Council of the European Union

Brussels, 1 February 2019
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NOTE

From:	General Secretariat of the Council
To:	Delegations
Subject:	The EU list of non-cooperative jurisdictions for tax purposes – Letters seeking commitment on the replacement by some jurisdictions of harmful preferential tax regimes with measures of similar effect

The Code of Conduct Group (Business Taxation) agreed, for transparency reasons, at its meeting of 30 January 2019 to publish on the Council's website the letters seeking commitment set out in annex to this document. These letters, signed by the Chair of the Code of Conduct Group, were sent by the General Secretariat of the Council to Barbados, Belize, Curaçao, Mauritius, Saint Lucia and Seychelles on 1 February 2019.

ANNEX

The Honourable Ronald TOPPIN
Minister of International Business and Industry
8th Floor, Baobab Tower
Warrens
St. Michael
BARBADOS

Brussels, 1 February 2019

Subject: Replacement of Barbados' harmful preferential tax regimes with measures of similar effect

Your Excellency,

We would like to thank you once again for the cooperation you have shown so far in the context of our dialogue on tax good governance standards.

As Barbados abolished its preferential tax regimes[1] at the request of the Council of the European Union by introducing regressive corporate income tax rates (as low as 1%) applicable to all entities, which fails to remove the harmful features or effects of the original regimes[2], the Code of Conduct Group has decided that Barbados should be treated as a jurisdiction that applies "a nominal corporate tax rate equal to zero or almost zero".

The Code of Conduct Group has for this reason identified these amendments to Barbados' Income Tax Act as a new measure falling under EU listing criterion 2.2.

This criterion has been agreed by the EU Finance Ministers in November 2016[3] and its scope has been further defined by the same Ministers in 2017 and finally in June 2018. This guidance is summarized in a "Scoping paper on criterion 2.2" (including two annexes), which is available at the following link: http://data.consilium.europa.eu/doc/document/ST-10421-2018-INIT/en/pdf

According to criterion 2.2, jurisdictions should not facilitate offshore structures or arrangements aimed at attracting profits which do not reflect real economic activity in the jurisdiction.

On this basis, Barbados needs to comply with the requirements under criterion 2.2, including by ensuring that legal mechanisms do not exist that enable the granting of advantages only to non-residents or in respect of transactions carried out with non-residents and that sufficient substance is required for entities doing business in or through your jurisdiction. The absence of adequate legal substance requirements increases the risk that profits registered in a jurisdiction are not commensurate with economic activities and substantial presence which is a concern from the

[1] Namely the International Business Companies (BB001), International Financial Services (B002), Exempt Insurance Company (BB003), Qualifying Insurance Companies (BB004), International Societies with Restricted Liability (BB005), International Trusts (BB007), Fiscal Incentives Act (BB008) and Foreign Currency Earnings Credit (BB009) regimes

[2] No further relevant data was provided by Barbados.

[3] The official publication of these Council Conclusions can be found in the *Official Journal of the European Union*: OJ C 461, 10.12.2016, page 2.

perspective of criterion 2.2.

Against this background, we would welcome to receive a commitment at a high political level that Barbados will address concerns outlined in line with the EU Terms of Reference and the above-mentioned scoping paper on criterion 2.2 by 31 December 2019, without any grandfathering mechanism.

In this case, the Code of Conduct Group will not recommend to the Council of the EU to include Barbados in the EU list of non-cooperative jurisdictions for tax purposes, as long as no other criteria have been failed.

With a view to demonstrate that Barbados has made meaningful commitments at high political level to take the necessary steps to address the issues identified by the EU, we would furthermore seek your consent to publish this commitment letter on the Council's website. This will ensure the transparency of the process.

Finally, the Code of Conduct Group would like to inform Barbados that no further replacement with measures of similar effect or delays will be accepted when assessing at the beginning of 2020 whether the requested commitments will have been implemented.

We would be grateful for your response to reach us by 15 February 2019.

Sincerely,

Fabrizia Lapecorella

c.c. General Secretariat of the Council
Unit DG G 2B – Tax Policy, Export Credits and Regional Policy
secretariat.cocg-jurisdictions@consilium.europa.eu
tel. +32 (0)2 281 72 75

Hon. Dean O. BARROW
Prime Minister and Minister of Finance
Charles Bartlett Hyde Building
Mahogany Street Ext.
Belmopan
BELIZE

Brussels, 1 February 2019

Subject: **Replacement of Belize's harmful preferential tax regimes with measures of similar effect**

Your Excellency,

We would like to thank you once again for the cooperation you have shown so far in the context of our dialogue on tax good governance standards.

As part of the assessment of the measures enacted by Belize to comply with its commitment to amend or abolish by the end of 2018 the preferential tax measures that the Council of the European Union had considered as harmful in December 2017 (International Business Companies - BZ001, and Export processing zones - BZ002), the Code of Conduct Group has identified the introduction of a new preferential tax measure: exemption of foreign income[1] (BZ006).

This measure was assessed by the Code of Conduct Group at its meeting of 30 January 2019 and deemed to have similar harmful effects as the harmful regimes that Belize had abolished at the end of 2018. You will find a copy of this assessment in annex to this letter.

Against this background, we would welcome to receive a commitment at a high political level that Belize will amend or abolish this regime by 31 December 2019, without any grandfathering mechanism.

In this case, the Code of Conduct Group will not recommend to the Council of the EU to include Belize in the EU list of non-cooperative jurisdictions for tax purposes, as long as no other criteria have been failed.

With a view to demonstrate that Belize has made meaningful commitments at high political level to take the necessary steps to address the deficiencies identified by the EU, we would furthermore seek your consent to publish this commitment letter on the Council's website. This will ensure the transparency of the process.

Finally, the Code of Conduct Group would like to inform Belize that no further replacement with measures of similar effect or delays will be accepted when assessing at the beginning of 2020

[1] New provisions introduced in the Income and Business Tax Act to include International Business Companies (IBCs) and companies operating in a Designating Processing Area (DPA) in the exemption of foreign income, and the general exemption of foreign source income included in the Income and Business Tax Act since 2001.

whether the requested commitments will have been implemented.

We would be grateful for your response to reach us by 15 February 2019.

Sincerely,

Fabrizia Lapecorella

c.c. General Secretariat of the Council
Unit DG G 2B – Tax Policy, Export Credits and Regional Policy
secretariat.cocg-jurisdictions@consilium.europa.eu
tel. +32 (0)2 281 72 75

Belize's exemption of foreign income regime (BZ006)

Gateway criterion - Significantly lower level of taxation:

"*Within the scope specified in paragraph A, tax measures which provide for a significantly lower effective level of taxation, including zero taxation, than those levels which generally apply in the Member State in question are to be regarded as potentially harmful and therefore covered by this code*"

The general income tax rate in Belize is 25%.

The income tax payable is reduced by the amount of business tax payable at the rate of 3% of all gross contract payments in excess of BZD 3,000.

IBCs and companies operating in a DPA are taxed at a special rate of 3% up to 3,000,000 BZD and at the rate of 1.75% above 3,000,000 BZD.

Under Section 4 and 7 of the Income and Business Tax Act, income derived by IBCs outside of Belize is exempt from income and business tax.

Under Section 4 of the Income and Business Tax Act, income derived outside of Belize by companies operating in a DPA is exempt from income tax. Companies operating in DPAs are exempt from business tax.

Therefore, the measure provides for a significant lower level of taxation and is potentially harmful under the Code.

	1a	**1b**	**2a**	**2b**	**3**	**4**	**5**
Belize – Exemption of foreign income	V	?	V	?	V	X	X

V = harmful

X = not harmful

<u>Explanation:</u>

Criterion 1 – Targeting non-residents:

"*whether advantages are accorded only to non-residents or in respect of transactions carried out with non-residents*"

Criterion 1a: The exemption from taxation of foreign source income is only applied in respect of transactions carried out with non-residents and it does not affect the national tax base. The measures are therefore ring-fenced.

Criterion 1b: There is a high risk that the new provision will have a de-facto ring-fencing effect, considering that the new provisions are likely to apply to those who benefited from the regime that Belize has amended, which were declared ring-fenced.

Information was requested from Belize in order to assess potential de facto ring-fencing. However, very little information was provided. There are currently 42,559 active IBC companies and 9,097 inactive IBCs as well as 3,341 new incorporations of IBCs in 2018 (table attached). Information provided on DPAs concern the types of activities as well as employment data.

Belize was unable to provide information on the type of activities (offshore and/or onshore) in which Belize IBCs were engaged. Belize also did not provide information the proportion of domestic owned/foreign owned entities (including IBC and companies operating in DPAs) as well as their average income.

More information should be gathered from Belize to be able to conclude on this point.

Criterion 2 – Ring-fencing:

"whether advantages are ring-fenced from the domestic market, so they do not affect the national tax base"

As the exemption on taxation applies only to transactions with non-residents, the national tax based is not affected.

What has been written above under criterion 1a and 1b also applies to criterion 2a and 2b.

Criterion 3 - Substance:

"*whether advantages are granted even without any real economic activity and substantial economic presence within the Member State offering such tax advantages*"

According to the standard practice for the evaluation of a measure against criterion 3, a measure is found harmful under this criterion if there are no specific requirements with regard to real economic activities and notably any requirement with respect to employment obligations.

The Income and Business Tax Act does not impose substance requirements for companies benefitting from the tax exemption. Some pieces of legislation may impose specific substance requirements for some type of companies, e.g. IBCs and DPAs. However, as mentioned above, the requirements concerning IBCs are of a limited nature. Moreover, the tax exemption on foreign source income under the Income and Business Tax Act covers a much broader range of entities and income.

It should also be noted that the exemption of foreign source income in Belize is broadly similar to participation exemption regimes in other jurisdictions. Regimes such as these should be properly contained by appropriate anti-abuse measures, in order to tackle tax-planning opportunities.

Paragraph L of the Code of Conduct states that anti-abuse provisions or countermeasures contained in tax laws and in double taxation conventions play a fundamental role in counteracting tax avoidance and evasion. In past assessments, the Code Group has taken into account, in the overall assessment of various regimes, the existence of appropriate anti-abuse rules. Such measures would include CFC rules or a switchover clause, in line with the agreed Code Guidance and previous assessments. The Income and Business Tax Act does not contain any of these measures.

Criterion 4 – Internationally accepted principles:

"*whether the rules for profit determination in respect of activities within a multinational group of companies departs from internationally accepted principles, notably the rules agreed upon within the OECD*"

The measures do not contain elements that would be relevant from the point of view of internationally accepted principles as referred to in criterion 4 of paragraph B of the Code.

Criterion 5 - Transparency

"whether the tax measures lack transparency, including where legal provisions are relaxed at administrative level in a non-transparent way"

All preconditions necessary for the granting of a tax benefit should be clearly laid down in publicly available laws, decrees, regulations etc. before a measure can be considered transparent.

Overall assessment:

In the light of the assessment made under all Code criteria, the regime would be considered as overall harmful.

Mr Kenneth A. GIJSBERTHA
Minister van Financiën
Ministerie van Financiën
Pietermaai 17
Willemstad
CURAÇAO

Brussels, 1 February 2019

Subject: Replacement of Curaçao's harmful preferential tax regimes with measures of similar effect

Your Excellency,

We would like to thank you once again for the cooperation you have shown so far in the context of our dialogue on tax good governance standards.

As part of the assessment of the measures enacted by Curaçao to comply with its commitment to amend or abolish by the end of 2018 the preferential tax measures that the Council of the European Union had considered as harmful in December 2017 (eZone - CW001, Export companies - CW002, and Investment Company - CW003), the Code of Conduct Group has identified the introduction of a new preferential tax measure: exemption of foreign income[1] (CW006).

This measure was assessed by the Code of Conduct Group at its meeting of 30 January 2019 and deemed to have similar harmful effects as the harmful regimes that Curaçao had abolished at the end of 2018. You will find a copy of this assessment in annex to this letter.

Against this background, we would welcome to receive a commitment at a high political level that Curaçao will amend or abolish this regime by 31 December 2019, without any grandfathering mechanism.

In this case, the Code of Conduct Group will not recommend to the Council of the EU to include Curaçao in the EU list of non-cooperative jurisdictions for tax purposes, as long as no other criteria have been failed.

With a view to demonstrate that Curaçao has made meaningful commitments at high political level to take the necessary steps to address the deficiencies identified by the EU, we would furthermore seek your consent to publish this commitment letter on the Council's website. This will ensure the transparency of the process.

Finally, the Code of Conduct Group would like to inform Curaçao that no further replacement with measures of similar effect or delays will be accepted when assessing at the beginning of 2020 whether the requested commitments will have been implemented.

[1] National Ordinance on Profit Tax of 1940 (section 1A, as amended).

We would be grateful for your response to reach us by 15 February 2019.

Sincerely,

Fabrizia Lapecorella

c.c. General Secretariat of the Council
Unit DG G 2B – Tax Policy, Export Credits and Regional Policy
secretariat.cocg-jurisdictions@consilium.europa.eu
tel. +32 (0)2 281 72 75

Curaçao's exemption of foreign income regime (CW006)

Gateway criterion - Significantly lower level of taxation:

"*Within the scope specified in paragraph A, tax measures which provide for a significantly lower effective level of taxation, including zero taxation, than those levels which generally apply in the Member State in question are to be regarded as potentially harmful and therefore covered by this code*"

The general tax rate in Curacao is 22%. Under the Ordinance on Profit Tax of 1940, certain foreign sourced incomes are tax exempted.

If a jurisdiction has introduced a general exemption / zero taxation in the general tax system, to replace the previous harmful regime, it needs to be considered whether the new measures pass the Gateway criterion of the Code. This Gateway criterion covers "*tax measures which provide for a significantly lower effective level of taxation, including zero taxation, than those levels which generally apply". That level "may operate by virtue of the nominal tax rate, the tax base or any other relevant factor*".

In the case of the Ordinance on Profit Tax of 1940, no tax is levied, compared to the general rate of 22%.

The provisions at issue operate by exempting foreign income from taxation. The beneficial tax treatment therefore seems only to apply to companies previously covered by the reformed regimes, which are only foreign companies. The tax base of domestic companies will therefore in effect be untouched.

As the Code of Conduct looks at the effects that tax legislation may have on the location of business activities in general terms, a full tax exemption may be regarded as one of the reasons for a business to establish in one jurisdiction over another. In this sense, the new provisions are relevant for the Code.

The Code of Conduct uses a broad term ('tax measures') to describe what should be assessed under its criteria. This definition is not limited to specific pieces of legislation nor does it circumscribe the meaning of what should be intended as a 'tax measure'. In the specific case of the measures introduced by Curacao, it is relevant to take into account the tax in order to understand whether the legislation provides for a significantly lower level of taxation.

A full exemption is lower than 22%. The measures cannot be viewed as generally applicable, as they result in only certain types of income being untaxed. Furthermore, the exemption is applied exclusively to transactions carried out with non-residents and almost exclusively concerns foreign entities. The intended result is a significantly lower level of taxation than the levels which generally apply.

	1a	1b	2a	2b	3	4	5
Curaçao - Exemption of foreign income	V	?	V	?	V	X	X

V = harmful

X = not harmful

Explanation:

Criterion 1 – Targeting non-residents:

"*whether advantages are accorded only to non-residents or in respect of transactions carried out with non-residents*"

Criterion 1a: The exemption from taxation of foreign source income is only applied in respect of transactions carried out with non-residents and it does not affect the national tax base. The measures are therefore ring-fenced.

Criterion 1.b: More information should be gathered from Curaçao to be able to make an assessment.

Criterion 2 – Ring-fencing:

"whether advantages are ring-fenced from the domestic market, so they do not affect the national tax base"

As the exemption on taxation applies only to transactions with non-residents, the national tax based is not affected.

What has been written above under criterion 1a and 1b also applies to criterion 2a and 2b.

Criterion 3 - Substance:

"*whether advantages are granted even without any real economic activity and substantial economic presence within the Member State offering such tax advantages*"

According to the standard practice for the evaluation of a measure against criterion 3, a measure is found harmful under this criterion if there are no specific requirements with regard to real economic activities and notably any requirement with respect to employment obligations.

Art. 1A of Ordinance on Profit Tax of 1940 does not impose substance requirements for companies benefitting from the tax exemption. Some pieces of legislation may impose substance requirements for certain type of companies, e.g. profits deriving from insurance and reinsurance services, income deriving from IP and from investment companies. However, the tax exemption on foreign source income under the Business Tax Act covers a broader range of income.

It should also be noted that the new provisions in Curacao are broadly similar to participation exemption regimes in other jurisdictions. Regimes such as these should be properly contained by appropriate anti-abuse measures, in order to tackle tax-planning opportunities.

Paragraph L of the Code of Conduct states that anti-abuse provisions or countermeasures contained in tax laws and in double taxation conventions play a fundamental role in counteracting tax avoidance and evasion. In past assessments, the Code Group has taken into account, in the overall assessment of various regimes, the existence of appropriate anti-abuse rules. Such measures would include CFC rules or a switchover clause, in line with the agreed Code Guidance and previous assessments. It is unclear whether certain measures included in the legislation are applicable.

Criterion 4 – Internationally accepted principles:

"*whether the rules for profit determination in respect of activities within a multinational group of companies departs from internationally accepted principles, notably the rules agreed upon within the OECD*"

The measures do not contain such elements that would be relevant from the point of view of internationally accepted principles as referred to in criterion 4 of paragraph B of the Code.

Criterion 5 - Transparency

"whether the tax measures lack transparency, including where legal provisions are relaxed at administrative level in a non-transparent way"

All preconditions necessary for the granting of a tax benefit should be clearly laid down in publicly available laws, decrees, regulations etc. before a measure can be considered transparent.

Overall assessment:

In the light of the assessment made under all Code criteria, the regime is overall harmful.

Mr Pravind JUGNAUTH
Prime Minister and Minister of Finance and
Economic Development
Prime Minister's Office
New Treasury Building
Intendance Street
Port Louis
MAURITIUS

Brussels, 1 February 2019

Subject: Replacement of Mauritius' harmful preferential tax regime(s) with measures of similar effect

Your Excellency,

We would like to thank you once again for the cooperation you have shown so far in the context of our dialogue on tax good governance standards.

As part of the assessment of the measures enacted by Mauritius to comply with its commitment to amend or abolish by the end of 2018 two of the preferential tax measures that the Council of the European Union had considered as harmful in December 2017 (Global Business Licence 1 - MU001, and Global Business Licence 2 - MU002), the Code of Conduct Group has identified the introduction of a new preferential tax measure: the Partial Exemption system[1] (MU010).

This measure was assessed by the Code of Conduct Group at its meeting of 30 January 2019 and deemed to have similar harmful effects as the harmful regimes that Mauritius had abolished at the end of 2018. You will find a copy of this assessment in annex to this letter.

Against this background, we would welcome to receive a commitment at a high political level that Mauritius will amend or abolish this regime by 31 December 2019, without any grandfathering mechanism.

In this case, the Code of Conduct Group will not recommend to the Council of the EU to include Mauritius in the EU list of non-cooperative jurisdictions for tax purposes, as long as no other criteria have been failed.

With a view to demonstrate that Mauritius has made meaningful commitments at high political level to take the necessary steps to address the deficiencies identified by the EU, we would furthermore seek your consent to publish this commitment letter on the Council's website. This will ensure the transparency of the process.

Finally, the Code of Conduct Group would like to inform Mauritius that no further replacement with measures of similar effect or delays will be accepted when assessing at the beginning of 2020

[1] Introduced by the Finance Act 2018 (of 9 August 2018)

whether the requested commitments will have been implemented.

We would be grateful for your response to reach us by 15 February 2019.

Sincerely,

Fabrizia Lapecorella

c.c. General Secretariat of the Council
Unit DG G 2B – Tax Policy, Export Credits and Regional Policy
secretariat.cocg-jurisdictions@consilium.europa.eu
tel. +32 (0)2 281 72 75

Mauritius' Partial Exemption system (MU010)

Gateway criterion - Significantly lower level of taxation:

"*Within the scope specified in paragraph A, tax measures which provide for a significantly lower effective level of taxation, including zero taxation, than those levels which generally apply in the Member State in question are to be regarded as potentially harmful and therefore covered by this code*"

The general tax rate in Mauritius is 15%. However, as a result of the reform enacted by the Finance Bill 2018, Mauritius introduced the Partial Exemption regime where 80% of specified income of global business companies will be exempted from corporate tax. The income categories exempt from tax are:

1. Partial Exemption for foreign source dividends,

2. Exemption for profits attributable to a foreign PE,

3. Exemption for dividends and interest income derived by a company whether from a local source or foreign source; and

4. Exemption for income from provision of specified financial services (investment management and investment advisory activities conducted in and from within Mauritius, ship and aircraft leasing, CIS/CEF).

This measure provides for a significant lower level of taxation and is therefore potentially harmful under the Code of Conduct.

	1a	**1b**	**2a**	**2b**	**3**	**4**	**5**
Mauritius – Partial Exemption system (MU10)	X	?	X	?	V	X	X

V = harmful

X = not harmful

Explanation:

Criterion 1 – Targeting non-residents:

"*whether advantages are accorded only to non-residents or in respect of transactions carried out with non-residents*"

Criterion 1a: The partial exemption regime is available to both residents and non-residents and does not require that the beneficiaries carry out transactions only with non-residents.

Criterion 1b: There is no information on the de facto effect of the measure. However on the basis of publicly available information (from the Mauritius Financial Services Commission) collected by the Commission Services on the usage of the GBL 1, regime it appears that the Partial Exemption regime will mostly benefit companies not doing business in Mauritius. This information was presented to the Group at the meeting of 12 October 2018 (document ST12967/2018):

Licensees under domestic regime

- Financial service providers: 40
- Specialised financial services / institutions: 30
- Corporate trust service providers: 181
- Insurers: 274
- Pensions: 65
- Intermediaries: 238

Total of domestic licensees: 828

Licensees under Global Business Regime

- GBC 1: 10'756
- GBC 2: 10'688

Total of offshore licensees: 21'444

On the basis of the above figures, a preliminary assessment would suggest that the 80% exemption on income from financial services would mostly benefit companies not doing any business in Mauritius. Mauritius has challenged these statistics and disagrees with our conclusions. According to Mauritius, 1,153 (or less) GBL1 companies are likely to benefit from the new regime, and 1,700 non-GBL companies are expected to benefit.

Since the conclusions were based on the statistics for the abolished GBL 1 regime and no statistics are available for the use of the new regime, the usage of this regime will be monitored by the Group in order to establish if a situation of de facto ring-fencing exists.

Criterion 2 – Ring-fencing:

"*whether advantages are ring-fenced from the domestic market, so they do not affect the national tax base*"

As regards criterion 2 the division between criteria 2a and 2b is done in the same way as in the case of criterion 1 (i.e. de jure interpretation and de facto analysis). In general, a measure is caught by criterion 2 if the advantages are ring-fenced from the domestic market so that they do not affect the national tax base. In most cases, the evaluation against criterion 2 follows closely that of criterion 1.

What has been written above under criterion 1a and 1b also applies to criterion 2a and 2b.

Criterion 3 - Substance:

"*whether advantages are granted even without any real economic activity and substantial economic presence within the Member State offering such tax advantages*"

According to the standard practice for the evaluation of a measure against criterion 3, a measure is found harmful under this criterion if there are no specific requirements with regard to real economic activities and notably any requirement with respect to employment obligations.

While the Partial Exemption regime does have substance requirements, they are not entirely in line with international best practice, in particular in terms of how they treat outsourcing. As agreed by the Code Group in the meeting of 21 September 2018, based on the progress report on the Crown Dependencies (ST 12196/2018), outsourcing should not be a practice used to circumvent the need for economic substance within a jurisdiction. Therefore, the outsourcing of core income generating activities is only permitted to occur within the jurisdiction concerned. In addition the primary entity should have the capacity to properly supervise and control the work of the entity to which the core functions have been outsourced; and the substance of the outsourcing provider (employees, expenditure and premises) should not be used multiple times by multiple primary entities that outsource to the same outsourcing provider. Jurisdictions should demonstrate that outsourcing is not used to circumvent compliance with the requirements. A similar approach to outsourcing is also included in the OECD FHTP draft document *Approach to review of substantial activities requirements for no or only nominal tax jurisdictions*[2].

Regimes such as the partial exemption regime should also be properly contained by appropriate anti-abuse measures in order to tackle tax-planning opportunities.

Paragraph L of the Code of Conduct states that: "anti-abuse provisions or countermeasures contained in tax laws and in double taxation conventions play a fundamental role in counteracting tax avoidance and evasion". In past assessments, the Code Group has taken into account, in the overall assessment of various regimes, the existence of appropriate anti-abuse rules.

Such measures would include CFC rules or a switchover clause, in line with the agreed Code Guidance and previous assessments. In response to our queries Mauritius outlined certain provisions in its legislation such as the application of the arm's length test and a general anti-abuse rule. However, our understanding is that the Mauritius general anti-avoidance rule only covers transactions aimed at avoiding tax that should have been due in Mauritius. Therefore any schemes

[2] CTPA/CFA/FHP/NOE2(2018)15 approved by the FHTP but still to be approved by CFA.

involving Mauritius but aimed at eroding other countries' tax bases would not be covered. Mauritius did not agree to introduce CFC rules or a switchover clause.

Criterion 4 – Internationally accepted principles:

"*whether the rules for profit determination in respect of activities within a multinational group of companies departs from internationally accepted principles, notably the rules agreed upon within the OECD*"

The measures do not contain such elements that would be relevant from the point of view of internationally accepted principles as referred to in criterion 4 of paragraph B of the Code.

Criterion 5 - Transparency

"whether the tax measures lack transparency, including where legal provisions are relaxed at administrative level in a non-transparent way"

All preconditions necessary for the granting of a tax benefit should be clearly laid down in publicly available laws, decrees, regulations etc. before a measure can be considered transparent.

Overall assessment:

The overall assessment is that this regime is harmful.

H.E. Allen M. CHASTANET
Prime Minister & Minister for Finance,
Economic Growth, Job Creation, External
Affairs and the Public Service
Office of the Prime Minister
Greaham Louisy Administrative Building
Waterfront, Castries
SAINT LUCIA

Brussels, 1 February 2019

Subject: Replacement of Saint Lucia's harmful preferential tax regime(s) with measures of similar effect

Your Excellency,

We would like to thank you once again for the cooperation you have shown so far in the context of our dialogue on tax good governance standards.

As part of the assessment of the measures enacted by Saint Lucia to comply with its commitment to amend or abolish by the end of 2018 the preferential tax measures that the Council of the European Union had considered as harmful in December 2017 (International Business Companies - LC001, International Trusts - LC002, and Free trade zones - LC003), the Code of Conduct Group has identified the introduction of a new preferential tax measure: exemption of foreign income[1] (LC005).

This measure was assessed by the Code of Conduct Group at its meeting of 30 January 2019 and deemed to have similar harmful effects as the harmful regimes that Saint Lucia had abolished at the end of 2018. You will find a copy of this assessment in annex to this letter.

Against this background, we would welcome to receive a commitment at a high political level that Saint Lucia will amend or abolish this regime by 31 December 2019, without any grandfathering mechanism.

In this case, the Code of Conduct Group will not recommend to the Council of the EU to include Saint Lucia in the EU list of non-cooperative jurisdictions for tax purposes, as long as no other criteria have been failed.

With a view to demonstrate that Saint Lucia has made meaningful commitments at high political level to take the necessary steps to address the deficiencies identified by the EU, we would furthermore seek your consent to publish this commitment letter on the Council's website. This will ensure the transparency of the process.

Finally, the Code of Conduct Group would like to inform Saint Lucia that no further replacement with measures of similar effect or delays will be accepted when assessing at the beginning of 2020

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[1] Income Tax Act, as amended by Act N°12 of 11 December 2018 (sections 8, 10A and 76).

whether the requested commitments will have been implemented.

We would be grateful for your response to reach us by 15 February 2019.

Sincerely,

Fabrizia Lapecorella

c.c. General Secretariat of the Council
Unit DG G 2B – Tax Policy, Export Credits and Regional Policy
secretariat.cocg-jurisdictions@consilium.europa.eu
tel. +32 (0)2 281 72 75

Saint Lucia's exemption of foreign income regime (LC005)

Gateway criterion - Significantly lower level of taxation:

If a jurisdiction has introduced a general exemption / zero taxation in the general tax system, to replace the previous harmful regime, it needs to be considered whether the new measures pass the Gateway criterion of the Code. This Gateway criterion covers "*tax measures which provide for a significantly lower effective level of taxation, including zero taxation, than those levels which generally apply*". That level "*may operate by virtue of the nominal tax rate, the tax base or any other relevant factor*".

In the case of the Income Tax Act, no tax is levied, compared to the general rate of 30%.

The provisions at issue operate by exempting foreign income from taxation. The beneficial tax treatment therefore seems only to apply to companies previously covered by the IBC regime, which are only foreign companies. The tax base of domestic companies will therefore in effect be untouched.

As the Code of Conduct looks at the effects that tax legislation may have on the location of business activities in general terms, a full tax exemption may be regarded as one of the reasons for a business to establish in one jurisdiction over another. In this sense, the new provisions are relevant for the Code.

The Code of Conduct uses a broad term ('*tax measures*') to describe what should be assessed under its criteria. This definition is not limited to specific pieces of legislation nor does it circumscribe the meaning of what should be intended as a '*tax measure'*. In the specific case of the measures introduced by Saint Lucia, it is relevant to take into account the tax in order to understand whether the legislation provides for a significantly lower level of taxation.

A full exemption is lower than 30%. The measures cannot be viewed as generally applicable, as they result in only certain types of income being untaxed. Furthermore, the exemption is applied exclusively to transactions carried out with non-residents and almost exclusively concerns foreign entities. The intended result is a significantly lower level of taxation than the levels which generally apply.

	1a	**1b**	**2a**	**2b**	**3**	**4**	**5**
Saint Lucia – Exemption of foreign income	V	?	V	?	X	X	X

V = harmful

X = not harmful

Explanation:

Criterion 1 – Targeting non-residents

"*whether advantages are accorded only to non-residents or in respect of transactions carried out with non-residents*"

and Criterion 2 – Ring-fencing:

"whether advantages are ring-fenced from the domestic market, so they do not affect the national tax base"

Criteria 1a and 2a: The measures excepting certain income from tax relate to foreign income and profit distributions related to that foreign income only. Domestic income and domestic profit distributions are taxed at a higher rate (30%). This is a clear case of ring-fencing under criterion 1 and 2 of the Code of Conduct, as it is limited to transactions carried out with non-residents.

Criteria 1b and 2b: There are no statistics on the actual use of the new provisions yet.

Criterion 3 - Substance:

"*whether advantages are granted even without any real economic activity and substantial economic presence within the Member State offering such tax advantages*"

Saint Lucia has introduced a substance requirement under Section 5A(3) of the amended IBC regime by requiring that IBCs: *"(b) shall — (i) have an adequate number of employees with the necessary level of qualifications and experience, (ii) have an adequate amount of operating expenses, (iii) have an adequate amount of investment and capital that is commensurate with the type and level of activity undertaken by the company,*"

Any company which qualifies as an IBC would have to comply with the substance requirement. It appears that the new measures are intended to benefit mainly IBCs. Therefore, it can be assumed that the majority of companies benefitting from the exemptions will satisfy the substance requirement.

However, the Income Tax Act does not seem to contain a substance requirement. Therefore, companies that do not benefit from the status of IBCs would not seem to have to comply with any substance requirements.

As we assume that almost all companies benefitting from the exemption will be IBCs, it follows that there is a sufficient substance requirement.

Criterion 4 – Internationally accepted principles:

"*whether the rules for profit determination in respect of activities within a multinational group of companies departs from internationally accepted principles, notably the rules agreed upon within the OECD*"

Saint Lucia has sufficient provisions on transfer pricing based on the arm's length principle.

Criterion 5 - Transparency

"whether the tax measures lack transparency, including where legal provisions are relaxed at administrative level in a non-transparent way"

The conditions for benefitting from the beneficial tax treatment are sufficiently set out in the legislation.

Overall assessment:

The regime is overall harmful as it is ring-fenced to transactions carried out with non-residents.

Ambassador Maurice LOUSTAU-LALANNE
Minister of Finance, Trade, Investment and
Economic Planning
Ministry of Finance, Trade, Investment and
Economic Planning
P.O. Box 313
SEYCHELLES

Brussels, 1 February 2019

Subject: Replacement of Seychelles' harmful preferential tax regimes with measures of similar effect

Your Excellency,

We would like to thank you once again for the cooperation you have shown so far in the context of our dialogue on tax good governance standards.

As part of the assessment of the measures enacted by Seychelles to comply with its commitment to amend or abolish by the end of 2018 the preferential tax measures that the Council of the European Union had considered as harmful in December 2017[1], the Code of Conduct Group has identified the introduction of a new preferential tax measure: exemption of foreign income[2] (SC011).

This measure was assessed by the Code of Conduct Group at its meeting of 30 January 2019 and deemed to have similar harmful effects as the harmful regimes that Seychelles had abolished at the end of 2018. You will find a copy of this assessment in annex to this letter.

Against this background, we would welcome to receive a commitment at a high political level that Seychelles will amend or abolish this regime by 31 December 2019, without any grandfathering mechanism.

In this case, the Code of Conduct Group will not recommend to the Council of the EU to include Seychelles in the EU list of non-cooperative jurisdictions for tax purposes, as long as no other criteria have been failed.

With a view to demonstrate that Seychelles has made meaningful commitments at high political level to take the necessary steps to address the deficiencies identified by the EU, we would furthermore seek your consent to publish this commitment letter on the Council's website. This will ensure the transparency of the process.

Finally, the Code of Conduct Group would like to inform Seychelles that no further replacement with measures of similar effect or delays will be accepted when assessing at the beginning of 2020

[1] Namely the International Business Companies (SC00), International trade zone (SC002), Offshore banks (SC003), Offshore insurance (SC004), Companies special license (SC005), Securities Business under the Securities Act (SC007), and the Fund Administration Business (SC008).

[2] Business Tax Act, as amended (sections 2, 5, 8, 11 and 67).

whether the requested commitments will have been implemented.

We would be grateful for your response to reach us by 15 February 2019.

Sincerely,

Fabrizia Lapecorella

c.c. General Secretariat of the Council
Unit DG G 2B – Tax Policy, Export Credits and Regional Policy
secretariat.cocg-jurisdictions@consilium.europa.eu
tel. +32 (0)2 281 72 75

Seychelles' exemption of foreign income regime (SC011)

Gateway criterion - Significantly lower level of taxation:

"*Within the scope specified in paragraph A, tax measures which provide for a significantly lower effective level of taxation, including zero taxation, than those levels which generally apply in the Member State in question are to be regarded as potentially harmful and therefore covered by this code*"

The general tax rate in Seychelles is either 25%, or 33% if the income exceeds 1.000.000 SCR. If a jurisdiction has introduced a general exemption / zero taxation in the general tax system, to replace the previous harmful regime, it needs to be considered whether the new measures pass the Gateway criterion of the Code. This Gateway criterion covers "*tax measures which provide for a significantly lower effective level of taxation, including zero taxation, than those levels which generally apply". That level "may operate by virtue of the nominal tax rate, the tax base or any other relevant factor*".

In the case of the Business Tax Act, no tax is levied, compared to the general tax rate of 25 or 33%.

The provisions at issue operate by exempting foreign income from taxation. The beneficial tax treatment therefore seems only to apply to companies previously covered by the reformed regimes, which are only foreign companies. The tax base of domestic companies will therefore in effect be untouched.

As the Code of Conduct looks at the effects that tax legislation may have on the location of business activities in general terms, a full tax exemption may be regarded as one of the reasons for a business to establish in one jurisdiction over another. In this sense, the new provisions are relevant for the Code.

The Code of Conduct uses a broad term ('tax measures') to describe what should be assessed under its criteria. This definition is not limited to specific pieces of legislation nor does it circumscribe the meaning of what should be intended as a 'tax measure'. In the specific case of the measures introduced by Seychelles, it is relevant to take into account the tax in order to understand whether the legislation provides for a significantly lower level of taxation.

A full exemption is lower than 25 or 33%. The measures cannot be viewed as generally applicable, as they result in only certain types of income being untaxed. Furthermore, the exemption is applied exclusively to transactions carried out with non-residents and almost exclusively concerns foreign entities. The intended result is a significantly lower level of taxation than the levels which generally apply.

	1a	1b	2a	2b	3	4	5
Seychelles – Exemption of foreign income	V	?	V	?	V	X	X

V = harmful

X = not harmful

Explanation:

Criterion 1 – Targeting non-residents:

"*whether advantages are accorded only to non-residents or in respect of transactions carried out with non-residents*"

Criterion 1a: The exemption from taxation of foreign source income is only applied in respect of transactions carried out with non-residents and it does not affect the national tax base. The measures are therefore ring-fenced.

Criterion 1b: there is a high risk that the new provision will have a de-facto ring-fencing effect, considering that the new provisions are likely to apply to those who benefited from the regimes that Seychelles has abolished which were declared ring-fenced. However, more information should be gathered from Seychelles to be able to conclude on this point.

Criterion 2 – Ring-fencing:

"whether advantages are ring-fenced from the domestic market, so they do not affect the national tax base"

As the exemption on taxation applies only to transactions with non-residents, the national tax based is not affected.

What has been written above under criterion 1a and 1b also applies to criterion 2a and 2b.

Criterion 3 - Substance:

"*whether advantages are granted even without any real economic activity and substantial economic presence within the Member State offering such tax advantages*"

According to the standard practice for the evaluation of a measure against criterion 3, a measure is found harmful under this criterion if there are no specific requirements with regard to real economic activities and notably any requirement with respect to employment obligations.

The Business Tax Act does not impose substance requirements for companies benefitting from the tax exemption. Some pieces of legislation may impose substance requirements for certain type of companies, e.g. certain type of financial services companies under the Security Act. However, the tax exemption on foreign source income under the Business Tax Act covers a much broader range of income.

It should also be noted that the new provisions in the Seychelles are broadly similar to participation exemption regimes in other jurisdictions. Regimes such as these should be properly contained by appropriate anti-abuse measures, in order to tackle tax-planning opportunities.

Paragraph L of the Code of Conduct states that anti-abuse provisions or countermeasures contained in tax laws and in double taxation conventions play a fundamental role in counteracting tax avoidance and evasion. In past assessments, the Code Group has taken into account, in the overall assessment of various regimes, the existence of appropriate anti-abuse rules. Such measures would include CFC rules or a switchover clause, in line with the agreed Code Guidance and previous assessments. The Business Tax Act does not contain any of these measures.

Criterion 4 – Internationally accepted principles:

"*whether the rules for profit determination in respect of activities within a multinational group of companies departs from internationally accepted principles, notably the rules agreed upon within the OECD*"

The measures do not contain such elements that would be relevant from the point of view of internationally accepted principles as referred to in criterion 4 of paragraph B of the Code.

Criterion 5 - Transparency

"whether the tax measures lack transparency, including where legal provisions are relaxed at administrative level in a non-transparent way"

All preconditions necessary for the granting of a tax benefit should be clearly laid down in publicly available laws, decrees, regulations etc. before a measure can be considered transparent.

Overall assessment:

In the light of the assessment made under all Code criteria, the regime is overall harmful.