ECONOMIC SUBSTANCE (COMPANIES AND LIMITED PARTNERSHIPS) ACT, REVISED EDITION 2020 (as amended)

RULES ON ECONOMIC SUBSTANCE IN THE VIRGIN ISLANDS

RELEASE DATE: 9 OCTOBER 2019

UPDATE (v2): 10 FEBRUARY 2020

UPDATE (v3): 24 FEBRUARY 2023

ISSUED BY: INTERNATIONAL TAX AUTHORITY

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1. Introduction

1.1 These rules are issued under the authority of the International Tax Authority ("ITA") pursuant to sections 17 of the Economic Substance (Companies and Limited Partnerships) Act, Revised Edition 2020 (as amended) ("ESA") and 16B of the Beneficial Ownership Secure Search System Act, Revised Edition 2020 (as amended) ("BOSSs Act"). Section 17(3) of the ESA gives the ITA the power to issue rules on how the economic substance requirements may be met, including without prejudice to the generality of the foregoing, rules on the interpretation meaning of any expression used in the ESA or in regulations made under section 17(1) of the ESA by the Minister. Section 16B of the BOSSs Act gives the ITA the power to issue rules on how the duties imposed on corporate and legal entities and registered agents under the BOSSs Act, or any regulations made under it, may be met, including, without prejudice to the generality of the foregoing, rules on the interpretation or meaning of any expression used in this Act or in such regulations. Section 17(4) of the ESA and section 16B of the BOSSs Act state that regard shall be had to any rules concerning the interpretation of any expression. These rules comprise of the following:

(a) extracts from legislation, which appear in *italic font*;
(b) rules made by the ITA which appear in **bold font**; and
(c) explanatory notes which appear in regular font.

1.2 Appendix 1 sets out the abbreviations used in these rules.

1.3 The first version of these rules was published on 9 October 2019 and was effective as a result of the Beneficial Ownership Secure System (Amendment) (No. 3) Act, 2019, was entered into force on the 16 June 2019.

Unofficial consolidations of the ESA and the BOSSs Act can be found under the Action 5 tab at the following link: https://bviita.vg/library/legislation/.

1.4 The extracts from legislation in these rules are reflected as at the date of release of these rules and it is the responsibility of the user to keep up to date with any amendments made to legislation. These rules must be read in conjunction with the legislation and are not intended to substitute the requirements or definitions outlined in the legislation.

1.5 These rules are not intended to be a substitute for legal advice in the particular circumstance of individual cases. Legal entities are encouraged to seek professional advice if they are uncertain in any way of their obligations under the relevant legislation.

1.6 From time to time, it may be necessary to revise or expand these rules. Where any significant change in the content of rules occurs, the ITA will take account of the fact that a legal entity may have relied upon the previous form of rules in ordering its affairs and will afford a reasonable time for the legal entity to adjust to the new rules.

1.7 The economic substance regime in the Virgin Islands ("BVI") is two-fold. Firstly, there is the declaration stage whereby a legal entity via its registered agent must declare the information outlined in section 10(3) of the BOSSs Act to the ITA. Secondly, the ITA is required to assess the compliance of legal entities with the laws. This assessment

begins with the evaluation of the information provided during the declaration stage, but also involves the ITA gathering further information on the position of the legal entity.

2. An overview of the economic substance legislation

2.1 The basic obligation imposed by the economic substance legislation is set out in ESA section 5:

(1) A legal entity which carries on a relevant activity during any financial period must comply with the economic substance requirements in relation to that activity.

(2) A legal entity which carries on more than one relevant activity shall comply with the economic substance requirements in respect of each such relevant activity.

Rule 1

A legal entity will be treated as carrying on a relevant activity during any financial period in which it receives income from that activity.

2.2 In order to be subject to the economic substance requirements, a legal entity must be conducting a relevant activity (see section 5 of the ESA) which generates (or may be expected to generate) gross income for the legal entity. For all relevant activities except holding business and intellectual property business, income is not of itself a relevant consideration in determining whether the legal entity is conducting a relevant activity during any specific financial period except in the circumstances outlined in Rule 1. Rule 1 makes it clear that the mere receipt of income during a financial period, if derived from business operations, will be treated as carrying on the relevant activity. This situation could arise if business operations carried on in financial period 1 result in income which is only received in financial period 2. Even if the only activity which takes place in financial period 2 is the receipt of income, that will still be treated as conducting the relevant activity in that financial period. Of course, if all the legal entity is doing in financial period 2 is receiving income, the degree of economic substance required (see below) will be assessed accordingly. It is only in these circumstances, aside from the definition of relevant activity, that a legal entity should consider income when determining if they are conducting a relevant activity during a specific financial period.

2.3 The following will be considered in order to determine whether an entity is obliged to comply with the economic substance requirements in the ESA:

(a) is the entity of a type which falls within the economic substance legislation?
(b) if it is, 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) (see further rules 5 and 5A concerning the definition of resident 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 legal entity.

2.4 If it has been determined that the legal entity is required to comply with the economic substance requirement it must be noted that, different economic substance requirements apply depending on whether the legal entity is carrying on:

(a) holding business,
(b) intellectual property business, or
(c) any other type of relevant activity.

It is a common requirement for all three of the above categories that, in relation to the relevant activity in question, the legal entity has an adequate number of employees and has adequate premises. It is, in addition, a requirement for categories (b) and (c) that the relevant activity is directed and managed from the BVI, that adequate expenditure is incurred in the BVI and that core income generating activity ("CIGA") is carried on in the BVI. Activities within category (b) may, in addition, be subject to presumptions against compliance with the economic substance requirements which the legal entity may have to displace by evidence.

2.5 The various categories of relevant activities can be found in section 6 of the ESA and the economic substance requirements are explained in more detail below.

2.6 Economic substance is assessed over a financial period as defined in section 4 of the ESA.

2.7 It is possible for an entity to carry on more than one relevant activity at a time. In that situation the economic substance requirements must be satisfied in relation to each relevant activity.

2.8 Legal entities which carry on a relevant activity, which cannot demonstrate tax residence outside the BVI, and fails to meet the economic substance requirements will be subject to enforcement action. This can result in substantial fines, and the liquidation of the legal entity.

2.9 Any legal entity carrying on a relevant activity which is potentially within the scope of the legislation has, broadly speaking, three options:

(a) it can ensure that the substance of the relevant activity is carried on within the BVI,
(b) it can discontinue the activity, or modify it so it no longer falls within the scope of a relevant activity, or
(c) it can demonstrate tax residence in a jurisdiction outside the BVI.

A legal entity which does not take steps either to take its relevant activity outside the scope of the legislation, or to bring it into compliance with the legislation, can expect to be the subject of enforcement proceedings.

2.10 The ESA has been amended to exclude investment fund business from the list of relevant activities. However, an investment fund is deemed to be exempt only to the extent that it acts as an investment fund. "Investment fund business" means the business of operating an investment fund and the term "investment fund" is defined as follows:

an entity whose principal business is the issuing of investment interests to raise funds or pool investor funds with the aim of enabling a holder of such an investment interest

to benefit from the profits or gains from the entity's acquisition, holding, management or disposal of investments and includes any entity through which an investment fund directly or indirectly invests or operates (but not an entity that is itself the ultimate investment held), but does not include a person licensed under the Banks and Trust Companies Act, 1990 or the Insurance Act, 2008, or a person registered under the Cooperatives Societies Act 1979 or the Friendly Societies Act 1928;

A legal entity that is carrying on investment fund business will not be conducting a relevant activity. It is important to note that any activities that a legal entity conducts in the course of being an investment fund will not be treated as a relevant activity. The particular activity needs to be seen as a business activity in its own right and separate from the primary or principal business. For a legal entity that is an investment fund to be found to be conducting a relevant activity, it will therefore need to be shown that it is conducting a separate and distinct business activity in its own right. Otherwise, an investment fund will be submitting a filing stating that it is not conducting a relevant activity for each financial period.

2.11 Some legal entities which carry on a relevant activity will also hold a license from the Financial Services Commission ("FSC") in respect of that activity (e.g., legal entities carrying on banking or insurance activities). The requirements imposed in order to be granted and to maintain that license must continue to be observed, in addition to the economic substance requirements. Additionally, those legal entities that are subject to supervision by the FSC and are licensed to carry on banking business, insurance business or licensed fund management business will already generally be operating in the BVI with adequate resources and expenditure, however, those relevant legal entities will still be subject to the ESA (i.e., filing requirements, CIGA performed in the BVI and the monitoring by the ITA).

2.12 Below is a guide to the general approach which the ITA will take to the construction and application of the legislation.

(1) The ITA will take a pragmatic and commercially realistic approach to the interpretation of the legislation.

(2) The ITA will apply criteria such as the "adequacy" of expenditure and employment, the "suitability" of employee qualifications and the "appropriateness" of premises having regard to the usual way in which businesses carrying on the relevant activity on a commercial basis are structured and operate.

(3) In the event that a legal entity carrying on a relevant activity outside the BVI notifies the ITA of its intention to re-locate that activity to the BVI, so as to enable it to comply with the economic substance requirements, the ITA may agree with that legal entity a compliance plan, as prescribed or otherwise agreed with the ITA, which will set out a timetable which ensures that the relocation occurs as soon as practicable. The maximum timescale set for a legal entity to come into full compliance would not typically extend beyond two financial periods i.e. the financial period in which the legal entity notified the ITA of its intention to re-locate the activity to the BVI (the first financial period) and the subsequent financial period (the second financial period). In the event that a legal entity had not come into compliance by the end of the first financial period, that non-compliance would trigger the spontaneous exchange of information

with the relevant overseas competent authorities (discussed in section 14.2 below) in accordance with the timetable for such exchanges set by the Forum on Harmful Tax Practices.

3. Entities within the scope of the legislation

3.1 The basic obligation to comply with the economic substance requirements is imposed by ESA section 5(1) which reads:

A legal entity which carries on a relevant activity during any financial period must comply with the economic substance requirements in relation to that activity.

3.2 The key concept for determining which legal entities fall within the economic substance legislation is therefore the concept of "legal entity". That is defined as follows:

"legal entity" means a company and a limited partnership;

"company" is defined as follows:

"company" includes:

(a) a company within the meaning of section 3(1) of the BVI Business Companies Act, 2004;
(b) a foreign company within the meaning of section 3(2) of the BVI Companies Act, 2004 which is registered under Part XI of that Act,
but does not include a non-resident company;

"limited partnership" is defined as follows:

"limited partnership" includes:

(a) an existing limited partnership within the meaning of section 2 of the Limited Partnership Act, 2017;
(b) a limited partnership within the meaning of section 2 of the Limited Partnership Act, 2017; and
(c) a foreign limited partnership within the meaning of section 2 of the Limited Partnership Act, 2017 which is registered under Part VI of that Act, but does not include a non-resident limited partnership.

3.3 Leaving aside for the moment the concepts of non-resident company and non-resident limited partnership, legal entities comprise:

(1) BVI companies;
(2) Non-BVI companies which are registered under Part XI of the Business Companies Act 2004; and
(3) All limited partnerships and existing limited partnerships (BVI and foreign) for the purposes of section 2 of the Limited Partnerships Act 2017.

3.4 A RA must ensure that they have entered the particulars of the prescribed information outlined in section 10 of the BOSSs Act into the RA database in relation to all legal

entities for which they act as RA. Section 10 of the BOSSs Act sets out a combination of beneficial ownership information and economic substance information. The details to be included in relation to each legal entity will be dependent on whether the legal entity is conducting a relevant activity, if they have made a claim of non-residence or if they are required to meet substance in the BVI.

4. Tax residence outside the BVI

4.1 As noted above, the economic substance legislation applies to a legal entity. "Legal entity" is defined in ESA section 2 as meaning a company and a limited partnership. However, the definitions in ESA section 2 of "company" and "limited partnership" exclude from those concepts a "non-resident company" and a "non-resident limited partnership". Those concepts are defined in ESA section 2 in the following terms:

"non-resident company" means a company which is resident for tax purposes in a jurisdiction outside the Virgin Islands which is not on Annex 1 to the EU list of non-cooperative jurisdictions for tax purposes;

"non-resident limited partnership" means a limited partnership which is resident for tax purposes in a jurisdiction outside the Virgin Islands which is not on Annex 1 to the EU list of non-cooperative jurisdictions for tax purposes;

4.2 The most recent EU list of non-cooperative jurisdictions can be found at:

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

Such list is generally updated at least once every six months and any legal entity which has claimed or may claim to be regarded as tax resident under the laws of any other jurisdiction is encouraged to monitor any updates to such list and to seek professional advice if it is uncertain of its position.

Rule 2

Any legal entity which claims to fall outside the definitions of company or limited partnership by reason of being a non-resident company or non-resident limited partnership, must make a claim to that effect and must support that claim to the ITA. A legal entity must consider the jurisdiction in which they are claiming to be tax resident and pay close attention to the evidence required in each instance. Where the jurisdiction of tax residence is Guernsey, Jersey or Isle of Man the procedure outlined in Rule 5A applies. Where the jurisdiction of tax residence is any other jurisdiction (that is not on the list of non-cooperative jurisdictions) then the evidence outlined in Rule 3 applies. A legal entity cannot claim to be tax resident in a jurisdiction such as Guernsey, Jersey or Isle of man where they are a transparent entity.

Rule 3

Evidence which the ITA will accept to support the claim in rule 2 includes:

(a) Certificates or letters issued by the competent tax authority of the other jurisdiction;

(b) tax assessments, demands, or evidence of payment issued by the competent tax authority of the other jurisdiction;
(c) tax returns submitted to the competent tax authority of the other jurisdiction; or
(d) rulings issued by the competent tax authority of the other jurisdiction.

4.2A Only where evidence of the types described in rules 3 or 5A submitted to the ITA require clarification will the ITA accept a letter addressed to it from suitably qualified professional(s) (e.g., lawyer(s) or chartered accountant(s) qualified to practice in the relevant jurisdiction(s) in question) stating that, in the opinion of the professional in question, the legal entity is considered to be resident for tax purposes in that jurisdiction (or, in cases where deemed tax residence under Rule 4 below is claimed, the basis on which it applies having regard to the precise requirements of Rule 4). In the case of a disregarded entity for United States income tax purposes, a signed statement from an external tax advisor or "C" level officer stating that all of that legal entity's income has been included on the corporate tax return of the parent company in the U.S. will be accepted. This evidence must include the name of the parent entity and evidence relating to the tax declaration made by the parent entity on its behalf.

Rule 4

In the case of a transparent entity, tax residence in another jurisdiction must be demonstrated by reference to each of the participators or partners on whom the legal entity's profits are taxable. "Transparent entity" means a legal entity in respect of which the entire profits and gains are treated under the law of another jurisdiction as attributable to and taxable on some or all of the direct or indirect participators or partners in the legal entity in question.

4.3 The evidence and claim under rules 2, 3 and 5A form part of the prescribed information that is required to be uploaded to the RA database under section 10(3)(h) of the BOSSs Act. All evidence and information provided to the ITA must be provided in English. For any official documentary evidence that is not in English, a certified English translation of that documentary evidence must be provided.

Rule 5

A legal entity whose only sources of income from relevant activities are subject to tax in a jurisdiction outside the BVI will be regarded as resident for tax purposes in that jurisdiction. Therefore, a legal entity cannot be regarded as resident for tax purposes in a jurisdiction that does not have a corporate income tax system. Jurisdiction including:

1) Anguilla;
2) Bahamas;
3) Bahrain;
4) Barbados;
5) Bermuda;
6) Cayman Islands;
7) Turks and Caicos Islands; and
8) United Arab Emirates.

Rule 5A

Entities claiming to be tax resident in Guernsey, Isle of Man or Jersey can only make such a claim if the legal entity is resident for corporate income tax purposes and subject to the relevant corporate income tax law and sufficient proof of this must be provided as follows:

1) **tax assessments, demands, or evidence of payment issued by the competent tax authority of the other jurisdiction;**
2) **tax returns submitted to the competent tax authority of the other jurisdiction;**
3) **confirmation that the entity is required to submit a corporate income tax return to the competent tax authority of the jurisdiction.**

4.4 It is accepted that some jurisdictions charge tax by reference to a criterion other than residence. What matters is whether the tax authority in the jurisdiction in question has accepted that the legal entity (or its participators in the case of a transparent entity) is liable to tax (to the extent that the jurisdiction charges tax on income) in that jurisdiction by reference to the relevant local criteria. By virtue of Rule 5, this may also include situations where all of the legal entity's income from relevant activities is attributable to a branch or other permanent establishment which is regarded as tax resident under the laws of a jurisdiction other than the BVI (provided that the jurisdiction does not appear on the EU list of non-cooperative jurisdictions for tax purposes).

4.5 Economic substance is assessed by reference to financial periods, which will normally be one year in length. Where it is claimed that a legal entity is tax resident in a jurisdiction outside the BVI, it will be necessary to demonstrate this non-residence throughout the financial period under consideration. The financial period may not be the same period as a legal entity's tax accounting period, although the financial period (or the accounting period) can be adjusted so as to bring about that result if that is thought convenient. Some tax documents may relate to fiscal years, or years of assessment, which may be different again from the legal entity's tax accounting period. For a legal entity which is relying on the types of evidence specified in rule 3 or 5A, and that evidence does not relate specifically to the legal entity's financial period, it will usually be necessary to produce further evidence which spans the entire financial period. However, where a legal entity changes its tax residence part way through a financial period (in a manner that would otherwise enable it to qualify as non-resident), the ITA will only expect to see compliance with the applicable economic substance requirements for that part of the relevant financial period during which it did not qualify as non-resident.

Example:

A legal entity has a financial period beginning on 1 January each year. It claims to be tax resident in a jurisdiction whose fiscal year begins on 1 April. It is relying on tax assessments to demonstrate its tax residence. For the financial period commencing 1 January 2021, the legal entity would need to produce a tax assessment for the year of assessment ending on 30 March 2021, and a tax assessment ending on 30 March 2022.

4.5A For the avoidance of doubt withholding taxes are not considered when making a determination of tax residence.

Rule 6

Where a legal entity is unable to provide evidence of the sort required under rules 3 or 5A in respect of any financial period within the reporting period (i.e. 6 months following the end of the legal entity's financial period), the legal entity may apply to be treated as provisionally resident in a jurisdiction outside the BVI pending submission of the evidence required to establish that fact. The ITA shall accede to that application only if one or more of the conditions set out in rule 10 are met. This provisional treatment application must be made before the end of the reporting period.

Rule 7

Where such an application is made, the ITA, if it accedes to the application, must specify a reasonable period within which the necessary evidence is to be submitted ("the provisional extension period").

Rule 8

During the provisional extension period, and during any period prior to the ITA taking a decision, the legal entity shall be treated for the purpose of the economic substance legislation as if it were resident for tax purposes in a jurisdiction outside the BVI.

Rule 9

In the event of the ITA refusing the application for provisional treatment, or in the event of the legal entity failing to supply the necessary evidence within the period fixed under rule 7, the legal entity shall, notwithstanding the provisional treatment afforded under rule 8, be treated as not being non-resident in the BVI throughout the financial period in question.

Rule 10

The conditions for granting provisional treatment as tax resident outside the BVI are as follows:

(1) The legal entity has established its tax residence in the jurisdiction in question for the previous financial period to the satisfaction of the ITA, and certifies that its tax residence has not changed in the intervening period, or

(2) The legal entity supplies (within the reporting period) the most recent available documentary evidence of tax residence in that jurisdiction which complies with the requirements of rules 3 and 5A, and certifies that its tax residence has not changed in the time since the period to which the documentary evidence relates, or

(3) The legal entity evidences either that it has been too recently formed, or that it has too recently assumed tax residence in the jurisdiction in question, for there to be any documentary evidence of its tax residence which satisfies the requirements of rules 3 or 5A, and produces other evidence to demonstrate

that it met the criteria for tax residence in that jurisdiction during the financial period in question.

In each case the evidence in support of the application of the condition must be supplied within the reporting period of the financial period in question.

4.6 Documentary evidence of tax residence will often not be available for an entire financial period until sometime after the financial period has ended, and outside the reporting period. The ITA accepts that this will be the case, and will be prepared to treat the entity as provisionally tax resident outside the BVI during a reasonable period, which the ITA will specify, following the end of the financial period in question, provided certain conditions are met. This "reasonable period" mentioned in rule 7 set by the ITA for a legal entity to submit the evidence required by rules 3 or 5A typically would not extend beyond two financial periods inclusive of the financial period for which the legal entity has applied for provisional treatment in accordance with rule 6. If the necessary documentary evidence is not provided during the specified period, or any extension which the ITA may permit, the legal entity will be treated as having failed to establish tax residence outside the BVI. The ITA will then require it to demonstrate economic substance in BVI in the usual way for that period. If the legal entity cannot do that, it will be subject to enforcement action.

4.7 The conditions for granting provisional treatment as tax resident outside the BVI are set out in rule 10.

4.8 A legal entity which establishes that it is impossible, for the reasons given in rule 10, to produce documentary evidence of its tax residence must produce other evidence to demonstrate that it met the criteria for tax residence in that jurisdiction during the financial period in question. The nature of the evidence to be supplied will depend on the criteria for tax residence laid down by the law of the jurisdiction in question. That evidence must be provided within the information time limit for the financial period in question.

4.9 The provision in rule 5 that a legal entity will be treated as non-resident if all its activities are taxed in another jurisdiction is intended to cater for a legal entity which, for example, is taxed on a branch or agency basis on all its activities in a jurisdiction outside the BVI, even if it is not necessarily tax resident in that jurisdiction.

4.10 It is possible that a legal entity may be tax resident in a jurisdiction subsequently placed on the EU list of non-cooperative tax jurisdictions. The ITA will consider allowing a reasonable time for a legal entity to adjust its business in these circumstances.

4.11 Legal entities should be aware that exchange of information will take place between the BVI and the tax authority of any jurisdiction in which a legal entity claims to be tax resident, as well as with any EU member state where the legal entity has one or more beneficial or legal owners resident.

5. Relevant activities

5.1 The relevant activities to which the economic substance requirements relate are set out in section 6 of the ESA:

> *In this Act, unless the context otherwise requires, "relevant activities" mean any of the following activities:*
>
> *(a) banking business;*
> *(b) insurance business;*
> *(c) fund management business;*
> *(d) finance and leasing business;*
> *(e) headquarters business;*
> *(f) shipping business;*
> *(g) holding business;*
> *(h) intellectual property business;*
> *(i) distribution and service centre business.*
>
> *but does not include investment fund business.*

These are discussed in more detail below.

5.2 Although the two concepts serve distinct purposes under the legislation, and are discussed separately in these rules, there is a clear relationship between a relevant activity and the CIGA which relates to it. The activities which form the CIGA are likely to be the most important activities which a legal entity carrying on the related relevant activity will be undertaking. As such they can assist in an understanding of the scope of the relevant activity itself. In cases of difficulty the ITA will take account of the content of the CIGA in determining whether a particular business comprises a relevant activity.

<u>Banking business</u>

5.3 Banking business is defined in the ESA section 2:

> *"banking business" has the meaning specified in section 2(1) of the Banks and Trust Companies Act, 1990.*

That definition reads as follows:

> *"banking business" means the business of accepting deposits of money which may be withdrawn or repaid on demand or after a fixed period or after notice, by cheque or otherwise and the employment of such deposits, either in whole or in part,*
>
> *(a) in making or giving loans, advances, overdrafts, guarantees or similar facilities, or*
> *(b) the making of investments, for the account and at the risk of the person accepting such deposits.*

5.4 The effect of sections 3 and 4 of the Banks and Trust Companies Act, 1990 is that any legal entity which is either incorporated in the BVI or a foreign entity doing business

in the BVI, which is carrying on banking business must have a license from the FSC, in order to carry on the business lawfully.

5.5 The ITA will adopt any guidance or interpretation issued by the FSC concerning banking business.

Insurance business

5.6 Insurance business is defined in the ESA section 2:

"insurance business" has the meaning specified in section 3(1) of the Insurance Act, 2008

That definition reads as follows:

"Insurance business" means the business of undertaking liability under a contract of insurance to indemnify or compensate a person in respect of loss or damage, including the liability to pay damages or compensation contingent upon the happening of a specified event, and includes life insurance business and reinsurance business.

5.7 Reference should be made to the Insurance Act, 2008 for further definitions of life insurance business and reinsurance business. Section 4(1)(a) requires any person carrying on, or holding himself out as carrying on, insurance business of any kind in or from within the BVI to have a license under section 8 of that Act. A BVI business company is deemed to be carrying on business in the BVI even if its insurance business is in fact located outside the BVI.

5.8 The ITA will adopt any guidance or interpretation issued by the FSC concerning insurance business.

Fund management business

5.9 Fund management business is defined in the ESA section 2:

"fund management business" means the conduct of an activity that requires the legal entity to hold an investment business license pursuant to section 4 and category 3 of Schedule 3 of the Securities and Investment Business Act, 2010.

Category 3 of Schedule 3 of SIBA reads as follows:

Investment Management
Sub-category A: Managing Segregated Portfolios (excluding Mutual Funds)
Sub-category B: Managing Mutual Funds
Sub-category C: Managing Pension Schemes
Sub category D: Managing Insurance Products
Sub-category E: Managing Other Types of Investment.

Reference should be made to SIBA and to the FSC Code for a more detailed understanding of these concepts. It should be noted that management of funds is contrasted with the business of being a custodian of investments, which falls within Category 5 of SIBA.

5.10 The ITA will adopt any guidance or interpretation issued by the FSC concerning Category 3.

Finance and leasing business

5.11 Finance and leasing business is defined in ESA section 3.

(1) In this Act, unless the context otherwise requires, "finance and leasing business" means the business of providing credit facilities of any kind for consideration.

(2) For the purposes of subsection (1) but without limiting the generality of that section
(a) consideration may include consideration by way of interest;
(b) the provision of credit may be by way of instalments for which a separate charge is made and disclosed to the customer in connection with

(i) the supply of goods by hire purchase,
(ii) leasing other than any lease granting an exclusive right to occupy land, or
(iii) conditional sale or credit sale.

(3) Where an advance or credit repayable by a customer to a person is assigned to another person, that other person is deemed to be providing the credit facility for the purposes of paragraph (1).

(4) Any activity falling within the definition of "banking business", "fund management business" or "insurance business" is excluded from the definition in paragraph (1).

5.12 A legal entity which provides credit as an incidental part of a different sort of business will not thereby be treated as carrying on a finance and leasing business. In this context, "incidental" means occasional or minor activity. Thus, for example, a merchant which supplies goods on account, thereby offering short term credit, will not be carrying on a finance and leasing business. Only where the provision of credit can be seen to be a business activity in its own right will the legal entity be treated as if its business, or part of its business, is a finance and leasing business. Legal entities which carry on a factoring activity, by which they purchase and then collect another business's book debts, will be treated as carrying on a finance and leasing business by virtue of subsection (3). The ITA will regard "goods" for the purposes of the ESA as including all kinds of property, excluding immovable property, securities, money or choses in action.

5.13 Legal entities which hold debt or debt instruments for the purpose of investment will not be regarded as being in the business of providing credit facilities.

5.14 Although the activity is described as finance and leasing, the essence of the activity, as the definition makes clear, is the provision of credit facilities for consideration. The scope does not extend to cases where credit is offered and there is no expectation of

receiving consideration from the credit when providing it (e.g., the grant of security). So, the mere fact that a legal entity leases items does not mean it is carrying on a finance and leasing business. So, short-term hiring out of vehicles, boats or equipment is not caught provided that there is no separate credit charge made and disclosed to the customer. Consideration clearly includes interest but also includes any other form of consideration which may generate income for the legal entity (e.g., arrangement or commitment fees or other separate charges for the credit being provided). Where the provision of credit is separated from the consideration received, this may also be in scope (i.e., where a loan advanced for consideration by one company, which is within the scope of this relevant activity, is transferred to a different company which then receives the loan capital payments and consideration).

Example

A legal entity carries on a factoring business, by which it purchases and then collects another business' book debts. The activity falls within the definition of finance and leasing business.

Example

Credit is offered with a grant of security in favour of the lender, but the credit is interest free and there are no lending fees or other consideration. For the avoidance of doubt, the grant of security by any other party in favour of the lender would not constitute consideration.

Headquarters business

5.15 Headquarters business, and the related concept of a "group" are defined in ESA section 2:

"group" has the meaning specified in regulation 2(1) of the BVI Business Companies Regulations, 2012, modified so that references to a company include references to a limited partnership, and other expressions appropriate to companies shall be construed as including references to the corresponding persons, documents or organs, as the case may be, appropriate to limited partnerships;

"headquarters business" means the business of providing any of the following services to an entity in the same group:

- *(a) the provision of senior management;*
- *(b) the assumption or control of material risk for activities carried out by any of those entities in the same group; or*
- *(c) the provision of substantive advice in connection with the assumption or control of risk referred to in paragraph (b),but does not include banking business, financing and leasing business, fund management business, intellectual property business, holding business or insurance business.*

5.16 Regulation 2(1) of the BVI Business Companies Regulations 2012, referred to in the definition of "group" reads as follows:

"group", in relation to a company (the "first company"), means the first company and any other company that is:

(a) a parent of the first company;
(b) a subsidiary of the first company;
(c) a subsidiary of a parent of the first company; or
(d) a parent of a subsidiary of the first company;

5.17 The regulations define "parent" and "subsidiary" as follows:

"parent", in relation to a company (the "first company"), means another company that, whether acting alone or under an agreement with one or more other persons,

(a) holds, whether legally or equitably, a majority of the issued shares of the first company;

(b) has the power, directly or indirectly, to exercise, or control the exercise of, a majority of the voting rights in the first company;

(c) has the right to appoint or remove the majority of the directors of the first company;

(d) has the right to exercise a dominant influence over the management and control of the first company pursuant to a provision in the constitutional documents of the first company; or

(e) is a parent of a parent of the first company;
"subsidiary", in relation to a company (the "first company"), means a company of which the first company is a parent;

5.18 Whether a legal entity carries on headquarters business is not dependent on its position in the group structure. It is entirely dependent on the services it provides to other companies in the group as part of its income-generating activities, whether parents or subsidiaries.

For example:

A group includes, as a subsidiary, a service company which employs all the employees in the group. If senior management in the group are employed by the service company, it will be providing headquarters services to the group.

5.19 The concluding words of the definition of headquarters business make clear that any activity which might otherwise fall within the definition of headquarters' business, but which in fact forms part of another relevant activity, will fall outside the definition of headquarters' business.

For example:

A subsidiary in a group which is a captive insurance company will not also be carrying on headquarters business simply because it assumes material risk on behalf of the group.

A subsidiary in a group which carries on banking business, and is the primary operating company in the group, will not also be carrying on headquarters business simply because the bank's senior management also sit on the board of the top company in the group.

5.20 That said, it is in theory possible for a company to carry on both headquarters business and another form of relevant activity if the activities form two distinct business activities.

For example:

A legal entity carrying on the activity of finance and leasing business may also carry on headquarters business if it also employs, and then supplies to other entities in the group, the senior management of the group as a separate business activity. To be regarded as a separate business and a relevant activity, the activity must be more than occasional or minor transactions within the relevant description which are profit-making, form part of a business and are not merely ancillary to the relevant activity. In such circumstances, the legal entity would be required to comply with the economic substance requirements applicable to each separate relevant activity.

Shipping business

5.21 "Ship" and "shipping business" are defined in ESA section 2 as follows:

"ship" has the meaning specified in section 2(1) of the Merchant Shipping Act, 2001 but does not include a fishing vessel, a pleasure vessel or a small ship (in each case, as defined by section 2(1) of that Act);

"shipping business" means any of the following activities involving the operation of a ship anywhere in the world other than solely within Virgin Islands waters (as defined in section 2(2)(a) of the Merchant Shipping Act, 2001)

- *(a) the business of transporting, by sea, persons, animals, goods or mail;*
- *(b) the renting or chartering of ships for the purpose described in paragraph (a);*
- *(c) the sale of travel tickets or equivalent, and ancillary services connected with the operation of a ship;*
- *(d) the use, maintenance or rental of containers, including trailers and other vehicles or equipment for the transport of containers, used for the transport of anything by sea;*
- *(e) the management of the crew of a ship.*

Reference should be made to the Merchant Shipping Act for the precise definitions of "fishing vessel" and "pleasure vessel". A "small ship" is a ship less than 24 metres in length. For the purposes of construing the "pleasure vessel" definition in the context of

the ESA, the ITA considers "shareholders of the body corporate" includes direct and indirect shareholders (i.e., beneficial owners). "Pleasure vessels" are acquired and used by their owners, disponent owners or charterers for the sport or pleasure of the shareholder/ultimate beneficial owner, employees, officers or charterers and their respective family and friends and are not operated as a genuine commercial enterprise. The function of chartering a pleasure vessel serves only to defray the costs of owning and operating the vessel. Hence, the ownership, chartering and operation of a "pleasure vessel" as defined in the Merchant Shipping Act does not fall within the definition of shipping business. Likewise, a charter by demise or bareboat charter for sport or pleasure by the charterer, their family or friends does not constitute shipping business. As a result, the ownership, operation or chartering of yachts, whether used privately or chartered, does not fall within the definition of shipping business and as such the owners or operators of same are not required to meet the economic substance requirements.

5.22 Each of the activities has to "involve the operation of a ship" if it is to constitute a relevant activity. However, the ship does not have to be operated by the same legal entity as the legal entity carrying out the activities listed at (a) to (e).

5.23 The ITA will always consider whether activities which may appear to fall within the letter of paragraphs (a) to (e) do in fact constitute a shipping business, or whether they are merely incidental activities to what is properly regarded as a different sort of business. The content of the CIGA for a shipping business (see below) is of particular relevance here.

For example:

A legal entity which carries on the business of a general travel agent will not be treated as carrying on a shipping business merely because, amongst other things, it sells tickets for passenger cruises.

A legal entity which manufactures goods for export will not be treated as carrying on a shipping business merely because it arranges for those goods to be dispatched by sea, in containers or otherwise.

Holding business

5.24 "Holding business" and the related term "pure equity holding entity" are defined in ESA section 2 as:

"holding business" means the business of being a pure equity holding entity
"pure equity holding entity" means a legal entity that only holds equity participations in other entities and only earns dividends or capital gains.

5.25 The definition of pure equity holding entity is deliberately framed in narrow terms. A legal entity will only fall within the definition if it holds nothing but equity participations, yielding dividends or capital gains. The ownership of any other form of investment (such as an interest-bearing bond) will take the legal entity outside this definition.

5.26 Equity participation includes shares in a company and encompasses other forms of investment in a legal entity which give the investor the right to participate in the profits of the legal entity. The interest of a limited partner in a limited partnership will usually be of this quality.

5.27 Legal entities which own other forms of asset (e.g., bonds, government securities, legal or beneficial interests in real property) will clearly not be pure equity holding entities (even if they also own equity participations) and will not be treated as carrying on holding business.

5.28 A legal entity which holds assets other than equity participations or carries on other business activities must always consider whether it carries on another relevant activity. Where a legal entity undertakes other activities or earns income other than dividends and capital gains, it is outside the scope of the pure equity holding entity business definition and instead will need to meet the higher substance requirements, if applicable, for any relevant activity it carries on.

Example:

ShipServices Ltd is an intermediary holding company in an international shipping group which holds equity participations in various subsidiaries but also provides ancillary services connected with the operation of large ships owned by such subsidiaries, for which it receives quarterly fees. ShipServices Ltd's business is not that of a pure equity holding entity but the business activity of supplying the shipping-related services falls within the definition of shipping business.

Example:

Trustee Ltd acts as trustee to number of trusts, holding trust assets in its fiduciary capacity under the terms of the trusts. As Trustee Ltd provides trust services and is not the beneficial owner of the assets, it will not be a holding business (but should consider whether it carries out any other relevant activities for its own account, not acting as trustee).

Example:

InvestCo Ltd has a brokerage account. The brokerage account only holds equity participations in underlying entities. InvestCo Ltd is not a pure equity holding entity because its only asset is a claim against the broker. It does not directly hold or manage equity participations; these are held by the broker.

5.29 Legal entities which hold assets which consist of or include assets which are not equity participations will not be pure equity holding entities, but likewise may be found to carry on other relevant activities.

Intellectual property business

5.30 "Intellectual property business" and the related concept of "intellectual property asset" are defined in ESA section 2 as follows:

"intellectual property business" means the business of holding intellectual property assets;

"intellectual property asset" means any intellectual property right in intangible assets, including but not limited to copyright, patents, trademarks, brand, and technical know-how, from which identifiable income accrues to the business (such income being separately identifiable from any income generated from any tangible asset in which the right subsists);

"Income" in respect of an intellectual property asset is defined in ESA section 2 as follows:

"income" in respect of an intellectual property asset includes:

(a) royalties;
(b) capital gains and other income from the sale of an intellectual property asset;
(c) income from a franchise agreement; and
(d) income from licensing the intangible asset;

5.31 Most legal entities will own some form of intellectual property (such as trademark protection, copyright in their advertising material and technical know-how relating to their processes) and will receive income from an intellectual property asset in a number of different scenarios:

Example:

A legal entity holds a brand, the rights of which are licensed to others in return for a license fee. The activity falls within the definition of an intellectual property business.

Example

A legal entity manufactures and markets a trademarked product to unrelated third parties. The legal entity is not an intellectual property business because its income is derived from the sale of finished goods to third parties, not the exploitation of intellectual property assets. The use of the trademark is an adjunct to the business.

Example

A legal entity has developed IT software that it holds and uses within its own business for online marketing and also licenses others to use the software within their online marketing business. The users pay a license fee in order to use the copyrighted software. The activity falls within the definition of an intellectual property business.

Example

A legal entity has developed IT software and manufactures computers which it sells to consumers. The consumers pay a license fee for the use of the software which is included within the purchase price of the computer although the license fee is not visible to the consumer. The activity would fall within the definition of intellectual property business.

5.32 Appropriate action will be taken against any legal entity which seeks to manipulate its income to avoid being subject to substance requirements by, for example, disguising royalties as part of sales income.

Distribution and service centre business

5.33 "Distribution and service centre business" is defined in ESA section 2 as follows:

"distribution and service centre business" means the business of either or both of the following:

(a) purchasing from foreign affiliates
(i) component parts or materials for goods; or
(ii) goods ready for sale;
and reselling such component parts, materials or goods;

(b) providing consulting or administrative services to foreign affiliates,
but does not include any activity included in any other relevant activity except holding business;

5.34 "Affiliate" is defined in ESA section 2 as follows:

"affiliate" bears the same meaning as an "affiliated company" specified in regulation 2(2) of the BVI Business Companies Regulations, 2012, modified so that references to a company include references to a limited partnership, and other expressions appropriate to companies shall be construed as including references to the corresponding persons, documents or organs, as the case may be, appropriate to limited partnerships;

Regulation 2(2) of the BVI Business Companies Regulations provides as follows:

… a company is affiliated with another company if it is in the same group as the other company

5.35 For a legal entity to carry on distribution and service centre business it must have a business which consists of purchasing assets from other entities in the same group, and/or a business providing services to entities in the same group. The affiliates in question must be "foreign" – that is to say an affiliate which is an entity which is incorporated, registered or formed outside the BVI unless it is registered in the BVI.

5.36 It should be noted that the following do not constitute distribution and service centre business:

(a) the business of purchasing and reselling assets from, or providing services to, entities in the same group both of which are located in the BVI,

(b) the business of purchasing and reselling assets from, or providing services to, entities which are not part of the same group as the entity carrying on the business, even if located outside the BVI, or

(c) occasional or minor transactions within the description which do not form part of a business but are undertaken ancillary to a different business and such other activity is recharged at cost or less i.e., the legal entity does not profit from the other activity. (If the entity's business falls within the description of a relevant activity, substance requirements would apply in respect of that relevant activity.).

Example of (c)

ABC Ltd is the service company for a construction group whose main activity is to provide construction services to customers in the BVI. ABC Ltd employs the staff and owns premises used for its business. DEF, another group company based in South America, has a one-off request for quantity surveying skills that certain of ABC employees have although ABC Ltd is not in the business of quantity surveying. DEF has requested those quantity surveying skills for a period of 1 month, agreeing to reimburse costs. As ABC Ltd is not in the business of providing quantity surveying services to other group companies, nor does it offer/solicit such services or maintain employees to provide such services, ABC Ltd is not considered to be providing services and is therefore not conducting the relevant activity.

5.37 Transactions which fall within any other type of relevant activity, as well as being capable of being distribution and service centre business, will be treated as falling within that other activity, and will not be treated as distribution and service centre business. Thus, for example, the provision, by way of business, of banking, insurance or shipping services to foreign affiliates will be treated as banking, insurance or shipping business, not distribution and service centre business. The exception to this rule is holding business, to which special considerations apply as set out above and in Part 8 below.

6. Core income generating activity

6.1 A legal entity which carries on one or more relevant activities must conduct CIGA in the BVI relating to each such activity (ESA section 8(1)(c)). This requirement does not apply to a holding business (ie the business of being a pure equity holding entity). CIGA are any activities of the legal entity that are of central importance to a relevant activity in terms of generating relevant income. This CIGA, in order for the legal entity to meet the economic substance requirement, must be carried out in the BVI.

6.2 Section 7 of the ESA defines CIGA as including the following:

(a) in respect of banking business

(i) raising funds, managing risk including credit, currency and interest risk;
(ii) taking hedging positions;
(iii) providing loans, credit or other financial services to customers;
(iv) managing regulatory capital;
(v) preparing regulatory reports and returns;

(b) in respect of distribution and service centre business

(i) transporting and storing goods;
(ii) managing stocks;
(iii) taking orders;
(iv) providing consulting or other administrative services;

(c) in respect of insurance business

(i) predicting and calculating risk;
(ii) insuring or re-insuring against risk;
(iii) providing insurance business services to clients;

(d) in respect of fund management business

(i) taking decisions on the holding and selling of investments;
(ii) calculating risks and reserves;
(iii) taking decisions on currency or interest fluctuations and hedging positions;
(iv) preparing relevant regulatory or other reports for government authorities and investors;

(e) in respect of finance or leasing business

(i) agreeing funding terms;
(ii) identifying and acquiring assets to be leased (in the case of leasing);
(iii) setting the terms and duration of any financing or leasing;
(iv) monitoring and revising any agreements;
(v) managing any risks;

(f) in respect of headquarters business

(i) taking relevant management decisions;
(ii) incurring expenditures on behalf of affiliates;
(iii) co-ordinating group activities;

(g) in respect of shipping business

(i) managing the crew (including hiring, paying and overseeing crewmembers);
(ii) hauling and maintaining ships;
(iii) overseeing and tracking deliveries;

(iv) determining what goods to order and when to deliver them;
(v) organising and overseeing voyages;

(h) in respect of intellectual property business

(i) where the business concerns intellectual property assets such as patents, research and development;
(ii) where the business concerns non-trade intangible assets such as brand, trademark and customer data, marketing, branding and distribution.

6.3 The definition of core income generating activity is non-exclusive. CIGA "includes" the activities listed but is not confined to them. What constitutes the CIGA of a particular activity is a fact sensitive issue which can vary from business to business. In some cases, it may be possible to carry on a relevant activity without also conducting all the related core income generating activities listed in the statute.

6.4 CIGA indicates that income must flow from the activity and the ITA will consider the level of income generated when evaluating whether or not a legal entity meets substance in the BVI. A legal entity which carries on a relevant activity, but which has no gross income from such activity in a specific financial period will not be expected to meet the economic substance requirements in respect of that relevant activity and financial period but will still be required to satisfy its notification and reporting requirements (i.e., the reporting expected will be akin to a "nil report").

7. Substance requirements - general

7.1 Section 8 of the ESA sets out the requirements which must be met if a legal entity is to have economic substance. Subsection (1)(a) to (d) sets out the requirements for relevant activities other than pure equity holding entities. This Part deals with these requirements. Part 9 sets out the requirements for pure equity holding companies. Part 16 considers how these requirements should be applied in the context of limited partnerships.

7.2 Subsection (1) reads as follows:

(1) Subject to subsection (2), a legal entity complies with the economic substance requirements if:

(a) the relevant activity is directed and managed in the Virgin Islands;

(b) having regard to the nature and scale of the relevant activity

(i) there are an adequate number of suitably qualified employees in relation to that activity who are physically present in the Virgin Islands (whether or not employed by the relevant legal entity or by another entity and whether on temporary or long-term contracts);

(ii) there is adequate expenditure incurred in the Virgin Islands;

(iii) there are physical offices or premises as may be appropriate for the core income-generating activities; and

(iv) where the relevant activity is intellectual property business and requires the use of specific equipment, that equipment is located in the Virgin Islands;

(c) the legal entity conducts core income-generating activity in the Virgin Islands;

(d) in the case of income-generating activity carried out for the relevant legal entity by another entity

(i) no core income generating activity is carried on outside the Virgin Islands;

(ii) only that part of the activities of that other entity which are solely attributable to generating income for the relevant legal entity and not for any other legal entity shall be taken into account when considering if the relevant legal entity meets the economic substance requirements;

(iii) the relevant legal entity is able to monitor and control the carrying out of that activity by the other entity.

7.3 There are therefore three general aspects to economic substance under subsection (1):

(a) direction and management in the BVI,

(b) adequate expenditure and employees and appropriate premises in the BVI, and

(c) CIGA carried on in the BVI.

While each of these requirements must be fulfilled, there is a degree of overlap between them, and compliance with the economic substance requirements will require a judgment which takes account of the degree of compliance under each of these three heads. Each head will be discussed in turn. The impact of outsourcing is then considered.

<u>Direction and management in the BVI</u>

7.4 It should be noted that what is required is that the relevant activity is directed and managed in the BVI, not the legal entity which carries on the relevant activity. Strategic decisions for the relevant activity are required to be taken in the BVI in order to meet the requirement for direction and management under 7.3(a). Where the legal entity's only business is the relevant activity or activities in question, then that will mean that the legal entity itself must be directed and managed from the BVI. Strategic decisions as to management of the legal entity, where the legal entity's only business is the relevant activity, will be expected to be taken by the Board in the BVI.

7.5 For the relevant activity to be directed and managed from the BVI there must be an adequate number of board meetings held in the BVI, having regard to the actual frequency of meetings required for the relevant activity, the nature of the relevant activity, and its importance in the overall business of the legal entity (although it is not necessary for all meetings to be held in the BVI). For a board meeting to be held in the BVI there must be a quorum of directors physically present in the BVI. The directors of the legal entity attending such meetings must include among their number adequate expertise to direct the relevant activity. Decisions of the Board regarding the relevant activity must be minuted, and minutes of those decisions are expected to be kept in the BVI. In the case where there are corporate directors, the requirements will apply to the individual(s) (i.e., the authorised representatives or officers of the corporate director) actually performing the duties.

Adequate expenditure, adequate number of suitably qualified employees and appropriate premises in the BVI

7.6 There are no definitions of the words "adequate", "suitable" or "appropriate", which must be given their ordinary English meaning. For these purposes, the ITA considers that "adequate" means "as much or as good as necessary for the relevant requirement or purpose" and "suitable" and "appropriate" mean "suitable or fitting for a particular purpose, person or occasion". What is adequate or appropriate will be dependent on the particular facts of the entity and its business activity. As such, the directors (or equivalent) of the entity should address their minds to these questions and make their determination in good faith. A legal entity must ensure that it maintains and retains appropriate records to record the basis on which it reached its determination of its status under the ESA and to demonstrate the adequacy, appropriateness or suitability of the resources utilized and expenditures incurred.

7.7 Businesses come in different sizes, and the employees, expenditure and premises which are adequate or appropriate for a small business will not suffice for a large business. Nor is it the function of the legislation to require an entity to incur more expenditure or engage more employees than it really needs, if it is genuinely carrying on a relevant activity and carrying on CIGA in the BVI with the expenditure, staff and premises that it actually has.

Rule 11

The expression "expenditure" where it is used in section 8 of the ESA and section 10 of the BOSSs Act means expenditure incurred in the operation of the relevant activity.

7.8 Expenditure can only be taken account of if it is incurred in the operation of the relevant activity.

7.9 Normally, if a business is carrying on a relevant activity, and all, or substantially all, of its expenditure is in the BVI, and all or substantially all of its employees work in the BVI, the adequacy of its expenditure and employees will be self-evident. However, the ITA will be concerned to ensure that the business is not relying unduly on expenditure incurred, or employees based, outside the BVI, in order to enable its relevant activity and CIGA to be carried on in the BVI. Thus, the amount of expenditure incurred, and the number of employees (and their qualifications) employed globally in the relevant

activity, will be highly relevant to the question whether expenditure and employment in the BVI is or is not adequate.

7.10 Where a legal entity outsources part of its relevant activity, and that work meets the requirements for outsourcing, the expenditure on the outsourcing will be taken into account when assessing the adequacy of the legal entity's expenditure in the BVI.

7.11 The following rules clarify how to compute the number of employees for the purpose of section 8(1).

Rule 12

For the purpose of section 8 of the ESA, the number of employees engaged in a relevant activity shall be computed on the basis that:

(i) an employee who has worked for only part of the financial period in question shall be counted as part of an employee, proportionate to the amount of time he has worked during the financial period,

(ii) a part-time employee shall be counted as part of an employee proportionate to the amount of time he has worked in the financial period when compared with a full-time employee of equivalent grade.

(iii) where an employee spends only part of his time working in connection with the relevant activity in question and part of his time working in connection with other activities, he shall be treated as a part-time employee, as regards the amount of time spent on the relevant activity.

(iv) An employee who is based in the BVI may be treated as physically present in the BVI throughout the period of his employment, notwithstanding that part of his duties fall to be performed outside the BVI.

(v) An employee who is not based in the BVI may not be treated as physically present in the BVI at any time notwithstanding that part of his duties fall to be performed within the BVI.

(vi) For the purpose of paragraphs (iv) and (v), an employee will be treated as based in the BVI if he spends the majority of his working time in the BVI.

7.12 In order to count as an employee for the purpose of section 8(1), it is not necessary that the individual be an employee of the legal entity carrying on the relevant activity. But that individual must be the employee of somebody and must be managed as an employee by the legal entity in question. This means that, for example, a business which has engaged staff employed by an agency (perhaps for temporary cover) can count those staff as part of its employees.

7.13 Where a legal entity outsources part of its relevant activity, and that work meets the requirements for outsourcing, the extent of the work done under the outsourcing arrangement will be taken into account when assessing the adequacy of the number of the entity's employees, and the suitability of their qualifications. The more work is outsourced, the fewer the number of employees which need to be employed "in house" in order to have an adequate number of employees.

7.14 Rule 12 (i) to (iii) set out the approach to computing the number of employees in relation to a relevant activity in situations where the employee does not work solely in

connection with the relevant activity. The RA database allows the RA to enter a decimal to reflect where an employee does not work solely in relation to a relevant activity. The number of employees must NOT be entered as 1 where the employee is not a full time.

7.15 Rule 12 (iv) to (vi) set out the approach to computing the number of employees in relation to a relevant activity where part of the employee's time is spent outside the BVI. As long as most of the employee's working time is spent within the BVI, the fact that his employment in connection with the relevant activity takes him outside the BVI (e.g., a sales representative, or a professional person who visits clients overseas) will not prevent the whole of his employed time being counted as within the BVI. But occasional work in the BVI by an employee based outside the BVI cannot be counted.

7.16 The requirement for employees to be suitably qualified is intended to ensure that the qualifications of employees in the BVI are commensurate with the relevant activity, and the CIGA, being carried on in the BVI. Thus, it would not be sufficient to show that the bulk of the employees employed in connection with the relevant activity are based in the BVI, if the only employees with the technical qualifications actually to manage or transact the relevant activity are based overseas.

7.17 The legal entity must have appropriate premises in the BVI for the carrying out of the CIGA related to the relevant activities. For an office-based business this should comprise an office premises from which the employees can operate. Account will be taken, where appropriate, of flexible working practices (provided that the homes or premises from which employees work when not in the office must themselves be in the BVI if time spent working there is to be counted). Some types of relevant activity (e.g., shipping and distribution and service centre business) will, in addition to office premises, require appropriate premises for non-office-based activities (e.g., ship maintenance or warehousing).

7.18 The premises need not be owned by the legal entity – they may be rented or used on license.

<u>Conducting core income-generating activity in the BVI</u>

7.19 The legal entity must conduct CIGA in the BVI. It is not necessary for a legal entity to perform all the CIGA listed in the legislation for a particular sector, but it must perform the CIGA that generates the income it has. CIGA will be carried on in the BVI if it is carried on by employees working in the BVI or is outsourced to a person whose own employees work in the BVI. As discussed above, the level of expenditure in BVI must be proportionate to the activities of the entity.

7.19A The ITA will take account of evidence regarding normal business practices for a particular relevant activity which are permitted in other jurisdictions subject to the FHTP's "substantial activities" requirements for preferential regimes. This may include, for example, where there are commercial (i.e., non-tax related) reasons for cross-border business to be conducted outside the jurisdiction or to acquire or utilise specialist goods or services available exclusively in a particular location or to serve clients or to deal with counterparties necessarily located outside the BVI. Such activities may be permitted outside of the BVI, provided that CIGA is undertaken in the BVI.

Example:

The master of a ship may perform some activities which are ancillary to or in support of the management of crew for shipping entities.

A fund manager in the BVI may appoint and oversee sub-managers or advisors in jurisdictions outside the BVI to advise on jurisdiction-specific risks or to hold or sell investments in other jurisdictions and provide reports, all in furtherance of the overall strategic risk investment decisions taken by the fund manager in the BVI, and in support of the preparation of reports by the fund manager in the BVI in connection therewith.

Outsourcing

7.20 It is recognised that many entities outsource at least part of their operations to a third party. There is nothing inherently objectionable in entities doing this. However, outsourcing may not be done in such a way that will pose a risk to the substance requirements.

7.21 ESA section 8(1)(d) is intended to address these risks, by permitting an entity to outsource income-generating activity to a third party, but only if certain conditions are satisfied. The first is that no part of the entity's CIGA may be outsourced outside the BVI – that requirement is designed to counter risk (i) above. The second is that when considering the extent of the outsourcing legal entity's economic substance in BVI, it can only count the work done by the entity to which work is outsourced which actually relates to the outsourcing legal entity.

Example

A BVI company with 5 employees carries out outsourced work for 5 other BVI legal entities carrying on relevant activities. Assuming the amount of work done for each legal entity is the same, each of the legal entities can claim that the outsourced work is being done by the equivalent of one employee. Section 8(1)(d)(ii) prevents each of the legal entities claiming that the company is doing work equivalent to 5 employees.

7.22 The requirement that the legal entity is able to monitor the outsourced activity (with that monitoring being undertaken in the BVI) is designed to ensure that there is genuine outsourcing, with work genuinely being done on behalf of the legal entity which has commissioned the outsourcing. A legal entity may outsource activities which are not CIGA to service providers which are located outside the BVI. Such activities may include, for example, back-office or general support functions, IT, payroll, HR, legal services, or other expert advice or specialist services provided that, in each case, they are not of central importance to the legal entity in terms of generating the gross income from the relevant activity.

7.23 A legal entity conducting a regulated activity under license from the FSC must comply with any relevant restrictions on outsourcing imposed by that license, or by the relevant financial services law, in addition to the requirements set out above under the ESA (including any Rules or Regulations made under it).

8. Substance requirements – pure equity holding entities

8.1 The substance requirement for a pure equity holding entity is outlined in section 8(2) provides as follows:

> *(2) 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, has adequate substance if it*
>
> *(a) complies with its statutory obligations under the BVI Business Companies Act, 2004 or the Limited Partnership Act, 2017 (whichever is relevant);*
>
> *(b) has, in the Virgin Islands, adequate employees and premises for holding equity participations and, where it manages those equity participations, has, in the Virgin Islands, adequate employees and premises for carrying out that management.*

8.2 For a pure equity holding entity there is no requirement that the entity is directed or managed in the BVI. Nor is there a requirement that the entity carries on CIGA in the BVI (there is no CIGA relating to holding business), although it remains necessary to have in the BVI adequate employees and premises for holding or managing its equity participations.

8.3 Condition (a) is met by complying with the legislative requirements imposed by the Business Companies Act or the Limited Partnerships Act, 2017 as appropriate.

8.4 What is required for compliance with condition (b), as with economic substance generally, will be a fact sensitive question, dependent on the nature of the activity being carried on. At one extreme, the requirement for being a pure equity holding entity is simply holding equity participations. If this is all the legal entity does during a given financial period, the relevant activity will be entirely passive in nature and the requirements for adequate and suitably qualified employees and for appropriate premises will be applied accordingly. Any legal entity will of course retain the services of a RA, and the performance of those services will be taken into account when assessing economic substance for pure equity holding entities.

8.5 On the other hand, the legal entity may actively manage its equity participations, in which case it should have adequate and suitably qualified employees, and appropriate premises, in the BVI to carry out this function.

9. Intellectual property business - presumptions against compliance

9.1 Income derived from intellectual property assets can pose a higher risk of artificial profit shifting than non-IP assets. This higher risk is reflected in the presumptions of non-compliance with the economic substance requirements which apply in the two scenarios identified in ESA section 9(2).

9.2 Those presumptions are rebuttable and are intended to serve the purpose of addressing the higher risk of artificial profit shifting, whilst not inadvertently prohibiting activities

that constitute real economic activity. What is required to rebut those presumptions is set out below.

ESA section 9(2)(a)

9.3 The principal core income-generating activities associated with intellectual property business are as follows (as set out in ESA section 7(h)):

(i) where the business concerns intellectual property assets such as patents, research and development;

(ii) where the business concerns non-trade intangible assets such as brand, trademark and customer data, marketing, branding and distribution.

9.4 ESA section 9(2)(a) establishes the following presumption:

There is a presumption that a legal entity does not conduct core income-generating activity if

(a) the activities being carried on from within the Virgin Islands do not include any of the activities identified in section 7(h)

9.5 That presumption (where it applies) may be rebutted in the circumstances described in ESA section 9(3):

The presumption in subsection (2)(a) may be rebutted where the activities being carried on from within the Virgin Islands include

(a) taking the strategic decisions and managing (as well as bearing) the principal risks relating to the development and subsequent exploitation of the intangible asset generating income;

(b) taking the strategic decisions and managing (as well as bearing) the principal risks relating to acquisition by third parties and subsequent exploitation of the intangible asset;

(c) carrying on the underlying trading activities through which the intangible assets are exploited and which lead to the generation of revenue from third parties.

9.6 In determining whether the presumption has been rebutted, the ITA will need to be satisfied on the basis of the information provided by the entity that the activity taking place in the BVI is more than local staff passively holding intangible assets whose creation and exploitation is a function of decisions made and activities performed outside of the jurisdiction. Equally, periodic decisions of non-resident board members will not suffice. Instead, the legal entity must employ local, permanent and qualified staff who make active and ongoing decisions in relation to the generation of income in the BVI.

ESA section 9(2)(b)

9.7 ESA section 9(2)(b) establishes the following presumption:

> *There is a presumption that a legal entity does not conduct core income-generating activity if*
> …
> *(b) the legal entity is a high-risk IP legal entity.*

9.8 A "high risk IP legal entity" is defined in ESA section 2 as:

> *a legal entity which carries on an intellectual property business and which*
>
> *(a) acquired the intellectual property asset*
>
> *(i) from an affiliate; or*
> *(ii) in consideration for funding research and development by another person situated in a country or territory other than the Virgin Islands; and*
>
> *(b) licences the intellectual property asset to one or more affiliates or otherwise generates income from the asset in consequence of activities (such as facilitating sale agreements) performed by foreign affiliates*

9.9 There is a high evidential threshold for rebutting this presumption. As set out in ESA section 9(4):

> *The presumption in subsection (2)(b) may be rebutted where a high degree of control over the development, exploitation, maintenance, enhancement and protection of the intellectual property asset is exercised by suitably qualified employees of the relevant legal entity who are physically present and perform their functions from within the Virgin Islands and who are on long-term contracts.*

In addition, the Economic Substance (Companies and Limited Partnerships) Act, 2018 (Intellectual Property Business Requirements) Regulations, 2019 provide as follows:

> *The requirements imposed by section 9(4) of the [ESA] on a high-risk IP legal entity in order for it to rebut the presumption set out in section 9(2) of the [ESA] must be satisfied not only at the point in time at which the legal entity seeks to rebut the presumption but also during any historic periods when the legal entity was carrying on the intellectual property business in question.*

9.10 In determining whether the presumption has been rebutted, the ITA will take into account the same factors which it takes into account when determining whether the presumption under ESA section 9(2)(a) has been rebutted. In addition, the ITA will need stronger evidence of the decision-making, which is taking place in the BVI, and that there is (and historically has been) a high degree of control over the development, exploitation, maintenance, enhancement and protection of the intangible asset.

10. Financial periods

10.1 The concept of "financial period" for the purposes of ESA is important in three respects:

(1) Economic substance is assessed by reference to financial periods. In particular, the question of whether an entity is required to comply with the economic substance requirements depends on whether it has carried on a relevant activity during a financial period (see ESA section 5(1)). Further, the issue of whether a legal entity has complied with the economic substance requirements is determined by reference to its activities (including its turnover, expenditure, staff, premises, location of equipment, and direction and management) over the course of a financial period.

(2) The trigger for the commencement of a legal entity's obligations to comply with the provisions of the ESA is the start of its first financial period.

(3) Time starts to run for the purposes of a legal entity's periodic reporting obligations from the end of the financial period (see section 9(6A) of the BOSSs Act).

10.2 "Financial period" is defined in ESA section 4(1) as follows:

In this Act, unless the context otherwise requires, "financial period" means

(a) in the case of a company incorporated on or after 1 January 2019, such period of not more than one year from the date of incorporation as the company shall notify to the competent authority and thereafter each successive period of one year running from the end of that period;

(b) in the case of a limited partnership with legal personality formed on or after 1 January 2019, such period of not more than one year from the date of formation as the limited partnership with limited personality shall notify to the competent authority and thereafter each successive period of one year running from the end of that period;

(c) subject to paragraphs (d) and (e), in any other case such period of one year commencing on a date no later than 30 June 2019 as the legal entity shall notify to the competent authority and thereafter each successive period of one year running from the end of that period;

(d) in the case of a limited partnership without legal personality formed prior to 1 July 2021, such period of one year commencing on a date no later than 1 January 2022 as the limited partnership without legal personality shall notify to the competent authority and thereafter each successive period of one year running from the end of that period; and

(e) in the case of a limited partnership without legal personality formed on or after 1 July 2021, such period not more than one year from the date of formation as the limited partnership without legal personality shall

notify to the competent authority and thereafter each successive period of one year running from the end of that period.

10.3 As can be seen from this definition, for existing legal entities, there is a certain amount of flexibility as to when the first financial period begins, save that it must have begun no later than 30 June 2019 (or 1 January 2022, the case of a pre-existing limited partnership without legal personality). The rules for notification are as follows:

10.4 Under section 4(1)(a) of the ESA, the first financial period of a legal entity that has been incorporated on or after 1 January 2019 shall begin on its date of incorporation and end one year later. The legal entity may alter the length of that financial period by giving notice to the ITA. Any notice to alter the length of that first financial period must be given in line with Rule 13.

Rule 13

A legal entity which wishes to give notice to the ITA to alter its first financial period in line with 10.4 must give such notice to the ITA within three months of the date of incorporation. Such a legal entity may not elect to terminate its first financial period on a date prior to the date of the notice.

10.5 Under section 4(1)(b) of the ESA, the first financial period of Limited Partnership with legal personality formed on or after 1 January 2019 shall begin on its date of formation and end one year later. The Limited Partnership with legal personality may later the length of that financial period by giving notice to the ITA. Any notice to alter the length of that first financial period must be given in line with Rule 14.

Rule 14

A legal entity which wishes to give notice to the ITA to alter its first financial period in line with 10.5 must give such notice to the ITA within 3 months of the date of its formation. Such a legal entity may not elect to terminate its first financial period on a date prior to the date of the notice.

10.6 Under section 4(1)(c) of the ESA, the first financial period of a Company or Limited Partnership with legal personality incorporated or formed before 1 January 2019 shall begin on a date no later than 30 June 2019 as the Company or Limited Partnership with legal personality shall notify the ITA. Rule 15 provides clarity on the first financial period of a Company or Limited Partnership with legal personality incorporated or formed before 1 January 2019.

Rule 15

A legal entity which wishes to provide a notification to the ITA on the beginning of its first financial period in line with 10.6 shall do so by 31 December 2019. Such a legal entity may not elect to commence its first financial period on a date prior to 1 January 2019. Where such a notification has not been received the first financial period of the legal entity shall begin on 30 June 2019 and shall end one year later.

10.7 Under section 4(1)(d) of the ESA, the first financial period of a Limited Partnership without legal personality formed prior to 1 July 2021 shall be a date no later than 1 January 2022 as the Limited Partnership without legal personality shall notify the ITA.

Rule 16

A legal entity which wishes to provide a notification to the ITA on the beginning of its first financial period in line with 10.7 shall do so by 31 December 2023. Such a legal entity may not elect to commence its first financial period on a date later than 1 January 2022. Where such a notification has not been received the first financial period of the legal entity shall begin on 1 January 2022 and shall end one year later.

10.8 Under section 4(1)(e) of the ESA, the first financial period of a Limited Partnership without legal personality formed on or after 1 July 2021 shall begin on the date of formation and end one year later unless the Limited Partnership without legal personality notifies the ITA that they would like to alter the end of their first financial period.

Rule 17

A legal entity which wishes to give notice to the ITA to alter its first financial period in line with 10.5 must give such notice to the ITA within 3 months of the date of its formation. Such a legal entity may not elect to terminate its first financial period on a date prior to the date of the notice.

Rule 17A

Any notice given under rules 13, 14, 15, 16 and 17 must, in addition to stating the date when its first financial period is to commence or, as the case may be, end, include the following information:

(a) Its registered name;
(b) Its registered number;
(c) Its date of incorporation or formation (as appropriate);
(d) The name and address of its RA;
(e) Brief reasons for the change in financial period, (where a notification is required under the ESA no reason is required).

10.9 A response to a notification will only be given by the ITA where information is missing, or the ITA requires further information from the legal entity concerning the alteration of its financial period. Legal entities must be in a position to comply with the requirements of the ESA as from the specified or deemed date of commencement of their first financial period.

10.10 A legal entity can at any time apply to alter its financial period. For example, it may wish to do so to bring its financial period into line with its tax accounting period. The power to make such an application is conferred by ESA section 4(2), which provides as follows:

On an application by the legal entity the competent authority may permit an alteration in the legal entity's financial period by shortening or (where the legal entity's existing financial period is less than 12 months) lengthening a financial period so as to alter the commencement date for successive financial periods but so that no such altered period shall exceed twelve months in length.

Rule 18

An application by a legal entity to alter any other financial period (except its first financial period) should be made by way of notice to the ITA containing the following information:

(a) Its registered name;
(b) Its registered number;
(c) The name and address of its RA;
(d) The current commencement date of its next financial period;
(e) The proposed new commencement date of its next financial period; and
(f) Brief reasons for the proposed alteration in the commencement date.

10.11 A notice to the ITA under Rule 18 must be made before the end of the financial period of the legal entity. Where this notice would negatively affect the 6 month filing period of the legal entity (i.e. the legal entity would not be able to complete a filing because the timing of the alteration and its effect on the reporting period) the ITA will not accept the application. The ITA is likely to accede to an application by an entity to alter its financial period, provided that the effect of the alteration is not to extend the length of the financial period beyond 12 months. It is only in limited circumstances that the ITA is likely to refuse such an application. Such circumstances include where the ITA is of the view that the entity is seeking to alter its financial period with a view to enabling itself to avoid the application of the economic substance legislation.

10.12 It is possible that a legal entity will only start a relevant activity part way through a financial period. That is especially likely to be true for new legal entities, which will typically have a period of minimal activity between date of incorporation or formation and commencing to do business. In those circumstances the economic substance requirements will only apply for that part of the financial period during which the relevant activity is being conducted.

10.13 It is expected that the economic substance requirements will be complied with during the time the entity is in liquidation. If all the legal entity is doing is passively receiving income during the relevant financial period, the degree of economic substance required will be assessed accordingly. If a legal entity is in liquidation or is being wound up, it must continue to comply with any applicable economic substance requirements under the ESA for any financial period during which it carries on relevant activities but is not required to satisfy economic substance requirements after it ceases to carry on relevant activities (for example, where the business constituting relevant activity has ceased and no further gross income is being received from such activity for the purposes of rule 1). Any liquidators (or equivalent) or other representatives of a legal entity who were responsible for the entity's liquidation or dissolution have duties to maintain the entity's records and to respond to the ITA's information requests under section 11 of the ESA. The ITA will generally expect such records to be maintained for no less than six years from the end of the financial period in which the entity is finally dissolved. For these

purposes, final dissolution refers to the date on which the certificate of dissolution in the case of a company (or equivalent, where available, for other types of entity) is issued. Such records may be held by a service provider if located in the BVI. For the avoidance of doubt, a non-resident legal entity that has entered liquidation may continue to claim that it is resident for tax purposes in a jurisdiction outside the BVI, provided that such legal entity will in any event remain subject to any applicable requirements in relation to claiming and evidencing such claim of tax residency.

11. Application of the substance legislation to foreign legal entities

11.1 The scope of the ESA extends not just to entities that are incorporated or formed in the BVI, but also to foreign legal entities in specified circumstances.

11.2 This follows from the definition of "legal entity" in ESA section 2. That provision defines "legal entity" as "a company and a limited partnership". For the purposes of ESA, the definition of company includes "a foreign company within the meaning of section 3(2) of the BVI Business Companies Act, 2004 which is registered under Part XI of that Act", and the definition of limited partnership includes "a foreign limited partnership within the meaning of section 2 of the Limited Partnership Act, 2017 which is registered under Part VI of that Act". These definitions are explored in more detail below.

Foreign company

11.3 A "foreign company" must have the following two characteristics in order to fall within the meaning of "company" for the purposes of ESA:

11.4 First, it must be a foreign company within the meaning of section 3(2) of the BVI Business Companies Act, 2004;

11.5 Secondly, it must be registered under Part XI of the BVI Business Companies Act, 2004.

11.6 So far as the former is concerned, section 3(2) of the BVI Business Companies Act, 2004 provides:

> *"foreign company" means a body corporate incorporated, registered or formed outside the Virgin Islands but excludes a company within the meaning of subsection (1).*

11.7 For the avoidance of doubt, a company within the meaning of section 3(1) of the BVI Companies Act, 2004 is also within the scope of ESA (see the definition of "company" in ESA section 2).

11.8 As for the latter, Part XI of the BVI Business Companies Act, 2004 concerns the registration of foreign companies, and contains the following general prohibition (in section 186(1)):

> *A foreign company shall not carry on business in the Virgin Islands unless*

(a) it is registered under this Part; or
(b) it has applied to be so registered and the application has not been determined.

11.9 Part XI contains detailed registration and ongoing requirements to which a foreign company which carries on business in the BVI is subject, including an obligation to have a RA in the BVI (BVI Business Companies, Act 2004, section 189(1)).

11.10 In summary, a body corporate which is (a) incorporated in the BVI (b)registered in the BVI or (c) incorporated or registered either as per subsection (a) or (b) above or is otherwise incorporated or formed outside the BVI and which is lawfully carrying on business in the BVI shall be subject to the requirements of Economic Substance Act. For the avoidance of doubt, subsection (c) includes any foreign company engaging in a relevant activity from within the BVI.

Foreign limited partnership

11.11 In order to fall within the meaning of "limited partnership" for the purposes of ESA, a foreign limited partnership must have the following three characteristics:

11.12 First, it must be a foreign limited partnership within the meaning of section 2 of the Limited Partnership Act, 2017;

11.13 Secondly, it must be registered under Part VI of the Limited Partnership Act, 2017; and

11.14 Thirdly, it must have legal personality.

11.15 In relation to the first of these requirements, section 2 of the Limited Partnership Act, 2017 defines "foreign limited partnership" as follows:

"foreign limited partnership" means a partnership formed or established under the law of a jurisdiction other than the Virgin Islands with

(a) one or more partners who are liable for all the debts and liabilities of the partnership; and
(b) one or more partners whose liability for the debts and liabilities of the partnership is limited.

Reporting requirements

11.16 The reporting requirements under the BOSSs Act apply to foreign companies and foreign limited partnerships as well as BVI companies and limited partnerships. This follows from the expansion of the definition of "corporate and legal entity" for the purposes of that act to include "a foreign company as defined under section 3 of the BVI Business Companies Act 2004" and "a foreign limited partnership as defined under section 2 of the Limited Partnership Act 2017".

11.17 Only those foreign companies which are registered under Part XI and those foreign limited partnerships which have applied to continue under Part VI are subject to the reporting requirements: it is only those companies and limited partnerships which are subject to ESA and accordingly in whose affairs the ITA is interested.

12. Reporting requirements

12.1 Central to the effective administration and enforcement of the economic substance requirements is the collection and submission of information that will enable the ITA to monitor whether an entity is carrying on relevant activities and (if so) whether it is complying with the economic substance requirements.

The BOSSs Act regime

Reporting Duties

12.2 The reporting regime introduced by ESA by way of amendment to the BOSSs Act builds upon the pre-existing regime for the collection of information relating to beneficial ownership under the BOSSs Act. The reporting regime was modified for financial periods commencing on or after 1 January 2022 via amendments to the BOSSs Act and it is the modified reporting regime which is set out below. Entities considering their reporting obligations for financial periods commencing before such date should refer to version 2 of these rules (published on 10 February 2020).

12.3 Under the reporting regime, the content of the RA database, which a RA is obliged to establish and maintain in respect of each entity for which it acts as RA, has been expanded to include additional information which enables the ITA to determine (i) whether the relevant legal entity is subject to economic substance requirements and (ii) if so, whether the relevant entity is complying with them. It has also been expanded to include limited partnerships.

12.4 The information which the RA database must hold with respect to an entity is set out in section 10(3) of the BOSSs Act and is referred to as "the prescribed information". The BOSSs Act was further amended to separate beneficial ownership information which is found in section 13(3)(a), (d) and (g), 10(3)(a)(vii), (viii), (ix), and (x) and economic substance information which is the information found in 10(3) other than the beneficial ownership information. Section 10(3) reads as follows:

> *(a) the particulars of each corporate and legal entity including*
>
> *(i) the name, including alternative names;*

(ii) the incorporation number or its equivalent;
(iii) date of incorporation;
(iv) status;
(v) registered address;
(vi) business address (if different from the registered address);
(vii) whether it carries on a relevant activity;
(viii) any relevant activities which it carries on;
(ix) the name of its ultimate parent;
(x) the name of its immediate parent; and
(xi) any other particulars as the Minister may by Order prescribe.

(b) with respect to each beneficial owner of the corporate and legal entity:
(i) name;
(ii) residential address;
(iii) date of birth;
(iv) taxpayer identification number ("TIN") or other identification reference number, if any; and
(v) nationality;

(c) with respect to each registrable legal entity of the corporate and legal entity:

(i) details of the registrable legal entity as outlined in subsection (3)(a) (i) to (v);
(ii) jurisdiction in which the registrable legal entity is formed;
(iii) the basis or bases upon which the legal entity is designated as a registrable legal entity;
(iv) where the registrable legal entity is a foreign regulated person, the name of the jurisdiction of regulation and the name of the foreign regulator; or
(v) where the registrable legal entity is a sovereign state or a wholly owned subsidiary of a sovereign state the name of that sovereign state and (if applicable) wholly owned subsidiary.

(d) with respect to an exempt person

(i) the details of the exempt person as outlined in subsection (3)(a); and
(ii) the basis or bases upon which the exempt person is designated as an exempt person.

(e) with respect to the immediate parent (if any) of any corporate and legal entity

(i) details of the immediate parent as outlined in subsection (3)(a) (i) and (ii);
(ii) taxpayer identification number ("TIN") or other identification reference number of the immediate parent;
(iii) jurisdiction in which the immediate parent is formed;

(f) with respect to the ultimate parent (if any) of any corporate and legal entity

(i) details of the ultimate parent as outlined in subsection (3)(a)(i) and (ii);
(ii) taxpayer identification number ("TIN") or other identification reference number of the ultimate parent;
(iii) jurisdiction in which the ultimate parent is formed;

(g) with respect to any corporate and legal entity which is registered on a recognised exchange, details of the recognised exchange listing.

(h) with respect to any corporate and legal entity which carries on a relevant activity and claims to be outside the scope of the economic substance requirements by reason of being a non-resident company or a non-resident limited partnership,

(i) the jurisdiction in which it is tax resident;
(ii) taxpayer identification number ("TIN") or other identification reference number;
(iii) name of MNE group, if different; and
(iv) evidence to support that tax residence;

(i) with respect to any corporate and legal entity which carries on a relevant activity, and which does not claim to be outside the scope of the economic substance requirements by reason of being a non-resident company or a non-resident limited partnership, in relation to each such activity which it carries on during a financial period, and in respect of each financial period

(i) taxpayer identification number ("TIN"), if any;
(ii) type of mobile income;
(iii) amount and type of gross income in relation to the relevant activity;
(iv) the total amount of expenditure incurred on the relevant activity generally;
(v) the amount of expenditure incurred on the relevant activity within the Virgin Islands;
(vi) amount and type of assets and premises held in the course of carrying out the relevant activity;
(vii) net book values of tangible assets held in the course of carrying out the relevant activity;
(viii) the total number of employees of the corporate and legal entity;
(ix) the total number of employees engaged in the relevant activity, generally;
(x) the number of employees engaged in the relevant activity within the Virgin Islands;
(xi) details of the employees engaged in the relevant activity including
a. name; and
b. whether the employee is full time or part time; and
c. qualification; or
d. years of relevant experience;
(xii) the core income generating activity in relation to each relevant activity being conducted;

(xiii) the address of any premises within the Virgin Islands which is used in connection with the relevant activity;

(xiv) details of the persons responsible for the direction and management of the relevant activity, together with their relationship to the corporate and legal entity and whether they are resident in the Virgin Islands;

(xv) details of the board meetings held by the corporate and legal entity including

a. total number of board meetings held generally;
b. total number of board meetings held in the Virgin Islands;
c. the quorum for board meetings;
d. whether the meetings and decisions were minuted and kept in the Virgin Islands;
e. whether the quorum of directors was physically present in the Virgin Islands;
f. details of the directors of the corporate and legal entity including:
i. name;
ii. qualifications;
iii. year of relevant experience; and
iv. whether they are physically present in the Virgin Islands;

(i) with respect to any corporate and legal entity which carries on an intellectual property business, and which does not claim to be outside the scope of the economic substance requirements by reason of being a non-resident company or a non-resident limited partnership, in addition to the particulars supplied under section 10(3)(i), in relation to that activity

(i) the nature of any equipment located within the Virgin Islands which is used in connection with the relevant activity;

(ii) whether or not the corporate and legal entity is a high-risk IP legal entity as defined under section 2 of the Economic Substance (Companies and Limited Partnerships) Act, (Revised Edition 2020);

(iii) whether the corporate and legal entity wishes to contest the rebuttable presumption introduced by section 9(2)(a) or, as the case may be 9(2)(b) of the Economic Substance (Companies and Limited Partnerships) Act, (Revised Edition 2020);

(iv) if the corporate and legal entity wishes to contest the rebuttable presumption introduced by section 9(2)(a) of the Economic Substance (Company and Limited Partnerships) Act, (Revised Edition 2020), it must provide the following information

a. the relevant tangible asset which the corporate and legal entity holds;
b. explanation of how that intangible asset is being used to generate income;

c. identity the decisions for which each employee is responsible for in respect of the generation of income from the tangible asset;
d. the nature and history of the strategic decisions (if any) taken by the entity in the Virgin Islands;
e. the nature and history of trading activities (if any) carried out in the Virgin Islands by which the intangible asset is exploited for the purpose of generating income from third parties;

(v) if the corporate and legal entity wishes to contest the rebuttable presumption introduced by section 9(2)(b) of the Economic Substance (Company and Limited Partnerships) Act, (Revised Edition 2020), it must provide the following information

a. identify the relevant intellectual property asset which it holds;
b. provide detailed business plans which explain the commercial rationale of holding the intellectual property assets in the Virgin Islands;
c. identify the decisions for which each employee is responsible for in respect of the generation of income from the intangible asset; and
d. provide concrete evidence that decision-making is taking place within the Virgin Islands, including but not limited to, minutes of meetings which have taken place in the Virgin Islands;

(j) with respect to the corporate and legal entity which carries on holding business, and which does not claim to be outside of the scope of the economic substance requirements by reason of being a non-resident company or a non-resident limited partnership, the prescribed information in subsection (3)(i) shall be limited to subparagraphs (i) to (viii), and

(i) whether the activities carried out by the corporate and legal entity are active or passive;

(ii) whether the activities of the corporate and legal entity are active

a. details of qualified employees engaged in the relevant activity including:
i. name; and
ii. whether the employee is full time or part time; and
iii. qualifications; or
iv. years of relevant experience

b. details of the appropriate premises;

(iii) where the activities of the corporate and legal entity are passive, a statement that the corporate and legal entity complies with its statutory obligations under the BVI Business Companies Act, (Revised Edition 2020) or the Limited Partnership Act, (Revised Edition 2020);

(k) with respect to any corporate and legal entity which carries on a relevant activity and which does not claim to be outside the scope of the economic substance requirements by reason of being a non-resident company or a non-resident limited partnership, but for which core income-generating activity is carried out by another entity, the name of the entity which carries out that activity on its behalf, together with details of the resources deployed by that entity in carrying out the activity on its behalf.

12.5 Both the relevant entity and its RA have obligations in respect of the prescribed information. These duties are set out in section 9(1) to (4) of the BOSSs Act.

(1) A registered agent shall take reasonable steps to

(a) identify the beneficial owners and registrable legal entities of each corporate and legal entity for which it acts as registered agent;
(b) collect the prescribed information with respect to each corporate and legal entity for which it acts as registered agent,
in accordance with this Act.

(2) A corporate and legal entity shall

(a) identify any person who is a parent, immediate parent, ultimate parent, a beneficial owner or registrable legal entity of that corporate and legal entity, or, if it is registered on a recognised exchange, shall give details of its stock exchange registration;
(b) identify whether it carries on one or more relevant activities, and if so which relevant activities; and
(c) ascertain the information prescribed in sections 10(3)(e) and (f).

(3) A registered agent is not required to identify any beneficial owner of a corporate and legal entity under subsection (1) who holds its interest, directly or indirectly, in the corporate and legal entity through a registrable legal entity if the registered agent identifies that registrable legal entity for that purpose.

(4) For the purposes of this section, a registered agent who takes steps to identify and verify the identity of the beneficial owners of a corporate and legal entity in accordance with its obligations under the AML/CFT legislation shall have taken all reasonable steps in accordance with this section, and references to beneficial owners and registrable legal entities of a corporate and legal entity shall be interpreted accordingly.

12.6 The RA is required to take reasonable steps to "identify" the beneficial owners or registrable legal entities (as appropriate) of the corporate and legal entity. This obligation remains unchanged from the original BOSSs Act (save that it is expanded to cover limited partnerships). It is also liable to take reasonable steps to "collect" the prescribed information (which includes the beneficial owner and registrable legal entity information). Consequently, so far as beneficial owners and registrable entities are concerned, the RA is obliged to take reasonable steps both to identify and collect this information. So far as the remainder of the prescribed information is concerned, the RA is only liable to take reasonable steps to collect it from the relevant corporate and legal

entity. It has no duty to identify that information for itself, or to ascertain its truth. The RA is then under a duty to enter particulars of the prescribed information collected on the RA database (section 10(1)).

12.7 A corporate and legal entity must identify or ascertain all of the relevant prescribed information. That duty is not qualified by a requirement that it need only take "reasonable steps".

12.8 So far as the RA is concerned, section 9(4) of the BOSSs Act outlines that a RA has identified and verified the identity of the beneficial owner for the purposes of AML/CFT legislation in the BVI shall have taken all reasonable steps for the purposes of that section.

12.9 Although the prescribed information is extensive, not all of it needs to be ascertained and collected for each corporate and legal entity. The prescribed information can be divided into economic substance information and beneficial ownership information (both defined in section 2 of the BOSSs Act). These rules focus on the prescribed information with relation to economic substance requirements and do not take into account what is required by the corporate and legal entity for beneficial ownership information purposes. Thus, a corporate and legal entity will be required to provide economic substance information based on the circumstances of the corporate and legal entity as follows:

(i) if the corporate and legal entity declares that it does not carry on a relevant activity then it is required to provide the prescribed information outlined in section 10(3)(a), (e), (f) and (g), unless the corporate and legal entity is an "exempt person" in which case it and its registered agent are subject to the exemptions set out in section 7(1) of the BOSSs Act;

(ii) if the corporate and legal entity carries on a relevant activity but claims to be a non-resident company or a non-resident limited partnership, the economic substance information required by paragraphs 10(3)(a), (e), (f), (g) and (h), but not any information required by the remaining paragraphs;

(iii) if the corporate and legal entity carries on a relevant activity but does not claim to be a non-resident company or a non-resident limited partnership, the economic substance information required will depend on the relevant activity/activities being conducted by the corporate and legal entity.

Rule 19

The term "MNE Group" where used in the BOSSs Act shall be construed consistently with the term as defined for the purposes of Part IV of the Mutual Legal Assistance (Tax Matters) Act, Revised Edition 2020, as amended.

Rule 20

Gross Income means all income from whatever source derived, including revenues from sales of inventory and properties, services, royalties, interest, premiums, dividends and any other amounts.

12.10 The scope of prescribed economic substance information for holding business is clarified by rule 21.

Rule 21

Where the relevant activity is holding business, the legal entity must report the prescribed information in section 10(3)(a), (e), (f), (g) and (k) of the BOSSs Act unless the legal entity claims to be outside of the scope of the economic substance requirements by reason of being a non-resident company or a non-resident limited partnership.

12.11 Registrable legal entity is defined in the BOSSs Act section 8.

12.12 The duty on a corporate and legal entity to ascertain prescribed information and notify its RA arises in two circumstances, as provided for in section 9(6A):

(6A) A corporate and legal entity shall notify the registered agent of the economic substance information within a period following the end of the financial period to be fixed by regulations, and shall notify the registered agent of the beneficial ownership information within 15 days of identifying those matters, for those limited partnerships without legal personality, the beneficial ownership information shall be reported within 15 days of identifying those matters following the 1 January 2022.

The period fixed by regulations is 6 months from the end of the financial period (see the Beneficial Ownership Secure Search System (Time for Filing Prescribed Information) Regulations, 2019).

12.13 This means that for the purpose of determining when the corporate and legal entity's obligation to ascertain prescribed information and pass it on to the RA arises, prescribed information is divided into 2 categories:

(1) beneficial ownership information (as defined in section 2 of the BOSSs Act); and
(2) economic substance information (as defined in section 2 of the BOSSs Act).

12.14 Prescribed information within (1) must be ascertained immediately and provided within 15 days of the information being ascertained to the RA. Corporate and legal entities which are subject to the BOSSs Act before the amendments came into force should already have performed this initial duty as regards information regarding the corporate and legal entity itself, and its beneficial owners and registrable legal entities, and need not repeat it. Corporate and legal entities (other than limited partnerships without legal personality) which become subject to the BOSSs Act as a result of the amendments in the ESA (due to the amended wider definition of "corporate and legal entity") came under a duty to ascertain all the information within (1) with effect from 1 October 2019. Similarly, the requirements for limited partnerships without legal personality will only take effect from 1 January 2022 and the requirement after that point is also to provide the information within 15 days to the RA.

12.15 The duty to provide the information within (1) above about beneficial owners and registrable legal entities is a continuing duty, as a result of the terms of BOSSs Act section 12(1), which reads as follows:

A corporate and legal entity shall within 15 days of becoming aware of a change of any of the prescribed information relating to beneficial owners or registrable legal entities notify its registered agent of such changes and the date such changes took place.

12.16 Information within (2) must be provided in respect of a financial period within the reporting period i.e., 6 months of the end of the financial period of the legal entity.

Information and evidence which is required in support of specific submissions in the BOSSs Act return.

12.17 Under the reporting regime, an entity is only required to submit documentary evidence where that is specifically asked for (e.g., in support of a submission that it is tax resident outside the BVI (BOSSs Act, section 10(3)(l)), where it carries on IP business (BOSSs Act, section 10(3)(j)) or under Rule 22, 23 or 24 below). Otherwise, it must submit the facts and matters on which it relies in the BOSSs Act return and should be prepared to evidence those facts and matters if the ITA requests that evidence following a review of the BOSSs Act return.

Intellectual property business

12.18 The following rules apply in relation to entities which carry on intellectual property business:

Rule 22

A legal entity which wishes to contest the rebuttable presumption introduced by ESA section 9(2)(a) must, as part of its submissions under section 9(6A) of the BOSSs Act:

- **(a) identify the relevant intangible asset which it holds;**
- **(b) explain how that intangible asset is being used to generate income;**
- **(c) identify the staff in the BVI and (in each case) their qualifications, level of experience, the duration of their employment and the decisions for which they are responsible in respect of the generation of income from the intangible asset;**
- **(d) the nature and history of the strategic decisions (if any) taken by the entity in the BVI;**
- **(e) the nature and history of the risks (if any) being managed and borne by the entity in the BVI;**
- **(f) the nature of the trading activities (if any) carried on in the BVI by which the intangible asset is exploited for the purpose of generating income from third parties.**

Rule 23

A legal entity that wishes to contest the rebuttable presumption introduced by ESA section 9(2)(b) must, as part of its submissions under section 9(6A) of the BOSSs Act:

- **(a) identify the relevant intellectual property asset which it holds;**
- **(b) provide detailed business plans which explain the commercial rationale of holding the intellectual property asset in the jurisdiction;**
- **(c) identify the staff in the BVI and (in each case) their qualifications, level of experience the duration of their employment and the decisions for which they are responsible in respect of the generation of income from the intellectual property asset; and**
- **(d) provide concrete evidence that decision-making is taking place within the jurisdiction, for example in the form of detailed minutes of meetings which have taken place within the jurisdiction.**

Outsourcing

12.19 The following rules apply where a legal entity carrying on a relevant activity outsources work to another person:

Rule 24

Where any aspect of relevant activity is carried out for a legal entity by a third party, the legal entity must, as part of its submissions under section 9(6A) of the BOSSs Act:

- **(a) identify the name of the third party which carries out the income-generating activity on its behalf;**
- **(b) identify what activities, and what proportion of the entity's total income-generating activity, is carried out by the third party;**
- **(c) identify the geographical location of the activities carried out by the third party**
- **(d) state how the legal entity monitors and controls the activity carried out on its behalf by the third party;**
- **(e) state the resources employed by the third party in performing the outsourced activity.**

Information requests by the ITA

12.20 In some instances, the information submitted under the reporting regime may not be sufficient to enable the ITA to determine whether an entity is complying with the economic substance requirements. In addition, the ITA may seek further information from a legal entity in order to check the accuracy of its return.

12.21 The ITA has the power under ESA section 11 to serve a notice on any person, requiring that person to provide, within the period specified in the notice and at such place as is specified in the notice, such documents and information as the ITA may reasonably require for the purpose of facilitating the ITA's exercise of its functions under ESA. A failure to provide the information without reasonable excuse, or the provision of false information, is an offence.

12.22 Likewise, there is no restriction on the types of information which the ITA can ask for, save that in certain circumstances the recipient of a notice under section 11 may have a reasonable excuse for refusing to provide the information. For example, such an excuse includes where the person would be entitled to refuse to provide the requested information on grounds of legal privilege.

13. Enforcement and Penalties

13.1 The ITA is responsible for assessing and enforcing compliance with the requirements imposed by ESA.

13.2 The penalties imposed by ESA and the BOSSs Act are intended to be rigorous, effective and dissuasive, ranging from financial penalties to (in the case of individuals) imprisonment. Broadly speaking, they arise in two circumstances:

(1) where there has been a failure to provide information, or information provided is inaccurate; and

(2) where there has been a failure to comply with economic substance requirements.

13.3 For the avoidance of doubt, the penalties set out in ESA and the BOSSs Act are not exhaustive.

Assessment of compliance

13.4 Responsibility for assessing compliance is conferred on ITA by ESA section 10:

> *(1) The competent authority may determine that a legal entity has not complied with the economic substance requirements during any financial period of the legal entity ending on or after 31 December 2019, provided that such determination is made no later than 6 years after the end of the financial period to which the determination relates.*
>
> *(2) The time limit in subsection (1) does not apply if the competent authority is not able to make a determination within the 6-year period by reason of any deliberate misrepresentation or negligent or fraudulent action by the legal entity or by any other person.*

Failure to provide accurate information

13.5 A failure to provide information without reasonable excuse and the intentional provision of false information, whether pursuant to an information request from the ITA under ESA section 11 or as part of the reporting regime under the BOSSs Act, attracts penalties. The persons who may be liable for penalties include not only the relevant entities to whom the information relates and their RAs but any person on whom the ITA serves a notice under ESA section 11.

13.6 Those penalties are severe:

(1) A person who fails to provide information without reasonable excuse or who intentionally provides false information in response to a request under ESA section 11 is liable: (i) on summary conviction, to a fine not exceeding forty thousand dollars or to imprisonment for a term not exceeding two years, or both; or (ii) on conviction on indictment, to a fine not exceeding seventy five thousand dollars or to imprisonment for a term not exceeding five years, or both (ESA section 11(3)).

(2) The same penalties apply where a RA intentionally provides false information relating to an entity on its RA database or where the entity intentionally provides false information under section 9(2) or 12(1) of the BOSSs Act (BOSSs Act section 16).

(3) Where an entity fails to comply with a requirement of section 9 of the BOSSs Act without reasonable excuse, it commits an offence and is liable: (i) on summary conviction to a fine not exceeding forty thousand dollars or to imprisonment for a term not exceeding six months, or both; or (ii) on conviction on indictment, to a fine not exceeding two hundred and fifty thousand dollars or to imprisonment for a term not exceeding five years, or both (BOSSs Act section 9(6)).

(4) Where a RA fails to comply with a requirement of section 9 without reasonable cause, it commits an offence and is liable: (i) on summary conviction to a fine not exceeding twenty thousand dollars; or (ii) on conviction on indictment, to a fine not exceeding forty thousand dollars (BOSSs Act section 9(7)).

13.7 As can be seen, save where there has been an intentional provision of false information, there is a defence of 'reasonable excuse' (see ESA section 11(3); BOSSs Act sections 9(6), 9(7) and 10(4)). Whilst ultimately this is a question for the court, the ITA anticipates that what amounts to a reasonable excuse will depend on the facts and circumstances of the breach, including the identity of the infringer, on whom the burden of demonstrating 'reasonable excuse' will fall.

Failure to comply with the economic substance requirements

13.8 The regime which applies where an entity fails to comply with the economic substance requirements is intended to serve, at least in the first instance, the twin purposes of (i) penalising both the entity and those responsible for the breach and (ii) compelling the entity to take corrective action. If the latter purpose cannot be achieved, then the entity risks being struck from the register or liquidated by court order.

13.9 In the majority of cases there will be a three-stage regime for sanctions:

(1) On a first determination of non-compliance, the ITA will issue a first determination, explaining the reasons for the determination, the amount of the penalty and the date from which the penalty is due and the action which the ITA considers should be taken by the entity and the date by which such action needs to be taken. It will also notify the entity of its right of appeal under section 13 (ESA section 12(1).)

(2) If the entity fails to take the action demanded of it in the first determination within the prescribed time, or within such longer period as the ITA may allow, the ITA will issue a second determination. That notice will have the same elements as that issued on a first determination of non-compliance, save that it will also notify the entity that the ITA may make a report to the Financial Services Commission (ESA section 12(4)).

(3) Following the issue of a second determination of non-compliance, the ITA may, if it considers it appropriate to do so having regard to all the circumstances of the case, apply to court for it to be liquidated, as applicable.

13.10 In exceptional cases, the ITA may leapfrog this three-stage regime, and go straight to court to liquidate the entity, as applicable. It may exercise this power at any time following the service of a first determination of non-compliance where it decides that there is no realistic possibility of the entity meeting the economic substance requirements (ESA section 12(8)).

13.11 Liquidation ais an extreme sanction. The ITA will not resort to such sanctions without giving the entity in question a reasonable opportunity to state its case in opposition, and in every case will seek to ensure that the rights of third parties (such as customers of a bank or insurance company) are protected. On the other hand, the ITA will not hesitate to resort to such sanction where it considers that an entity has been guilty of clear, deliberate or egregious breaches of the economic substance requirements.

13.12 Under the Insolvency Act and the Limited Partnership Act the ITA has the right to seek the liquidation of a company and a limited partnership respectively on public interest grounds where a legal entity has been found to be in breach of the substance requirements.

13.13 Once it has determined that an entity is in breach of the economic substance requirements, the ITA has no discretion as to whether to impose a financial penalty but must impose a minimum penalty of five thousand dollars on a first determination of non-compliance and ten thousand dollars on a second determination of non-compliance (ESA section 12(2) and 12(4)). If an entity wishes to challenge the imposition of the minimum penalty on the grounds that it is too high, it must submit an appeal under ESA section 13.

13.14 Subject to the requirement that the ITA must impose a minimum penalty on a determination of non-compliance, the ITA has a broad discretion as to the amount of any penalty, provided that it does not exceed the maximum penalty which: on a first determination of non-compliance, is fifty thousand dollars in the case of a high risk IP legal entity and twenty thousand dollars in all other cases (ESA section 12(2)); and, on a second determination of non-compliance, is four hundred thousand dollars in the case of a high risk IP legal entity and two hundred thousand dollars in all other cases (ESA section 12(5)).

13.15 In determining the amount of the penalty, the ITA will take into account the following factors:

(1) The nature and seriousness of the non-compliance;

(2) The reason for the breach;
(3) Whether this is the first financial period in which the entity has failed to comply with the economic substance requirements, or whether it has previously been deemed non-compliant;
(4) The total turnover of the entity;
(5) The entity's conduct during the assessment process and (where relevant) following the first determination of non-compliance, and in particular whether it has been cooperative with the ITA;
(6) What steps (if any) the entity has taken to prevent a recurrence of the breach.

Appeal

13.16 A legal entity who has been served with a notice of non-compliance by the ITA under ESA section 12 has a right of appeal against both the determination of non-compliance and against the amount of any penalty imposed, including where the amount of the penalty is the minimum prescribed (ESA section 13).

13.17 However, notice of the appeal stating the ground of appeal must be filed at the Court within 30 days of the date of the notice of non-compliance (ESA section 14(1)). The ITA, on whom the notice of appeal must be served, is entitled to appear and be heard at the hearing of the appeal (ESA section 14(2)).

13.18 The powers of the court on an appeal comprise the power to confirm, vary or revoke the determination of non-compliance, and to confirm, vary or cancel the penalty (ESA section 14(3)).

13.19 Where notice of appeal has been lodged, the time for complying with the requirements specified in the notice of non-compliance only starts to run from the date on which the appeal is finally determined or withdrawn (ESA section 15).

14. The ITA's obligations to disclose information to overseas authorities

14.1 In certain circumstances, Schedule 4 of the BOSSs Act requires the ITA to disclose or procure the disclosure of the relevant information stored in the RA database in respect of an entity with a "relevant overseas competent authority". "Relevant overseas competent authority" is defined by paragraph 1 of Schedule 4 as follows:

> *"relevant overseas competent authority" means, in relation to any corporate and legal entity, the competent authority for each state in which*
>
> *(a) a beneficial owner resides; or*
> *(b) within which a registrable legal entity is registered; or*
> *(c) within which the corporate and legal entity is registered; or*
> *(d) within which a parent of the corporate and legal entity is registered; or*
> *(e) within which the corporate and legal entity claims to be tax resident;"*

14.2 The triggering events for the spontaneous exchange of information with the relevant overseas competent authorities are (i) there has been a breach of the economic

substance requirements or (ii) the relevant entity carries on an intellectual property business and falls within the presumption that it does not conduct core-income generating activity in the BVI set out in ESA section 9(2).

14.3 In addition to these triggering events, where an entity claims to be tax resident in another jurisdiction, the competent authority of that jurisdiction will receive a notification. This is so as to bolster the policing of non-residence claims by the ITA.

14.4 Where an entity is carrying on relevant activities and claims to be tax resident outside the BVI:

(1) A notification of this claim should be sent to the jurisdiction in which the entity claims to be tax resident; and

(2) If a beneficial owner or legal owner of the entity is resident in an EU Member State, the competent authority of that Member State must also be notified that the legal entity is claiming tax residence outside the BVI and be provided with the name of the jurisdiction in which tax residence is claimed. For these purposes, the legal owner is the person who is the ultimate parent and immediate parent of the entity.

15. Timing of the introduction of the economic substance and reporting requirements

15.1 Save for the new reporting regime under the BOSSs Act introduced by ESA (which was modified for financial periods commencing on or after 1 January 2022), the provisions of ESA came into effect on 1 January 2019 (or 1 July 2021, in the case of limited partnerships without legal personality) subject to a six-month transitional period for entities registered in the BVI prior to the relevant date. However, the date from which an entity is obliged to comply with the economic substance requirements depends upon when the entity was incorporated or formed.

15.2 In particular, as described in Part 2, the basic obligation to comply with the economic substance requirements is imposed by ESA section 5(1) which reads:

> *A legal entity which carries on a relevant activity during any financial period must comply with the economic substance requirements.*

15.3 The date on which an entity's first "financial period" for the purposes of ESA commences depends upon when the entity was formed or incorporated, as set out in section 4 of the ESA and Part 10 of these rules.

15.4 It therefore follows that:

(1) A company or limited partnership (other than a limited partnership without legal personality) incorporated or formed on or after 1 January 2019 must comply with the economic substance requirements as from the date of incorporation or formation, because its first financial period will begin on its incorporation or formation;

(2) A company or limited partnership incorporated (other than a limited partnership without legal personality) or formed prior to 1 January 2019 is not obliged to comply with the economic substance requirements until 30 June 2019, save where it notifies the ITA that its financial period for the purposes of ESA will commence on a date earlier than 30 June 2019;

(3) A limited partnership without legal personality formed on or after 1 July 2021 must comply with the economic substance requirements as from the date of formation, because its first financial period will begin on its formation;

(4) A limited partnership without legal personality formed prior to 1 July 2021 is not obliged to comply with the economic substance requirements until 1 January 2022, save where it notifies the ITA that its financial period for the purposes of ESA will commence on a date earlier than 1 January 2022.

15.5 The financial period that some entities have commenced prior to when the new reporting regime came into force i.e., 1 January 2022. Where that is the case, the relevant entity must still comply with the economic substance requirements from the commencement of their financial period, notwithstanding the fact that the new reporting regime was not yet in force. This does not cause any difficulties, as the obligation to report on the relevant activity does not arise until after the end of each financial period.

16. Modifications for limited partnerships

16.1 Limited partnerships have many legal characteristics distinct from companies. For example, under the Limited Partnership Act 2017 (the "LPA"):

(1) subject to LPA subsection 29(4), the general partners are responsible for the management of the limited partnership;

(2) a general partner is the agent of the limited partnership for the purposes of the business and activities of the limited partnership;

(3) a limited partner shall not, in the capacity of limited partner, take part in the management of the limited partnership or transact the business of, sign or execute documents for or otherwise bind the limited partnership; and

(4) typically, the assets of a limited partnership with legal personality are held by the general partner(s) as agent(s) for the limited partnership (and, in the case of a limited partnership without legal personality, are deemed to be held by the general partner(s) on trust).

16.2 For these reasons, the requirements of the ESA and the BOSS Act and related definitions (including without limitation the definitions of a "group" and "affiliate" in the ESA) must be modified accordingly in the case of limited partnerships.

16.3 Where a limited partnership is subject to the "direction and management" requirement under the ESA, it will be required to demonstrate that the relevant activity is directed and managed by its "governing body" in the BVI. The governing body is the person or group of persons responsible for making the limited partnership's strategic and

management decisions (i.e., it has the general supervision of the affairs of the limited partnership). Subject to the limited partnership agreement and any specific circumstances applicable to the limited partnership, the general partners in the limited partnership (or their duly authorised representatives responsible for decisions of a general partner which is itself a company or body corporate) will usually be regarded as the governing body – and not as separate entities for the purposes of the ESA, provided that CIGA must be carried on in the BVI.

16.4 It is expected that any limited partnership will need to have meetings of its governing body in line with the levels of activities it conducts, and it is at those meetings that the decisions required to run the business are made.

16.5 The governing body should meet in the BVI at an adequate frequency given the level of decision making required in respect of the relevant activity. Strategic decisions must be set at those meetings with the minutes reflecting those decisions. The governing body, as a whole, must have the necessary knowledge and expertise to discharge their duties. All minutes must be kept in the BVI.

16.6 Expenditures may include expenditures incurred by, for or on behalf of the limited partnership (for example, by its general partner(s)) in relation to its business. Similarly, premises or equipment may include premises or equipment used by, for or on behalf of the limited partnership in relation to its business.

16.7 Employees of a limited partnership would generally include any employed by, for or on behalf of the limited partnership, including:

(1) the governing body, including a general partner, or the limited partnership;

(2) persons to whom activities have been outsourced, where the person meets the test set out in explanatory note 7.12 above.

APPENDIX 1

Abbreviations used in these Rules

Abbreviations

AML/CFT	Anti-Money Launder and Counter Financing of Terrorism
BOSSs Act	The Beneficial Ownership (Secure Search System) Act, Revised Edition 2020, as amended
BVI	British Virgin Islands
CIGA	core income generating activity
ESA	The Economic Substance (Companies and Limited Liability Partnerships) Act Revised Edition 2020, as amended
EU	European Union
FSC	Financial Services Commission of the BVI
FSC Code	BVI Regulatory Code, Revised Edition 2020, issued under section 41(1) of the Financial Services Commission Act, Revised Edition 2020
FHTP	OECD Forum on Harmful Tax Practices
HR	Human Resources
IP	Intellectual Property
IT	Information Technology
ITA	International Tax Authority
LPA	Limited Partnership Act, Revised Edition 2020
RA	Registered Agent
SIBA	The Securities and Investment Business Act, 2010 (as amended) and all relevant regulations and guidance notes issued thereunder.
TIN	Taxpayer Identification Number
U.S	United States of America