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REPORT

From:	General Secretariat of the Council
To:	Permanent Representatives Committee/Council
Subject:	Code of Conduct Group (Business Taxation) – Report to the Council = Endorsement

Cook Islands' Overseas insurance regime (CK003):

Final description and assessment

STANDSTILL REVIEW PROCESS (JANUARY 2019)

During the 2017 screening process, the COCG could not reach a conclusion on whether the Cook Islands' Overseas insurance companies regime (CK003) meets the Code of Conduct gateway criterion. It should be recalled that the regime imposes a 3% CIT rate on gross income.

The Cook Islands provided to the COCG at the beginning of 2019 additional information to clarify the regime. In particular, Cook Islands compared the CIT that the three companies benefitting from the regime would have paid for income years 2014-2016 with the 3% placement tax they paid. Had these three companies paid company tax based on their net profits, they would have paid a total of

$557,068.14. Under the regime, they paid $591,572.53 tax, based on 3% of their gross premiums derived from business transacted in the Cook Islands.

On the basis of this information, the Code of Conduct Group meeting of 30 January 2019 concluded that this regime does not meet the Code of Conduct gateway criterion, as the regime does not provide for a significantly lower level of taxation.

Annex 1: Preliminary COCG assessment of the CK003 regime in 2017 (standstill review)

ANNEX 1: Preliminary assessment of the CK003 regime in 2017

a. Description

According to the Income Tax Act overseas insurance companies other than life insurance companies are taxed at the rate of 3% (Section 74 of and Schedule 1 to the Income Tax Act). "Overseas company" means any company other than one incorporated in the Cook Islands.

It is not entirely clear but it would appear that Category B licensees under the 2008 Insurance Act would be considered as “overseas insurance companies”. A Category B license can be issued to an external insurer carrying on insurance business in the Cook Islands that forms a branch office. This entitles the holder to carry on domestic insurance business. “External insurer” means an insurer incorporated, constituted or formed outside the Cook Islands.

b. Preferential features

Overseas insurance companies are taxed at the rate of 3%. Resident companies are taxed at a rate of 20%. Non-resident companies are taxed at a rate of 28%.

c. Possible concerns

A regime limited to foreign tax payers and/or to operations outside the territory of the jurisdiction (ring fenced regime) does not meet criteria 1 and 2 of the Code of Conduct which forbid this type of ring fencing. The overseas insurance companies’ regime seems targeted to foreign enterprises since tax advantages are granted only to external insurers whose main place of business is situated outside the Cook Islands.

Sources of information: IBFD

d. Assessment

	1a	1b	2a	2b	3	4	5
The Cook Islands – Overseas Insurance Companies	V	V	V	V	V	X	X

V = harmful

X = not harmful

Explanation

Gateway criterion - Significantly lower level of taxation:

"*Within the scope specified in paragraph A, tax measures which provide for a significantly lower effective level of taxation, including zero taxation, than those levels which generally apply in the Member State in question are to be regarded as potentially harmful and therefore covered by this code*"

The general tax rate for companies in the Cook Islands is 20%. According to the Income Tax Act overseas insurance companies other than life insurance companies are taxed at the rate of 3% (Section 74 of and Schedule 1 to the Income Tax Act). "Overseas company" means any company other than one incorporated in the Cook Islands.

The Cook Islands argues that the 3 % tax is levied on gross premiums derived by the company in respect of business transacted in the Cook Islands, i.e. it is a tax on turnover and should not be compared to a company tax calculated on a company's net profit. The Cook Islands does not see any preference being afforded to overseas insurance companies. The 3 % on premiums is seen as a proxy for what may otherwise be payable in the Cook Islands and is granted to mitigate the disproportionate administrative compliance expense that would otherwise be incurred on this insignificant proportion of the companies' overall business. The Cook Islands has, however, not provided any statistical information that would support the argument that the 3 % tax levied on gross premiums is comparable to the normal tax rate paid by domestic insurance companies. Without any further information/statistics, it is not possible to determine whether the gateway criterion is met or not.

Criterion 1 – Targeting non-residents:

"*whether advantages are accorded only to non-residents or in respect of transactions carried out with non-residents*"

The Overseas Insurance Companies regime seems targeted to foreign owned enterprises since tax advantages are granted only to foreign companies. The tax exemption is only granted to a company that is not incorporated in the Cook Islands. We therefore propose a tick ("V" - harmful) for criterion 1a." [*de lege*].

Criterion 2 – Ring-fencing:

"*whether advantages are ring-fenced from the domestic market, so they do not affect the national tax base*"

The Overseas Insurance Companies regime seems targeted to foreign enterprises since tax advantages are granted only to foreign companies. Since the income of foreign companies is not fully taxable in the Cook Islands, the advantages are ring-fenced from the domestic market and thus, does not, affect the national tax base.

Criterion 3 - Substance:

"*whether advantages are granted even without any real economic activity and substantial economic presence within the Member State offering such tax advantages*"

The measure does not include any express requirement for real economic activity or substantial economic presence.

Criterion 4 – Internationally accepted principles:

"*whether the rules for profit determination in respect of activities within a multinational group of companies departs from internationally accepted principles, notably the rules agreed upon within the OECD*"

A tax exemption does not contradict any internationally embraced principle.

Criterion 5 - Transparency:

"*whether the tax measures lack transparency, including where legal provisions are relaxed at administrative level in a non-transparent way*"

The measure is fully set out and published in the relevant legislation and the practice should not involve any administrative discretion.

Overall assessment

"*Without prejudice to the respective spheres of competence of the Member States and the Community, this code of conduct, which covers business taxation, concerns those measures which affect, or may affect, in a significant way the location of business activity in the Community*"

Without any further information/statistics, it is not possible to determine whether the gateway criterion is met or not. If the gateway criterion is met and an assessment is made under all Code criteria, the regime should be considered overall harmful from a Code of Conduct point of view.

The main concerns which deviate from the Code of Conduct criteria relate to:

- The international business company regime seems **targeted at activities carried out by foreign entities** since tax advantages are granted only to companies that are not incorporated in the Cook Islands.

- The measure **does not include any express requirement for real economic activity or substantial economic presence**.