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OUTCOME OF PROCEEDINGS

From:	General Secretariat of the Council
To:	Delegations
Subject:	The EU list of non-cooperative jurisdictions for tax purposes • Bahamas: final legislation and assessment under criterion 2.2

A/ FINAL LEGISLATION:

On 21 December 2018, Bahamas published the Commercial Entities Substance Requirements (the "CESR") Act, 2018. This Act was amended in February 2019:

https://www.bahamas.gov.bs/wps/wcm/connect/41a2d4b2-8cae-4635-ba24-c54c5c77a70d/Commercial+Entities+%28Substance+Requirements%29+%28Amendment%29+Bill%2C+2019.PDF?MOD=AJPERES

Substance Requirements Act Guidelines:

https://www.bahamas.gov.bs/wps/wcm/connect/1637cd31-c0fe-4580-8be1-9146e2815007/CESR+GUIDELINE+GAZETTE000.pdf?MOD=AJPERES

Removal of Preferential Exemptions Act, 2018:

https://bfsb-bahamas.com/wp-content/uploads/2019/01/REMOVAL-OF-PREFERENTIAL-EXEMPTIONS-ACT-21-DECEMBER-2018-GAZETTE-1.pdf

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Register of Beneficial Ownership Act, 2018:

https://bfsb-bahamas.com/wp-content/uploads/2019/01/REGISTER-OF-BENEFICIAL-OWNERSHIP-ACT-31-DECEMBER-2018-GAZETTE-1.pdf

B/ FINAL ASSESSMENT:

With regard to criterion 2.2, the dialogue with the Bahamas on the introduction of substance requirements was constant and constructive, with several conference calls and meetings on which the Commission Services reported regularly to Member States. The Bahamas shared draft legislation and sought feedback from the Code of Conduct Group.

The following assessment only highlights the remaining issues identified and still pending at the beginning of 2019 following such feedback provided throughout 2018.

I - On ring-fencing

The "Removal of preferential exemptions Act, 2018" was published on 21 December 2018. The legislation does not eliminate the prohibition for entities[1] to operate within the Bahamas but eliminates the preferential tax treatment applicable to those entities. It also introduces a 3 years grandfathering period (up to 31 December 2021) for entities incorporated, registered or continued and in existence prior to the commencement of the Act.

Conclusion:

The issue is settled, as the Bahamas eliminated the ring-fencing elements of their legislation.

II - On the introduction of substance requirements

1 – Identification of the relevant activities and included entities

1.1 – On relevant activities

The Bahamas have identified the relevant sectors of activity in line with the 2.2 Scoping Paper.

[1] A body incorporated, registered or continued in accordance with the International Business Companies Act, the Exempted Limited Partnership Act, the Investment Condominium Act or the Executive Entities Act.

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Conclusion:

This issue is settled.

1.2 – On included entities

The Bahamas substance requirements apply to entities incorporated, registered or continued under the Companies Act or the International Business Act. Following a request from the Commission services, the Bahamas have clarified their treatment of partnerships and made clear that:

- Domestic partnerships are not separate legal entities. The following domestic partnerships are:

  - Exempted limited partnerships: at least one general partner has to be resident in the Bahamas (if an individual) or incorporated under the IBC or Companies Act (or registered under Part VI of the Companies Act if the general partner is a foreign partnership). In any of these cases, the Bahamas confirmed that any corporate partner of a domestic partnership would be in the scope of the CESR as an included entity.

  - Partnerships registered under the Partnerships Limited Liability Act: such partnerships are expressly allowed to have limited liability only for business within the Bahamas.

  - General partnerships under common law: the Bahamas clarified that general partnerships arise when persons agree to engage jointly in a business. It governs such arrangements, which often arise under common law merely by an informal course of dealings between persons. Such informal business arrangements are not a facet of the financial services sector, and only occur in the Legal, Accounting and Medical Professions, and these have inherent physical presence, substance and CIGA in The Bahamas.

- Foreign partnerships have to be registered in the Bahamas under Part VI (sections 170-172) of the Companies Act. Accordingly, the Bahamas confirmed that any foreign partnership conducting business in the Bahamas would be in the scope of CESR as an included entity.

Conclusion:

This issue is clarified and that the risk of BEPS is limited. However, the COCG will monitor over the coming months whether Bahamas should include all partnerships in the scope of substance requirements.

2 - Imposition of substance requirements

2.1 – Income threshold

The Bahamas have deleted the reference to an income threshold in their draft legislation.

Conclusion:

This issue is settled.

2.2 – Tax residence

After a meeting in Brussels on 8 February 2019 followed by email exchanges, The Bahamas shared the final version of their Guidelines[2].

It includes a tax residence test based on central management and control of the relevant entities. The entities claiming to be tax resident in another jurisdiction will have to certify in writing and substantiate their claim with satisfactory evidence:

- tax identification number issued by the foreign jurisdiction;

- tax residence certificate issued by the foreign jurisdiction;

- official receipt or statement issued by the foreign jurisdiction;

- certification by the entity that the majority of meetings of the board of directors, or controlling persons of a non-corporate entity, in any financial year, took place in the foreign jurisdiction and the ordinary residence of the majority of the board of directors, or controlling persons of a non-corporate entity.

[2] Guidelines on the Commercial Entities (Substance requirements) Act, 2019 adopted and published on 22 February 2019.

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The Bahamas have confirmed that all these elements will need to be filed to evidence tax residence in another jurisdiction as part of their annual filing requirements together with the information on the jurisdiction of tax residence and the jurisdiction of its legal or beneficial owner.

The Bahamas have amended Section 12 of the Principal Act[3] in order to provide for spontaneous exchange of information with the jurisdiction of the legal or beneficial owner as well as the jurisdiction of its claimed tax residence.

Conclusion:

This issue is settled.

2.3 – Specific CIGAs for IP assets

The Bahamas have amended their legislation to make a direct link between the type of IP assets and the relevant CIGAs.

Conclusion:

This issue is settled.

2.4 – CIGAs in or from within the jurisdiction

The Bahamas legislation provides that an included entity carrying on relevant activities must conduct CIGAs in the Bahamas.

Conclusion:

This issue is settled.

[3] Commercial Entities (Substance Requirements) (Amendment) Bill, 2019 as adopted on 15 February 2019 with effect as of 31 December 2018.

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2.5 – Outsourcing safeguards

The Bahamas have amended Section 6 of the Principal Act to make clear that:

- No included entity shall outsource any of its core income generating activities (CIGAs) to an entity or person outside of The Bahamas;
- An included entity may outsource any of its CIGAs to an outsourcing provider in The Bahamas provided that the entity is able to demonstrate supervision and control of the outsourcing service provider;
- The resources of the outsourcing service provider must not be counted multiple times in respect of outsourced CIGAs to multiple included entities.

The previous exceptions to the last safeguards have been deleted.

The Bahamas have also ensured proper reporting of the outsourcing arrangements.

Conclusion:

This issue is settled.

2.6 – Regulated activities

The final legislation provides for the same reporting obligations for regulated activities as for all other activities.

Conclusion:

This issue is settled.

Conclusion

Leaving aside the issue of collective investment funds, the Bahamas have implemented their commitment to introduce substance requirements.

ANNEX 1: assessment by COCG experts in 2017

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ASSESSMENT BY COCG EXPERTS IN 2017

	1a	1b	2a	2b	3	4	5
BAHAMAS	V	V	V	V	V	?	X
Criterion 2.2: "The jurisdiction should not facilitate offshore structures or arrangements aimed at attracting profits which do not reflect real economic activity in the jurisdiction" *In light of the assessment made under all Code criteria applied by analogy, the tax system of BAHAMAS should be considered overall harmful from a Code of Conduct point of view.* *The main concerns on deviations from the Code of Conduct criteria as applied by analogy relate to the lack of legal substance requirements and the de facto lack of substance.* *In addition there are legal or de facto mechanisms that enable the granting of advantages only to non-residents or in respect of transactions carried out with non-residents.*						Overall: V	

Explanation

Absence of a corporate tax system or applying a nominal corporate tax rate equal to zero or almost zero: In this respect, where criterion 2.1 is inapplicable solely due to the fact that the jurisdiction concerned does not meet the gateway criterion under Paragraph B of the Code of Conduct, because of the "absence of a corporate tax system or applying a nominal corporate tax rate equal to zero or almost zero", then the five factors identified in paragraph B of the Code of Conduct should be applied by analogy to assess whether the criterion 2.2 has been met.

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Relevant questions (Q 1.2)

BAHAMAS does not apply any corporate tax system. We therefore suggest that this jurisdiction meets the gateway test of the criterion 2.2.

Criterion 1:

“whether advantages are accorded only to non-residents or in respect of transactions carried out with non-residents”

Relevant questions (Q 2.1, Q 2.2, Q 2.3, Q 1.1, Q 1.2, Q 1.5, Q 1.8,)

The absence of CIT is de lege available to both residents and non-residents and does not require that the beneficiaries carry out transactions only with non-residents.

However, when assessing a jurisdiction without CIT for the purpose of the list of non-cooperative jurisdictions, it should be assessed whether aspects of the legal framework, including non-CIT aspects, effectively provide for a ring-fenced scenario.

In this respect, according to subsection 187(1) of the International Business Companies act, neither such companies nor the members and shareholders thereof shall be subject to business license fees and other taxes. Subsection 187(3) exempts transaction in respect of the shares, debt and obligations of the securities of an IBC as well as all other transactions relating to the business of such companies. However, subsection 187(4) excludes residents of Bahamas from the benefit of subsection 187(3).

Moreover, such companies are restricted by subsection 187(6) to carry business with persons resident in The Bahamas, as it must first obtain a permission from the Central Bank.

Regarding partnerships, Exempted Limited Partnership Act provides in subsection (17)(1) that such partnerships or a partner thereof “shall not be subject to any business license fee, income tax, capital gain tax or any other tax on income or distribution accruing to or derived from such partnership or in connection with any transaction to which the partnership or the partner, as the case may be, is a party”.

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Meanwhile, subsection (4)(1) of this Act prohibits such entity to "undertake business with the public in The Bahamas other than so far as may be necessary for the carrying on of the business of that [entity] exterior to The Bahamas".

It shall be noted that BAHAMAS applies a business license fee, a broad turnover tax, to all entities operating in BAHAMAS.

Therefore, we shall conclude that there is a de lege ring-fencing.

Moreover, BAHAMAS was not able to provide for the number of registered and/or legal entities controlled by non-resident legal entities or individuals.

We would propose a tick ("V" – harmful) for criterion 1a) and criterion 1b).

Criterion 2:

"whether advantages are ring-fenced from the domestic market, so they do not affect the national tax base"

Relevant questions (Q 2.1, Q 2.2, Q 2.3, Q 1.1, Q 1.2, Q 1.5, Q 1.8,)

By analogy to the assessment against criterion 1a/b. We would propose a cross ("V" – harmful) for criterion 1a) and criterion 1b).

Criterion 3:

"whether advantages are granted even without any real economic activity and substantial economic presence within the jurisdiction offering such tax advantages"

Relevant questions (Q 1.1, Q 1.7, Q 1.9, Q 2.4, Q 2.5, Q 2.6, Q 2.7, Q 2.8)

- Facts :

According to Bahamas's answer to the questionnaire, there is no legislation nor regulation that provide for any economic substance requirements applicable to companies.

Registered entities (companies and partnerships): 241,570, including 73,738 active entities.

Employees: 188,360 (13,120 in financing, insurance, real estate and other business services)

Population: 0,4 million

GDP: $9,2 billion

- Assessment :

The majority of the members of the Panel would propose a tick ("V" - harmful) for criterion 3. Indeed, conditions attached to the advantages at stake (e.g. requirements for incorporation or operations) do not include any express requirement for real economic activity or substantial economic presence. This alone justifies a conclusion on the lack of substance.

From this it follows that it is highly questionable whether there is an adequate de facto link between profits and underlying substance.

A minority of the Panel provided the following assessment:

The agreed terms of reference for the assessment of jurisdictions under Criterion 2.2 states the following:

A jurisdiction can only be deemed to have failed the assessment under this criterion when 'offshore structures and arrangements attracting profits which do not reflect real economic activity in the jurisdiction' are due to rules or practices, including outside the taxation area, which a jurisdiction can reasonably be asked to amend, or are due to a lack of those rules and requirements needed to be compliant with this test that a jurisdiction can reasonably be asked to introduce.

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The introduction of a CIT system or a positive CIT rate is not amongst the actions that a third country jurisdiction can be asked to take in order to be in line with the requirements under this test, since the absence of a corporate tax base or a zero or almost zero level tax rate cannot by itself be deemed as criterion for evaluating a jurisdiction as non-compliant.

- *This states that a jurisdiction can only be deemed to have failed the assessment under Criterion 2.2 where reasonable/proportionate actions have been identified that a jurisdiction could take to avoid being listed.*

- *It remains unclear what exactly we would be asking jurisdictions to amend/introduce in response to their deemed failure under Criterion 3. It might be suggested that a jurisdiction should have a de jure requirement for substance as part of their company law, but it's not clear what that would entail i.e. what the test of substance would be, when that test of substance would be applied, what the implication would be of a company failing that test.*

- *Those are important questions in being able to test the reasonableness of such a requirement.*

- *If we can't demonstrate that such requirements are reasonable, and we can't demonstrate that they are commonly replicated by other countries/Member States, then the failing of a jurisdiction due to the lack of such a requirement would amount to a failing of a jurisdiction on the basis of it not having a CIT regime which is incompatible with the terms of reference. This part of Panel III would therefore propose a question mark ("?") for Criterion 3 until this has been discussed further.*

Criterion 4:

"whether the rules for profit determination in respect of activities within a multinational group of companies departs from internationally accepted principles, notably the rules agreed upon within the OECD"

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Relevant questions (Q 2.9, Q 2.10, Q 2.11, Q 2.12)

BAHAMAS does not apply neither OECD transfer pricing rules nor alternative transfer pricing rules for profit determination in line with internationally accepted principles. This situation seems to negatively affect a proper allocation of profits. It should be noted that such rules would be relevant for domestic purposes in Bahamas, because the business license tax is based on turnover and profitability.

Moreover, BAHAMAS does not apply any transfer pricing documentation, including CBCR, to resident companies. However, the panel is not sure, whether it is adequate to ask countries without a CIT-system to set rules for profit determination in respect of activities within a MNE in place or if the commitment to CbCR, which gives relevant information to the other states, should be enough to fulfil criterion 4. In light of the above we would propose a "?" for criterion 4.

Criterion 5:

"whether the features of the tax system lack transparency, including where legal provisions are relaxed at administrative level in a non-transparent way"

Relevant questions (Q 2.13, Q 2.14, Q 2.15, Q 2.16)

All the elements of the legal system which are relevant for benefiting from the advantages at stake (including rules for the granting of tax residence or the setting up of companies) are clearly set by the law and the practice does not involve any administrative discretion.

We would therefore propose a cross ("X" – not harmful) for criterion 5.

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