Council of the
European Union

**Brussels, 12 March 2019**
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**FISC 157**

**OUTCOME OF PROCEEDINGS**

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| From: | General Secretariat of the Council |
| To: | Delegations |
| Subject: | The EU list of non-cooperative jurisdictions for tax purposes<br>• Turks and Caicos Islands: final legislation and assessment under criterion 2.2 |

## A/ FINAL LEGISLATION:

The Companies and Limited Partnerships (Economic Substance) Ordinance, 2018 was passed in Parliament on 27 December 2018, with the Cabinet approving Companies and Limited Partnerships (Economic Substance) Regulations under the new Ordinance on the same day. Statutory notice was issued and the Ordinance and Regulation came into force on 1 January 2019.

https://www.gov.tc/agc/laws/annual-laws/2018-laws/2018-ordinances

https://www.gov.tc/agc/laws/annual-laws/2018-laws/2018-subsidiary-legislation

An amendment to the Companies and Limited Partnerships (Economic Substance) Ordinance was subsequently adopted and published on 20 February 2019:

https://www.gov.tc/agc/laws/annual-laws/2019-laws/2019-ordinances

**B/ FINAL ASSESSMENT:**

Although limited at first, the dialogue with Turks and Caicos Islands (TCI), which is a small jurisdiction with capacity constraints, improved in autumn 2018 with a note followed by first draft legislation for Member States' feedback in December 2018. The following assessment only highlights the remaining issues identified and still pending at the beginning of 2019 following such feedback.

**1 – Identification of the relevant activities and included entities**

**1.1 – On relevant activities**

Section 7(j) distinguishes between pure equity holdings subject to minimum substance requirements (complying with statutory obligations as well as, under Section 8-5 having an adequate number of persons and premises for managing the shares or equitable interests it holds) and other types of holdings that are considered together with the relevant activities for which they receive income.

*Conclusion:*

This issue is settled.

**1.2 – On included entities**

TCI decided to include in the scope of substance requirements body corporates as well as limited partnerships incorporated in or outside TCI.

It remains unclear whether other types of partnerships are allowed under TCI legislation. From publicly available information, it seems however that TCI allows for two types of partnerships (ordinary common law partnerships with unlimited liability and limited partnerships).

*Conclusion:*

This issue is clarified and the risk of BEPS should be limited. However, over the coming months, the situation will be monitored to determine if it is necessary to include all types of partnerships in the scope of the substance requirements.

## 2 – Imposition of substance requirements

### 2.1 – Income threshold

Following the guidance received from the Code of Conduct Group, section 8 of the Act no longer refers to an income threshold.

*Conclusion:*

This issue is settled.

### 2.2 – Tax residence

TCI has amended its rules on exclusions from the scope of substance requirements of entities based on tax residence in another jurisdiction.

Companies and Limited Partnerships that are incorporated in TCI or registered as foreign companies are prima facie considered as tax resident in TCI.

By exception, such an entity that is tax resident in another jurisdiction which is not on the EU list of non-cooperative jurisdictions for tax purposes is not considered as resident in TCI and thus not subject to substance requirements.

The Regulation provides that the entity claiming to be tax resident in another jurisdiction will have to report which jurisdiction it considers to be a tax resident in and other information relating to its residency as specified in the form. We don't have the form for filing information. However, Regulation 5(5) provides that a TCI entity that claims to be tax resident in another country shall provide a tax certificate or equivalent document issued by the tax authority in the country concerned or, if such document is not available, such other documents that the Competent Authority considers demonstrates its tax residency.

Section 18 of the Ordinance provides for spontaneous exchange of information with the Member States in which the TCI entity claims to be tax resident, in which each holding and ultimate holding entity of the TCI is located, in which each ultimate beneficial owner of the TCI entity is located.

A remaining issue is that, for newly incorporated companies or partnerships, TCI considers that such entity is not resident in TCI in its first accounting period, provided that it is resident in another jurisdiction which is not on the EU list for at least 50% of the accounting period. In its explanatory note, TCI explains it adopted this provision so that newly incorporated companies and partnerships have time to organise their tax residence outside of TCI.

*Conclusion:*

This issue is settled.

**2.3 – Specific CIGAs for IP assets**

The Code of Conduct Group agreed that R&D should to be considered as the appropriate CIGA for patents whereas marketing, branding and distribution should to be considered as the appropriate CIGAs for non-trade intangibles such as brand, trademark and customer data. Other CIGAs can only be allowed in exceptional cases when the main CIGAs are not present.

Section 7(g) of the Ordinance makes a direct link between patents and R&D.

Section 7(h) of the Ordinance makes a direct link between other IP assets and marketing, trading and distribution. It also allows, for other IP assets and in exceptional cases, to take into consideration the other IP CIGAs such as taking strategic decisions and managing, as well as bearing the principal risks related to the development or acquisition by third parties and subsequent exploitation of the IP asset and carrying on the underlying trading activities.

*Conclusion:*

This issue is settled.

**2.4 – CIGAs in or from within the jurisdiction**

CIGAs have to be carried on in the jurisdiction.

Section 7(2) was amended in that sense.

*Conclusion:*

This issue is settled.

**2.5 – Outsourcing safeguards**

Outsourcing safeguards were not sufficient as there was no reference to prohibition of double counting of the resources of the service providers.

Section 8(4) was amended to include reference that "*only that part of the activities of the outsourcing service provider which are attributable to generating income for the relevant legal entity shall be taken into account when considering if the relevant legal entity meets the economic substance requirements*".

The Regulation provided that if the activity was outsourced, the entity shall file information demonstrating that the activity is conducted in TCI, adequate supervision of the outsourced activity and that only the part of the activities of the outsourcing service provider that is attributable to generating income for the relevant legal entity is taken into account.

The wording in TCI legislation was similar to the one previously used by the BVI and that was considered as not sufficient. When taking into account the part of the activities of the service provider linked to the generation of income for the primary entity, it should be clearly ensured that there will be no double counting of resources of service providers.

The explanatory note to the Ordinance clarified the intent of TCI to prohibit multiple counting of the resources of the service provider. However, if the resources of the service provider could be considered to generate income for several entities, the current wording did not prevent each entity from counting the resources in its own substance test. As amended by the BVI, it should be clear that only the part of the activities of the service providers that is solely attributable to generating income for the legal entity and not for any other legal entity will be taken into account.

The Commission services therefore reported to TCI a negative assessment of the outsourcing safeguards, in particular, on the prohibition of double counting of the resources of the service providers. After further discussion and exchanges of emails with the Commission services, Turks and Caicos have amended Section 8 of their Principal Act[1] in order to improve the wording on the prohibition of double counting:

1 Companies and Limited Partnerships (Economic Substance) (Amendment) Ordinance 2019 as adopted and published on 20 February 2019.

"*Only that part of the activities of the outsourcing service provider which are* <u>*solely attributable*</u> *to generating income for the relevant entity* <u>*and not for any other entity*</u> *shall be taken into account when considering if the relevant entity meets the economic substance requirements*".

With this new wording, the risk of double counting of the substance of a service provider by several relevant entities should more efficiently be contained.

<u>*Conclusion:*</u>

This issue is settled.

**2.6 – <u>IP low-risk and high-risk scenarios</u>**

One issue in the definition of high-risk IP scenarios was the additional condition that the company did not "create" the intellectual property in the asset, which could create cases in which not all situations would be covered.

The final legislation provides for an alternative definition of high-risk IP scenarios either:

- the entity acquired the IP asset from a group entity or in consideration for funding R&D by another person situated outside TCI and licenses the IP asset to one or more group entities or otherwise generates income from the asset in consequence of activities performed by foreign group entities; or

- the entity does not carry out either R&D or branding, distribution as part of its CIGAs in TCI.

The first alternative corresponds to the definition of the Scoping Paper. The second one is an additional option to be considered as high-risk IP and subject to additional requirements.

Another issue with high-risk IP scenarios was that TCI introduced the presumption of non-compliance but did not detail the higher evidential threshold.

Section 8(6) and (7) of the Ordinance provide for the presumption of non-compliance in high-risk IP scenarios together with a need to demonstrate that there is, and in the past there has been, a high degree of control over the development, exploitation, maintenance, enhancement and protection of the IP asset exercised by an adequate number of suitably qualified full-time employees who reside in, and perform their functions from within TCI.

The Regulation provides that those entities have to file additional information in that sense with detailed business plan that demonstrate the rationale for holding the IP asset in TCI, information relied on to rebut the presumption that the entity does not conduct CIGAs in TCI. In particular, information to demonstrate matters specified in Section 8(7) is required.

*Conclusion:*

This issue is settled.

**3 – Enforcement and sanction mechanism**

**3.1 – Filing obligations**

There was a lack of information on the filing obligations.

Section 5 of the Regulation provides for an extensive set of information to be provided by entities, in line with the scoping paper.

*Conclusion:*

This issue is settled.

**2.5 Sanctions framework**

TCI's sanctions framework was not dissuasive enough because of the absence of fixed or minimum amounts of civil penalty, absence of a fixed deadline for actions to be taken and the strike-off only considered as an option after 2 years of non-compliance.

The amount of penalties and deadline for actions to be taken have not been modified. However, TCI legislation now prescribes that the authority shall apply to the Court for an order during the accounting period that follows the first notice of non-compliance. The court may order actions to be taken or a strike-off the register.

*Conclusion:*

This issue is settled. The efficient enforcement of the substance legislation will be monitored over the coming years.

**Conclusion**

Turks and Caicos Islands have implemented their commitment to introduce substance requirements.

ANNEX 1: assessment by COCG experts in 2017

**ANNEX 1**

## ASSESSMENT BY COCG EXPERTS IN 2017

<table>
<tr><th></th><th>1a</th><th>1b</th><th>2a</th><th>2b</th><th>3</th><th>4</th><th>5</th></tr>
<tr><td>Turks and Caicos Islands</td><td>V</td><td>V</td><td>V</td><td>V</td><td>V</td><td>?</td><td>?</td></tr>
<tr><td colspan="6">Criterion 2.2: "The jurisdiction should not facilitate offshore structures or arrangements aimed at attracting profits which do not reflect real economic activity in the jurisdiction"<br><br>In light of the assessment made under all Code criteria applied by analogy, the tax system of the TCI should be considered overall harmful from a Code of Conduct point of view.<br><br>The main concerns on deviations from the Code of Conduct criteria as applied by analogy relate to the lack of legal substance requirements.<br><br>In addition there are legal and de facto mechanisms that enable the granting of advantages only to non-residents or in respect of transactions carried out with non-residents.</td><td colspan="2">Overall:<br><br>V</td></tr>
</table>

Explanation

**Absence of a corporate tax system or applying a nominal corporate tax rate equal to zero or almost zero:**

In this respect, where criterion 2.1 is inapplicable solely due to the fact that the jurisdiction concerned does not meet the gateway criterion under Paragraph B of the Code of Conduct, because of the "absence of a corporate tax system or applying a nominal corporate tax rate equal to zero or almost zero", then the five factors identified in paragraph B of the Code of Conduct should be applied by analogy to assess whether the criterion 2.2 has been met.

Relevant questions (Q 1.2)

*TCI does not apply any corporate tax system. We therefore suggest that this jurisdiction meets the gateway test of the criterion 2.2.*

**Criterion 1**:

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

Relevant questions (Q 2.1, Q 2.2, Q 2.3, Q 1.1, Q 1.2, Q 1.5, Q 1.8,)

*The absence in principle of CIT in the TCI is de lege applicable to both residents and non-residents. On the other hand a significant number of entities registered in the TCI are not allowed to operate and carry on business in the TCI.*

*We would therefore propose a tick ("V" - harmful) for criterion 1a).*

*According to data provided by TCI, in 2018 out of the 16,491 legal entities registered in this jurisdiction, 10.605 are "exempted" companies (i.e. those restricted from carrying on business in TCI) and 164 are "foreign exempted". The situation will not change with the new law to be in force as of 1 November 2018, since in any case exempted companies will become "international companies", which will continue to have a restriction from carrying on business in the islands. Based on figures provided by TCI, by 1st November 2018 there should be 10786 international companies, based on current data. TCI was not able to provide data on how many exempt/foreign exempt/international companies are owned by non-resident but said this data will be available once the new beneficial ownership requirements will be in force.*

*We would therefore propose a tick ("V" - harmful) for criterion 1b).*

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| **Criterion 2**:<br><br>“whether advantages are ring-fenced from the domestic market, so they do not affect the national tax base” |
| <u>Relevant questions (Q 2.1, Q 2.2, Q 2.3, Q 1.1, Q 1.2, Q 1.5, Q 1.8,)</u><br><br>*By analogy to the assessment against criterion 1a/b. We would propose a tick ("V" –harmful) for criterion 2a) and b).* |

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| **Criterion 3**:<br><br>“whether advantages are granted even without any real economic activity and substantial economic presence within the jurisdiction offering such tax advantages” |
| <u>Relevant questions (Q 1.1, Q 1.7, Q 1.9, Q 2.4, Q 2.5, Q 2.6, Q 2.7, Q 2.8)</u><br><br>*According to the reply to the questionnaire, there are no substance requirements in TCI to be satisfied by companies doing business in the jurisdictions (see reply to Q. 2.4). Some sort of substance requirements could be deemed to exist within the new procedure for granting licenses to Company Managers (see reply to Q. 1.9), which are providers of company management services in TCI. In this case in fact the authorising office has to verify certain requirements, in particular: "<u>the company has personnel with relevant skill and expertise</u>, the company is solvent, the company is adequately insured, the company has a sound business plan, AML and other regulatory procedures in place".*<br><br>*However these requirements are not in line with the 2.2 ToRs and are limited to a specific procedure without being applicable to all the relevant companies incorporated and/or operating in the jurisdiction.*<br><br>*The conditions attached to conducting business in the TCI do not include then an express requirement for a minimum number of adequately qualified employees, physical presence requirements and (for non-resident companies) that management and control should be in TCI. To be noted that TCI was not able to provide data on the number of employees in the* |

*jurisdictions.*

*We would therefore propose a tick ("V") for criterion 3.*

**Criterion 4**:

"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"

Relevant questions (Q 2.9, Q 2.10, Q 2.11, Q 2.12)

*No information has been provided by the jurisdiction on rules for profit determination. TCI is of the opinion that this issue is not relevant for theme since "the majority of trade is with the US economy and the currency used in the Turks and Caicos Islands is the US dollar".*

*As for the other jurisdictions assessed under this analysis, it is unclear whether a country without CIT should be asked to set rules for profit determination in respect of activities within a MNI in place or if the commitment to implement CbCR which gives relevant information to the other states should be considered as sufficient to comply with criterion 4. It has to be noted that even if TCI said they joined the IF on BEPS and committed to the BEPS minimum standards, they replied "not applicable" to the questions (2.12) relative to CBCR.*

*We would therefore propose a question mark ("?") for criterion 4.*

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| **Criterion 5**:<br><br>“whether the features of the tax system lack transparency, including where legal provisions are relaxed at administrative level in a non-transparent way” |
| <u>Relevant questions (Q 2.13, Q 2.14, Q 2.15, Q 2.16)</u><br><br>*TCI provided detailed information on the legislative requirements to set up a company and conducting business in the jurisdictions. This information is publicly available and can be found on the official website. However, no specific information where provided on the possibility to take decisions by the relevant authorities on the basis of discretional procedures, including bilateral agreements (e.g. rulings). TCI said that this section of the questionnaire (q. 2.13-2.15) is not applicable to them since they do not have CIT regime in place.*<br><br>*We would therefore propose a question mark (?) for criterion 5.* |