

The term "gross receipts" does not include special rules for income taxed in other jurisdictions, so arguably the gross receipts of a foreign PE should be included in the calculation of whether the 10 percent threshold under the anti-treaty shopping rule is met. However, it probably still would be necessary to demonstrate a business purpose for the chosen structure and that the head office has holding company-specific substance in place and engages in typical holding company activities.

This scenario may be especially relevant after December 2007 when cross-border mergers will be possible in the E.U. from a legal perspective. A cross-border merger of a subsidiary corporation in another E.U. member state into the holding company should usually lead to a situation where the foreign holding company will no longer hold a corporate subsidiary but

a PE in the operating company's country of residence after the merger. If it is impossible to eliminate German withholding tax by a cross-border merger of the German operating entity (or a conversion of the company into a partnership because neither income transfers from a German PE to the head office nor withdrawals from a partnership trigger German withholding tax), a cross-border merger of another E.U. entity into the holding company should increase the gross receipts from "own business activity" of the foreign holding company, because the PE's income should be included in the calculation.

Christian Ehlermann is a Partner in the Munich office of Deloitte and may be contacted by email at: cehlermann@deloitte.de. Katja Nakhai is a Senior Manager also in the Munich office of Deloitte and may be contacted by email at: knakhai@deloitte.de

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Understanding the Rules of the Game: Taxation Issues Surrounding the Ever Changing UK Gambling Industry

*Julie Butler
Butler & Co, Alresford*

The taxation of the UK gambling industry has been brought to the forefront of the financial world in 2006 by the US crackdown that so adversely affected internet gambling in the UK. Further attention has been brought by the European Union efforts to abolish Gibraltar's exempt company tax regime. Most on-line gambling companies are based in the offshore tax haven of Gibraltar. 2006 has seen a flurry of VAT business briefs, a tax case and attention from the European Union. Is there any other industry in the UK that received so much "tax" attention in just one year? Perhaps the size, growth and continual change of this industry dictate such attention.

The US congress passed the Unlawful Internet Gambling Enforcement Act in September. This US legislation apparently wiped £3.7bn off the value of a market previously worth £6.5bn in a single day. PartyGaming, which had generated 75 percent of its revenues from the US, dropped out of the FTSE 100.

I. The Low Tax Jurisdiction of Gibraltar

The December 2006 Pre-Budget Report did not address the issue of the apparently high rate of UK Corporation tax of 30 percent.

As on-line gaming companies are all "dotcom" businesses, it has been easy for them to establish headquarters in the low tax jurisdiction of Gibraltar. One of the main reasons that the on-line gambling industry suits Gibraltar is because there is a small staff and premises cost which is one of main basis of the advantage of the Gibraltar tax system. This has provided the on-line companies with a significant edge on other sectors because they have not had to pay the UK corporation tax rate of 30 percent. But these significant tax benefits have been under threat from the European Union, which has been working to abolish Gibraltar's exempt company tax regime.

In April 2004 the European Commission (EC) said that tax rules in Gibraltar provided companies domiciled there with an unfair advantage over other Countries in the Union.

The EC said this amounted to "regional selectivity", and also took issue with the fact that taxes in Gibraltar were based upon payroll and the occupation of business premises, which meant that businesses would be unlikely to pay any corporation tax liability.

The EC said that by 2010 Gibraltar would have to abolish its exempt company regime and implement a replacement tax regime instead. This raised the possibility that on-line gaming groups based in Gibraltar could find themselves paying corporation tax of 30 percent. A recent European Court ruling, however, has indicated that the advantages will continue.

Gibraltar's 1969 constitution provides the territory with fiscal autonomy and the region should be able to continue providing companies with an attractive tax regime. Those involved with the on-line companies anticipate that when Gibraltar's tax exempt scheme is phased out by 2010 the replacement will be low cost.

II. What of the UK Tax Position of the Gambler?

Essentially betting is tax free – the professional gambler is outside the scope of tax.

The current case law is set out in *Graham v Green* (1925) 9 TC 309, a case which concerned a man whose sole means of livelihood came from betting on horses at starting prices, Rowlatt J says at 313:

"Now we come to betting, pure and simple... It has been settled that a bookmaker carries on a taxable vocation. What is the bookmaker's system? He knows that there are great many people who are willing to back horses and that they will back horses with anyone who holds himself out to give reasonable odds as a bookmaker. By calculating the odds in the case of various horses over a long period of time and quoting them so that on the whole the aggregate odds are in his favour, he makes a profit. That seems to me to be organising an effort in the same way that a person organises an effort if he sets out to buy himself things with a view to secure a profit by the difference in what I may call their capital value in individual cases.

"Now we come to the other side, the man who bets with the bookmaker, and that is this case. These are mere bets. Each time he puts on his money, at whatever may be the starting price. I do not think he could be said to organise his effort in the same way as the bookmaker organises his. I do not think the subject matter from his point of view is susceptible of it. In effect all he is doing is just what a man does who is a skilful player at cards, who plays every day. He plays today and he plays tomorrow and he plays the next day and he is skilful on each of the three days, more skilful on the whole than the people with whom he plays, and he wins. But I do not think that you can find, in his case, any conception arising in which his individual operations can be said to be merged in a way that particular operations are merged in the conception of a trade. I think all you can say of that man... is that he is addicted to betting. There is no tax on a habit. I do not think 'habitual' or even 'systematic' fully describes what is essential in the phrase 'trade, adventure, profession or vocation.'"

The principle in this case was followed in *Down v Compston* (1937) 2 All ER 475, (1937) 21 TC 60 where a professional golfer attached to a golf club habitually engaged in private games of golf for varying amounts and won substantial amounts. He was found not to be liable under Case 2 National Insurance on the basis that the bets did not arise from the playing services and that there was no organisation to support the view that he was carrying on the business of betting on the games of golf. It is possible however; that the courts might take a different view if this came to court today.

But these cases were 1925 and 1937 do these principles still apply to the professional "on-line punter" of today? Yes is the simple answer. This has caused some grief for the profession

bookmaker who is fully taxable. The on-line gambler can be more of a statistician – gambling is a fact based science.

Betting by professional bookmakers is assessable to tax even if carried on in an unlawful way (*Southern v AB* (1993) 18 TC 59). Private betting is not assessable, however habitual. Its profits, if any, are also exempt from CGT (Capital Gains Tax) (TCGA 1992, s 51(1)). Receipts from newspaper articles based on a betting system were, however, held to be assessable to income tax in *Graham v Arnott* (1941) 24 TC 157. This is the profession of a journalist not the profession of a bookmaker.

III. Why is Gambling Tax Free?

The simple answer is that HMRC could not cope with the tax claim for gambling losses!

The sporting world involves a large amount of gambling at all levels. In practice, if the HMRC tried to assess the "winners" to tax there would be a deluge of tax loss claims. The cautious tax practitioner should advise clients to keep a record of their winnings in case evidence is required at a later stage. The HMRC always need to verify sources of income and windfalls in an enquiry situation so it is important to keep records to avoid any future problems over the identification of any capital introduced in to a business. The money laundering provisions have a large potential impact for tax advisers, their clients and illustrate the need for information of gambling activities to be provided by the taxpayer to the tax adviser even it is only as information held on the file.

IV. The UK Bookmaker is Taxable

Whilst the professional gambler escapes the tax "net" the UK bookmaking business is assessable to income and corporation tax. If it is possible to feel sorry for a UK bookmaker perhaps it is the fact that the on-line industry has managed to escape corporation tax.

A professional bookmaker systematically attended racecourses for the purpose of carrying on that activity; although he could not legally recover amounts due to him, he was held to be carrying on a vocation. It has also been held that betting by professional bookmakers is assessable even if it is carried on in an unlawful way. See *Southern v AB* (1933) 18 TC 59 where it was held that there is no tax on a habit. It has been considered that the words "habitual" or even "systematic" do not fully describe what is a trade, adventure or professional vocation.

V. What of the New Breed of Exchange Pro-Punters?

So is an on-line gambler still just operating a system by habit or are they trading?

The exchanges have produced a large number of pro-punters who approach their work on a scientific well-researched basis and the profit is tax free. It is certainly good news for professional exchange players that there will be no distinction between recreation and non-recreational layers. So how does the pro-punter deal with the issues of compliance?

If a pro-punter has a small amount of self-employed earnings they can use the tax-free personal allowance for income tax purposes and pay the self-employed NIC AND claim business expenses AND be on the tax return "system". Pro-punter results can be included in the additional information section of

the Tax Return (the white box). A mix of pro-punter profits and some earnings or self-employed earnings is very efficient.

Gambling on-line has given rise to a new breed of statisticians with clear use of available data. There is a different TYPE of pro-punter than before the birth of the exchanges as the earlier tax cases explained. Sometimes the cool headed calculation of statistics is now the order of the day as opposed to the possible appreciation of the racehorse or the unsupported "hot tip" or "whisper". (The placing of a bet is exempt for VAT but this is not the case with gaming machines).

VI. Gaming Machines – Failure to License

The latter part of 2006 saw a plethora of VAT business briefs trying to regularise the VAT position in gaming machines. The placing of a bet, the act of gambling is an exempt supply for VAT but the supply of a gaming machine is subject to a charge for output VAT.

Business brief 15/06 dated September 27 2006 sets out the position on VAT and Gaming Machines and the failure to license.

HMRC are concerned that, despite their statement in December 2005 that for the purpose of VAT with regard to gaming machines, it was irrelevant where the element of chance in the game is provided, some businesses failed to license or account for VAT on these machines or have submitted claims requesting repayment of VAT that had been paid.

HMRC says that as VAT was correctly payable on these machines, repayments will not be made and where tax has been under declared, assessments will be issued. If a business considers it has been misdirected, it should contact the VAT office. The key here is location of the machine – It does not matter where the game of chance is located. Gaming machines in clubs, bars, pubs and bookmakers will have to be considered as to the charge of output VAT and the potential loss of margin and profits.

VII. The Pinball Wizards

The flow of business briefs explaining VAT and gaming machines/games of chance etc continue at a pace. Business brief 16/06 dated October 12 2006 sets out the following:

Two new Treasury Orders have been laid before Parliament that came into effect on November 1 2006. The new Orders continue to update VAT law in light of the Gambling Act and will:

- Remove the separate definition of "gaming machine" from VATA 1994, Sch 9 Group 4, replacing it by a cross reference to the identical definition in VATA 1994, s 23.
- Provide a new definition of "game of chance" in Group 4 and s 23, replacing the cross reference to the Gaming Act 1968 definition.
- Ensure that the definition of 'game of chance' is the same across the UK for both Group 4 and s 23.
- Restore the application of VAT to pinball machines.
- Ensure that any game of chance which is not played for a prize does not fall within the exemption.

VIII. Bookmakers, Gaming Machines and Specialist TV Racing

There was some minor VAT relief for the bookmaker in 2006.

Business brief 17/06 dated October 19 2006, again concentrated on the gambling industry and the complexity of VAT. This followed the result in the tribunal decision in *Town and Country Factors* (19616). Gambling/betting is an exempt supply for VAT purposes. Bookmakers who also supply gaming machines and refreshments are making a taxable supply. The company argued that VAT incurred on specialist TV facilities and Sky Sports was partly recoverable because they had a direct and immediate link with taxable supplies of gaming machines and refreshments, as well as exempt supplies of betting. HMRC's view was that the costs related wholly to exempt supplies so that no VAT was recoverable.

The tribunal supported the company, finding that VAT incurred on specialist racing TV was residual because the company added content to the broadcasts advertising their taxable services and because TV attracts customers in to shops to play gaming machines. Bookmakers may wish to claim input tax which was incorrectly treated as exempt. HMRC say that they must use the partial exemption method applicable to each accounting period unless there are exceptional circumstances as to why an alternative method is needed.

IX. Gaming Machines and Fiscal Neutrality

Business Brief 20/2006, dated November 9 2006, notes that claims for repayments of VAT on gaming machine takings have been received, following the decision of the European Court of Justice in *Linneweber* (Case C453/02, available for downloading from www.curia.eu). In this case, the Court held that the German Government had breached the principle of fiscal neutrality by taxing some gaming machines, but exempting others, depending on the type of premises in which they were installed. The Brief explains why HMRC considers a situation parallel to *Linneweber* is very unlikely to arise under United Kingdom law and sets out what traders would have to prove to demonstrate a breach of fiscal neutrality.

X. Definition of a Bet – Accepting a Bet is not a Betting Transaction

The UK gambling industry has both a complex structure and infrastructure to cope with demands of the clients and the need for traditional and on-line markets to ease.

The case of *United Utilities v CCE* (Case C – 89/05) European Court of Justice July 13 2006 helped define a bet. Customs disagreed with the claim by the company that there was an exempt supply. Appeals to the VAT tribunal, High Court and Court of Appeal all found for Customs. On further appeal to the House of Lords, it referred to the European Court of Justice for a preliminary ruling. The basic outcome was that it was considered that accepting the bets is just a stage in the process; it could not be classified as a betting transaction within the meaning of Article 13B(f).

The basic facts were, Littlewoods decided to outsource part of its telephone bookmaking operations to Vertex. Under the contract, Vertex was authorised to act as Littlewoods' agent and was required to provide staff, premises and telephone equipment necessary to take bets. Littlewoods decided what

could be bet upon, and managed the relevant revenue and expenditure. Vertex simply took the calls and recorded the bets in accordance with conditions stipulated by Littlewoods.

The final decision was that the provision of call centre services to a telephone bookmaking organiser did not constitute a betting transaction and was therefore subject to a VAT charge. As the final transaction was exempt this would cause a disadvantage.

XI. Conclusion

The on-line gambling/gaming business is growing at a vast rate. The profit potential is gigantic – Sportingbet announced a £103m profit in October 2006. It is considered in this case that both on-line Poker and Casino drove the growth. Party Casino was launched in 2006. There are always “emerging games” being launched such as Backgammon. This is in addition to all the horseracing and sports betting.

It is an industry that will involve a lot of regulation and as the market grows “like topsy” it will continue to need new

dedicated business briefs to control the VAT treatment and no doubt due to the large sums involved, it will need decisions to be made in the European Court of Justice.

For those involved in the industry, a simple blink could miss a change and it is unthinkable what you would come back to after a two week holiday without your email and your mobile contact...

For the tax adviser the gambling industry will impact upon virtually all practices within the UK. Most firms have a client base that somewhere will include a gaming machine, a bookmaker, a (possibly hidden) number of gamblers and tipsters together with a large number of investors (and potential investors) in this vibrant world. It will be essential to understand all the basic rules of the game...

Julie Butler F.C.A. is the author of Tax Planning for Farm and Land Diversification and Equine Tax Planning. She may be contacted by tel on 01962 735544 or by Email at j.butler@butler-co.co.uk.

An Overview of Jersey's Tax Regime

*Jonathan Bale,
Walkers, Jersey*

Jersey considers itself to be a “low-tax”, rather than a “non-tax”, jurisdiction. Provisions do exist which ameliorate the position of corporate bodies or limited partnerships that are beneficially owned by non-Jersey residents and which might otherwise be deemed to be resident in Jersey for the purposes of the Law. However, those provisions are considered to be generally consistent with the approach that income tax is charged on the worldwide income of Jersey residents and on the Jersey-source income of non-Jersey residents.

Jersey actively promotes itself as a well-regulated, stable and high quality international finance centre, not as a “tax haven”. Jersey's prosperity as an independent international finance centre depends not on an absence of taxation, but on Jersey's ability to demonstrate the many positive factors that lead clients to conclude that it is a suitable jurisdiction for the location of high quality international financial business.

The principal tax legislation in Jersey is the Income Tax (Jersey) Law 1961 as amended (the “Law”), which is administered by the Comptroller (the “Comptroller”) and his department. The States of Jersey (Jersey's legislative assembly) approves the appointment of the Comptroller, and the present Comptroller was appointed in 1984.

The continued effectiveness of the Law owes much to the sensible use of concessions and the Comptroller's

practical approach. This approach is evidenced by, for example, a general willingness to give advance written confirmation as to the tax treatment of specific proposals.

Each year, the Comptroller issues a comprehensive guide detailing available concessions and the Comptroller's practices. These concessions and practices supplement the Law, and they add significantly to the Comptroller's ability to act both pragmatically and in a manner consistent with maintaining Jersey's position and reputation as a high quality international finance centre.

This article sets out to provide the reader with a broad overview of the tax system in Jersey and recent developments in that system.

I. Taxes and Fees

Jersey does not currently tax supplies of goods or services, capital gains, or gifts, although there are plans afoot to tax supplies of the majority of goods and services in the Island.

A. Inheritance Tax and Probate Fees

Jersey does not seek to tax inheritances or succession to the ownership of property, although probate fees are payable on the grant of probate in respect of the net value of the relevant personal estate of a deceased individual. Probate fees are