



Economic Substance - Bermuda, BVI & Cayman Islands

Economic Substance – An overview and comparison summary of requirements in Bermuda, BVI & Cayman

In the ever changing space of tax compliance, tax transparency and exchange of tax information, the European Union (the EU) and the OECD made a decision in 2016 to adopt criteria looking at tax transparency and fair taxation across the globe in order to curb abusive tax practices known as Base Erosion and Profit Shifting (BEPS).

The major outcome relating to offshore jurisdictions was for the requirement to have “substance” in the country of incorporation / registration. The intention was and is to prevent international businesses from benefitting from countries’ differing tax laws by artificially transferring profits to jurisdictions that impose little or no income tax. Thus in response to increasing pressure from the EU and the OECD, and to avoid being placed on the EU Council’s list of non-cooperative jurisdictions for tax purposes (or “blacklist”), each of Bermuda, BVI and Cayman have introduced economic substance legislation (**ES Legislation**) effective 1 January 2019 to satisfy such requirements.

The ES Legislation varies slightly by jurisdiction based on differences between each jurisdiction’s economies, legal framework and understanding and interpretation of the EU and OECD’s expectations. In general, under ES Legislation applicable to each jurisdiction, unless an exemption applies, “relevant entities” incorporated or registered in an offshore jurisdiction which carry on a “relevant activity” are required to demonstrate economic

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substance pursuant to the ES legislation. Such economic substance requirements would include, *inter alia*, that the relevant entity:

- is directed and managed in its jurisdiction; and
- conducts core income-generating activity in its jurisdiction; and
- has adequate people, premises and expenditure in its jurisdiction.

Whilst very similar, it is important to note that there are some significant differences in the application of the ES Legislation in each of the jurisdictions. Marbury has prepared a brief comparison and overview (see page 3) relating to the similarities and differences in respect of each of Bermuda, BVI and Cayman Islands for your reference.

It must also be noted that there are a number of areas within the ES Legislation that are still being clarified by the relevant authorities in each of Bermuda, BVI and Cayman, with supplementary guidance notes to aid compliance still pending or in the process of being finalised. We will provide further updates once clarification and any amendments have been published at which point we will be contacting clients regarding concrete actions to take.

In the meantime, Marbury advises clients to start the process of reviewing their offshore entities to ensure compliance. If you have any queries about the content of this update or would like assistance in determining whether you are affected and/or to what degree, please contact your usual Marbury adviser or info@marburys.com.

Disclaimer

The information in this article is of a general nature and does not constitute legal or tax advice. Any person considering a transaction in relation to which this article could be relevant is advised to take their own legal and tax advice based on their own circumstances. The information in this article is believed to be correct as at 28 June 2019. It does not take account of any changes in law or practice after that date.

Marbury – Economic Substance Comparison Summary

as at 28 June 2019



Jurisdiction	Relevant Entity	Relevant Activity	Exceptions & *Reduced/Enhanced Requirements	Penalties	Key Dates	Comments
Cayman Islands	Cayman companies	Fund management	Investment funds (or entities through which investment funds directly or indirectly invest or operate)	USD12,200 for first year of non-compliance	Effective 1 Jan 2019	ELPs used by PE funds appear to be exempt from these rules for the time-being Appears to target corporate entities used by multinationals for strictly tax purposes SIBL Excluded Persons are subject to the ES Test
	Cayman Limited Liability Companies (LLCs)		Entities which are tax resident outside the Cayman Islands	USD122,000 for subsequent years		
	Cayman Limited Liability Partnerships (LLPs)	Banking	Domestic Cayman entities carrying on a Cayman business	Non-compliant entities will be required to apply to the Grand Court of the Cayman Islands for an order requiring remedial action to avoid de-registration		
	Foreign companies registered in the Cayman Islands	Insurance	Cayman exempted limited partnerships (ELPs) and trusts <i>*Pure equity holding companies are subject to a reduced substance test (IP companies are subject to an enhanced substance test)</i>	Criminal penalties for knowingly making a false economic substance declaration (up to USD10,000 and five years' imprisonment)		
Bermuda	All registered entities (includes companies, limited liability companies, and partnerships (which have elected to have "separate legal personality") and overseas companies with a permit to engage in business in Bermuda)	Leasing	Limited partnerships (LPs) without separate legal personality	Civil penalties of up to USD250,000, subject to discretion of Bermuda Registrar of Companies	Entities in existence prior to 1 Jan 2019 must comply by 1 July 2019, with first return due in 2020	Unless partnerships have elected to have separate legal personality, partnerships used by PE Funds (LPs) appear to be exempt. Query what the policy is for applying the rule to flow-through entities.
		Distribution and service centre businesses	Entities which are tax resident outside Bermuda <i>*Pure equity holding companies are subject to a reduced substance test (IP companies are subject to an enhanced substance test)</i>	Registrar may require court order for remedial action or de-register entity Criminal penalties for knowingly making a false economic substance declaration (up to USD10,000 and two years' imprisonment)		
BVI	Companies incorporated or registered under the BVI Business Companies Act (excluding companies not resident in BVI) Limited partnerships (whether local or foreign) with separate legal personality	Headquarters businesses		Graduated penalties up to USD400,000 for "high-risk" IP legal entity and up to USD200,000 for all other entities	New entities must comply upon incorporation, with first return due in 2020	Unless partnerships have elected to have separate legal personality, partnerships used by PE Funds (LPs) appear to be exempt. Query what the policy is for applying the rule to flow-through entities. Appears to impose steeper criminal penalties than other jurisdictions. Query whether these may apply in cases of mere non-compliance (as opposed to in cases of false statements) Although not specifically carved out of the definition of relevant activity, it is noted that the business of being an investment fund is not a relevant activity.
		IP businesses	Investment funds Entities which are tax resident outside the BVI	Registrar may de-register the entity Criminal penalties of up to five years' imprisonment may apply in certain cases of non-compliance		
		Shipping	Limited partnerships (whether local or foreign) without separate legal personality <i>*Pure equity holding companies are subject to a reduced substance test (IP companies are subject to an enhanced substance test)</i>			
		Holding companies				

Please contact your Marbury advisor or info@marburys.com for further information and guidance