RDG Fiduciary Services

BVI Economic substance for private wealth – snagging items?

In May this year I flagged some areas of uncertainty in the BVI economic substance regime from a private wealth perspective[1]. Following discussion with the BVI ITA and a number of practitioners / service providers, it would appear that the issues relating to the requirement for income and PTCs appear to have been dealt with.

There seem to be two primary areas of confusion/ ambiguity at present. One relates to companies which have been struck off and the other is the classification in respect of pure equity holding companies. I shall look at each in turn.

Struck-off companies

The current position[2] is that since struck-off companies are legal entities in the BVI, they are required to comply with the economic substance obligations. The requirement[3] only catches those entities which were struck-off post 1 January 2016.

Struck-off companies still exist, in most cases have a Registered Agent[4] and are restricted by the provisions of the Business Companies Act. Such restrictions[5] *inter alia* prevent the company from carrying on any business and prevent the directors/members dealing with any of its assets or "acting in

[1] https://www.linkedin.com/pulse/bvi-economic-substance-some-further-clarity-richard-grasby-tep
[2] Under review.
[3] See s 11(2) of the Beneficial Ownership Secure Search System Act ("BOSS") as extended to the remainder of the Act.
[4] The BCA does allow registered agents to resign – see s93 BCA.
[5] Principally s215.

any way with respect to the affairs of the company". A struck-off company can continue to incur liabilities.

If we assume, as is often the case with a struck-off company, communication between the Registered Agent ("RA") and the directors/ultimate beneficial owners/"client of record" of the company has ceased and the RA is not being compensated, then the economic substance requirements are somewhat unfair on the RA. Per section 10 of BOSS, the database obligations fall on the RA in respect to such struck-off company. There are also AML/CFT obligations on the RA which are not affected by the striking-off.

The RA is required to maintain prescribed information relating to whether the entity carries on a relevant activity[6]. This should be "no" but does the fact that the law would not allow a struck-off entity to carry on any business put the RA in a position to say so without any knowledge?

BOSS section 9 sets out the duties of the RA which include taking "reasonable steps to…collect the prescribed information with respect to each corporate and legal entity for which it acts as registered agent[7]."

What are reasonable steps? BOSS s9(4) suggests that compliance with AML requirements is sufficient to constitute reasonable steps "in accordance with this section". That should cover an RA which requests but does not receive the information.

However, the ES Data Model Description[8] stipulates the "relevant activity" question[9] as a mandatory question and therefore the RA has to answer. Absent confirmation from the struck-off entity, is the RA covered by inserting "No[10]"? This has to be assumed.

The same section also imposes an obligation on the company to "identify whether or not it carries on one or more relevant activities..."[11] Rule 12.7 states that the duty to provide the prescribed information "is not qualified by a requirement that it need only take "reasonable steps"".

BOSS s9(6) states the offence for the company failing to provide the information "without reasonable cause". Under ES there is an offence of "failure to provide information without reasonable excuse".

Is being struck-off so "reasonable"? The punishment for non-compliance with BOSS and ES includes fines. Most struck-off companies don't have any assets.

Perhaps for struck-off companies the data could be pre-populated based on the year of being struck-off and continue each year thereafter? Further clarification is to be welcomed.

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[6] BOSS s10(3)(va)-(vi)
[7] BOSS s9(1)(b)
[8] See the memorandum from BDO
[9] Referred to as 7a
[10] Assuming that the RA has no knowledge to the contrary.
[11] BOSS s9(2)(b)

Pure equity holding entities

The first query relates to the definition of the holding of equity participations. Using a nominee shareholder or broker to hold equities means that in many cases, the investor does not "only hold equity participations[12]". Is this the same analysis in BVI? The Cayman Islands Guidance[13] provides an example at F3(b) on p67 which reads thus:

"CayCo Ltd, a relevant entity, has a brokerage account. The brokerage account only holds equity participations in underlying entities. This is CayCo Ltd's only activity. CayCo Ltd is not a pure equity holding company because CayCo Ltd's only asset is a claim against the broker. CayCo Ltd does not directly hold or manage equity participations; these are held by the broker. CayCo Ltd is therefore not conducting holding company business."

This is notwithstanding the same definition of equity participation in both jurisdictions.

The second query is one which I have raised for a long time. That of passive and active management of pure equity holding entities.

Rule 8(2)(b) is the provision this states that substance is met if the entity:

"has, in the Virgin Islands, adequate employees and premises for holding equity participations and, where it manages those equity participations, has, in the Virgin Islands, adequate employees and premises for carrying out that management."

There has been little clarification as to what is needed in the BVI to "hold" equity participations and what is needed in the BVI where equity participations are "managed". It is clear that such company does not need to be directed and managed in the BVI; nor is there a CIGA requirement. Redemptions, voting, sales and other decisions relating to the equity participations are not -in most cases -going to take place in the BVI. Does the "management" then refer to book-keeping, consolidation and other record keeping? What premises are needed for this?

It is interesting that the "decision tree" regarding entities which carry on holding business has changed in respect of this issue and this is replicated in the ES Data Model Description.

The "old" decision tree required the entity to determine whether or not the equity participations were being actively managed. The "new" decision tree requires employees and premises to be reported for all entities carrying on holding business. The ES Data Model Description accordingly, for all entities which select "holding business" (9h), has mandatory questions for employees and premises (9h.1a -9h.2a). This is followed by an "optional" question (9h.3a) relating to compliance with the BCA[14] and then a "recommended" question (9h.3b) asking "does the entity actively manage its equity participations?". It

[12] But does "have the right to participate in the profits of the entity" per Rule 5.26
[13] 19 July 2020
[14] As per Rule 8(2)(a)

appears therefore that the BVI ITA will determine what is adequate. It seems a little counter-intuitive that “zero” can be adequate. Guidance would be welcomed.

September 2020.

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