

Guernsey Economic Substance Requirements

The Guernsey Revenue Service introduced economic substance from 1 January 2019 as part of the islands commitment with the EU for tax transparency and alignment with Base Erosion and Profits Shifting (“BEPS”) measures.

A key concern prior to the introduction of Economic substance was that Guernsey companies could be used to artificially attract profits here and that these profits would be out of step compared to the actual economic activity of the company in Guernsey.

Economic substance initially encompassed Guernsey tax resident companies with the Guernsey corporate tax residency rules being simultaneously updated. A company is now considered as tax resident in Guernsey, broadly where:

- It is controlled (by shareholder) Guernsey, or
- Is centrally managed and controlled in Guernsey, or
- Is registered in Guernsey.

The law also provides that even where a company may be controlled (by shareholder) or incorporated in Guernsey that it would not be tax resident in Guernsey if:

- It is a tax resident in a second jurisdiction under that jurisdiction's domestic tax law, and
- Is centrally managed and controlled in that jurisdiction, and either;
 - Resident in that jurisdiction by virtue of
 - arrangements for double taxation (i.e., tax treaty), or
 - specific international agreement.
 - The highest rate of tax in that jurisdiction is at least 10%.
- Residence in that jurisdiction is not motivated by avoidance or reduction in liability.

The Economic substance law has now been extended to include Guernsey branches, self-managed funds and, from 1 January 2022, partnerships.

Self-Managed Funds

If a Guernsey Collective Investment Vehicle (“CIV”) has no other person or body conducting fund management in respect of it, the CIV could be considered a self-managed fund.

From October 2020, self-managed funds are required to demonstrate they have sufficient economic substance in Guernsey, as if they are carrying on the relevant activity of fund management (see below).

Partnerships

For Guernsey economic substance purposes, the term partnership includes general partnerships and limited partnerships formed in Guernsey and foreign partnerships (including limited partnerships and limited liability partnerships) formed outside of Guernsey which have their place of effective management in Guernsey and carry on a business activity in Guernsey.

A number of exemptions exist which may place a partnership outside the scope of Guernsey economic substance. However, where a partnership cannot be exempt and income is received from a relevant activity, the partnership will be required to demonstrate its compliance with Economic substance.

The requirements for partnerships came into force for accounting periods commencing on or after 1 January 2022 for partnerships existing as at 30 June 2021. For partnerships formed on or after 1 July 2021, they will be within scope from accounting periods commencing from 1 July 2021.

Relevant activities

Where an entity within the scope of economic substance receives income from a ‘relevant activity’ it is required to meet specific economic requirements. The relevant activities are:

- Banking;
- Insurance;
- Shipping;
- Fund Management;
- Financing & leasing;
- Headquarters;
- Distribution and service centres;
- Intellectual property holding ‘IP’
- A pure equity holding company that has income from their activity.

Economic substance requirements

Any entity within the scope of economic substance should ensure that:

- It is directed and managed in Guernsey (a slightly different test to central management and control), and that
- It carries on core income generating activities (‘CIGA’) in Guernsey (the legislation does not prohibit an entity from outsourcing some or all of its activity within Guernsey), and that
- It has adequate employees, expenditure and physical presence in Guernsey. In addition, any entity with IP income should be aware that this is an area of additional complexity and that specific CIGA requirement must be met.

Practical Guidelines

Entities should keep records of all activities undertaken on Island, especially those relating to CIGA, including the level and seniority of staff, the amount of time spent on an activity and all decisions made relevant to such activity. For decisions taken which would usually be at board level, detailed records should be kept to include notes of all matters considered when reaching a decision and the names of the individuals attending the meeting.

Not all CIGA needs to be performed by the entity as outsourcing and delegation is permitted. However, it must be undertaken on Island and any outsourcing should be adequately supervised.

The term adequate is undefined in the legislation and guidance. As such its ordinary meaning should be used. What is adequate will be fact and circumstance dependant and will be different from company to company.

The sanctions for non-compliance are graduated and penal, and lead to a company being struck off. The Guernsey Revenue Service has wide powers within economic substance legislation, including right of entry and will also conduct annual reviews to ensure the substance requirements are being met.

To enable the Guernsey Revenue Service to monitor whether entities within the "Economic Substance" regime are compliant, there is a requirement to provide additional information when completing annual tax returns. At a high level, an entity within economic substance should provide the following information;

- Amount and type of gross income;
- A breakdown of income streams in order to identify the type by relevant activity;
- Confirmation of the CIGAs conducted for each relevant activity;
- Confirmation of whether any CIGA have been outsourced and if so relevant details;;
- Number of (qualified) employees, specifying the number of full-time equivalents;
- The amount of operating expenditure by relevant activity;
- Details of premises;
- Financial Statements.

Guernsey tax compliance

We have created an Economic Substance Register ("ESR"), which helps:

- Ensure an entity which falls within Guernsey economic substance is considering the relevant requirements;
- Provide a framework to record the relevant information;
- Reduces time and cost when preparing a Guernsey tax return; and
- Helps demonstrate the rationale behind tax return certain declarations should an entity be audited by the Guernsey Revenue Service.

Please get in touch with any of the below, or your usual contact for further information.



Natalie Chamberlain CTA
Executive Director, LTS Tax Limited
DD: +44 (0)1481 747753 T: +44 (0)1481 755862
E: natalie.chamberlain@lts-tax.com



Julian Turian ATT FMAAT
Executive Director, LTS Tax Limited
DD: +44 (0)1481 743045 T: +44 (0)1481 755862
E: julian.turian@lts-tax.com



Sarah Kenealy CTA
Associate Director, LTS Tax Limited
DD: +44 (0)1481 747744 T: +44 (0)1481 755862
E: sarah.kenealy@lts-tax.com



Jonny Woodgate
Manager, LTS Tax Limited
DD: +44 (0)1481 755873 T: +44 (0)1481 755862
E: jonny.woodgate@lts-tax.com

