

Guernsey substance rules – the Banking and Finance perspective

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The Guernsey government has approved new regulations which impose an economic substance test for Guernsey tax-resident companies to meet the requirements of the EU Code of Conduct Group. These regulations were approved by the EU's ECOFIN council on 12 March 2019 and as a result, Guernsey was re-affirmed as a co-operative jurisdiction in terms of tax transparency and for action 5 of BEPS.

The regulations came into force on 1 January, establishing tests for tax resident companies carrying on "relevant activities", including "fund management". The tests require companies that are in scope to demonstrate that they have economic substance in Guernsey, including that they are "directed and managed" in Guernsey, that certain of their "core income generating activities" are undertaken here, and that the companies have "adequate" premises, employees and expenditure in Guernsey proportionate to the level of relevant activity carried on in Guernsey.

"Relevant activities" for the purposes of this briefing include:

- Companies that carry on banking business
- Companies involved in financing and leasing; and
- Companies that carry on insurance business

Please see [here](#) for Ogier's briefing applicable to fund managers and [here](#) for Ogier's briefing in respect of holding, distribution and services companies.

Our view, set out below, is that specific consideration should be given to the outsourcing arrangements of each company within a relevant structure, and to updating Policies and Procedures. Further consideration also needs to be given in respect of the detailed guidance on the definition of "adequacy" that we anticipate soon, and in respect of companies generating income from intellectual property, which will be subject to more stringent tests.

The Direction and Management Test

The proposed regulations provide that the Direction and Management test would be met if the following are adhered to:

- There must be meetings of the Board of Directors in Guernsey at adequate frequencies given the level of decision making required;
- During these meetings, there must be a quorum of the Board of Directors physically present in Guernsey;
- Strategic decisions of the company must be set at meetings of the Board of Directors and the minutes must reflect those decisions;
- All company records and minutes must be kept in Guernsey; and
- The Board of Directors, as a whole, must have the necessary knowledge and expertise to discharge their duties as a board.

Core Income Generating Activities

Guernsey tax resident entities which carry on relevant activities will need to demonstrate that they carry out core income generating activities (**CIGA**) in Guernsey. The nature of the CIGA varies by industry sector and are summarised below.

CIGA for Banks

Companies undertaking banking business will need to demonstrate that the following CIGA are carried out in Guernsey:

- Raising funds;
- Managing risk;
- Providing loans, credit or other financial services for customers;
- Managing regulatory capital; and
- Preparing regulatory reports and/or returns.

CIGA for Finance and Leasing companies

Financing and leasing companies will need to demonstrate that the following CIGA take place in Guernsey:

- Agreeing funding terms;
- Identifying or acquiring assets to be leased (in the case of leasing);
- Setting the terms and duration of acquiring assets to be leased (in the case of leasing);
- Monitoring and revising agreements; and
- Managing any risk.

CIGAs for Insurance Businesses

Companies undertaking insurance business will need to demonstrate the following CIGA are carried out in Guernsey:

- Predicting and calculating risk;
- Providing client services.

What is the impact of carrying on a "relevant activity"?

Companies carrying on a "relevant activity" must be able to demonstrate:

- An adequate number of employees in Guernsey, or adequate level of expenditure on outsourcing to service companies in Guernsey, proportionate to the activities of the company.
- An adequate level of annual expenditure incurred in Guernsey proportionate to the activities of the company.
- Adequate physical offices and/or premises in Guernsey, or adequate level of expenditure on outsourcing to service companies in Guernsey, for the activities of the company carried on in Guernsey.

The proposed regulations impose sanctions for non-compliance to include progressive financial penalties, ultimately leading to strike-off from the register of Guernsey companies, and

reporting to any relevant tax or regulatory authorities in the EU.

The Ogier view

- Affected entities should review outsourcing arrangements (where relevant) in respect of Guernsey tax-resident companies that fall within the scope of the new law and determine whether the third-party service provider agreements in place meet the relevant tests.
- It is anticipated that many structures will be compliant with the new requirements already – consideration should still be given to whether amendments and updates are required to any Policies and Procedures as a result of the new law.
- IP income generating companies (ie tax resident companies with income from intellectual property) will be subject to enhanced requirements, which will be the subject of a separate briefing in due course.
- We anticipate further detailed guidance on the precise definition of activities to fall within the scope of the law, and the definition of adequacy in respect of employees, expenditure and premises under the "Core Income Generating Activities" test.

If you require further information or would like to discuss how the proposals may impact your business, please get in touch with your usual Ogier contact.

Bulletin on the 2020 Guernsey Substance Amendment Regulations and the treatment of funds under the substance regime can be [found here](#).

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