



# EU Economic Substance Legislation



## Cayman Islands Economic Substance Legislation in Effect

On December 27, 2018, the Cayman Islands released the anticipated EU Economic Substance Bill. The bill is effective on formation for newly-formed entities (entities formed January 1, 2019 or later) and for pre-existing entities (in existence prior to January 1, 2019) it is effective as of July 1, 2019.

**Failure to Comply: Penalties for not meeting the substance requirements are \$10,000 in year one and \$100,000 in year two. Continued failure to meet substance requirements may result in a possible court-ordered strike-off of the Cayman entity.**

The economic substance measures are intended to apply to certain Cayman-based entities ("Relevant Entities") engaging in relevant activities, depending on the nature of the business ("Relevant Activities").

**Relevant Entities** definition includes Cayman Companies, LLCs and LLPs. Additionally, some foreign companies registered under the Cayman Companies Law (2018) may be impacted.

Notably, limited partnerships as well as investment funds are not included in the scope of the Law.

Additionally, Cayman entities that are not centrally managed and controlled from Cayman and which are tax resident outside of Cayman are not considered to be a relevant entity. Tax residency outside of Cayman is expected to require supporting evidence (e.g. tax residency certificate or letter from foreign tax authority).

**Relevant Activities** definition includes the following types of businesses:

- Banking business
- Financing & leasing business
- Fund management business
- Holding company business

- Insurance business
- Intellectual property business
- Headquarters business
- Distribution & service centre business
- Shipping business

As specifically stated in the law, the Relevant activities definition does not include an investment fund business.

**A relevant entity satisfies the economic substance test in relation to a relevant activity if the relevant entity:**

1. Conducts Cayman Islands core-income generating activities;
2. Is directed and managed in an appropriate manner from the Cayman Islands; and
3. Carries out certain operating functions in Cayman adequately (expenditure, physical presence, full time employees or other personnel in the Cayman Islands).

### KPMG Observations

**Each Cayman business needs to consider if they are a relevant entity conducting a relevant activity.**

- We anticipate intellectual property businesses will be impacted the most by the Substance Bill in Cayman, based on transfer pricing risk and potential lack of significant substance in Cayman.
- Insurance industry awaits more guidance on how the law impacts them.
- Holding companies business definition currently is limited to pure equity holding companies.
- While we expect to see some management companies within the scope of the Law, if the company is not registered under the Companies Law, it is not a Relevant Entity.
- A Cayman entity which is centrally managed and controlled outside of Cayman and tax resident outside of Cayman is not a Relevant Entity.

### Next Steps

- It is anticipated that EU approval of Cayman Economic Substance Law will be issued the end of February or early March.
- OECD review of Cayman Economic Substance Law is expected by end of June.
- Version 1.0 of the Cayman Economic Substance Guidance Notes is expected to be released by the end of February 2019. The guidance notes should provide additional insight on the implementation of the law.

### How KPMG in the Cayman Islands can assist your business

KPMG Cayman has been working closely with the Cayman Tax Information Authority and Industry Groups to provide clarity around the Cayman Economic Substance legislation and guidance notes.

- We can provide an initial analysis of the extent to which the Law may impact your business and organizational structure.
- We can also provide assistance with the implementation of the Law including:
  - Compliance with the economic substance annual notification and reporting requirements.
  - Advice on the requirements for your business to ensure compliance with the Law.

### Have questions on how this impacts your Cayman entities?

Please contact your KPMG Cayman contact or one of our tax advisors below to assist with all your questions and concerns. Contact us [here](#).



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If you have any questions, please send an email to [marketing@kpmg.ky](mailto:marketing@kpmg.ky).

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