

# **SAINT LUCIA ECONOMIC SUBSTANCE GUIDELINES**



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# 1 Abbreviations

**BEPS**-Base Erosion Profit Shifting

**CA**-Competent Authority

**CARICOM**- Caribbean Community

**CIGA**-Core Income Generating Activities

**CoCG**-Code of Conduct Group

**DTA**-Double Taxation Agreement

**ESA**-Economic Substance Act No. 33 of 2019 and Economic Substance (Amendment) Act # 15 of 2020

**EU**-European Union

**FHTP**-Forum on Harmful Tax Practices

**FSI**-Foreign Source Income

**IP**-Intellectual Property

**ITA**-Income Tax Act Cap 15.02

**OECD**-Organization for Economic Cooperation and Development

## 2 Introduction and Purpose

1. The Economic Substance Act No. 33 of 2019 (ESA) was introduced on December 23<sup>rd</sup> 2019 and amended on December 30<sup>th</sup> 2020, to ensure that Saint Lucia meets the substantial activity requirements prescribed by the Organization of Economic Cooperation and Development-Forum on Harmful Tax Practices (OECD- FHTP) and the European Union (EU) Code of Conduct Group (CoCG) (Business Taxation). These organizations seek to reduce the occurrence of base erosion profit shifting<sup>1</sup> (BEPS) by requiring that taxes within jurisdictions be aligned with value creation.
2. Section 11 of the ESA requires that relevant entities i) have adequate operating expenses, physical presence (premises) and employees commensurate with revenue generated; ii) are directed and managed in Saint Lucia and iii) engage in core income generating activities (CIGA) in Saint Lucia.
3. In accordance with section 14 of the ESA all relevant entities must meet prescribed economic substance requirements in order to qualify for the exemption on foreign source income<sup>2</sup>. The exemption on foreign source income was introduced in 2018 through an amendment of the Income Tax Act, Cap.15.02 (ITA) and applies to corporate income earned outside of Saint Lucia. The island's move to a territorial tax system inadvertently means that the corporate tax system does not entirely fit into the categories recognized by the OECD-FHTP or the EU<sup>3</sup>. Notwithstanding, the guidelines rely heavily on the standards set by the OECD, in particular the Base Erosion Profit Shifting Action 5 Reports (2015 and 2017), to prescribe best practice principles. The reports can be accessed at <https://www.oecd.org/tax/countering-harmful-tax-practices-more-effectively-taking-into-account-transparency-and-substance-action-5-2015-final-report-9789264241190-en.htm> and <https://www.oecd.org/tax/beps/harmful-tax-practices-2017-progress-report-on-preferential-regimes-9789264283954-en.htm> respectively.
4. The guidelines will be updated annually, or as the need arises, to meet revised standards or to clarify concepts. It should also be noted that these guidelines are principle- based and do not cover all possible eventualities.

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<sup>1</sup> Base Erosion Profit Shifting occurs where multinational enterprises exploit gaps and mismatches in tax regimes between jurisdictions.

<sup>2</sup> Income accruing from a source outside Saint Lucia.

<sup>3</sup> Jurisdictions with corporate tax or no and nominal tax jurisdictions (OECD-FHTP); or 2.1 and 2.2 jurisdictions (EU) respectively.

5. This document must be used in conjunction with the Economic Substance Act # 33 of 2019; the Economic Substance (Amendment) Act #15 of 2020, the Income Tax Act, Cap.15.02 and any other information provided by the Competent Authority (CA) of Saint Lucia.
6. In accordance with section 24 of the ESA, the Competent Authority may issue and revise guidelines under the ESA.

### 3 Scope

7. Any entity that carries out activities or functions whether wholly or in part, in any of the relevant sectors listed in section 3.1 of these guidelines (Schedule 1 of the ESA) is a relevant entity. Relevant entities are subject to the ESA unless they fall into section 3, the non-application section of the ESA, as provided in 3.2 of these guidelines. Please note that the generation of income will not be used to determine whether an entity is subject to the ESA. The determining factor is whether the entity operates or carries on business (in other words performs functions) in any of the relevant sectors listed. For example, the main function of a holding company is therefore to hold an asset(s). An entity performing this function will be required to have economic substance, whether or not it has operations (like rental) and whether or not income is earned, and irrespective of the jurisdiction within which the asset is held.
8. The definition of relevant entity, as presented in section 2 of the ESA, includes: any company incorporated whether inside or outside of Saint Lucia but registered in Saint Lucia; any limited liability partnership registered in Saint Lucia and any international trust in Saint Lucia.

### 3.1 Relevant Sectors

9. In accordance with Schedule 1 of the ESA, companies operating or carrying on business (functioning whether in whole or in part) in the following sectors, which are not excluded with respect to the non-application section, are relevant entities:
  1. Banking Business.
  2. Insurance Business.
  3. Shipping.
  4. International mutual funds business.
  5. Financing and leasing.
  6. Headquartering.
  7. Activities of a company holding tangible assets.
  8. Activities of a company holding intangible assets.
  9. Activities of a pure equity holding company.
  10. Distribution and service centre business.
  11. A combination of business or activity carried on between paragraphs 1 to 10.
10. In addition to the above, and in accordance with section 9 of the ESA, please note that the Competent Authority may by publication in the *Gazette*, declare an entity to be a relevant entity.

### 3.2 Non-Application

11. Section 3 of the ESA does not currently apply to international business companies, international partnerships or international trusts created before the 1<sup>st</sup> day of January 2019. **It should be noted however that the entities created prior to this date will fall under the scope of the ESA from the 1<sup>st</sup> day of July 2021.**
12. The ESA does not apply to domestic companies. A domestic company, as defined in section 2 of the ESA, operates in Saint Lucia and provides goods and services solely for Saint Lucia, and is not part of a multinational enterprise group.
13. Section 2 of the ESA also defines a multinational enterprise group as a group of associated companies with business in two or more jurisdictions. This means that once a group of associated companies operates in Saint Lucia and within another jurisdiction, irrespective of where the other jurisdiction is located, the entity is part of a multinational group enterprise.

### 3.3 Examples of application of ESA:

#### 14. Example 1

Institution Y is incorporated in Saint Lucia and only provides banking services to the domestic market. Institution Y does not operate in any other Caribbean island or elsewhere in the world. Institution Y is therefore not subject to the ESA (domestic entity).

#### 15. Example 2

Institution Z is incorporated in Saint Lucia and provides banking services to the domestic market and also operates in a neighbouring island. Since Z operates in more than one jurisdiction, the entity is subject to the ESA.

#### 16. Example 3

Company A is incorporated in Saint Lucia and is a multinational group enterprise involved in distribution. Company A purchases raw materials or finished products for resale to other group members. Company A is therefore a distribution and service centre business, as defined in section 2 of the ESA.

*If however no intragroup resale or provision of services occurs then the entity will not fall into the definition of a distribution and service centre business. See section 6.5.*

#### 17. Example 4

Company X is a multinational enterprise with headquarters in Saint Lucia. All senior managers are resident outside of Saint Lucia while some board members reside in Saint Lucia. The Board meets in Saint Lucia annually to make decisions. Company X is subject to the ESA.

*18. An issue may arise as Company X will have to show how decisions are made given that the management team is outside of Saint Lucia. Bear in mind that CIGA may be outsourced but must be performed in Saint Lucia. The onus will be on the company to show how the resident Board members are suitably qualified to carry out the CIGA associated with revenue generation, and that they are indeed carrying out those tasks.*



#### 19. Example 5

Company Q 's sole purpose is to hold art for a wealthy European businessman. No income is earned. The company is a holding company and is therefore subject to the ESA. The company does not qualify for reduced economic substance requirements as it does not hold equity participations. The CA will however take into consideration the fact that the entity is passively holding the asset. In general, the level and type of income, if earned, and the nature of a business will be used to make a determination. Please see 6.3.

20. Section 10 of the ESA also permits the Competent Authority to exclude, by publication in the Gazette, relevant entities wholly owned by the Government.

## 4 Interpretation of “Adequate”

21. For the purposes of the ESA, the ordinary dictionary meaning of the word adequate, as provided in the Oxford Dictionary of English, that is “*satisfactory or acceptable in quality and quantity*” will be used for interpretation. What is adequate for each relevant entity will depend on the nuances of that entity and directors and managers should, in good faith, make arrangements to suit. It is therefore envisaged that every entity will use good business sense and judgement in order to determine the minimum standards necessary for efficient operation, please see Table 1, on page 11.
22. At present, the best practice guidance for the interpretation of the word adequate is the OECD standard. Said standard does not currently prescribe specific figures, calculations, or ratios to further define the term. The CA will therefore follow best practice principle and will not venture to define the term at this point in time.
23. Pursuant to section 15 of the ESA, the CA may issue notice to a relevant entity to comply with economic substance requirements.
24. The CA will continue to monitor directives issued by the OECD in relation to the definition and interpretation of ‘adequate’, as it pertains to economic substance, and will make the necessary updates to this document as time progresses.
25. Pursuant to section 11 (9), each relevant entity must ensure that records, which demonstrate the adequacy of the arrangements, are kept, and maintained for a period of up to six (6) years after the end of each year of income.

#### 4.1 Adequate physical presence:

26. All relevant entities are expected to have a physical presence in Saint Lucia. Where premises are shared, it will be necessary for a relevant entity to show that the space allocated for business is adequate for its operation.
27. The premises whether leased, rented, or owned, in Saint Lucia must be adequate for the effective management of the relevant entity.
28. Over time, comparative data will be gathered to further assist in determining the adequacy of physical presence.

#### 4.2 Adequate expenditure proportionate to the level of activity

29. It is necessary in every instance for a relevant entity to show that it has incurred adequate expenses commensurate with the CIGA being conducted in Saint Lucia.
30. Over time, comparative data will be gathered to further assist in determining the adequacy of expenditure.

Table 1 Adequacy

Adequate in the case of:	Means
Physical assets	Appropriate place of business, plant, property and equipment whether leased, owned or rented, in Saint Lucia
Employees	Suitably qualified whether full time or part time. Hours of work must be monitored and readily available if individuals work for more than one unrelated entity. Individuals cannot simultaneously perform tasks for different relevant entities.
Directors/Management	Have necessary knowledge and expertise and must be able to make critical decisions.
Operating Expenses of an Intellectual Property (IP)	Level of operating expenses must be commensurate with income generated by the entity.

## 5 Core Income Generating Activities

31. In accordance with section 12 of the ESA, each relevant entity **must engage** in the CIGA associated with its relevant sector, as shown in Table 4 in the Appendix. CIGA are the critical activities that generate the income of an entity. One or more of the activities listed must be performed in Saint Lucia in order for the relevant entity to meet the economic substance requirement. Where there is a combination of relevant sector activities, the relevant entity must show evidence of economic substance in relation to each activity.
32. For the purposes of the ESA, CIGA may be outsourced; however, relevant entities must be able to demonstrate adequate supervision of the activities that must be conducted in Saint Lucia.
33. Where the CIGA involves making relevant decisions, a quorum of directors with the necessary knowledge and expertise must make the decisions in Saint Lucia. Meetings of the board must be conducted in Saint Lucia at a frequency appropriate for effective decision making. Again,

- the CA is relying on the best practice provided by the OECD. At present, the frequency of meetings has not been prescribed by the body.
34. It is not necessary for a relevant entity to perform every CIGA listed in the legislation in relation to its relevant sector

## 6 Elements of Economic Substance

35. In order to satisfy the economic substance requirements stipulated in section 11 of the ESA, a relevant entity must meet the following criteria **annually**:
1. Be directed and managed in Saint Lucia;
  2. Have an adequate number of qualified employees; whether employed directly or by third parties and whether employed full time or part time;
  3. Have an adequate physical presence;
  4. Have adequate operating expenditure proportionate to the level of activity in Saint Lucia; and
  5. Conduct core-income generating activities in accordance with section 12 of the ESA, please see Table 4 in the Appendix.
36. Notwithstanding the above, the requirements of economic substance are reduced for pure equity holding companies. In addition, intellectual property companies must utilise the nexus calculation, in schedule 2, to determine the amount of income which will qualify for the foreign source income exemption. Conversely, it is presumed that high-risk intellectual property companies do not have economic substance and that such entities must provide additional information and undergo further scrutiny and stricter review to rebut this. (Please see 6.1.5)

## 6.1 Holding Intangible Assets

### 6.1.1 Intellectual Property Assets

37. Section 2 of the ESA provides the following definition:

“intellectual property asset” means –

- (a) a patent;
- (b) technical know-how;
- (c) an industrial design;
- (d) copyrighted software;
- (e) other similar assets which are functionally equivalent to patents and;
- (f) assets that are non-obvious, useful or novel;

where said assets are legally protected and subject to approval and registration processes.

38. Given the list above, trademarks and other similar forms of IP; that is IP related to marketing and branding activities, are not eligible for the foreign source income exemption. IP entities holding such assets will therefore be taxed at the corporate tax rate under the Income Tax Act, Cap.15.02. In accordance with section 2 of the ESA, holding intangible assets such as trademarks and similar assets relevant to marketing and branding do not form part of a relevant sector.

39. Notwithstanding the above, the provisions of Articles 6, 7, 8, 11, 12, 13 and 14 of the CARICOM Double Taxation Agreement, Cap.19.05 take precedence and will be applied to income accruing from a source within CARICOM.

## 6.1.2 Nexus Approach

40. Saint Lucia introduced a territorial tax regime in December 2018. This regime does not fit entirely into the standards set for no and nominal tax jurisdictions and jurisdictions with corporation tax requirements as they relate to economic substance. As such, a mixed approach, particularly with respect to companies holding intangible assets was required. Hence the utilization of the nexus approach.

41. Pursuant to section 11 of the ESA, an intellectual property company must establish a relationship between the expenditure and income of IP assets. To determine the amount of IP income which can benefit from the exemption on foreign source income, an entity needs to apply the formula below. In addition, the entity must receive no more than 50 million Euros (or XCD equivalent) globally and 7.5 million Euros (or XCD equivalent) locally, in turnover using a five (5) year average.

## 6.1.3 The Nexus ratio

42. The formula and criteria required to apply this ratio are presented in section 11 and schedule 2 of the ESA. These are elaborated upon below:







$$\frac{\text{Qualifying expenditures incurred to develop IP asset}}{\text{Overall expenditures incurred to develop IP asset}} \times \text{Overall income from the IP asset} = \text{Income receiving tax benefit}$$

43. *Qualifying taxpayers* include i) resident companies ii) domestic permanent establishments of foreign companies and iii) foreign permanent establishments of resident companies which are taxable in Saint Lucia. (The permanent establishment must be in operation when the income is earned for the income earned by the head office to qualify.)

44. *Qualifying expenditure* must be incurred by a qualifying taxpayer and must be directly connected to the IP asset. Qualifying expenditure includes salaries, wages, direct costs, overhead costs associated with research and development, cost of supplies used to advance knowledge and overcome obstacles related to technology.

46. Interest payments, building costs, acquisition costs and other costs which cannot be directly linked to research and development do not qualify.
47. Qualifying expenditures should be used in the calculation in the year they are incurred irrespective of the accounting treatment used in tax calculations.
48. *Uplift* allows entities to include the costs of acquiring IP assets and or outsourcing research and development. A 30% uplift may be applied to qualifying expenditures, provided that the new amount does not exceed overall expenditure. The maximum amount admissible is therefore 100%.
49. *Overall expenditures* are the sum of qualifying and non-qualifying expenditure. Expenditure on failed research and development is not typically included in the nexus calculation. Shared research and development costs however, can be apportioned on a pro rata basis.
50. *Overall income* is limited to IP income and should be calculated using the formula; overall income = gross IP income minus IP income allocable to IP income. (IP income includes royalties, capital gains and income from the sale of IP assets.)
51. The qualifying taxpayer should undertake most of the research and development activities. Tasks may however be outsourced to unrelated parties.
52. Only the expenditure incurred for improving acquired IP is allowed. If IP is acquired from related parties then, additional transfer pricing documentation is required.

#### 6.1.3.1 *Required documentation*

53. The following documentation is required for IP entities operating in Saint Lucia:
  -  Information on how the IP assets are being tracked
  -  The IP business model
  -  Information on the qualifying IP asset
  -  Deductions made in calculations
  -  Link between IP asset and research and development
  -  Information tracking expenditure

#### 6.1.4 Rebuttable Presumption

54. In accordance with section 11(8) of the ESA, a high risk intellectual property company will be given the opportunity to prove that more income should be permitted to benefit from the IP regime, if they have undertaken substantial qualifying research and development costs.
55. As part of the rebuttal, entities would need to demonstrate economic substance by providing additional information including, but not limited to:
- Detailed business plans, which demonstrate the commercial rationale for holding the IP assets in Saint Lucia.
  - Employee information, including level of experience, type of contracts, qualifications, and duration of employment; and
  - Evidence that decision-making is taking place within Saint Lucia as opposed to the periodic decisions of non-resident board members.

#### 6.1.5 High Risk Intellectual Property Companies

56. A high risk intellectual property company is defined in section 2 of the ESA as one which:
- a. Owns intellectual property (IP) assets which i) have been acquired from related parties or are funded by research and development which takes place outside of Saint Lucia and ii) are licensed to related parties or generate income as a consequence of activities which are performed by foreign related parties.

**Or**

- b. Owns IP assets but does not carry out research and development CIGA in Saint Lucia.
57. Income derived from such intellectual property assets can pose a high risk for the artificial shifting of profits. The mitigation of this high risk is evidenced by the presumption of non-compliance with the economic substance requirements. Notwithstanding, this presumption is rebuttable in order to prevent attempts to reduce risk from inadvertently prohibiting activities that constitute real economic activity.
58. In accordance with section 11(8) a relevant entity would need to provide evidence that the income generated is directly linked to activities undertaken in Saint Lucia as opposed to in a foreign jurisdiction, in order to rebut the presumption.



59. In this regard, entities need to provide current and historic evidence that shows that there is a high degree of control over the development, exploitation, maintenance, enhancement and protection of the intangible asset in Saint Lucia. There should also be evidence that this is overseen by an adequate number of full-time employees with the necessary qualifications to carry out the required tasks. These employees must reside in Saint Lucia permanently and must perform their key business-related activities in Saint Lucia.

## 6.2 Pure Equity Holding Companies

60. Pure equity holding companies are defined as those which hold only equity participations<sup>4</sup> and earn only dividends and capital gains. Pure equity holding companies are subject to reduced economic substance requirements and are merely expected to:

- a. Comply with applicable filing requirements under the Companies Act, Cap.13.01, the Income Tax Act, Cap.15.02 and the International Business Companies Act, Cap.12.14.
- b. Show evidence of adequate human resource capacity for holding and managing the interests and shares of the entity in Saint Lucia.

61. Income which is incidental to holding pure equity assets (for example, interest earned from depositing dividends in a bank) will not change the nature of this type of entity to the extent that this is not actively managed by the entity to earn income. In the event that the entity is actively investing and calculating risks associated with the assets; such an entity cannot be deemed a pure equity holding company. In such cases the entity holding the asset may then be deemed a headquarter company.

62. It is critical that relevant entities provide a complete list of their CIGA; so that they can be categorized appropriately.

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<sup>4</sup> Equity participations are interest in a firm in the form of equities. <https://stats.oecd.org/glossary/>

### 6.3 Holding tangible assets (house, art, land)

63. A company which holds assets, whether passively or actively, **other than equity participations is not a pure equity holding company**, and as such said entity does not automatically qualify for reduced economic substance requirements. Such entities will need to show proof that they have engaged in core activities associated with the type of income generated.
64. **If the asset is being passively held and earns no income however, then the CA will not expect that CIGA, staff or premises will be required for holding this asset (except for the office of its Registered Agent and the functions carried out by this agent to manage the asset).** Monitoring will however be required. To this end, the economic substance filing for this entity will include financial information (expenses, value of assets) and a list of the assets and their location.
65. If an entity passively holds a portfolio (including bonds) and earns interest as well as dividends but does not actively trade, then the CA will also take this into consideration when determining the physical premises and employees required to merely hold said assets. If active trading and calculation of risk occurs, then the entity is not merely holding the asset. The CIGA performed by each entity will therefore be considered to determine the economic substance required.
66. Please bear in mind that entities can operate in one or more relevant sector.
67. Example 1

Holding company EFG is incorporated in Saint Lucia and holds a house in island B for non-residents. The house is a **family property and earns no income**. EFG is subject to the ESA as it operates in a relevant sector, however since the entity is not earning income it is not an immediate BEPS concern. EFG will be required to provide the CA with financials (expenses, value of assets) and details of the assets held including their value but will not be required to have CIGA or provide information on staff and premises required to manage the assets; beyond the resources of the Registered Agent/Trustee.

In the event that EFG begins to earn income from this asset, the entity will need to provide additional information, consistent with the economic substance requirements in section 12 of the ESA, to the Competent Authority in terms of staff, CIGA and premises.

68. Example 2

Boat and Art Co. is a Saint Lucian international business company holding a boat and artwork for an individual who lives in country Z. The company earns no income as it is passively holding the asset. The entity will not be required to have economic substance in terms of CIGA, staff and premises but will file information regarding the assets held and financials. If the assets of the company are rented then additional economic substance requirements, consistent with section 12 of the ESA, will be imposed.

69. Notwithstanding, companies holding tangible assets are subject to the provisions of Article 6 the CARICOM Double Taxation Agreement, Cap.19.05, if said assets are located in a CARICOM member state.

### 6.3.1 Personal Portfolio Holding Companies

70. A personal portfolio holding company, is a holding company set up to hold assets for individuals. These assets may be tangible or intangible.

71. Personal portfolio holding companies hold a variety of assets for private individuals. If these entities hold only equity participations in more than one company and hold no other type of financial instrument, they are deemed to be pure equity holding companies. However, if said entities hold more than equity participations, then they do not fall into the category of pure equity holding companies and would need to meet the economic substance requirements of holding companies. These entities will be required to show the CIGA which lead to the generation of the income earned.

72. Example 1

Entity D is a personal portfolio holding company which holds assets for a businessman. The portfolio is diversified and includes stocks and bonds. Entity D actively trades and invests assets on behalf of the businessman. Entity D will be required to show the core activities associated with the type of income earned.

## 6.4 Fund Management (International mutual fund business)

73. Section 2 of the International Mutual Fund Management Act, Cap. 12.16 defines an international mutual fund business as engaging in the business of establishing and operating or attempting to establish or operate mutual funds in Saint Lucia. An international fund manager is a person who holds a valid international public mutual fund manager licence; whose services include i) the management of the International mutual fund business and ii) the provision of investment advice to the mutual fund.
74. Please note that only international mutual fund managers, as defined by the International Mutual fund Act, Cap.12.16, currently fall into the scope of the ESA. The CA however envisages that a broader and more appropriate definition will be released shortly.
75. The taxation of the fund manager in non-IP regimes is the focus of the OECD. As such, neither the investment fund nor the investors in the fund come into question. International mutual fund managers incorporated in Saint Lucia must therefore have a staff complement and premises to conduct their duties. Please note that international mutual fund managers do not outsource their CIGA. They actively engage in buying and selling assets and calculating the risks associated with these decisions.
76. Example 1
- If there is a standing order instruction given to indicate that interest should be deposited in Bank A once received and there is no further decision making in this regard, then this is different to the entity seeking and making investment decisions. The treatment of the entity will therefore be determined on a case-by-case basis.
77. Example 2
- Investments Inc. is an international public mutual fund registered in Saint Lucia which currently has 10 million USD in assets under management. The international mutual fund manager and international mutual fund administrator are also Saint Lucian based IBC's. Portfolio management / custodian and sub administration services are outsourced to entities outside of Saint Lucia.

78. For the international mutual fund manager to have economic substance, the entity will have to conduct the CIGA in Saint Lucia. If the international mutual fund manager in Saint Lucia does not take strategic decisions in relation to the fund or does not actively make any investment decisions, but outsources these services to an overseas fund manager, then the international mutual fund manager in Saint Lucia does not meet the economic substance requirements.

79. Please note that relevant entities need not perform all the CIGA in the Appendix. However, the CIGA critical to the generation of income must be performed in Saint Lucia and the income earned must be associated with the type of activities the relevant entity engages in.

## 6.5 Distribution and Service Centre Business

80. Distribution and service centre business is defined in section 2 of the ESA. These businesses exist to re-sell goods or provide services to group members. This is therefore their main activity. It is however recognized that group entities, which exist to provide services to third parties, may from time to time provide service to other group members at cost or less. Such activities would not fall into the scope of the ESA.

### 81. Example 1

Company C is a multinational company which consists of a Computer Retail Company D, located in jurisdiction K and a Call Centre Company O which is located in Saint Lucia. The Call Centre only provides services to Company D and deals with all customer service issues and queries. These services are provided at cost or less. Company O is a distribution centre and is therefore subject to the ESA.

### 82. Example 2

Company R is the service company for a telecommunications company incorporated in Saint Lucia. Company R's main activity is to provide IT support services to customers throughout the Caribbean region. Company R employs its own staff and owns the premises used for the business. Another group company based in Saint Lucia enlists the IT services of Company R for a period of 3 months, agreeing to reimburse costs. Company R is not in the business of providing those services to other group companies, nor does it offer/solicit such services or maintain employees to provide such services. Company R is therefore not a distribution and

service centre business and is therefore not a relevant entity. Company R is not subject to the ESA.

## 6.6 Directed and Managed in Saint Lucia:

83. The ESA requires that:

- a. An entity's directors have the necessary knowledge and expertise to discharge the duties of the board of directors in relation to the relevant sector;
- b. The meetings of the board of directors are conducted with a quorum in<sup>5</sup> Saint Lucia at a frequency that is appropriate to the decision-making required for the relevant sector.

84. In the case of **board meetings impacted by the COVID-19 pandemic**, the number of meetings '*appropriate to the decision-making required by the relevant sector*', will be examined on a case by case basis (each relevant entity affected). In this regard, each relevant entity is required to i) keep records of the adjustments to its operating practices and ii) provide sufficient evidence of the specific circumstances that have hindered compliance. Please note that where necessary, this information will be exchanged spontaneously, with relevant jurisdictions, in accordance with Article 7 of the Multilateral Convention on Mutual Administrative Assistance in Tax Matters [https://read.oecd-ilibrary.org/taxation/the-multilateral-convention-on-mutual-administrative-assistance-in-tax-matters\\_9789264115606-en#page1](https://read.oecd-ilibrary.org/taxation/the-multilateral-convention-on-mutual-administrative-assistance-in-tax-matters_9789264115606-en#page1).

## 6.7 Employees

85. A relevant entity must employ persons commensurate with the nature and size of its operation. Relevant entities will need to determine the adequate number of staff required for business success and make adjustments where necessary. Said entities will determine the adequate number of employees. An entity would be allowed to count working directors as employees however; double counting will not be permitted. This means that a director or any other person cannot be counted twice for companies which may be interrelated.

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<sup>5</sup> Covid-19 has affected the normal course of business and there has been an adjustment in how business functions are conducted. The impact of this pandemic will be given consideration on the conduct of business and business operations.

## 6.8 Core-income generating activities (CIGA)

86. CIGA must be conducted in Saint Lucia to meet economic substance requirements. To this end it is important that all letter box or shelf companies are eliminated in Saint Lucia. A list of the CIGA associated with each relevant sector is presented in the Appendix.

## 6.9 A Relevant Entity with minimum or no income

87. Any relevant entity that operates with low or no income will be required to have economic substance. Income levels will not be used to determine the need to comply with the ESA. Notwithstanding, a relevant entity that is not yet in operation will not have to meet the economic substance requirements, but will be required to provide documentation as requested by the CA.
88. The CA will determine the level of information and documents required for entities which are not yet in operation or which have no income, on a case-by-case basis.
89. In future, however, it is the desire of the CA to establish a minimum level criterion. This of course will be done based on the guidelines of the OECD and EU.

## 7 Outsourcing

90. Outsourcing includes the contracting or delegating of functions/roles to third parties or to entities within a group. It is evident that entities may outsource at least part of their operations; and this is certainly not cause for concern. Outsourcing must however not be done in a manner that will pose a risk to the economic substance requirements. Although a relevant entity may outsource any of its functions, this must be done with careful consideration of its CIGA and non-CIGA. CIGA being critical functions that generate income for the relevant entity.
91. Pursuant to section 11 (5) CIGA may only be outsourced to entities located in Saint Lucia and the contracting/delegating entity must be able to show adequate supervision (monitoring and control) of these functions, in order to meet economic substance requirements. Back-office activities, which are not of central importance to the generation of revenue, such as IT, payroll, and expert specialist services may be procured from entities outside of Saint Lucia; as they are not CIGA.

92. Where CIGA are outsourced in Saint Lucia, the resources of the service provider will be taken into consideration (employees, physical assets) when determining whether the economic substance requirements have been met. Tasks must be verified to ensure that only the portion of time equivalent to full time employment directly used in the service of the company is counted. Time sheets and time logs are therefore critical documents that need to be carefully maintained in this regard.
93. Double counting is not allowed. For example, if an employee of a service provider spends an hour performing the CIGA for a relevant entity A, then this employee cannot spend the same hour performing CIGA for a different relevant entity B. In addition, the staff of service providers should not simultaneously carry out CIGA for multiple relevant entities (such as combined board meetings). Tasks should therefore be specific to each relevant entity so that there is no double counting of any specific task.
94. Notwithstanding the above, the relevant entity remains responsible for ensuring that accurate information is reported on its return and this will include precise details of the resources employed by its service providers, for example based on the use of timesheets. Relevant entities engaged in banking business, insurance business and international mutual funds business will be subject to the industry specific guidance in addition to the principles set in the ESA.
95. Relevant entities must not use outsourcing to circumvent economic substance requirements. Where there are corporate directors, these roles will be closely scrutinized to determine whether these individuals actually perform the duties of a director.

## 8 Economic Substance Return

96. An economic substance return must be submitted three months after the year of income of all relevant entities. However, entities will be given a year to file their first returns. As such, all entities formed after December 31<sup>st</sup>, 2018 will commence filing in 2021 while grandfathered entities will commence in 2022.
97. This grace period, provided in section 13 of the ESA, does not mean that the entities are not required to have economic substance. It should however be deemed as a time for preparation. The CA will continue to gather required economic substance information regarding entities



during the grace period to meet the requirements of the OECD. Monitoring may also occur during this period based on information already provided to the Competent Authority.

98. The return is to be submitted electronically. A relevant entity is to submit a report on all activities carried out in relevant sectors on the return. The elements of the economic substance return are provided in Table 2 below.

*Table 2 Elements of Economic Substance Return*

- ✓ The address and location of its registered office and place of operation, whether leased, rented or owned, in and outside of Saint Lucia.
- ✓ The name and jurisdiction of residence of the beneficial owners.
- ✓ The number of full-time employees or other personnel with appropriate qualifications, including contracted third parties, who are in Saint Lucia. (Double counting is not permitted)
- ✓ The amount and type of income earned by the relevant entity in respect of each relevant sector
- ✓ The amount and type of expenses incurred and assets held by the relevant entity in respect of each relevant sector
- ✓ A detailed description of its core-income generating activities undertaken in Saint Lucia, whether or not they have been outsourced.
- ✓ A statement of whether it considers that the mind and management of the relevant entity, in the relevant sector, are in Saint Lucia.

99. The CA will continue working with all entities to ensure compliance with the requirements of the ESA. The CA will also continue to monitor the implementation of the legislation to ensure its effectiveness.

## 9 Sanctions

### 9.1 Forfeiture of Foreign Source Income (FSI) Exemption

100. Pursuant to section 14 (2) of the ESA, the Competent Authority will notify the Comptroller of Inland Revenue when a relevant entity fails to qualify for the exemption on income that accrues from a source outside of Saint Lucia (foreign source income). This therefore means that failure to meet economic substance requirements will lead to taxation of foreign source income at the corporation tax rate, in the Income Tax Act, Cap.15.02.

#### 9.1.1 Foreign Source Income Exemption

101. The Income Tax (*Amendment*) Act No.12 of 2018 introduced a territorial tax system to Saint Lucia. This system exempts **resident companies** from corporate tax on foreign source income (FSI), which is any income that is earned outside of Saint Lucia. Section 8(3) of the ITA as amended now provides that:

102. *“Where a company is a resident, the assessable income of that company shall not include income accrued from a source outside Saint Lucia in accordance with section 10A.”*

103. Section 10A goes on to delineate income that is considered to be derived from a source outside of Saint Lucia or FSI, as follows:

*“(a) profits derived from —*

*(i) a permanent establishment outside Saint Lucia,*

*(ii) immovable property situated outside Saint Lucia;*

*(b) interest that is not specified under section 10(1)(c);*

*(c) income derived from investments in securities, such as, mutual funds, stocks and interest-bearing instruments, issued by a person outside Saint Lucia;*

*(d) management charges paid by a non-resident from a source outside Saint Lucia where the costs are not attributable to a permanent establishment in Saint Lucia;*

*(e) royalty payments received from a non-resident permanent establishment to a resident permanent establishment;*

*(f) a source of income which is deemed to accrue from a source outside Saint Lucia pursuant to an international agreement made under section 60.”.*

## 9.2 Other Penalties

104. Relevant entities may also be penalized as follows:

*Table 3 Penalties*

<b>Infraction</b>	<b>Section of ESA</b>	<b>Penalty</b>
<b>Failure to adhere to a notice to comply</b>	16	One thousand dollars for every month or part thereof for which the default continues
<b>Failure to adhere to a notice to comply in a subsequent year</b>	17	Disclosure of information to partner jurisdictions as applicable Notification of the Registrar who may strike off the relevant entity.
<b>Avoidance or seeking to avoid obligations under the Act</b>	19	Disclosure to a partner jurisdiction of any information related to the relevant entity.  Issue of notice of penalty that includes a penalty of fifty thousand dollars.
<b>Fraud</b>	19	Liable on summary conviction to a sum not exceeding twenty-five thousand dollars or imprisonment for a term not exceeding two (2) years or both.  Liable on conviction on indictment to a fine not exceeding one hundred thousand dollars or imprisonment for a term not exceeding seven (7) years or both.
<b>Failure to provide information</b>	7	Liable on summary conviction to a fine not exceeding ten thousand dollars or imprisonment for a term not exceeding two (2) years or both.
<b>Provision of False information</b>	7	Liable upon summary conviction to a fine not exceeding 50,000 dollars.

## 10 Secrecy

105. All persons performing official duties pursuant to the ESA must treat all information as confidential. Failure to adhere will result in a person facing a possible fine not exceeding ten thousand dollars or imprisonment for a term not exceeding two (2) years or both for disclosing information collected in or during official duties.

## 11 Exchange of Information

106. The ESA makes provision for the exchange of information in accordance with any Agreement which Saint Lucia may be signatory to. These agreements facilitate the exchange of information for tax purposes and ensure the integrity of the global tax system by reducing avoidance and tax evasion.

## 12 Bibliography

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# 13 APPENDIX

Table 4 Core Income Generating Activities by Relevant Sector (Section 12 of the ESA)

Relevant Entities	Core-income generating activities
<b>Banking Business</b>	<ul style="list-style-type: none"> <li>• Raising funds</li> <li>• Managing risk, including credit, currency and interest risk</li> <li>• Taking hedging positions</li> <li>• Providing loans, credit or other financial services or customers</li> <li>• Accepting monetary deposits, holding assets on behalf of customers and providing similar financial services</li> <li>• Managing regulatory capital</li> <li>• Preparing regulatory reports</li> </ul>
<b>Insurance Business</b>	<ul style="list-style-type: none"> <li>• Predicting and calculating risk</li> <li>• Insuring or re-insuring against risk</li> <li>• Providing client services; and</li> <li>• Preparing regulatory reports and returns</li> </ul>
<b>Shipping</b>	<ul style="list-style-type: none"> <li>• Managing crew, including hiring, paying and overseeing crew members</li> <li>• Hauling and maintaining ships</li> <li>• Overseeing and tracking deliveries</li> <li>• Determining the goods to order and when to deliver the goods.</li> <li>• Organizing and overseeing voyages</li> </ul>
<b>International Mutual Funds Business</b>	<ul style="list-style-type: none"> <li>• Taking decisions on the holding and selling of investments</li> <li>• Calculating risks and reserves</li> <li>• Taking decisions on currency or interest fluctuations and hedging positions</li> <li>• Preparing relevant regulatory or other reports for government authorities and investors</li> </ul>
<b>Distribution and Service Centre Business</b>	<ul style="list-style-type: none"> <li>• Transporting and storing goods</li> <li>• Managing stocks and processing orders</li> <li>• Providing consultation or administrative services</li> </ul>
<b>Financing and leasing</b>	<ul style="list-style-type: none"> <li>• In the case of leasing, identifying and acquiring assets to be leased.</li> <li>• Agreeing funding terms</li> <li>• Setting the terms and duration of any financing, leasing or hire-purchase agreement.</li> <li>• Monitoring and revising agreement</li> <li>• Managing risks</li> </ul>

<b>Headquartering</b>	<ul style="list-style-type: none"> <li>• Making management decisions on behalf of a foreign group entity</li> <li>• Taking decisions that are material for decision-making in a foreign group entity.</li> <li>• Incurring expenditure on behalf of a group entity</li> <li>• Co-ordinating group activities</li> </ul>
<b>Holding tangible assets</b>	<ul style="list-style-type: none"> <li>• Taking strategic decisions, managing and bearing principal risks relating to the development and subsequent exploitation of the tangible assets</li> <li>• Taking strategic decisions, managing and bearing principal risks relating to the third-party acquisition and subsequent exploitation of the tangible asset</li> <li>• Carrying on the underlying trading activities through which the tangible asset is exploited and leads to the generation of revenue third parties.</li> </ul>
<b>Holding intangible assets</b>	<ul style="list-style-type: none"> <li>• Conducting research and development without acquiring or outsourcing research and development</li> <li>• Taking strategic decisions, managing and bearing principal risks relating to the development and subsequent exploitation of the intangible asset</li> <li>• Taking strategic decisions, managing and bearing principal risks relating to the third-party acquisition and subsequent exploitation of the intangible asset</li> <li>• Carrying on the underlying trading activities through which the intangible asset is exploited and leads to the generation of revenue from third parties.</li> </ul>
<b>Pure Equity Holding</b>	<ul style="list-style-type: none"> <li>• Acquiring and holding equity participations or interest in other entities that generate only dividends and capital gains.</li> </ul>