

LEGAL UPDATE:

New Bahamas Legislation to Satisfy EU Economic Substance Requirements

In 2017, the European Union Code of Conduct Group extended its work on tax matters from its Member States to assessing the tax regimes of a number of other jurisdictions. All of the leading global financial centres committed to eliminating certain domestic regimes and implementing other global standards by the end of 2018, and The Bahamas likewise made commitments to address the following by way of legislation:

- Removing ring fencing – where advantages are ring fenced from the domestic market so that they do not affect the national tax base.
- Requiring substantial economic presence for entities involved in certain business activities to ensure that tax advantages are aligned with real economic activity.
- Implementing the Base Erosion and Profit Shifting (BEPS) minimum 5 standards established by the Organization for Economic Cooperation and Development (OECD) /G20.

A high-level summary of the new legislation follows:

1

The Register of Beneficial Ownership Act, 2018 (“ROBO”)

Commencement Date: 20th December 2018

Who does it apply to?

The ROBO applies to legal entities incorporated, registered, continued or otherwise established in accordance with the Companies Act or the International Business Companies Act subject to certain exemptions discussed below.

What are the main obligations?

A beneficial owner is a natural person who ultimately owns or controls a legal entity and includes, without limitation:

- (a) a natural person who ultimately owns or controls, whether directly or indirectly, ten or more per cent of the shares or voting rights of the legal entity;
- (b) a natural person who otherwise exercises control over the management of the legal person other than solely in the capacity of a director, advisor or professional manager.

Also included are the natural and legal persons appointed as liquidator, administrator or receiver of a legal entity and a creditor who appoints a receiver over 25% of the voting rights of a legal entity.

An entity may be required to disclose that it is beneficially owned by a registrable legal entity, without disclosing the beneficial ownership of such registrable legal entity. A registrable legal entity is a legal person who in relation to an entity to which ROBO applies, would be a beneficial owner of such entity if it were a natural person; and such registrable legal entity is either an exempt person; listed on a regulated securities exchange; a licensee or a foreign regulated person; or a foreign state or wholly owned subsidiary of a foreign state. Affiliates and wholly owned subsidiaries of registrable legal entities are also considered to be registrable legal entities, to the extent that they meet the ownership or control test in relation to a legal entity discussed above.

It should be noted that there are also entities which are exempt from the obligation to identify and report on their beneficial owners. They are “exempt persons,” defined as an entity meeting one or more of the following criteria:

- a. Listed on a regulated securities exchange;
- b. A licensee (defined as a licensee or registrant of the Central Bank of The Bahamas, Insurance Commission, or Securities Commission and includes affiliates of such licensee);
- c. A wholly owned subsidiary of a licensee; or
- d. Any other legal entity that the Minister exempts by regulations.

When do I have to comply?

The time period for compliance with ROBO is 1 year from the commencement date for existing entities. Entities incorporated after the commencement of ROBO must comply immediately. The information is to be maintained in a secure database which will be accessible by designated persons, who are persons designated by the Competent Authority. The Designated Person will be able to search the secure system at the request of regulatory authorities, such as the Office of the Attorney General, the Financial Intelligence Unit, the Central Bank of The Bahamas, the Compliance Commission, the Securities Commission and the Insurance Commission.

2

Commercial Entities (Substance Requirements) Act, 2018 (“CESA”)

Commencement Date: 31st December 2018

Who does it apply to?

The following commercial entities to the extent that they are engaged in “Relevant Activities”, are considered “Included Entities”:

- i) companies incorporated or continued under the International Business Companies Act (IBCs);
- ii) companies incorporated, continued, or registered as a foreign entity under the Companies Act (domestic companies);
- iii) partnerships under the Partnerships Act and limited liability partnerships under the Partnership Limited Liability Act; and
- iv) exempted limited partnerships registered under the Exempted Limited Partnership Act.

A non-included entity is one that is:

- i) owned by residents and centrally managed in The Bahamas, even if it conducts a relevant activity; or
- ii) tax resident in another jurisdiction and centrally managed outside of The Bahamas, even if it conducts a relevant activity; or
- iii) An entity not engaged in relevant activities itself or by any of its subsidiaries

A Relevant Activity is defined as follows:

- a. Banking business;
- b. Insurance business;
- c. Fund management business;
- d. Financing and leasing business;
- e. Headquarters business;
- f. Distribution and service centres business;
- g. Shipping business;
- h. Commercial use of intellectual property; or
- i. Where a holding company engages, or where one or more of its subsidiaries is engaged in one of the activities listed under paragraphs a- h.

Entities claiming to be non-included due to being centrally managed and tax resident in another jurisdiction are still required to report that they are a non-included entity and must provide evidence that they are compliant with the tax requirements of such jurisdiction.

What are the main obligations?

An “Included Entity” will now have to demonstrate economic substance in The Bahamas on a two pronged test:-

- a) That its core income generating activities (“CIGA”) take place in The Bahamas (including if outsourced in The Bahamas) which presupposes adequate amounts of annual operating expenditure; levels of qualified full-time employees; physical offices and levels of board management and control within The Bahamas.
- b) Direction and management in The Bahamas which is fulfilled by demonstrating all of the following:
 - i) An adequate number of board meetings in The Bahamas given the level of decision making required;
 - ii) That a quorum of the Board of Directors is physically present in The Bahamas during the meetings;
 - iii) That strategic decisions made at such meetings are recorded in minutes;
 - iv) That the books and records of minutes are kept in The Bahamas; and,
 - v) That the Board of Directors has the necessary knowledge and expertise to discharge its duties.

Pure equity holding companies and passive holding entities are subject to reduced economic substance requirements. An included entity that is in the business of being a pure equity holding company (i.e. it only earns dividends and capital

2

**Commercial Entities
(Substance Requirements)
Act, 2018 (“CESA”)***Continued*

gains or incidental income from the holding of a subsidiary that is engaged in a relevant activity), is required to comply with all applicable laws and regulations of The Bahamas; and it shall have adequate human resources and adequate premises in The Bahamas for holding and managing equity participation in other entities. A non-included entity that is a passive holding entity (i.e. it does not have subsidiaries conducting relevant activities, nor does it conduct a relevant activity) is required only to comply with all applicable laws and regulations in The Bahamas.

Enhanced economic substance is required of included entities carrying on low-risk and high-risk intellectual property activities who have to meet the two-pronged test mentioned above and must demonstrate that additional prescribed activities are undertaken in The Bahamas.

When do I have to comply?

The time period for compliance with CESA is 6 months from the date of commencement of CESA for entities incorporated prior to commencement. Newly incorporated entities must comply immediately.

All commercial entities (included and non-included) must report on their status under CESA within 9 months of the entity's fiscal year end. The Minister of Finance is the Competent Authority for CESA purposes and has authority to spontaneously exchange information with reportable jurisdictions of legal or beneficial owners of Included Entities in the following circumstances:

- a) Included Entities engaged in high risk intellectual property activities;
- b) Included Entities who do not comply with substance requirements; or
- c) Non-included entities that claim to be non-included due to tax residence outside of The Bahamas. In this case a report is also made to the reportable jurisdiction of claimed tax residence of a non-included entity.

The list of reportable jurisdictions contained in the schedule of CESA is aligned with The Bahamas' Common Reporting Standard (CRS) reporting partners.

3

Removal of Preferential Exemptions Act, 2018 (“RPEA”)

Commencement Date: 31st December 2018

Who does it apply to?

The RPEA addresses the removal of ring fencing provisions and applies to companies or entities the operations of which are, or are intended to be, exclusively carried on outside of The Bahamas, and which are entitled to preferential exemptions and such exemptions are not afforded to a company/entity the operation of which is carried out in The Bahamas or the company or entity is not authorized to operate in The Bahamas.

What are the main obligations?

International Business Companies, Executive Entities, Exempted Limited Partnerships and Investment Condominiums on the Bahamas Company Register prior to the commencement of the RPEA and which were deemed non-resident for exchange control purposes and thus previously enjoyed an exemption from all taxes from the date of incorporation/registration for a period of 20 years, will now lose such exemption/s effective 3 years from the date of commencement of the Act. Newly incorporated entities will have no express statutory exemption from taxation in The Bahamas.

The Government has issued a clarifying circular which indicates that certain entities (likely operating in the domestic

commercial sphere) will be required to register for a business licence and pay business licence tax at a rate of between 0% and 2.5%. All entities which are regulated financial institutions will be exempt from business license tax, but they will pay a flat registration fee which will be set on a sliding scale between B\$2,250.00 and B\$250,000 per annum.

Guidelines to the Commercial Entities (Substance Requirements) Act, 2018 (the “Guidelines”) have been issued and Gazetted. The above summary may not fully reflect interpretative assistance contained in such Guidelines and does not constitute legal advice. This summary is intended to be general and non-exhaustive in nature and may not cover all material aspects of the legislation or the Guidelines which could impact you or your clients. Please contact us at Graham Thompson if you have any questions on the legislation or require specific advice.