Jersey to reduce corporate tax bills

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Jersey has agreed to overhaul its corporate tax regime, in a sign of a broader shake-out under way in the world of offshore finance. Changes recently agreed by the island's parliament will reduce the burden on companies but at the expense of consumers, prompting a backlash in some quarters on behalf of the island's poorer residents.

As Jersey grapples to satisfy the demands of the international community without leaving a huge hole in its public finances, it is acting as an unwitting but revealing exemplar of the social fall-out from reforms taking place across the world's tax havens.

Ten years of intense political pressure from large countries has forced almost all tax havens to make far-reaching changes to their tax and regulatory regimes.

These changes are putting a strain on some jurisdiction's public finances, forcing them to impose unpopular additional taxes to stay afloat.

The small offshore centres targeted by new international regulations also complain that they are losing business to larger jurisdictions that are subject to laxer regulations.

The campaign by the European Union and Organisation for Economic Co-operation and Development against tax havens targeted both their secrecy and their imposition of little or no tax on income from sources outside their jurisdiction. The havens were forced to become more transparent and stop "harmful" tax practices designed to attract foreign investors, while ring-fencing the national tax base.

The small offshore centres have been forced to comply - or risk becoming international pariahs, which would damage their appeal to investors. The US Internal Revenue Service says that the largest concentrations of offshore assets, estimated at £5 trillion, are attracted by the stability and security of the established tax havens.

But if larger countries hoped that they could prevent a "race to the bottom" by stopping tax havens from offering tax breaks for non-resident companies, they have been disappointed. Tough competition between offshore centres for foreign investment has made it difficult for jurisdictions to raise corporate tax rates for non-resident companies.

The Channel Islands, for example, have come under particular pressure from the Isle of Man, which could reduce its corporate taxes without suffering a large deficit. Its champions claim it has a competitive advantage because it draws most of its revenues from the UK's value added tax system.

The reputation of offshore centres has improved as they have become better regulated and more transparent, allowing some to shed the "tax haven" tag. By 2002, the OECD's list of "unco-operative tax havens" was cut down to just five: Andorra, Liberia, Liechtenstein, the Marshall Islands and Monaco.

Some centres, such as the Isle of Man and the Channel Islands, argue that burnishing their image has been good for business. But many offshore centres have lost business in spite of improving their reputations, according to a report last year commissioned by the Commonwealth Secretariat.

This study, which focused on Barbados, Mauritius and Vanuatu, concluded that small offshore financial centres were suffering financially because of international rules countering money laundering, terrorist financing and tax evasion.

The small offshore centres complain that there is an uneven playing field. Howard Bilton of Sovereign Group, a specialist in offshore tax planning, says: "The big winners in the whole process are areas of the world outside the influence of the OECD and EU, particularly

Singapore, Hong Kong and Dubai."

International pressure on havens

By Vanessa Houlder

Pressure on the tax havens has come from three international sources: the Organisation for Economic Co-operation and Development, the European Union and the inter-governmental Financial Action Task Force, which combats money laundering and terrorist financing.

In 1997, the EU devised a tax package in response to concerns about "harmful" tax competition. It included a code of conduct to eliminate harmful business tax regimes and a measure to ensure that tax was paid on savings income. To the dismay of the tax havens with historic links to Britain, EU politicians agreed to apply the code to the dependent and associated territories of member states.

The OECD campaign against "harmful tax practices", which started in 1996, got under way with a list of several dozen jurisdictions deemed to be tax havens on grounds such as having no or nominal taxes, lacking transparency and refusing to exchange information with other authorities. The initiative proved highly controversial but the OECD says it has resulted in a marked improvement in the transparency of tax regimes.