

Guernsey economic substance update: COVID-19 concessions, self-managed funds and partnerships

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For many Guernsey tax resident companies, the onset of the COVID-19 pandemic created difficulties in complying with economic substance requirements.

Guernsey tax resident companies carrying out certain relevant activities have to comply with the substance requirements set out within the Income Tax (Substance Requirements) Implementation Regulations 2018 (as amended) (the **Regulations**). In particular, these include requirements that a company's activities be "directed and managed" from Guernsey, and that certain "core income-generating activities" (**CIGAs**) be carried out in Guernsey.

Difficulties they've encountered over the past year have included, for example, directors or other decision makers who might normally travel to Guernsey to attend board or other meetings in person found that they could not do so because of travel restrictions, while social distancing and self-isolation requirements meant that many activities needed to be carried out remotely.

In November 2020 the States of Guernsey Revenue Service (the **Revenue**) released guidance confirming that the Revenue Service will take a pragmatic approach when assessing whether the substance requirements have been met by a company during periods where government imposed restrictions were in place (including restrictions imposed by governments in other jurisdictions). The Revenue issued the following statements regarding matters they will consider as appropriate for any temporary framework for interpreting the Substance Requirements to take account of COVID-19 related adjustments to the operation of companies during the pandemic:

- "It is expected that COVID-19 measures will only impact on the ability of companies to comply with the directed and managed test of the economic substance requirements. It is still expected that companies will continue to meet the other economic substance tests.
- Companies should maintain and retain relevant records that show what their policy was in respect of restrictions on travel for the company officers and the period of time for which that policy was in place. Similarly for any government imposed restrictions.
- Where COVID-19 measures have meant that a company does not fully meet the economic substance requirements, a Revenue Inspector will undertake a review. Such a review may require the company to provide objective and sufficient evidence of their specific circumstances hindering their compliance.
- Where the Revenue is required to exchange information with EU Member States on a company as a result of its failure to comply, the exchange would include information that companies provide on the impact of COVID-19 measures."

In addition, the Revenue confirmed that this temporary framework will remain in place until the Guernsey border restrictions have been lifted.

Self-managed funds and fund vehicles

An important amendment has also been made to the Regulations pursuant to the Income Tax (Substance Requirements) (Implementation) (Amendment) Regulations 2020 (the **Amendment Regulations**) in relation to "self-managed collective investment schemes" (**SM Funds**). An SM Fund is defined as "a company which is a collective investment vehicle within the meaning of the Income Tax (Exempt Bodies) (Guernsey) Ordinance 1989 and which has no other person or body conducting fund management in respect of it, and for this purpose fund management means exercising any managerial function in relation to an investment or in relation to the assets underlying the investment". Therefore SM Funds are essentially corporate funds that do not appoint an external manager, but which are entirely managed internally by their board of directors.

The Amendment Regulations deem any SM Fund to be carrying on the relevant activity of "fund management" and to be in receipt of income in respect of such activity. As such, the CIGAs which apply in respect of fund management will be relevant for SM Funds and there will be no separate requirement that such funds generate gross income in order to be within the scope of the Regulations.

Partnerships

The Regulations as currently drafted do not apply to partnerships.

However, the European Union's Code of Conduct Group on business taxation gave a report to the Council of the European Union on 20 November 2020 in which it recommended that jurisdictions such as Guernsey with economic substance requirements applicable to companies should extend those requirements to partnerships. The report suggests that new partnerships should be in scope from 1 July 2021, with a transition period of no more than six months (i.e. running to 1 January 2022) for existing partnerships.

The EU report does not detail how partnerships are to be brought in to scope and it is anticipated that there may be challenges to do so, given their nature as tax transparent vehicles and, as such, do not have a tax residency independent to their partners. It is hoped that the financial services industry in Guernsey will be consulted on the form and manner of compliance with the EU's requirements.

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