

## UPDATE ECONOMIC SUBSTANCE LEGISLATION BRITISH VIRGIN ISLANDS (BVI) | AUGUST 2019

Under the Economic Substance Act (“ESA”), legal entities formed or registered in the BVI are required to have economic substance in the BVI.

The ESA also amends the BVI’s Beneficial Ownership Secure Search System Act, 2017 (“BOSS Act”) to add to the existing requirements such that a legal entity and its Registered Agent have obligations in respect of reporting prescribed information in relation to a legal entity’s economic substance.

### **Which entities will be affected?**

The ESA applies to certain BVI companies, BVI limited partnerships with legal personality, and foreign companies and foreign limited partnerships with legal personality registered in the BVI carrying on “relevant activities”. The ESA does not apply to limited partnerships that do not have legal personality.

Entities that are tax resident in a jurisdiction outside of the BVI (other than in a jurisdiction included on the EU non-cooperative jurisdictions list) do not need to comply with the economic substance requirements but will need to provide satisfactory evidence of their tax residency.

### **What activities are covered?**

Legal entities carrying on any “[relevant activities](#)” will be required to satisfy an economic substance test. Relevant activities include the following types of business/business activity:

- Banking Business
- Fund management Business
- Insurance Business
- Intellectual property Business
- Shipping Business
- Finance and leasing Business
- Headquarters Business
- Holding Business
- Distribution and service center Business

### **Test for Relevant Activity:**

An entity which carries on more than one relevant activity must comply with the economic substance requirements and must satisfy the economic substance test which is:

- A. Is the entity of a type which falls within the economic substance legislation?
- B. Is it carrying on a relevant activity?
- C. If it is carrying on a relevant activity, is it resident for tax purposes in a jurisdiction outside the BVI (and which is not on the EU list of non-cooperative jurisdictions for tax purposes).

Only if the answers to (A) and (B) are affirmative and the answer to (C) is negative will the economic substance requirements apply to the entity.

- for relevant entities in existence prior to 1 January 2019 – from 30 June 2019;
- for relevant entities established on or after 1 January 2019 – from the date on which the relevant entity commences the relevant activity.

Legal entities that fall within the scope of the BVI Law must notify their registered agent in the BVI of any relevant activities they carry on as well as certain other prescribed information. The draft Economic Substance Code states that this information must be provided within 6 months of the end of the relevant financial period (such financial period will normally be the one year period beginning on the date that the Economic Substance Test needs to be satisfied as set out above). The registered agent is also required to take reasonable steps to collect the prescribed information with respect to each such legal entity for which it acts as registered agent. This information is then made available to the ITA by means of a database whose contents is made accessible to designated persons.

### **Economic Substance Test**

Subject to below, in order to meet the Economic Substance Test, a legal entity carrying on a relevant activity must:

- conduct core income generating activities (“CIGA”) in the BVI;
- be directed and managed in the BVI; and
- taking into account the nature and scale of the relevant activity, have:
- an adequate number of suitably qualified employees physically present in the BVI;
- an adequate amount of expenditure incurred in the BVI; and
- appropriate physical offices for CIGA.

The Economic Substance Code does not seek to provide specific definitions of “adequate”, “suitable” or “appropriate” for the Economic Substance Test, instead noting that such terms should be given their ordinary English meaning and that the size of the particular business should be taken into consideration.

It is possible to outsource some or all of the BVI CIGA provided the legal entity is able to demonstrate that it is able to monitor and control the outsourced activities and that those activities are undertaken in the BVI.

Note that if a company is a “pure equity holding entity” which carries on no relevant activity other than holding equity participations in other entities and earning dividends and capital gains, the ES Act provides that it satisfies the Economic Substance Test if it (i) complies with its statutory obligations under the BVI Business Companies Act; and (ii) has in the British Virgin Islands adequate employees and premises for holding equity participations and, where it manages those equity participations, has in the British Virgin Islands adequate employees and premises for carrying out that management. A pure equity holding entity for these purposes means a legal entity that only holds equity participations in other entities and only earns dividends and capital gains.

On the other hand, high risk intellectual property (“IP”) businesses face more stringent requirements.

## **Enforcement and Penalties**

The ESA contains penalties for failure to satisfy the Economic Substance Test, including:

- for the first determination of non-compliance, a minimum penalty of \$5,000 and a maximum penalty of \$20,000 (\$50,000 for high risk IP entities) may be imposed by the ITA;
- for the second determination of non-compliance, a minimum penalty of \$10,000 and a maximum penalty of \$200,000 (\$400,000 for high risk IP entities) may be imposed by the ITA;

The ITA may also serve notice on the Financial Services Commission requiring that the legal entity be struck off the Register of Companies or Register of Limited Partnerships as applicable.

## **What to do now?**

Where a legal entity is subject to the economic substance regime, it will need to demonstrate that it adheres to the BVI Law. Full details on the requirements for compliance will follow once further clarification has been provided by the final Economic Substance Code. In the interim, the first step is to consider whether a legal entity is carrying on a “relevant activity”. If it is, the next step is to consider whether it has sufficient substance or is tax resident in another jurisdiction. If not, appropriate action, which will depend on the particular facts and circumstances, needs to be taken.

## **How can we help?**

In order to assist you in complying with this law, please complete the required ESA Declaration Form and return it to our office. If and when applicable, we will ask you to provide further information or evidence showing the legal entity is non-resident for tax purposes in the BVI.

For complex situations where legal advice is necessary to confirm if a legal entity must establish and demonstrate Economic Substance in the BVI, Quijano & Associates can assist you by obtaining a bespoke legal opinion from a BVI law firm.

Download Link: [Q&A – BVI ESA Declaration Form](#)

## **Compliance and Filing Fees**

Any relevant compliance and filing fees will be advised under private and separate correspondence.

## **Further Information/Whom to Contact**

For further information or clarification, please do not hesitate to contact us at [quijano@quijano.com](mailto:quijano@quijano.com)

Si usted desea consultar esta información en español, favor hacer clic en el siguiente enlace: [BVI ESA ESPAÑOL](#)