



New Economic Substance Requirements in the British Virgin Islands

On January 1, 2019 the BVI Economic Substance (Companies and Limited Partnerships) Act, 2018 came into force. This new legislation addresses the EU concerns about the use of BVI entities by non-residents for profit shifting. The act remedies the Territory's previously insufficient economic substance requirements for entities doing business in or through the BVI.

Scope of the Act

The new law imposes economic substance requirements on all BVI companies and limited partnerships (LPs) which are carrying on "Relevant Activities", unless they are resident for tax purposes in a jurisdiction other than the BVI, and on all foreign companies and LPs doing business in the BVI.

Relevant Activities

- Banking & Insurance
- Fund management
- Finance and leasing
- Headquarters
- Shipping
- Holding entities
- Intellectual property
- Distribution and service centres

What are the Economic Substance Requirements?

Broadly speaking, the economic substance requirements can be summarized as follows :

- a) Effective management of the relevant activity is in the BVI;
- b) Employees and expenses in the BVI must be in line with the nature and scale of the activity;
- c) Physical offices or premises in the BVI may be required;
- d) If the relevant activity is intellectual property business and requires specialist equipment, that equipment should be located in the BVI
- e) The legal entity itself conducts core income generating activity; if the core income generating activity is outsourced, it must be conducted in the BVI and the legal entity must be able to monitor and control the outsourced activity.

Pure Equity Holding Companies:

A pure equity holding legal entity; which does not carry on any relevant activity other than holding equity participations in other entities and only earns dividends and capital gains, will be subject to less onerous

economic substance requirements. There is, in particular, no obligation to carry out core income generating activities in the BVI and no obligation that the relevant activity is directed and managed from the BVI.

How soon will the substance requirements apply?

The Act differentiates between “new” companies and LPs respectively incorporated and formed on or after 1st January 2019 and companies and LPs which existed before that date.

New companies and LPs must comply with economic substance requirements immediately and meet the reporting obligations within one year of the date of incorporation or formation respectively.

Existing companies must comply with economic substance requirements by 30th June 2019 and meet reporting obligations within one year of that date.

Reporting Requirements and Penalties

Legal entities that are in scope will now have to provide certain information to their registered agent, including information on its jurisdiction of tax residence and confirmation as to whether or not it is engaged in one of the relevant activities. Where the legal entity is carrying on one or more of the relevant activities, it will be required to provide additional information in relation to each such activity.

Penalties will be imposed both for failure to provide required information, and for operating a company or LP in breach of the economic substance requirements.

The Next Steps

There are some uncertainties concerning how certain practical aspects of the Act will/should work and there are some areas of ambiguity that need to be clarified and the regulations which are to accompany and clarify the Act are yet to be disseminated.

Whilst we wait for further guidance from the relevant BVI authorities:

- Companies and limited partnerships that fall within the scope of the Act should start to evaluate whether or not they are tax resident in the BVI (or elsewhere); and whether they engage in any relevant activity;
 - They must then consider how they will comply with the economic substance requirements. For all activities, other than the activity of a pure equity holding company, the entity will need to demonstrate that the relevant activity is controlled and managed from within BVI and they will also have to carry out the core income generating activities which relate to the activity within the BVI.
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- They also need to consider the financial period that they will adopt for reporting purposes, as they will be required to provide this information to registered agents within the coming months. The substance requirements have to be complied with by reference to financial periods. In the case of a company or LP formed on or after 1 January 2019, such period of not more than one year from the date of formation and thereafter each successive period of one year running from the end of that period. For companies and LPs that existed prior to January 1, 2019, such period of one year commencing on a date no later than 30 June 2019 and thereafter each successive period of one year running from the end of that period.

Initiatives taken by GMG to prepare for this change

In the coming weeks, GMG intends to contact affected clients to discuss and work through the BVI substance requirements applicable to their BVI entities. Although the BVI is yet to issue regulations and guidelines around the implementation of the Act, GMG's view is that it is important that an assessment of a BVI entity's business activities starts sooner rather than later to ensure any possible implications and/or remedial steps required can be taken promptly. GMG continues to engage with lawyers and industry experts to stay abreast of any new developments and efficient means to meet the imposed substance requirements.

GMG will keep you updated of any material changes to the above. In the meantime, should you wish to discuss this matter with GMG, please do not hesitate to contact your Relationship Manager or your contact person.