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OUTCOME OF PROCEEDINGS

From:	General Secretariat of the Council
To:	Code of Conduct Group (Business Taxation)
Subject:	The EU list of non-cooperative jurisdictions for tax purposes – Barbados: final legislation and assessment under criterion 2.2

Barbados abolished its preferential tax regimes¹ at the request of the Council of the European Union but introduced regressive corporate income tax rates (as low as 1%) applicable to all entities. This failed to remove the harmful features or effects of the original regimes.² Therefore the Code of Conduct Group (business taxation) (COCG) decided that Barbados should be treated as a jurisdiction that applies “*a nominal corporate tax rate equal to zero or almost zero*” and identified these amendments to Barbados' Income Tax Act as a new measure falling under EU listing criterion 2.2.

On 31 December 2018, Barbados introduced economic substance requirements in its domestic legislation by virtue of Business Companies (Economic Substance) Act 2018-41, which came into effect 1 January 2019. However, the COCG considered that this Act did not meet the requirements of criterion 2.2.

As a result, Barbados committed at high political level in April 2019 to address these concerns by 31 December 2019, without any grandfathering mechanism, and was moved from Annex I to Annex II by the ECOFIN Council in May 2019.

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.

A/ FINAL LEGISLATION:

On 29 November 2019, Barbados adopted Companies (Economic Substance) Act, 2019-43, which entered into force 29 November 2019 (see doc. 7446/20 ADD 1-2), abolishing and substituting the aforementioned Act 2018-41. This Act 2019-43 was amended in December 2019 (see doc. 7446/20 ADD 3).

In addition, revised Economic Substance Guidelines were adopted on 11 March 2020 (see doc. 7446/20 ADD 4-5) with final wording submitted to MSs already in February 2020 to receive feedback.

B/ FINAL ASSESSMENT:

Following numerous exchanges in the course of 2019, Barbados adopted Companies (Economic Substance) Act, 2019-43, abolishing and substituting the Companies (Economic Substance) Act 2018-41, which was not in line with the scoping paper. However, this Act 2019-43 was also not fully compliant with the scoping paper. To address the outstanding issues, Act 2019-43 was amended in December 2019. In addition, Barbados drafted Economic Substance Guidelines to clarify the implementation of the above legislation. These Guidelines were further clarified and adopted according to the feedback of the Commission services and Member States.

The following assessment only highlights the remaining issues identified and still pending following the adoption of Act 2019-43 in November 2019.

Assessment of the Companies (Economic Substance) Act, 2019-43, as amended, and Economic Substance Guidelines

1/ Definitions of Relevant Activities

1.1 Banking business

Member States had concerns that the definition of this activity, by reference to the licensing requirement under specific financial services legislation, could lead certain relevant companies to be exempt from the substance requirements.

Barbados confirmed that this requirement now applies to all banks in Barbados.

1.2. Headquarter business

Member States had concerns that the definition of this activity referred to services provided in Barbados and hence could lead to services provided from within Barbados being exempt from substance requirements.

The Revised Guidance clarifies that services from within Barbados are relevant.

1.3. Holding company business

Member States had concerns that the definition of this activity did not require companies holding a variety of assets and earning various types of income to comply with substance requirements for that income. In particular, it was not clear if receipt of passive income triggered substance requirements.

The Revised Guidance clarifies that holding companies earning income from relevant activity must comply with substance requirements.

1.4 Pure Equity Holdings (PEHs)

Member States had concerns that the guidance on PEHs could exempt from the relevant requirements PEHs that hold participations in portfolio investment and/or are not the beneficial owner of relevant income.

The Revised Guidance does not include such limitations.

1.5. Intellectual property business (IP assets' definition)

Member States had concerns that the definition of IP asset, by reference to patents and assets with similar features, could lead IP activity in relation to other assets to be exempt from substance requirements.

The New Substance Act clarifies that marketable intangibles, e.g. trademarks and similar assets, are also IP assets.

1.6. Shipping business (and ships)

Member States had concerns that the definition of shipping business did not include the sale of tickets or similar documents and relevant services. Therefore it was not consistent with the definition endorsed in other 2.2 jurisdictions. In addition, Member States had concerns that certain terms used in the definition (“small commercial vessel” and “pleasure yacht”) were not clear.

The New Substance Act defines shipping business in line with other 2.2 jurisdictions and does not include the abovementioned unclear terms.

1.7 Distribution and service centre business

Member States had concerns that the guidance on this activity could lead to secondary activities being exempt from substance requirements.

The Revised Guidance does not distinguish secondary from main distribution and service centre activities.

2/ Not-for profit activities (Definition of “Carrying on business”)

Member States noted that the definition of the term “carrying on business” - by reference to gain - could exempt certain relevant activities, e.g. for charity purposes. This could be acceptable, but only if subject to safeguards to ensure the charitable purpose.

The definition in the Revised Guidance no longer refers to “gain”.

3/ Tax Residence Exemption and relevant SEOI (resident companies and EOI)

Member States had concerns that companies claiming tax residence outside Barbados were not required to systematically file relevant evidence in order to be exempt from substance requirements. The New Substance Act requires relevant companies to file an annual declaration, including evidence of tax residence outside Barbados, and clarifies that they can be exempt from substance requirements on condition that they satisfy the tax authority in their foreign residence.

Member States also had concerns in relation to spontaneous exchange of information (SEOI) in the case of non-resident companies. In particular, it was not clear that relevant information (i) should be exchanged systematically, (ii) include the evidence provided by the company and (iii) be exchanged with the jurisdiction of claimed tax residence and the jurisdictions of legal and beneficial owners.

The New Substance Act clarifies that all the information provided by the non-resident company should be exchanged with the jurisdiction of claimed tax residence and the jurisdictions of legal and beneficial owners. The Revised Guidance clarifies that SEOI must be systematic.

Finally, following respective concerns raised by Member States, the definitions of “resident company” in the Revised Guidance and the New Substance Act have been aligned.

4/ Substance test: CIGAs in the jurisdiction

Member States had concerns that the requirement for the relevant company to perform CIGAs in the jurisdiction was not adequately clear.

The New Substance Act provides that companies must conduct CIGAs in Barbados to meet the substance test for a relevant activity.

5/ Local business exemption: MNE group definition

Member States previously agreed that the provision for local business exemption was acceptable, taking into account a broad definition of MNE group by reference to enterprises.

The New Substance Act defines a group as including “*two or more companies for which tax residence is in different jurisdictions or includes a company that is resident for tax purposes in one jurisdiction and is subject to tax with respect to a business carried out through a permanent establishment in another jurisdiction*”. The Revised Guidance provides that group is “*a collection of companies or enterprises related through ownership or control such that it is either required to prepare Consolidated Financial Statements for financial reporting purposes under applicable accounting principles or would be so required if equity interests in any of the enterprises companies or enterprises were traded on a public securities exchange*”. Barbados affirmed that it will amend the New Substance Act to align the two definitions.

While Barbados confirmed that a company and an enterprise can constitute group, this needed to be clarified in the Revised Guidance, to prevent that the reference to “companies or enterprises” being interpreted as not covering cases where it is a company and an enterprise.

The amendment of the New Substance Act should in this respect be monitored and Barbados adopted revised Economic Substance Guidelines on 11 March 2020 (see above).

6/ High-risk IP

Member States had concerns that companies in high-risk IP scenarios were not required to systematically submit evidence for the rebuttal of the presumption of non-compliance. Instead, they only needed to submit it following a request by the competent authority.

The Revised Guidance clarifies that companies in high-risk IP scenarios must file the relevant evidence with their annual declaration. The reference to FHTP policies has also been removed from the Revised Guidance, to address Member States' concern that such reference undermined the relevant higher EU requirements.

7/ Sanctions framework

Member States considered acceptable that financial penalties would not be imposed for certain breaches, at a first notice of the breach to the company, provided that this was limited to minor breaches. The New Substance Act provides this option only in case of a failure to meet the substance requirements because of inadequate number of employees.

In addition, Member States had concerns that applicable penalties could be waived under certain circumstances and that such circumstances were not clear. The New Substance Act does not provide waiver of penalties.

Conclusion

Barbados has implemented its commitment under criterion 2.2 and was removed from Annex II at the ECOFIN meeting on 18 February 2020.

The definition of MNE Group in the Guidance was amended on 11 March 2020, i.e. after the ECOFIN meeting of 18 February 2020. This was in order to incorporate the recommendation of Member States for further clarification in the Guidance of the definition included in the legislation and while the Guidance had been positively assessed against the scoping paper.