

**C48 INTERACTION OF COMPANY PROFITS AND THE TAX CAP/STANDARD CHARGE (sections 5B, 39B-D and the Fourth Schedule)**

**Introduction**

In accordance with section 39B of the Law, an individual's income tax liability may be limited by virtue of the tax cap. The Sixth Schedule sets out the amount of the cap and the types of income to which it applies, i.e. qualifying and non-qualifying income.

An individual who is resident only may elect to pay the standard charge in accordance with section 5B of the Law. If this election is made, the individual will have no liability to tax on non-Guernsey source income but a liability will arise on total Guernsey source income (other than bank deposit interest). The amount of the standard charge paid can be set-off against the tax due on Guernsey source income.

When Zero-10 was introduced, it was recognised that any assets owned by a company could have been held by the beneficial members directly with any tax liability on that income being capped (typically land and property situate in Guernsey). As a consequence, the general practice was to allow tax paid by that company to offset the tax capped beneficial member's, or beneficial member that elected to pay the standard charge, own liability in that year.

With effect from 1 January 2013, following repeal of the deemed distribution provisions, and in accordance with the Law, a tax capped individual, or individual that elected to pay the standard charge, will only be entitled to a credit for any tax paid by a company to the extent that it relates to a distribution of its profits.

**Further explanation**

Section 68 of the Law requires a company, as a separate legal entity to the beneficial member, to file a tax return and to pay its tax liability in accordance with section 81. The Law does not enable a tax capped beneficial member, or beneficial member that elected to pay the standard charge, to reduce their own personal tax liability by crediting tax paid by a company in their beneficial ownership to their own account.

The Director is of the view that all companies required to complete an income tax return under the Law must submit their returns (together with supporting accounts and computations) whether or not they are beneficially owned by a tax capped individual(s), or an individual that has elected to pay the standard charge, and whether they are subject to the standard, intermediate or higher rate of tax for companies. A company must also settle its own liability in full.

The Director may, by concession, agree to a simplified distribution reporting for companies with income subject to the standard or intermediate company tax rates, that have beneficial members who are tax capped individuals, where deduction of tax would be unnecessary. The Director may, upon receipt of an application, issue a variation notice to the company, which would enable the company to pay distributions to a specified beneficial member without any further deduction of tax required by section 81B if, for instance, the full tax cap has been paid and further deductions would not be necessary.

The practice of allowing the beneficial member credit for tax paid by a company led to administrative complications for the Income Tax Office, particularly where the beneficial member did not wholly own the company. It was also necessary to ensure that an individual did not claim a "double credit". This may have occurred where a distribution is made from a company entitling the beneficial member to a repayable tax credit, when that tax paid by the company had previously been used to offset the individual's personal tax liability.

With the repeal of deemed distributions and extension of the 10% rate coming into effect on 1 January 2013, the Director feels that this is the appropriate date for this previous practice to cease.

It should be noted that on a distribution from a company with profits subject to tax at the company intermediate or higher tax rate, a tax capped individual, or individual that elected to pay the standard charge, may claim credit for Guernsey tax paid by the company in relation to those profits. Therefore, on distribution of a company's profits to a beneficial member, the tax capped individual will be in same position, i.e. they will receive the same cash amount.

### **Anti-avoidance provisions relevant to the tax cap**

#### **Section 39C**

If a resident individual, whose amount of tax is limited by the tax cap, receives a distribution of income, which arose prior to 2008, from a company which in the individual's hand carries a credit, then in accordance with section 39C(2), that individual is not entitled to any repayment of tax in respect of that credit.

In accordance with section 39C(3), for the purposes of calculating whether or not a repayment is due to any individual, any tax credit relating to other sources of income would be offset against the individual's liability in preference to the non-repayable tax credit referred to above.

#### **Section 39D**

If a tax capped individual receives a distribution consisting of Guernsey business income ("non-qualifying income"), the anti-avoidance provisions of section 39D apply. These provisions were introduced to prevent an individual rolling up all their profits over a number of years, and distributing them in one year to take advantage of the tax cap. The impact of these provisions is to calculate the additional tax that would have been payable by the individual in the year of charge in which the income arose/accrued to the company, had the income been distributed by the company in that year of charge. Please also refer to Statement of Practice [C44](#) "Distributions – treatment for purposes of tax cap".

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