

Cayman Islands Update: Economic Substance Guidance Notes v3.0 Issued

On 13 July 2020, the Cayman Islands Department for International Tax Cooperation (the "DITC") issued version 3.0 of the Guidance on Economic Substance for Geographically Mobile Activities¹ (the "Guidance") pursuant to the ES Law (as defined below). This replaces the previous version 2.0 of the Guidance issued on 30 April 2019.

The Guidance supplements the International Tax Co-operation (Economic Substance) Law (2020 Revision), as amended by the International Tax Co-Operation (Economic Substance) (Amendment) Law, 2020 and supplemented by the International Tax Co-Operation (Economic Substance) (Amendment of Schedule) Regulations, 2020 and the International Tax Co-Operation (Economic Substance) Regulations, 2020 (collectively, the "ES Law")².

As outlined in our previous client update³, the ES Law is responsive to global OECD Base Erosion and Profit Shifting ("BEPS") standards regarding geographically mobile activities. Requirements of this type have been implemented rapidly on a level playing field basis by all OECD-compliant 'no or only nominal tax' jurisdictions.

Version 3.0 of the Guidance reflects the amendment laws and regulations noted above, and

addresses certain important aspects of the ES Law's economic substance requirements and their practical implementation.

The ES Law and Guidance reflect both the Cayman Islands' ongoing adherence to global standards as one of over 135 countries and jurisdictions committed to the OECD's Inclusive Framework on BEPS, and commitments made by the Cayman Islands to the European Union.

Executive Summary

The ES Law contains certain reporting and economic substance requirements for 'relevant entities' conducting 'relevant activities'.

A relevant entity is defined as:

- a Cayman Islands company, limited liability company or limited liability partnership;
- a foreign company registered in the Cayman Islands,

unless such 'entity' is a 'domestic company'; an 'investment fund'; or 'tax resident' outside of the Cayman Islands for the purposes of the ES Law.

¹ https://www.ditc.ky/wp-content/uploads/Economic_Substance_-_Guidance_-_v3.0190713.pdf

² <https://www.ditc.ky/es/es-legislation-resources/>

³ <https://maples.com/Knowledge-Centre/Industry-Updates/2019/03/Cayman-Islands-Economic-Substance-Requirements-for-Certain-Entities-Overview>

The relevant activities definition under the ES Law are:

- [Banking business](#)
- [Distribution and service centre business](#)
- [Financing and leasing business](#)
- [Fund management business](#)
- [Headquarters business](#)
- [Holding company business](#)
- [Insurance business](#)
- [Intellectual property business](#)
- [Shipping business](#)

The ES Law and Guidance contain the full definitions of, and practical guidance in relation to, the terms used above.

Key Changes

The Guidance now includes, for the first time, sector specific guidance with respect to each relevant activity. This includes examples and commentary to determine whether a relevant entity is carrying on a relevant activity. We would encourage clients with Cayman Islands incorporated or registered entities who are unsure of the application of the ES Law to their entities to discuss this with their usual Maples Group contact.

The Guidance reflects a modified approach to notification and reporting which has already been partly implemented. In particular, all entities (as described above) are required to file an annual Economic Substance Notification ("ESN") via the Cayman Islands Registrar of Companies' corporate administration platform. For Cayman Islands entities, submission of the ESN is a prerequisite to submission of their Annual Return. Foreign companies registered in the Cayman Islands must

also file an ESN, despite not being required to file an Annual Return.

A relevant entity that has indicated in its ESN that it is carrying on a relevant activity, and is subject to the economic substance requirements under the ES Law, is required to report certain information⁴ on its relevant activities on an annual basis to the DITC via the DITC Portal (the "ES Return").

At the date of this update, the DITC Portal is still under construction. The first ES Return will, however, be due no later than 12 months after the last day of the relevant entity's financial year commencing on or after January 2019. This means, for example, that for a relevant entity with a 1 January to 31 December financial year that conducted a relevant activity during 2019, an ES Return must be submitted on or before 31 December 2020 in respect of its financial year 1 January 2019 to 31 December 2019. We expect to provide a further update in respect of the requirements for the ES Return process in due course.

In addition, an entity that is carrying on a relevant activity but is not a relevant entity due to being tax resident outside of the Cayman Islands (and is therefore not required to submit an ES Return or comply with the economic substance test under the ES Law) is now required to supply certain basic information, including with respect to its jurisdiction of claimed tax residence, its immediate ownership and ultimate beneficial ownership and its financial year end date, as part of its ESN. It will also be required to provide additional information and upload evidence to corroborate this claim. The DITC has released a form ("Sample Form") setting out the requisite information fields. Although not yet confirmed by the DITC, we expect that the

⁴ See section 7(4) of the International Tax Co-operation (Economic Substance) Law (2020 Revision) and the International Tax Co-Operation (Economic Substance) Regulations, 2020

information required by the Sample Form will be submitted via the DITC Portal once it is opened.

Therefore, entities that indicated on their first ESN that they are tax resident outside of the Cayman Islands may shortly be required to submit further details and supporting evidence.

In respect of relevant entities that outsource certain functions in order to comply with the economic substance test under the ES Law, the outsource service providers which have been nominated by a relevant entity will also be required to verify this outsourcing by providing prescribed information to the DITC.

The Guidance provides that the Tax Information Authority will monitor arrangements which appear to be circumvention mechanisms and will investigate cases where a person has entered into any arrangement that the main purpose or one of the main purposes of which is to circumvent any obligation under the ES Law. An example is provided of an entity which seeks to manipulate or artificially suppress its income to circumvent substance requirements.

Helping to Streamline the Process

Maples Group is working on a number of innovative solutions to assist our clients with the ESN process in the coming years and will provide further information in due course.

However, particularly now that the ES Law, Guidance and related requirements have crystallised in a number of important respects, we would encourage you to raise any questions with your usual Maples Group contact.

If you would like further information or assistance, please reach out to your usual Maples Group contact or any of the contacts listed below.

Jon Fowler

+1 345 814 5526

jon.fowler@maples.com

Jonathan Green

+1 345 814 5466

jonathan.green@maples.com

Matthew Gardner

+1 345 814 5453

matthew.gardner@maples.com

Christopher Capewell

+1 345 814 5666

chris.capewell@maples.com

Alasdair Robertson

+1 345 814 5345

alasdair.robertson@maples.com

September 2020

© MAPLES GROUP

This update is intended to provide only general information for the clients and professional contacts of Maples Group. It does not purport to be comprehensive or to render legal advice.