

ECONOMIC SUBSTANCE

Turks & Caicos Islands



Economic Substance

Quick reference guide enabling side-by-side comparison of local insights into economic substance regimes in offshore and other jurisdictions, including affected entities and activities; tax residence considerations; criteria used by tax authorities to determine whether an organisation has sufficient economic substance within a given jurisdiction; enforcement regimes; reporting and compliance requirements; and recent trends.

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LEGAL FRAMEWORK

Legislation

What legislation sets out the economic substance requirements in your jurisdiction?

The Turks and Caicos Islands (TCI) legislative framework is set out in the Companies and Limited Partnership (Economic Substance) Ordinance 2018 and accompanying Regulations (Substance Legislation), which came into force on 1 July 2019.

The Exchange of Information Unit (EOIU), the TCI's competent authority under the Substance Legislation, issued Guidance Notes in November 2020 to assist in understanding the requirements of, and practical assistance relating to, economic substance. While the Guidance Notes do not form part of the Substance Legislation nor have the force of law, they are a useful source of information and practical guidance relative to the economic substance test and requirements.

Law stated - 01 January 2023

Relevant entities

What types of entity are subject to the economic substance requirements in your jurisdiction?

A resident TCI entity that is carrying out a relevant activity is subject to the Substance Legislation. A resident TCI entity is:

- a TCI company incorporated under the Companies Ordinance 2017;
- a TCI limited partnership registered under the Limited Partnership Ordinance; or
- a foreign company registered in the TCI under the Companies Ordinance 2017.

Law stated - 01 January 2023

Relevant activities

What activities trigger the economic substance requirements in your jurisdiction?

Under the Substance Legislation, there are nine relevant activities that trigger compliance with the requirements and legislation. These are:

- banking business;
- distribution and service centre business;
- finance and leasing business;
- fund management business;
- headquarters business;
- holding entity business;
- insurance business;
- intellectual property holding business; and
- shipping business.

A resident TCI entity that does not carry out a relevant activity does not need to comply with the Substance Legislation.

By way of example, owning real estate in the TCI through a TCI entity is not a relevant activity.

Law stated - 01 January 2023

Tax residence requirements

Must entities be tax resident (or deemed tax resident) in your jurisdiction to be subject to the economic substance requirements? If yes, what are the tax residence rules and requirements? If not, do the economic substance requirements in your jurisdiction differ with respect to non-resident entities ?

Yes. All TCI entities incorporated or registered in the TCI are deemed tax resident in the TCI unless proven otherwise, and to the extent that the entity is not on the list of non-cooperative jurisdictions for tax purposes maintained by the European Union. There is no corporation tax in the TCI, nor are there any tax liabilities payable by an entity subject to tax in the TCI.

If the entity is claiming to be tax resident in a jurisdiction outside of the TCI, the entity must provide to the EOIU the following documents obtained from the relevant authority in the jurisdiction in which it is tax resident as evidence that it is not to be considered as a resident entity for the purposes of the Substance Legislation:

- a tax identification number;
- a tax residence certificate (or equivalent);
- an assessment or payment of corporate income tax liability on all of the entity's income in the TCI from a relevant activity; and
- details of its parent company, ultimate parent company and ultimate beneficial owners.

Law stated - 01 January 2023

Guidance

Has the government published guidance on the economic substance requirements?

Yes. The EOIU issued Guidance Notes in November 2020.

Law stated - 01 January 2023

ECONOMIC SUBSTANCE REQUIREMENTS

General requirements

What general economic substance requirements apply in your jurisdiction?

In general, the economic substance requirements apply to all entities that are incorporated, or registered, and resident in the Turks and Caicos Islands (TCI), unless they are subject to tax in another jurisdiction and can prove their residence for tax purposes in that other jurisdiction.

Law stated - 01 January 2023

'Directed and managed'

What requirements apply in relation to board meetings and the location where entities are directed and managed?

A TCI entity is directed and managed in the TCI if:

- meetings of the board of directors take place in the TCI with adequate frequency given the level of decision-making required;
- during these meetings, a quorum of directors is physically present in the TCI;
- strategic decisions are made at these meetings, with minutes recording those decisions being drawn up;
- the board of directors, as a whole, have sufficient knowledge, experience and expertise to discharge the duties of the board; and
- board meeting minutes and other company records are maintained in the TCI.

Law stated - 01 January 2023

Core income-generating activities

What requirements apply in relation to core income-generating activities?

A TCI entity carrying out a relevant activity must conduct core income-generating activities (CIGA) in the TCI associated with the relevant activity. CIGA vary by industry and sector and are listed in detail in the Companies and Limited Partnership (Economic Substance) Ordinance 2018 and accompanying Regulations (Substance Legislation). It is not necessary for the relevant entity to perform every element of the relevant activity that is listed. Rather, substance should be assessed by reference to the specific element of the CIGA being carried out in the TCI.

Law stated - 01 January 2023

Premises

What requirements apply in relation to the physical premises of relevant entities?

A TCI entity must have an adequate physical presence in the TCI. 'Adequate' is contingent on the nature, scale and complexity of the business that the relevant entity is carrying out in the TCI.

Law stated - 01 January 2023

Employees and personnel

What requirements apply in relation to the employees and personnel of relevant entities?

Employees of a TCI entity include individuals directly employed by the entity and also persons working for the company that are being subordinated to it and deemed to be employees under TCI law. Owner-managers and directors of a TCI entity are also considered employees. A TCI entity caught by the Substance Legislation must demonstrate, having regard to the level of relevant activity carried out in the TCI, an adequate number of appropriately experienced and qualified full-time employees in the TCI.

Law stated - 01 January 2023

Expenditure

What requirements apply in relation to expenditure?

A TCI entity caught by the Substance Legislation must demonstrate, having regard to the level of relevant activity carried out in the TCI, an adequate level of operating expenditure and details of its gross income. Operating expenditure includes the amount of operating expenditure by the relevant activity carried out in the TCI, as set out in the entity's financial statements (or equivalent), excluding capital. The TCI entity's gross income by relevant activity would be the turnover figure taken from its financial statements (or equivalent).

Law stated - 01 January 2023

Enhanced requirements

Are there any instances where enhanced substance requirements apply?

A TCI entity categorised as a high-risk IP entity is subject to enhanced substance requirements, as these entities are considered by the OECD to present greater risks. A high-risk IP entity is an entity carrying on intellectual property holding business and which acquired the intellectual property asset from a group entity or in consideration for funding research and development by another person situated outside of the TCI. The entity must also license that asset to one or more group entities, or otherwise generate income from the asset in consequence of activities performed by foreign group entities, or the entity does not carry out either research and development or branding and distribution as part of its CIGA in the TCI. There is a presumption that a high-risk IP entity does not carry on CIGA in the TCI (and therefore does not have economic substance in the TCI) unless it provides sufficient information that the test has been met by demonstrating control over the development, exploitation, maintenance, enhancement and protection of the intellectual property asset by an adequate number of suitably qualified full-time employees of the entity in the TCI.

For the Exchange of Information Unit (EOIU) to determine if a high-risk IP entity meets the substance test and requirements, the entity must provide the following information to the EOIU:

- a detailed business plan that demonstrates the commercial rationale for holding the intellectual property assets in the TCI;
- all employee information, including the level of experience, type of contracts, qualifications and duration of employment; and
- evidence that decision-making takes place in the TCI.

Law stated - 01 January 2023

Reduced requirements

Are there any instances where reduced economic substance requirements apply?

Any TCI entity categorised as a pure equity holding entity is subject to reduced tests for economic substance compliance. A pure equity holding entity is an entity that:

- is a holding entity – that is, an entity that holds a majority of shares or partnership interests or voting rights in another entity, or is a member or partner of another entity and controls a majority of the voting rights in that entity, or is a member or partner of another entity and may appoint or remove the majority of the directors of that entity, or is the holding entity of a holding entity of another entity;

- has, as its primary function, the acquisition and holding of shares or equitable interests in other entities; and
- does not carry on any commercial activity.

A pure equity holding entity satisfies the substance requirements if it has an adequate number of persons and has adequate premises for managing the shares or equitable interests that it holds.

Law stated - 01 January 2023

Outsourcing

What requirements apply in relation to outsourcing activities to entities located in your jurisdiction and entities located outside your jurisdiction?

While outsourcing of CIGA is permitted in certain limited circumstances, CIGA must still be undertaken in the TCI and adequately supervised by the relevant services provider or group company (or companies). Outsourcing includes outsourcing, contracting or delegating to a third-party services provider or group company (or companies). Oversight of the outsourced CIGA must be conducted in the TCI. The TCI entity remains responsible for ensuring that accurate information relating to the outsourcing is reported in its annual submissions and filings.

Law stated - 01 January 2023

ENFORCEMENT AND COMPLIANCE

Enforcement authorities

Which government authorities are responsible for the enforcement of economic substance requirements? What is the extent of their information-gathering powers?

The Exchange of Information Unit (EOIU) is the Turks and Caicos Islands (TCI) competent authority responsible for monitoring compliance with the Companies and Limited Partnership (Economic Substance) Ordinance 2018 and accompanying Regulations (Substance Legislation) and sharing information with other competent authorities. All TCI entities must provide to the EOIU information to enable it to monitor and determine whether the entity is carrying on relevant activities and, if so, has met the economic substance requirements applicable to it. The EOIU may require the production of other information and documents that it reasonably requires to reach its determination, and in certain circumstances may also apply for a search warrant to retrieve specific documents or information from the entity's premises.

Law stated - 01 January 2023

Reporting formalities

What reporting formalities apply with respect to the economic substance requirements?

All TCI entities must submit to the EOIU on an annual basis a return confirming whether the entity is carrying on relevant activities and, if so, whether it has met the substance test and requirements. The annual return sets out prescribed information relating to the entity. The first reporting period and round of submissions of annual returns commenced in 2021, covering the financial year ended 31 December 2020.

The annual return should include the following information and documentation:

- whether the entity is a resident entity and, if not, which jurisdiction is the entity resident for tax purposes;
- information on the entity's holding entity and where each holding entity is located;
- details of the beneficial owners;
- business and income types to identify the type of relevant activity;
- amount and type of gross income by relevant activity;
- amount of operating expenditure by relevant activity;
- details of premises;
- number of employees;
- names and physical address of the directors;
- confirmation of core income-generating activities (CIGA) conducted for each relevant activity;
- financial statements; and
- confirmation of whether any CIGA has been outsourced and, if so, the relevant detail.

Law stated - 01 January 2023

Demonstrating compliance

How does an entity in practice demonstrate its compliance with the economic substance requirements? How do the enforcement authorities assess compliance?

All TCI entities must file an annual return with the EOIU. The EOIU will review the annual return submitted and assess based on the information and documents provided whether the entity is complying with the Substance Legislation test and requirements. Entities should maintain and retain records to demonstrate the adequacy and appropriateness of the resources utilised and expenditure involved to determine adequacy of the same.

Law stated - 01 January 2023

Penalties

What are the potential penalties for failure to comply with the economic substance requirements?

Where the EOIU determines that a TCI entity carrying on a relevant activity has not satisfied the economic substance requirements during a particular accounting period, it has the power to impose a monetary penalty of up to US\$25,000 for the first period of default, and up to US\$150,000 for a second period of such default. The EOIU may also apply to the TCI courts to eventually have the TCI entity struck or removed from the Register of Companies, or placed into liquidation or dissolution, or both.

The EOIU also has wide-ranging exchange of information powers with other competent authorities in the EU. Where a TCI entity has not met the substance requirements, the EOIU may provide information it has received in connection with the annual return to the relevant authority of the EU member state in which the TCI entity claims to be resident, or in which each holding entity, or ultimate holding entity, or each ultimate beneficial owner, of the TCI entity is located. Disclosure of information to the relevant EU authority would be in accordance with existing exchange of information agreements permitting the automatic exchange of information.

Law stated - 01 January 2023

UPDATE AND TRENDS

Recent developments

What have been the most significant recent developments in the law on economic substance in your jurisdiction, including any notable regulatory actions or legislative changes?

As a consequence of the Companies and Limited Partnership (Economic Substance) Ordinance 2018 and accompanying Regulations (Substance Legislation) coming into force in 2019, the Turks and Caicos Islands (TCI) aim has been to be compliant with EU and other OECD substance requirements. In being compliant with the requirements, the TCI would be placed on a level playing field with other jurisdictions that are subject to the EU's economic substance requirements. In late 2020, the EOIU issued the economic substance Guidance Notes, providing more clarity and examples for the industry. The next stage of the process was commenced in earnest with the first disclosures and annual reporting to the EOIU having commenced in 2021. The EOIU's online portal for economic substance reporting went live in the second quarter of 2022. The portal rollout and launch were delayed, which resulted in the TCI not meeting the deadlines set by the EU. This has now been rectified and the portal is live. It is anticipated that this will result in TCI being compliant with economic substance regulations as far as the TCI is concerned at the earliest opportunity.

The EOIU is expected to release to the industry further user guidance and training (virtually, due to covid-19) on the disclosure and reporting process to applicants and registered agents.

Law stated - 01 January 2023

Jurisdictions

	Bahamas	McKinney Bancroft & Hughes
	Belize	Quijano & Associates
	Bermuda	Carey Olsen
	British Virgin Islands	Carey Olsen
	Cayman Islands	Carey Olsen
	Germany	Freshfields Bruckhaus Deringer
	Guernsey	Carey Olsen
	Jersey	Carey Olsen
	Mauritius	Venture Law llc
	Turkey	Nazali Tax & Legal Services
	Turks & Caicos Islands	Griffiths & Partners