exchange or provide information to other states, in particular the resident state of the foreign investor.

This creates an issue which the OECD and the US are seeking to address since the resident state (ie. the state of residence of the parent company) will have tax rules which often negate the tax-free status of the foreign investor's subsidiary in the tax haven.

In particular, controlled foreign company rules look to tax the profits of subsidiaries set up in tax havens and

tax such profits in the hands of the holding company in the resident state.

Further, if the company in the tax haven is actually "effectively managed" from the resident state, again it will typically be taxed in that resident state.

In order to obtain the necessary information regarding the nature of the operations of the subsidiary in the tax haven, the resident state often relies on information provided by the tax haven as part of an exchange of information process. This is to ensure that the subsidiary is not merely a sham or office with no substance. This information is necessary for the resident state to properly apply its own tax rules and should be provided by the tax havens.

Countries should not be too quick to castigate tax havens merely for looking to attract investment based on low or nil tax rates. In particular, the UK has often been referred to as one of the world's most successful tax havens.

Although the UK has in recent times re-looked these provisions, for years it has been possible for individuals to live in the UK as residents without being domiciled there and only to be taxed on any income derived from a UK source including income remitted to the country.

Ireland used to offer a beneficial tax system to non-residents. However, the European Union (EU) has clamped down on this practice. Ireland therefore amended its rules and now offers a 12.5% corporate tax rate to all companies including resident companies.

This is done on the basis that the loss in tax revenues would be more than offset by the additional revenues generated from additional foreign investment.

Many other countries offer benefi-

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