

Cayman Islands Economic Substance Requirements – Relevant Activity of Holding Company Business

For general background on The International Tax Co-operation (Economic Substance) Law, 2018 (as amended by relevant regulations, the "Economic Substance Law"), the related Guidance on Economic Substance for Geographically Mobile Activities (the "Guidance") and for the meaning of 'relevant entity', please refer to our main update.¹

This update assumes that an entity has already been determined to be a relevant entity under the Economic Substance Law and that the relevant entity is now considering whether it is carrying on one of the nine categories of geographically mobile 'relevant activities' - in particular, under the 'holding company business' category.

What is holding company business?

Holding company business in the Economic Substance Law is defined to mean "*the business of a pure equity holding company*", which itself is defined to mean 'a company that only holds equity participations in other entities and only earns dividends and capital gains'.

The Guidance confirms that dividend income should be interpreted to encompass any income payments made to a pure equity holding company in respect of equity participations and

will include distributions made by non-corporate entities that are equivalent to dividends. Equity participations include shares in a company, but also include other forms of investment in the equity of an entity which give the investor the right to participate in the profits of that entity. Equity participations do not include investments made by way of debt or other non-equity participations.

As part of the functions of a pure equity holding company, activities may include, for example, ownership of a bank account, governance decisions, entering into contractual arrangements with professional or other service providers, and the payment of fees and expenses.

Economic Substance Test

If a relevant entity **only** carries on a relevant activity that is the business of a pure equity holding company, it will be subject to a reduced economic substance test as set out in section 4(5) of the Economic Substance Law (the "Reduced ES Test").

¹<https://maples.com/Knowledge-Centre/Industry-Updates/2020/09/Cayman-Islands-Update-Economic-Substance-Guidance-Notes-v3-Issued>

The Reduced ES Test is satisfied if the relevant entity:

- (a) has complied with all applicable filing requirements under the Companies Law (2020 Revision); and
- (b) has adequate human resources and adequate premises in the Cayman Islands for holding and managing equity participations in other entities.

The Guidance on Holding Company Business

The holding company business sector-specific section of the Guidance explains that what is required for compliance with limb (b) of the reduced ES Test, as with the Economic Substance Law in general, will be dependent on how the holding company business is being conducted. A pure equity holding company maintaining a registered office in the Cayman Islands engaging its registered office service provider in accordance with the Companies Law (2020 Revision) may be able to satisfy the Reduced ES Test, depending on the level and complexity of activity required to operate its business.

What to Do if a Relevant Entity is Carrying On the Relevant Activity of Holding Company Business

It is worth noting that there are a range of consequences for breaches of the Economic Substance Law (including financial penalties and potential striking-off).

Further Information

If you have any specific questions in relation to a relevant entity conducting holding company

business or this update, please reach out to your usual Maples Group contact or:

Matthew Gardner
+1 345 814 5453
matthew.gardner@maples.com

Suzanne Correy
+1 345 814 5434
suzanne.correy@maples.com

Daniel Lee
+1 345 814 5508
daniel.lee@maples.com

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