

Cayman Islands Economic Substance Requirements – Relevant Activity of Financing and Leasing Business

For general background on The International Tax Co-operation (Economic Substance) Law (2020 Revision) (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 the 'relevant activity' of 'financing and leasing business'.

What is financing and leasing business?

Financing and leasing business in the Economic Substance Law is defined as *"the business of providing credit facilities for any kind of consideration to another person but does not include financial leasing of land or an interest in land, banking business, fund management business or insurance business."*

Economic Substance Test

If a relevant entity carries on the relevant activity of financing and leasing business it will

be subject to the economic substance test set out in the Economic Substance Law. The economic substance test can be satisfied in relation to that financing and leasing business if the relevant entity:

- (a) conducts 'core income generating activities' in the Cayman Islands in relation to the relevant activity
- (b) is directed and managed in an appropriate manner in the Cayman Islands
- (c) has adequate operating expenditure, physical presence and personnel in the Cayman Islands

Core Income Generating Activities

The relevant core income generating activities in the context of financing and leasing business include:

- (a) negotiating or agreeing funding terms
- (b) identifying and acquiring assets to be leased
- (c) setting the terms and duration of financing or leasing

¹<https://maples.com/knowledge/cayman-islands-update-economic-substance-guidance-notes-v3-0-issued>

- (d) monitoring and revising financing or leasing agreements and managing risks associated with such financing or leasing agreements

The Guidance on Financing and Leasing Business

The Guidance makes clear that, although the activity is described as financing and leasing, the essence of the activity is the provision of credit facilities. A relevant entity which offers credit or financing for any kind of consideration may be in scope.

The Guidance states that an entity which provides credit as an incidental part of a different sort of business will not be treated as carrying on financing and leasing business. In this context, the Guidance states that 'incidental' means occasional, minor activity with no profit making purpose.

The Guidance notes that where the provision of credit is separated from the consideration received, this may also be in scope. For example, where a loan advanced for consideration by one company is transferred to a different company which then receives the loan capital repayments and consideration.

'Credit facilities' is stated to include loans, hire purchase agreements, long term credit plans, and finance leases in relation to assets other than land. The consideration may take different forms but would typically include interest and / or lending fees in the case of financing and lease payments and, where applicable, residual value payments, in the case of a lease. The definition does not extend to cases where credit is offered and there is no expectation of consideration from the credit.

The Guidance confirms the scope does not extend to cases where a relevant entity has purchased debt securities as an investment, as opposed to providing a credit facility, for

example, where the relevant entity has purchased gilts, quoted bonds or similar securities.

The Guidance also contains examples of 'in scope' and 'out of scope' activities. In scope examples include:

- (a) unsecured lending where interest and / or a lending fee is charged
- (b) a relevant entity that operates as a treasury centre and provides interest-bearing credit facilities to subsidiaries and affiliated entities within a multi-national group of companies
- (c) a single interest-bearing loan made to another entity, which is the relevant entity's only activity. As such, an intra-group loan or single loan can constitute financing and leasing business, especially where it is the only activity of an entity and there are no other factors to take it out of scope
- (d) an aircraft finance company whose business is the financing of aircraft for customers, whereby the relevant entity purchases aircraft and leases the relevant aircraft to the relevant customer

Out of scope examples include:

- (a) an interest free loan where no interest, lending or other fee is charged and there is no other kind of consideration, regardless of any grant of security to the lender
- (b) ancillary business or activity that is incidental to a different sort of business

What to Do if a Relevant Entity is Carrying On the Relevant Activity of Financing and Leasing 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).

If you have any specific questions in relation to a relevant entity conducting financing and leasing business or this update, please reach out to your usual Maples Group contact or:

Wanda Ebanks

+1 345 814 5449

wanda.ebanks@maples.com

Scott Macdonald

+1 345 814 5317

scott.macdonald@maples.com

Jonathon Meloy

+1 345 814 5412

jonathon.meloy@maples.com

October 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