

Economic Substance Requirements for Bermuda

Guidance Notes

General Principles

(Issue Date – 24 December 2019)

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1. Definitions

1.1. Definitions

In these Guidance Notes, the following terms shall have the following meanings:

Term	Meaning
Act	Economic Substance Act 2018
Affiliate	Has the meaning provided in section 2 of the Act
CIGA	Core income generating activities as more particularly defined in the Regulations
COCG	EU Code of Conduct Group (Business Taxation)
Compliance Measures Act	Registrar of Companies (Compliance Measures) Act 2017, as amended from time to time
Declaration Form	Economic substance declaration form required to be filed pursuant to section 5(2) of the Act, in a form to be prescribed by the Registrar
ECOFIN	EU Economic and Financial Affairs Council
Entity(ies)	A company to which the Companies Act 1981 applies; a limited liability company formed under the Limited Liability Company Act 2016; an exempted partnership, exempted limited partnership or an overseas partnership that has a separate legal personality in accordance with section 4A of the Partnership Act 1902, in each case engaged in one or more Relevant Activity, but does not include a Non-resident entity
ES Laws	Collectively, the Act and the Regulations
ES Requirements	Economic substance requirements set forth in section 3 of the Act, and Regulation 3 and as further described in section 7 of these Guidance Notes
FHTP	OECD Forum on Harmful Tax Practices
Local Entity	A local company or local LLC which does not carry on banking or insurance business
Minister	Minister of Finance
MNE Group	For the purposes of the Act, means any Group that includes two or more enterprises for which the tax residence is in different jurisdictions or includes an enterprise that is resident for tax purposes in one jurisdiction and is subject to tax with respect to the business carried out through a permanent establishment in another jurisdiction
OECD	Organization for Economic Co-operation and Development
Non-resident entity	An entity that is resident for tax purposes in a jurisdiction outside of Bermuda that is not on Annex 1 to the EU list of non-cooperative jurisdictions for tax purposes.

Registrar	Registrar of Companies
Regulations	Economic Substance Regulations 2018, as amended
Regulatory Acts	Insurance Act 1978 and the Banks and Deposit Companies Act 1999
Relevant Activity	Relevant activity as defined in section 2 of the Act and described in section 6 of these Guidance Notes (and Relevant Activities means more than one Relevant Activity)

1.2. Terms

Terms not otherwise defined in these Guidance Notes shall have the meaning given to such terms in the ES Laws.

2. Introduction

The Minister of Finance is issuing these Guidance Notes pursuant to the provisions of section 12 of the Act.

The ES Laws became operative on 31 December 2018. The purpose of the ES Laws are to ensure that Bermuda does not facilitate the use of structures which attract profits but which do not reflect real economic activity that is being undertaken in Bermuda.

The purpose of these Guidance Notes is to: (i) assist entities to determine if they are in scope of the ES Laws and, if so, to assist them in understanding how to satisfy the ES Requirements; and (ii) provide guidance as to how the Registrar will measure and assess the criteria for meeting the ES Requirements. These Guidance Notes have been published in the Official Gazette and can be found on the Government of Bermuda website: <https://www.gov.bm/department/registrar-companies>.

In determining whether an entity has complied with the ES Laws, the Registrar will consider whether that entity has followed the principles set out in these Guidance Notes. However, these Guidance Notes are not intended to be prescriptive or to provide an exhaustive list of all matters that an entity should consider when assessing compliance with the ES Laws.

The Registrar will consider if and to what extent each Entity satisfies the ES Requirements in light of the applicable Relevant Activity(ies) being conducted by that Entity, having regard to the nature, scale and complexity of that Entity’s particular business. It is expected that many Entities will be required to adopt revised business practices, in accordance with the ES Laws and these Guidance Notes, in order to demonstrate compliance with the applicable ES Requirements. The directors (or equivalent) of each Entity should address their minds to the application of the ES Requirements (or, where applicable, minimum economic substance requirements), and make their determination as to that Entity’s compliance in good faith.

Entities are encouraged to seek professional advice if they are uncertain as to whether or to what extent they are subject to and comply with the ES Laws.

3. Background

In December 1997, the Council of the European Union and the representatives of the governments of EU Member States adopted a resolution on a Code of Conduct for business taxation, with the objective to curb harmful tax practices. The following year, ECOFIN (the organization responsible for EU economic policy, taxation issues and the regulation of financial services) established the COCG to assess certain tax measures.

Whilst the original focus of the COCG was on EU member states, the COCG began to turn its attention to third countries and territories to which EU treaties do not apply and began the process of applying the same principles to those countries and territories. Those principles include ensuring that jurisdictions do not facilitate the use of structures which attract profits but which do not reflect real economic activity that is being undertaken in that jurisdiction (the principle of “substantial economic presence”). The standards for substantial economic presence agreed upon by the COCG are set out in a scoping paper issued by the COCG and approved by ECOFIN in June 2018. The scoping paper is commonly referred to as the “2.2 *Scoping Paper*” and forms the basis for the ES Requirements.

4. Who do these economic substance requirements apply to?

ES Requirements apply to every Entity (as defined on page 1).

An Entity that is not engaged in any Relevant Activity is not subject to ES Requirements. However, such an entity will be required to indicate in its annual reporting to the Registrar that it is not engaged in any Relevant Activity.

A Non-resident entity is also not subject to ES Requirements but will be required to indicate in its annual reporting to the Registrar whether or not it is engaged in a Relevant Activity, and will provide the Registrar with evidence of its tax residency (see below).

5. Application of the Economic Substance Requirements

Any entity that is incorporated, formed and/or registered in Bermuda on or after 1 January 2019 is immediately subject to the ES Laws.

Any entity that was incorporated, formed and/or registered in Bermuda prior to 1 January 2019 will be subject to the ES Laws from 1 July 2019.

6. What are the Relevant Activities?

Relevant Activity means carrying on as a business any one or more of the following:

- (a) banking;
- (b) insurance;
- (c) fund management;
- (d) financing and leasing;
- (e) headquarters;
- (f) shipping;

- (g) distribution and service centre;
- (h) intellectual property; and
- (i) holding entity.

Each of these terms is defined in the Regulations.

The Registrar will consider that the above activities are being carried on as a business where the Entity earns any gross income in respect of such activity during the relevant financial period.

7. What are the Economic Substance Requirements?

7.1. ES Requirements

In order for an Entity to satisfy the requirement to maintain a substantial economic presence in Bermuda, it must demonstrate that it complies with the ES Requirements. An Entity complies with ES Requirements if:

- (a) it is managed and directed in Bermuda;
- (b) CIGA are undertaken in Bermuda with respect to the Relevant Activity;
- (c) it maintains adequate physical presence in Bermuda;
- (d) there are adequate full time employees in Bermuda with suitable qualifications; and
- (e) there is adequate operating expenditure incurred in Bermuda in relation to the Relevant Activity.

7.2. Minimum economic substance requirements

An Entity is subject only to “minimum economic substance requirements”, where such Entity is a “pure equity holding entity” (as defined in Regulation 14(2));

“Minimum economic substance requirements” for all such Entities include:

- (a) compliance with the corporate governance requirements set forth in the Companies Act, Limited Liability Companies Act 2016 or the relevant Partnerships Act (as applicable), including keeping records of account, books and papers and financial statements; and
- (b) the filing of a Declaration Form.

In addition to the minimum economic substance requirements outlined above, a pure equity holding entity must also have adequate people for holding and managing equity participations and have adequate premises in Bermuda.

It will never be acceptable for a pure equity holding entity to have no people in Bermuda to hold and manage its equity participations, and no premises in Bermuda; they must have people and premises adequate to meet the minimum economic substance requirements, having regard to the nature, scale and complexity of that entity’s business. The maintenance of separate office space or a physical registered office (or equivalent) in Bermuda, and the management of the equity participations held by such entity by employees or the board of directors (or equivalent) in Bermuda or through appropriate service providers in Bermuda (e.g. corporate service providers or outsourced management service providers), may be adequate for these purposes. The Declaration

Form filed by pure equity holding entities will be expected to demonstrate the adequacy of the resources (people and premises) that such entities have in place in order to meet these requirements.

8. Filing Requirements and Related Matters

8.1. Filing Requirements - General

An Entity must demonstrate it has satisfied the ES Requirements in respect of any relevant financial period by filing a Declaration Form with the Registrar in respect of that financial period.

The Declaration Form will collect the information that will be considered by the Registrar when determining whether an Entity meets the ES Requirements. The information to be provided by each Entity will include the items set out in section 5(2) of the Act and regulation 3 of the Regulations. The Registrar will have regard to the nature, scale and complexity of each Entity's business in his analysis of the information provided when determining if or to what extent the ES Requirements have been satisfied by that Entity.

8.2. Relevant Financial Period

The relevant financial period for an Entity or Non-resident entity will be the financial year of that Entity or Non-resident entity, as determined in accordance with its constitutional documents. The first relevant financial period for any Entity or Non-resident entity will be the first financial year of that Entity or Non-resident entity commencing after the operative date of the ES Laws (i.e. the first financial year commencing on or after the 1 January 2019).

Each Entity is required to file its Declaration Form, and each Non-resident entity is required to file its evidence of tax residency (see below), no later than 6 months after the last day of each relevant financial period.

Example: An Entity has a financial year ending on 31 March. For that Entity, the first relevant financial period for the purposes of the ES Law will be the financial year ending on 31 March 2020. The Entity will therefore be required to file its Declaration Form (or claim of tax residency outside of Bermuda, as the case may be) within six months after 31 March 2020 – i.e. on or before 30 September 2020.

8.3. E-Registration

The Registrar is in the process of building an e-registration system to accept and manage the information and data collected pursuant to the ES Laws. The e-registration system is scheduled to launch in the second quarter of 2020. To the extent necessary, these Guidance Notes will be amended to incorporate the rules and procedures for filing the requisite information necessitated by the e-registration system.

8.4. Local Entities

Local Entities that are carrying on a Relevant Activity, and which are subject to the requirement to be at least 60% beneficially owned and controlled by Bermudian persons, not part of an MNE

Group and carrying on business only in Bermuda, are subject to reduced economic substance requirements. Such Local Entities are required only to comply with corporate governance requirements set forth in the Companies Act, Limited Liability Companies Act 2016 or the relevant Partnerships Act (as applicable), including keeping records of account, books and papers and financial statements. Such entities will not be required to complete and file a Declaration Form. All Local Entities (whether or not subject to the ES Laws) will be required to report annually to the Registrar as to whether or not they are carrying on a Relevant Activity, in accordance with applicable annual filing requirements.

A Local Entity that is exempted from the requirement to be at least 60% beneficially owned and controlled by Bermudian persons or which is part of an MNE Group, or is carrying on business outside of Bermuda will not be subject to the reduced requirements described above, and will be subject to the full ES Requirements if such Local Entity is carrying on a Relevant Activity. The Registrar will consider that a Local Entity is carrying on business outside of Bermuda where that Local Entity establishes a physical presence outside of Bermuda at which it carries on any part of its business.

8.5. Regulated Entities

Entities licensed under either of the Regulatory Acts are generally considered to operate in Bermuda with adequate substance, and the Registrar will have regard to such Entities' compliance with the relevant Regulatory Act (in addition to compliance with the Companies Act) in his assessment of compliance with the ES Requirements. However, such Entities are still required to complete and file a Declaration Form, and the Registrar will also have regard to the information provided in that Declaration Form in making his assessment of compliance with the ES Requirements.

8.6. Entities engaged in more than one Relevant Activity

Where an Entity is engaged in more than one Relevant Activity during a relevant financial period, the Entity must comply with the ES Requirements for each applicable Relevant Activity but will be required to file one Declaration Form only.

8.7. Cessation of Relevant Activity

If an Entity ceases to engage in a Relevant Activity during a relevant financial period, the ES Requirements in respect of such Relevant Activity will not apply from the point at which the Relevant Activity ceases.

Example: An Entity has been engaged in more than one Relevant Activity, for these purposes, referred to as RA1 and RA2. The Entity ceases to engage in RA1 during a relevant financial period. The ES Requirements will not apply to the Entity in respect of RA1 from the point at which RA1 ceases, but the ES Requirements will continue to apply to RA2. The Entity will inform the Registrar on its Declaration Form of the cessation date of RA1.

If an Entity in liquidation is carrying on a Relevant Activity it continues to be subject to the ES Requirements.

When an Entity ceases to carry on any Relevant Activity, that Entity will no longer be subject to

the ES Requirements but will continue to be subject to the requirement to complete and file a Declaration Form in respect of the Relevant Activity that was carried on during that relevant financial period and will remain subject to review of its compliance with the ES Requirements in respect of the period prior to the cessation of the Relevant Activity.

9. Criteria for ES Requirements

9.1. The Registrar's approach to ES Requirements

As indicated in section 8.1 of these Guidance Notes, every Entity must demonstrate that it has satisfied the ES Requirements for the relevant financial period by filing a Declaration Form.

In general, the Registrar will take a practical approach to the interpretation and application of the ES Requirements. As noted above, in the analysis of each Entity, the Registrar will have regard to the nature, scale and complexity of that Entity's business, and will apply criteria such as "adequacy" in that context. The Registrar will apply a risk-based compliance assessment. An Entity that, in the Registrar's assessment, relies on limited people/employees in Bermuda, or has limited physical presence or expenditure in Bermuda, relative to the nature scale and complexity of that Entity's business, will generally be assessed as higher risk and may therefore be subject to further review by the Registrar's compliance team (whether through desktop review of the Entity's Declaration and related information or through on-site inspection or a combination thereof). As part of that further review, the circumstances which justify those resources being "adequate" for the purposes of the ES Laws would be assessed by the Registrar.

It is not the function of the ES Laws to require an Entity to incur more expenditure, engage more employees or establish more premises than it really needs in order to conduct its Relevant Activity in Bermuda in compliance with the applicable ES Requirements. However, the Registrar nonetheless expects that some Entities will be required to adopt revised business practices, in accordance with the ES Laws and these Guidance Notes, in order to demonstrate compliance with the applicable ES Requirements. The directors (or equivalent) of each Entity should address their minds to the application of the ES Requirements (or, where applicable, minimum economic substance requirements), and make their determination as to that Entity's compliance in good faith.

9.2. Management and Direction of the Entity

In considering whether or to what extent an Entity is "managed and directed in Bermuda", the Registrar will have regard to whether the Entity:

- (a) holds meetings¹ in Bermuda where strategic decisions are made ("strategic meetings"); and
- (b) has an adequate number of senior executives, employees and other persons in Bermuda who are suitably qualified and responsible for oversight or execution of the Entity's CIGA, and holds meetings at which risk management and operational decisions are made.

Each Entity will be expected to be managed and directed in Bermuda, through holding an adequate number of meetings in Bermuda, and having an adequate number of senior executives, employees and other persons in Bermuda who are suitably qualified and responsible for oversight and

¹ Meetings may include board meetings, managers' meetings and partnership meetings in the case of companies, LLCs and partnerships, respectively, as well as senior executive/management and committee meetings.

execution of the Entity's CIGA in Bermuda. Entities will be expected to have meetings, and particularly strategic meetings, at a frequency proportionate to the nature, scale and complexity of the Relevant Activities it conducts, and the Registrar would normally expect such meetings to be held in Bermuda in any relevant financial period.

It is expected that minutes will be kept of all key meetings and that such minutes will evidence all the relevant strategic or risk management and operational decisions taken. It is also expected that all such minutes will be available for inspection in Bermuda, whether held electronically or in hard copy. Where records are held electronically, it is sufficient that such records are maintained and accessible in Bermuda, and it is not necessary that the relevant data centre be located in Bermuda.

In respect of the senior executives, employees or other persons responsible for oversight or execution of an Entity's CIGA, the Entity in question will be expected to maintain records in (or accessible from) Bermuda that evidence that such persons are suitably qualified to hold such responsibilities.

9.3. CIGA

The CIGA of an Entity in respect of any Relevant Activity must be undertaken in Bermuda. Where the CIGA are undertaken by a service provider under an outsourcing arrangement or by an affiliate of the Entity, such activity must also be undertaken in Bermuda.

Where activities being undertaken by an Entity outside of Bermuda result in a foreign permanent establishment (as such term is understood in the OECD model tax convention), such that the Entity can evidence that it is earning income and performing CIGA within that foreign permanent establishment, that may be taken into consideration by the Registrar in its assessment. For the avoidance of doubt, activity resulting in gross income reported in Bermuda (and not in the foreign permanent establishment) would be subject to the ES Requirements in Bermuda.

In any event, an Entity must ensure that CIGA is undertaken in Bermuda to meet the ES Requirements (in addition to compliance with all other ES Requirements) and the Registrar will have strict regard to the need to ensure that the ES Requirements are not circumvented.

9.4. Adequate Physical Presence and Premises

The ES Laws include a requirement for an Entity to have an adequate physical presence in Bermuda. As noted above, what is considered "adequate" for any Entity will depend on the nature, scale and complexity of the business of that Entity. There is no one rule or formula that will fit all Entities or be suitable for all Relevant Activities.

It is expected that every Entity will maintain a physical presence in Bermuda. An Entity may have an adequate physical presence in Bermuda either itself or through appropriately monitored outsourcing arrangements with a service provider or an Affiliate (see below) which itself occupies premises in Bermuda. Provided that the Entity is able to demonstrate that the physical presence is adequate to undertake the Relevant Activity carried on by that Entity, this requirement would be satisfied.

Each Entity must maintain its own physical presence in order to meet this requirement. Where premises are shared with one or more Entities (for example, in the case of group companies sharing office space), each Entity must demonstrate that its share of those premises is adequate for the Relevant Activities undertaken by that Entity, and premises may not be double counted for this

purpose.

9.5. Annual operating expenditure in Bermuda

The Entity must incur adequate expenditure in Bermuda in relation to the Relevant Activity it is engaged in. Expenditure must be adequate relative to the CIGA undertaken in Bermuda and proportionate to the nature, scale and complexity of the business of the Entity in question. If the Entity engages in more than one Relevant Activity, the expenditure in respect of each Relevant Activity will be assessed separately. There is no exhaustive definition of what constitutes expenditure, but it will generally be expected to constitute business expenses, fees, goods, services and employment costs paid to individuals or entities located in Bermuda.

9.6. Adequate Employees

The ES Laws include a requirement for an Entity to have adequate full time employees in Bermuda with suitable qualifications in relation to its Relevant Activity(ies).

As noted above, what is considered “adequate” for any Entity will depend on the nature, scale and complexity of the business of that Entity. There is no one rule or formula that will fit all Entities or be suitable for all Relevant Activities. If the Entity, either itself or through some appropriately monitored outsourcing arrangements with a service provider or an Affiliate, has adequate employees to carry on the relevant CIGA, this requirement would be satisfied.

In calculating (and reporting) the number of employees carrying on the relevant CIGA, an Entity should base this on “full time equivalent” (“FTE”) units. FTE units are calculated on the basis of total hours worked divided by average annual hours worked in full-time jobs. For these purposes, the Registrar assumes “full-time” to be a standard 35 hour work week (i.e. 1540 total annual hours, allowing for standard public holidays and leave entitlements). The use of FTE units assists the Registrar in applying consistent analysis of employee data, while also allowing an Entity to hire individuals (which for these purposes could include contractors filling a role that would otherwise be filled by an employee) as is appropriate to that Entity’s business. By way of illustration:

- *An Entity with 1 full time employee working a 35 hour work week for a relevant financial period will report on its Declaration as having 1.0 FTE.*
- *An Entity with 3 part time employees, each working 17.5 hours a week for a relevant financial period, would report on its Declaration as having 1.5 FTE (i.e. 3 x 0.5 FTE).*

An individual may also work for more than one Entity (either directly or via an appropriately monitored outsourcing arrangement). The time of an individual can be allocated between activities or between Entities, if appropriate in the circumstances, provided that the time allocated in respect of that individual is not double counted, and provided that the time is adequate to carry on the Relevant Activity of each Entity.

In any event, an Entity must demonstrate that it has sufficient suitably qualified individuals in Bermuda to carry out the CIGA in respect of its Relevant Activity(ies). The directors or officers (or equivalent) of an Entity may sometimes perform CIGA in addition to performing their fiduciary duties for the Entity. In such cases, the Registrar may consider evidence of the CIGA performed by the directors or officers in Bermuda or, in the case of entities in liquidation, by the liquidator.

Each Entity will be expected to maintain records in (or accessible from) Bermuda that evidence

the time spent by employees or other persons in relation to each Relevant Activity (and in relation to each Entity, where time is spent in respect of more than one Entity), and that such employees or other persons are suitably qualified to fulfill the duties undertaken by them.

10. Outsourcing Arrangements and Activities other than CIGA

10.1. Outsourcing Generally

The criteria for outsourcing arrangements are set out in Regulation 3(2)(a) & (b).

It is permissible for an Entity to outsource any or all of its CIGA to an Affiliate or service provider provided that the outsourced activities are undertaken in Bermuda.

If an Entity does outsource any of its CIGA to an Affiliate or service provider in Bermuda, it must maintain records in (or accessible from) Bermuda that evidence that there are suitably qualified employees or other persons in that Entity in Bermuda who are responsible for the oversight and assessment of the implementation and execution of the outsourcing arrangement by the Affiliate or service provider, and that the Affiliate or service provider has adequate suitably qualified employees and premises in Bermuda to be able to implement and execute the outsourcing arrangement.

Where time spent by employees or service providers is spent in respect of more than one Entity or more than one Relevant Activity undertaken by any Entity, the records² maintained by the Entity in question will be expected to demonstrate that there has been no double counting of time spent by such employees or service providers. For these purposes, the principles described at 9.6 above will also be applicable to the calculation of FTE units for outsourced activities.

10.2. Activities other than CIGA

An Entity may outsource activities which are not CIGA to service providers which are located outside of Bermuda. Such activities may include, for example, back office functions, IT, payroll, legal services, or other expert advice or specialist services provided that, in each case, they are not of central importance to the Entity in terms of generating gross income from a Relevant Activity.

The Registrar may take account of evidence regarding normal business practices for a particular Relevant Activity which are permitted in other jurisdictions subject to the FHTP's "substantial activities" requirements for preferential regimes. This may include, for example, circumstances in which commercial (i.e. non-tax related) factors require that business be conducted cross-border. This may include scenarios such as the necessity to acquire or utilize specialist goods or services available exclusively in a particular location, or to serve clients or to deal with counterparties necessarily located outside the jurisdiction. For example:

- the master of a ship performing some activities ancillary to and in support of the management of crew for shipping entities; or
- loss adjusters necessarily being required to perform activities ancillary to and in support of client services in the jurisdiction where an insured party is located and

² Records for these purposes may include time sheets or other documented evidence of time spent and the nature of activities (particularly CIGA) undertaken by the person in question, in each case sufficient to calculate the necessary FTE units, and to demonstrate that the time spent by that person has not been "double-counted".

- where the insured loss is suffered; or
- fund managers in Bermuda appointing and overseeing sub-managers or advisors in jurisdictions outside of Bermuda to advise on jurisdiction-specific risks or to hold or sell investments in those jurisdictions and provide reports, all in furtherance of the overall strategic risk investment decisions taken by the fund manager in Bermuda, and in support of the preparation of reports by the fund manager in Bermuda in connection therewith.

Such activities may be permitted outside of Bermuda, provided that CIGA is undertaken in Bermuda.

11. Measuring Adequacy

“Adequacy” has its ordinary dictionary meaning. It means “enough or satisfactory for a particular purpose”. What will be adequate for each Entity to comply with ES Requirements in respect of its Relevant Activity(ies) will depend on the particular facts of the Entity and Relevant Activity having regard to the nature, scale, and complexity of the Entity and/or the Relevant Activity undertaken. The directors (or equivalent) of each Entity should address their minds to the application of the ES Requirements (or, where applicable, minimum economic substance requirements), and make their determination in good faith that the Entity’s resources are adequate for these purposes.

Every Entity is required to maintain and retain appropriate records in or accessible from Bermuda to demonstrate adequacy of the resources utilized and expenditures incurred.³

12. Tax Residency

12.1. *Resident for tax purposes outside of Bermuda*

An entity will be a Non-resident entity, and therefore out of scope of the ES Requirements, if it is resident for tax purposes in a jurisdiction outside of Bermuda provided that the jurisdiction in which the entity claims to be resident for tax purposes is not in Annex 1 to the EU list of non-cooperative jurisdictions for tax purposes⁴.

The Registrar will regard an entity as being resident for tax purposes in a jurisdiction outside of Bermuda if all of its income from Relevant Activities is liable to tax in that jurisdiction. This may include an entity all of whose income from Relevant Activities is taxed on a branch or agency basis in a jurisdiction outside Bermuda.

The Registrar acknowledges that some jurisdictions charge tax by reference to a criterion other than residence. The pertinent principle for the Registrar is whether or not the competent authority or tax authority in the jurisdiction in question has accepted that the entity (or its members or partners in the case of a transparent entity – see below) is liable to tax in that jurisdiction by

³ The duty to maintain and retain records of account are contained in section 83 of the Companies Act 1981; Section 50 of the Limited Liability Company Act 2016; and section 9A of the Limited Partnership Act 1883.

⁴ At the time of issuance of these Guidance Notes, the most recent version of Annex 1 to the EU list of non-cooperative jurisdictions for tax purposes could be found at <https://www.consilium.europa.eu/en/policies/eu-list-of-non-cooperative-jurisdictions/>

reference to the relevant criteria in that jurisdiction.

12.2. Claim of residency for tax purposes

Any entity that carries on a Relevant Activity, but asserts that it is a Non-resident entity, must make a claim to that effect to the Registrar. That claim must set out the jurisdiction in which the Non-resident entity claims to be resident for tax purposes and must provide sufficient evidence to support that claim. The claim of residency for tax purposes, and the evidence provided in support of that claim, must be provided to the Registrar within the time required for the filing of a Declaration Form as set out in 8.2 above.

12.3. Evidence to support claim of residency for tax purposes

Evidence that the Registrar will accept as sufficient to demonstrate that an entity is resident for tax purposes in another jurisdiction will include one or more of the following:

- (a) a letter or certificate from the competent authority or tax authority of the jurisdiction in question, stating that the entity is considered to be resident for tax purposes in that jurisdiction; or
- (b) an assessment to tax on the entity, a confirmation of self-assessment to tax, a tax demand, evidence of payment of tax or any other equivalent document issued by the competent authority or tax authority for the jurisdiction in question.

In circumstances where the evidence described above requires further clarification, the Registrar may also require that he be provided with a letter, addressed to the Registrar, from a suitably qualified professional (e.g. lawyer or chartered accountant qualified to practice in the jurisdiction in question) stating that, in the opinion of the professional in question, the entity is considered to be resident for tax purposes in that jurisdiction. Such opinion will not, on its own, be treated by the Registrar as being sufficient evidence of tax residency, and must be supported by objective evidence as described in (a) or (b) above.

In the case of a transparent entity, residency for tax purposes in another jurisdiction must be demonstrated by reference to the members or partners on whom the entity's profits are taxable. For these purposes, a "transparent entity" means an entity in respect of which the entire profits are treated under the law of another jurisdiction as attributable to and taxable on some or all of the members or partners in the entity in question.

12.4. Evidence to be provided for each relevant financial period

A Non-resident entity undertaking a Relevant Activity must make its claim of tax residence outside of Bermuda, and provide evidence to support that claim, in respect of each relevant financial period (as such term is described in section 8.2 of these Guidance Notes).

Where the relevant financial period is not the same period as the tax accounting period, fiscal period or year of assessment for tax purposes for the entity in question, evidence of tax residency must be provided by the Non-resident entity to span the entire relevant financial period.

12.5. Evidence to be provided in English

All evidence provided to the Registrar must be provided in English. For any official documentary

evidence that is not in English, a certified English translation of that documentary evidence must be provided.

12.6. Provisional claim of residency for tax purposes

The Registrar acknowledges that, in respect of an entity claiming to be a Non-resident entity, documentary evidence of tax residency may not be available for an entire relevant financial period until some time after that relevant financial period has ended, and outside the time otherwise required for the filing of a Declaration Form for that entity (if it was not a Non-resident entity) in respect of that relevant financial period. In such circumstances, the Registrar may regard that entity as a Non-resident entity on a *provisional* basis, and may specify a reasonable period within which the appropriate documentary evidence of tax residency must be provided by that entity in order for the Registrar to confirm that provisional finding. In considering the period of time that is deemed reasonable for the entity to provide final evidence of tax residency, the Registrar will expect the entity in question to justify the time required to provide such final evidence, and will allow no more time than is required for that purpose, having regard to the need to ensure that the ES Requirements are not circumvented. In any event, the Registrar will not permit a period of longer than 12 months from the date of a claim for provisional tax residency for an entity to provide the final evidence to support the claim of residency for tax purposes as set out in 12.3 above. If the necessary final documentary evidence is not provided by the entity within 12 months, or such shorter time as the Registrar may direct, the entity in question will be treated as having failed to provide sufficient evidence to support its tax residence and will not be regarded as a Non-resident entity.

The circumstances in which the Registrar may regard an entity as a Non-resident entity on a *provisional* basis include:

- (a) the entity has established its tax residence in the jurisdiction in question for the previous relevant financial period to the satisfaction of the Registrar, and certifies to the Registrar that its jurisdiction of tax residence has not changed in the intervening period; or
- (b) the entity supplies (within the time otherwise required for the filing of a Declaration Form) the most recent available documentary evidence of residency for tax purposes, and certifies to the Registrar that such residency has not changed since the period to which the documentary evidence relates; or
- (c) the entity evidences either that it was too recently formed or incorporated, or that it has too recently established tax residence in the jurisdiction in question, for there to be sufficient documentary evidence of its tax residence, and provides to the Registrar other evidence to demonstrate that it met or expects to meet the criteria for tax residence in that jurisdiction for the relevant financial period in question.

In each case, the evidence described above must be provided to the Registrar within the time required for the filing of a Declaration Form as set out in 8.2 above.

12.7. Changes to EU list of non-cooperative jurisdictions for tax purposes

The Registrar acknowledges that, from time to time, changes may be made to Annex 1 to the EU list of non-cooperative jurisdictions for tax purposes. In such circumstances, an entity affected by the change may wish to adjust its business operations such that it meets the ES Requirements in

Bermuda, or establishes residency for tax purposes in another jurisdiction outside Bermuda (that is not on Annex 1 to the EU list of non-cooperative jurisdictions for tax purposes). The Registrar may receive representations to that effect from the entity in question, and may allow a reasonable period within which the entity may adjust its business accordingly.

12.8. Non-resident entities in liquidation

For the avoidance of doubt, a Non-resident entity that has entered liquidation may continue to claim that it is resident for tax purposes in a jurisdiction outside Bermuda, provided that such entity will in any event remain subject to the requirements of this section in relation to evidencing such claim of tax residency.

12.9. Exchange of information in relation to claim for tax residency

Evidence provided by an entity in relation to its claim of residency for tax purposes in a jurisdiction outside Bermuda, including any provisional claim of tax residency, will be subject to spontaneous exchange of information as described in Section 14 below.

13. Sector-Specific Guidance on Relevant Activities

Regulations 7 to 16 set out the CIGA of the different Relevant Activities. Sector-specific guidance notes in relation to different Relevant Activities are set out in the Schedule hereto. Additional sector-specific guidance notes will be issued after further consultation with representatives of each specific sector. Such sector-specific guidance notes will also deal with the application of the adequacy test to particular Relevant Activities in further detail.

14. Reporting obligations of the Bermuda Government

If the Registrar determines that an Entity:

- (i) has not met the applicable ES Requirements in respect of its Relevant Activities; or
- (ii) is engaged in a high-risk IP related activity with an Affiliate outside Bermuda

the Registrar is required by law to provide to the Minister the information filed by such Entity pursuant to the ES Laws (e.g. the Declaration Form and related information).

Where a Non-resident entity has provided evidence to the Registrar of its claim to be resident for tax purposes outside of Bermuda (including any provisional claim of tax residency), the Registrar must also provide that information to the Minister.

Upon receipt of the above information from the Registrar, the Minister, as competent authority for exchange of information purposes, is required to provide that information to his counterpart in the relevant EU member state or other jurisdiction in which the relevant Entity or Non-resident entity has its holding entity, its ultimate parent entity, an owner or beneficial owner, or where the relevant Non-resident entity claims to be resident for tax purposes.

15. Monitoring and Enforcement

15.1. Registrar's Duty to Monitor

The Registrar has a duty to ensure that every Entity satisfies the ES Requirements. The process for enforcement is set out in sections 9A and 16A of the Compliance Measures Act. The sanctions for non-compliance run in two schemes which run successively to each other.

One scheme is the Notice to Comply. The other scheme is the civil penalty scheme, which is the result of the issuance of a Warning Notice and then a Decision Notice, with right of appeal.

15.2. Sanctions Schemes

The sanctions schemes can be summarized as follows (assuming the Entity continues non-compliance and does not remedy the failure at any stage):

- (a) First Notice to Comply -> Warning Notice -> Decision Notice, with right to appeal;
- (b) Second Notice to Comply -> Warning Notice -> Decision Notice, with right to appeal;
- (c) Third/final Notice to Comply -> Warning Notice -> Decision Notice, with right to appeal;
- (d) After exhaustion of all notice requirements and appeal rights, the Registrar will move to either restrict the Entity's business operations/activities or move to strike the Entity off the register.

The non-compliant Entity will be provided with no fewer than 30 days and no greater than 180 days to remedy its non-compliance. The time period provided will be based on Entity-specific facts and circumstances as to its non-compliance, depending on the nature, scale and complexity of the business.

By way of example, an Entity may have a new Chief Financial Officer scheduled to start work in Bermuda, and this would cure the non-compliance. The CFO may be delayed in her/his start date due to numerous factors such as fulfillment of a notice period at a prior position, or securing housing in Bermuda. Each of these factors is outside of the Entity's control, and yet detrimentally affects the Entity's compliance. The Registrar will seek to provide the Entity with an adequate time to comply, based on the facts and circumstances regarding the Entity's non-compliance. The Registrar will always endeavour to afford the Entity adequate time to remedy the failure.

15.3. Civil Penalty after the First Notice to Comply

Under section 11 of the Compliance Measures Act, the Registrar may impose a civil penalty on the Entity for failure to comply after the First Notice to Comply has been issued. The process starts with the issue of a Warning Notice, followed by the issuance of a Decision Notice, which is subject to appeal. The process is described in section 12 of the Compliance Measures Act.

Section 12(1) of the Compliance Measures Act empowers the Registrar to issue a Warning Notice to the Entity which informs the Entity that the Registrar is proposing to impose a civil penalty with reasons provided. The Registrar must also inform the Entity that it is allowed to make representations to the Registrar regarding this proposal within a specified time (which cannot be less than 28 days and as a matter of policy will not ordinarily exceed 56 days).

Pursuant to section 12(2), the Registrar must issue a Decision Notice per section 12(3) within 3 months of the end of the period for representations to be made (as described above), which informs the Entity that:

- (a) no penalty will be imposed (if the Entity has complied with ES Requirements); or
- (b) that a penalty is being imposed, the amount of the penalty, and the reasons for the decision.

The penalty ranges from a minimum amount of not less than \$7,500 and a maximum amount not exceeding \$50,000 pursuant to the first Decision Notice.

15.4. The Second Notice to Comply

Pursuant to section 9A(3) of the Compliance Measures Act, if the Entity which engages in a Relevant Activity has not complied with ES Requirements within the relevant timeframe set by the Registrar in the First Notice to comply, the Registrar will issue a Second Notice to the Entity. The Second Notice to Comply will set out the matters set forth in subsection 2(a) and (b) of section 9A as per the First Notice to comply.

If the Entity remedies its failure to comply with ES Requirements as per the Second Notice to Comply, the process ends. The Registrar can impose a civil penalty for an Entity's failure to comply in the same manner as described for the First Notice to Comply. However, the penalty range for the second notice increases to a minimum amount of not less than \$25,000 to a maximum amount not exceeding \$100,000.

In the case of a Second Notice to Comply, the Entity will be given a minimum of 15 days and a maximum of 90 days to comply. The timeframe will depend on the facts and circumstances of noncompliance.

If the Entity remedies by complying with ES Requirements, the process ends. If the Entity fails to comply, the Registrar has the power to impose a civil penalty with a view to ensuring compliance. The Warning Notice and Decision Notice procedures, as outlined above, would then be implemented with regard to the Second Notice to Comply.

The imposition of civil penalties is subject to appeal with 28 days of the decision.

15.5. The Third Notice to Comply

Pursuant to section 9A(4) of the Compliance Measures Act, if the Entity has not complied with ES Requirements within the relevant timeframe set by the Registrar in the Second Notice to Comply, he will issue a Third (and final) Notice to Comply to an Entity.

If the Entity remedies its failure to comply with ES Requirements as per the Third Notice to Comply, the process ends. The Registrar can impose a civil penalty for an Entity's failure to comply in the same manner as described above. However, the penalty range for the Third Notice increases to a minimum amount of not less than \$50,000 to a maximum amount not exceeding \$250,000.

In the case of a Third Notice to Comply, the Entity will be given a minimum of 8 days and a maximum of 45 days to comply. The timeframe will depend on the facts and circumstances of non-compliance.

If the Entity remedies by complying with ES Requirements, the process ends. If the Entity fails to

comply, the Registrar has the power to impose a civil penalty with a view to ensuring compliance. The Warning Notice and Decision Notice procedures, as outlined above, would then be implemented with regard to the Third Notice to Comply.

The imposition of civil penalties following the issuance of a Decision Notice under section 12(3) of the Compliance Act is subject to appeal within 28 days of the date of the Decision Notice.

15.6. Requirement for the Registrar to apply to the Court regarding continued non-compliance after Notices

If an Entity still does not meet the ES Requirements after the Third Notice to Comply has been issued, and the civil penalty scheme of Warning Notices and Decision Notices has been exhausted (including any appeal rights), the Registrar will apply to the Court for an order pursuant to section 9A(5). The court order may:

- (a) regulate the conduct of the Entity's business; or
- (b) restrict the Entity from carrying on business, which would result in the Entity becoming defunct; or
- (c) authorise such proceedings under the relevant Act to be taken by the Registrar, including strike-off.

For this purpose, the "relevant Act" means under any act pursuant to which the Registrar performs regulatory, administrative or other functions with respect to an Entity and includes the Companies Act 1981, the Partnerships Acts, and the Limited Liability Company Act 2016.

16. Offences

It is an offence to knowingly provide false information to the Registrar. Punishment for this offence on summary conviction is a maximum fine of \$10,000 or two years imprisonment or both.

Where the offence is committed by an Entity and proved to have been committed with the consent or connivance of an officer of the Entity, the officer as well as the body corporate commits the offence and will be liable to be proceeded against and punished accordingly.

An "officer" is:

- (a) a director as defined in section 2 of the Companies Act 1981;
- (b) a manager as defined in section 2 of the Limited Liability Company Act 2016; and
- (c) in the case of a partnership, a director or manager of the general partner of the partnership.

17. Confidentiality

The information and documents provided by an Entity to the Registrar in respect of the ES Requirements will be held in the strictest confidence except in so far as disclosure is necessary for the due performance of the Registrar's functions. Disclosure is permissible in the following circumstances –

- (a) to the Minister for the purpose of enabling or assisting him to discharge his statutory functions or in the public interest;

- (b) to the Bermuda Monetary Authority for compliance purposes;
- (c) if the information is available to the public from other sources;
- (d) in a summary or collection of information framed in such a way as not to enable the Entity to which the information relates to be ascertained; and
- (e) as otherwise authorised by law.

Otherwise, it is an offence to disclose or give access to ES Requirements related information or documents provided by an Entity to the Registrar which is punishable on summary conviction to a fine of \$50,000 or two years imprisonment or both and on indictment to a fine of \$100,000 or five years imprisonment or both.

18. PATI and PIPA

Economic substance information is not disclosable under the Public Access Information Act 2010. Nor is personal information disclosable pursuant to the Personal Information Protection Act 2016.

Schedule

Sector-specific Guidance applicable to Relevant Activities

A. Holding Entity

An entity will be a pure equity holding entity if its sole function is to acquire and hold shares or an equitable interest in other entities, and the shares or equitable interest are controlling stakes in other entities.

If an entity carries on any other Relevant Activity (whether or not for profit), then it would not fall within the definition of a pure equity holding entity. It would remain subject to the full ES Requirements applicable to that other Relevant Activity.

As specified on page 41 of the OECD Action 5 2017 Progress Report⁵ (“*Holding company regimes*”), for holding companies that hold a variety of assets and earn different types of income (e.g. interest, rents, and royalties), the core income generating activities would be those activities that are associated with the income that the holding companies earn, as determined by the discussion above. (For example, a holding company that receives benefits for banking income would be required to have the core income generating activities associated with banking companies.) Such entities must therefore comply with the full substance requirements of that Relevant Activity.

If an entity meets the criteria to be regarded as a pure equity holding entity, the placing of dividend monies received on deposit or using them to acquire and passively hold other securities such as gilts will not constitute a “commercial activity” and the entity will still be regarded as a pure equity holding entity and subject to applicable substance requirements.

Examples:

1. Midco Ltd. is an intermediate pure equity holding entity in a group structure. It holds 100% of the shares in three other companies and receives dividends annually. This is Midco Ltd.’s only activity. Midco Ltd. is a pure equity holding entity.
2. Restaurant Ltd. runs two restaurants. It also acquired all of the shares in another company, Bistro Ltd., which is constructing a new restaurant. Restaurant Ltd. will not be a pure equity holding entity as besides holding shares it is in the business of running restaurants.
3. Trust Services Ltd. acts as trustee to a number of unconnected trusts, holding assets in its capacity as trustee. As Trust Services Ltd. commercially provides trustee services and is not the beneficial owner of the assets, it will not be a pure equity holding entity, but should consider if it carries on any other relevant activities for its own account, not acting as trustee.

⁵ A copy of the OECD Action 5 2017 Progress Report can be found at <https://www.oecd-ilibrary.org>

[additional sector-specific guidance to be inserted]