

## British Virgin Islands Economic Substance Requirements – 'Relevant Activity' of 'Headquarters Business'

For general background on The Economic Substance (Companies and Limited Partnerships) Act, 2018 (the "Economic Substance Act"), the related draft International Tax Authority Economic Substance Code that was issued on 22 April 2019 (the "Guidance") and for the meaning of 'legal entity', please click [here](#).

This update assumes that an entity has already been determined to be a 'legal entity' under the Economic Substance Act and that the 'legal entity' is now considering whether it is carrying on one of the nine categories of geographically mobile 'relevant activities' - in particular, under the 'headquarters' category.

### What is 'Headquarters Business'?

'Headquarters business' in the Economic Substance Act is defined to mean 'the business of providing any of the following services to an entity in the same Group'<sup>1</sup>:

- (a) the provision of senior management;
- (b) the assumption or control of material risk for activities carried out by any of those entities in the same Group; or

- (c) the provision of substantive advice in connection with the assumption or control of risk referred to in paragraph (b), but does not include banking business, financing and leasing business, fund management business, intellectual property business, holding company business or insurance business.

### Economic Substance Test

If a 'legal entity' only carries on a 'relevant activity' that is a 'headquarters business', it will be subject to the economic substance test set out in the Economic Substance Act. The economic substance test can be satisfied in relation to that 'headquarters business' if the 'legal entity' ensures that:

- (a) the 'headquarters business' is directed and managed in the British Virgin Islands;
- (b) having regard to the nature and scale of the 'headquarters business':
  - (i) there are an adequate number of suitably qualified employees in relation to that activity who are physically present in the British Virgin Islands (whether or not employed by the relevant legal entity or by another entity and whether on temporary or long term contracts);

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<sup>1</sup> 'Group' is defined by reference to regulation 2(1) of the BVI Business Companies Regulations, 2012, and means 'a company (the "first company") and any other company that is (a) a parent of the first company; (b) a subsidiary of the first company; (c) a subsidiary of a parent of the first company; or (d) a parent of a subsidiary of the first company.'

- (ii) there is adequate expenditure incurred in the British Virgin Islands;
  - (iii) there are physical offices or premises as may be appropriate for the core income-generating activities (as described below in the context of 'headquarters business');
- (c) the legal entity conducts core income-generating activity in the British Virgin Islands as described below in the context of 'headquarters business': and
- (d) in the case of income-generating activity carried out for the relevant legal entity by another entity:
- (i) no core income generating activity is carried on outside the British Virgin Islands;
  - (ii) only that part of the activities of that other entity which are solely attributable to generating income for the relevant legal entity and not for any other legal entity shall be taken into account when considering if the relevant legal entity meets the economic substance requirements;
  - (iii) the relevant legal entity is able to monitor and control the carrying out of that activity by the other entity.
- (b) incurring expenditures on behalf of affiliates;
  - (c) co-ordinating group activities.

### The Guidance on 'Headquarters Business'

The Guidance contains some additional sector specific provisions in respect of 'headquarters business'. It provides that whether an entity carries on headquarters business is not dependent on its position in the group structure. It is entirely dependent on the services it provides to other companies in the group, whether parents or subsidiaries. For example, a group includes, as a subsidiary, a service company which employs all the employees in the group. If senior management in the group are employed by the service company it will be providing headquarters services to the group.

The Guidance further clarifies that the concluding words of the definition of headquarters business make clear that any activity which might otherwise fall within the definition of 'headquarters' business', but which in fact forms part of another relevant activity, will fall outside the definition of 'headquarters' business'. For example, a subsidiary in a group which is a captive insurance company will not also be carrying on headquarters business simply because it assumes material risk on behalf of the group. By way of another example, a subsidiary in a group which carries on banking business, and is the primary operating company in the group, will not also be carrying on headquarters business simply because the bank's senior management also sit on the board of the top company in the group.

### British Virgin Islands Core Income Generating Activities

The relevant British Virgin Islands core income generating activities in the context of 'headquarters business' include:

- (a) taking relevant management decisions;

However, the Guidance acknowledges that it is in theory possible for a company to carry on both headquarters business and another form of relevant activity if the activities form two distinct business activities. For example, an entity carrying on the activity of a holding company (which consists of owning only equity participations in other companies) may also carry on headquarters business if it also employs, and then supplies to other entities in the group, the senior management of the group.

### What to do if a Legal Entity is Carrying on the 'Relevant Activity' of 'Headquarters Business'

It is worth noting that there are a range of consequences for breaches of the Economic Substance Act (including financial penalties and potential striking-off).

If you have any specific questions in relation to a 'legal entity' conducting 'headquarters business' or this update, please speak to your usual Maples Group contact or:

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