

Tax Express - Immediate attention

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New Economic Substance Law in British Virgin Islands

In response to the European Union ("EU")'s pressure especially on tax transparency and compliance with OECD's Base Erosion and Profit Shifting ("BEPS") package, British Virgin Islands ("BVI") passed the Economic Substance (Companies and Limited Partnerships) Act, 2018 ("ES Law") which came into force on 1 January 2019.

Under the ES Law, legal entities carrying on the "relevant activities" are subject to the ES Law and required to comply with the Economic Substance requirements ("ES requirements"). For the existing entities incorporated prior to 1 January 2019, they must comply with the law by 30 June 2019. For the newly set-up entities, they must comply with the law immediately in relation to the relevant activity.

This express briefly provides an introduction of the ES requirements under the ES Law with an aim at drawing immediate attention of the entities and individuals that have or will set up companies in BVI for the purpose of meeting the ES requirements.

A brief introduction on scope of the ES Law

Legal entity

"Legal entity" means a company and a limited partnership.

The ES Law applies to all BVI companies or BVI limited partnerships which carry on any of the relevant activities, but excluding those which are tax residents outside the BVI (Details refer to section of Tax resident outside BVI).

Relevant activities

The relevant activities are:





ES test

A legal entity (other than a pure equity holding entity) satisfies the ES Test in relation to a relevant activity provided that it fulfills the following requirements in relation to the relevant activity:

- the relevant activity is directed and managed in BVI;
- having regard to the nature and scales of the relevant activity in term of adequate number of suitably qualified employees in BVI, adequate expenditure in BVI, and physical offices or premises appropriate for the core income generating activities ("CIGA"); and
- conducts CIGA.

Pure equity holding entity

Pure equity holding entity means a legal entity that only holds equity participations in other entities and only earns dividends and capital gains AND does not carry on any relevant activity.

For a pure equity holding entity, it is required to comply with its statutory obligations under the relevant company act or partnership act AND have adequate employees and premises for holding equitable interests or shares and, where it manages those equitable interests or shares, has adequate employees and premises for carrying out that management.

Tax resident outside BVI

Non-resident company / Non-resident limited partnership means a company / limited partnership which is resident for tax purpose in a jurisdiction outside BVI which is not on the EU list of non-cooperative jurisdictions for tax purpose. ***It is required to provide evidence to support that tax residence.***

Disclosure of information will be made by the BVI authorities to the relevant overseas tax authorities, according to the relevant agreements or requirements, in respect of the information of the company / limited partnership where it claims to be tax resident.

Newly required prescribed information in RA database

Pursuant to the Beneficial Ownership Secure Search System Act, 2017 ("2017 Act"), each registered agent shall enter in the "RA database" particulars of the prescribed information.

"RA database" is defined under the 2017 Act to be an IT solution established and maintained by a registered agent, to hold the prescribed information for each relevant corporate and legal entity for which it acts as registered agent.

The ES Law amended Section 10 (Duty to maintain RA database) of the 2017 Act. Certain prescribed information is newly required such as:

- for a non-resident company / limited partnership which carries on a relevant activity, the jurisdiction in which it is tax resident together with evidence.
- for a resident company / limited partnership which carries on a relevant activity during a financial period ending after 31st December 2019, the total turnover, expenditure amount incurred in BVI, total number of employees, number of employees in BVI, address of any premises in BVI, nature of any equipment in BVI and the names of person responsible for the direction and management (together with their relationship with the company / limited partnership and whether they are resident in BVI), in respect of that period for each relevant activity.

Notification and reporting

Timing of first notification and reporting are not clearly specified and guidance to the ES Law is not yet issued. Concerned parties should keep an eye on future publications to be released by the relevant BVI authorities.

Penalty

Penalties are heavy. Failure to provide information without reasonable excuse or provision of false information intentional is an offence and is liable to a fine of US\$40,000 to US\$75,000, and / or imprisonment for 2 to 5 years.

For failure to comply with the ES requirements, the penalties are US\$5,000 to US\$50,000 for intellectual property ("IP") legal entities and US\$5,000 to US\$20,000 for other legal entities. If the non-compliance was not rectified within a time allowed, the second penalty will be US\$10,000 to US\$400,000 for IP legal entities and US\$10,000 to US\$200,000 for other legal entities.

Our observations

It is a world-wide trend that all entities operating anywhere in the world are required, unless statutory exempted, to subject their income to a certain degree of taxation. All offshore centres are now required to comply with requirements under BEPS package otherwise they would be blacklisted as non-cooperative tax jurisdiction. According to the relevant requirements, they are

also enforcing stringent disclosure requirements including automatic exchange of information between the tax jurisdictions and spontaneous disclosure of the information upon confirmation of the company's non-compliance or non-resident status.

Although a number of legal, tax and / or practical questions in respect of the ES Law are still subject to further clarifications or elaborations, the potentially affected entities may consider to take immediately the following actions:

- Reviewing their shareholding and / or operation structure which includes BVI entity to evaluate and assess possible impacts of the ES Law;
- Considering what kind of actions should be undertaken for the purpose of complying with the ES Test (if applicable);
- Evaluating feasibility and applicability of establishing a tax resident status in a tax jurisdiction (e.g. Hong Kong) which is not on the EU list of non-cooperative jurisdictions for tax purpose.

Hong Kong is a financial center in Asia-Pacific and has adopted a simple and friendly taxation system. In addition, Hong Kong has world class financial infrastructure, excellent banking system, top quality professionals such as lawyers, accountants, financiers, and fairly extensive tax treaties for avoidance of double taxation;

- Monitoring any new developments closely as detailed guidance may be soon issued by BVI authority AND the EU will review the ES legislations issued by BVI which may affect the legal entities;
- Consulting with professional(s) for legal and tax advices in respect of how to fulfill and comply with the ES Law in relation to your operations.

Appendix

List of non-cooperative tax jurisdictions

As of 26 March 2019 (date of publication in the Official Journal), the EU list is composed of:

- American Samoa
- Aruba
- Barbados
- Belize
- Bermuda
- Dominica
- Fiji
- Guam
- Marshall Islands
- Oman
- Samoa
- Trinidad and Tobago
- United Arab Emirates
- US Virgin Islands
- Vanuatu

<https://www.consilium.europa.eu/en/policies/eu-list-of-non-cooperative-jurisdictions/>

Any readers or clients who would like to know further information and / or understand more, please contact our Tax Partners / Principal Advisors (Tax or Wealth Succession Consulting). They may visit the following link for more information:
<http://www.bvi.gov.vg/media-centre/legislation-passed-address-eu-economic-substance-concerns>

Contact us

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