

STATES OF JERSEY



DRAFT TAXATION (COMPANIES – ECONOMIC SUBSTANCE) (JERSEY) LAW 201- (P.132/2018): COMMENTS

**Presented to the States on 3rd December 2018
by the Economic Affairs Scrutiny Panel**

STATES GREFFE

COMMENTS

Background

[P.132/2018](#) “Draft Taxation (Companies – Economic Substance) (Jersey) Law 201-” was lodged on 25th October 2018 by the Minister for External Relations.

In 2017, the EU Code of Conduct Group (Business Taxation) conducted a screening process where the tax structures of different jurisdictions were subject to detailed analysis. At the end of 2017, EU Finance Ministers (“ECOFIN”) included a number of jurisdictions on an EU list of non-cooperative tax jurisdictions but ECOFIN Ministers identified Jersey as a cooperative tax jurisdiction¹.

As part of ongoing dialogue with the EU over this process, the EU Code of Conduct Group raised concerns that the Crown Dependencies did not have a “*legal substance requirement for entities doing business in or through the jurisdiction*”. The Code of Conduct Group was concerned that this “*increases the risk that profits registered in a jurisdiction are not commensurate with economic activities and substantial economic presence*”.² This draft Law has been drafted in response to addressing these concerns.

The Panel received a briefing on the draft Law on the 19th October 2018 from the Deputy Comptroller of Taxes, Officers from External Relations and the Financial Services Unit. The Panel’s primary concern centred around Article 16 which makes provision for persons authorised by the Comptroller of Taxes to enter business premises for the purpose of investigating compliance with any provision of the Law. As part of its follow up work the Panel posed a number of written questions, including questions on Article 16, to the Department which can be found in the **Appendix**.

The Draft Law

The draft Law intends to address concerns that companies could be used to artificially attract profits that are not proportionate with economic activities and substantial economic presence in Jersey. The draft Law will require certain companies to demonstrate they have substance in the Island by:

- **Being directed and managed in the Island** – this is to ensure that there are an adequate number of board meetings held and attended in the Island. It will also ensure that the associated minutes and records are kept in the Island and that the board is a decision-taking body with the necessary knowledge and experience³.
- **Conducting Core Income Generating Activities (CIGA) in the Island** – For each sector, the legislation provides a list of core activities a company could undertake in order to demonstrate economic substance but it is not necessary for companies to perform all of the activities listed⁴.

¹ Consultation on the introduction of substance requirements for companies tax resident Jersey, Taxes Office 2017

² [Key aspects](#) in relation to proposed economic substance requirements, as issued by Guernsey, Isle of Man and Jersey

³ Ibid

⁴ Ibid

- **Having adequate people, premises and expenditure in the Island** – This is to ensure that there are an adequate number of employees physically present in Jersey, there is adequate expenditure incurred in Jersey and that there is adequate physical assets in Jersey⁵.

During the briefing, Officers explained that implementation of the Law would follow a three step process:

1. **Step one:** Identify companies who were undertaking relevant activities.
2. **Step two:** Impose substance requirements (as identified in the draft Law).
3. **Step three:** Enforce substance requirements.

If companies fail to meet the substance requirements, financial penalties will be incurred on a progressive scale with the ultimate sanction leading to the company being taken off the Companies Register⁶.

Consultation

As part of its work on the legislation, the Government issued a [consultation](#) in August 2018 (between 6th and 31st) which sought feedback from key stakeholders on the proposals. A number of corporate groups (25), individuals (4) and industry groups (6) responded to the consultation (35 in total). The Panel notes the rather short timescale for the consultation and given the technical nature of the proposals, the Panel's view is that companies should have been given longer to respond.

The response report suggests that most companies within the scope of the substance requirements will be able to demonstrate they meet the requirements. Responses were generally supportive of the proposals, although there were some caveats and requests. In response to some of the questions, some respondents requested that quality guidance was provided and should be published as early as possible.

Following the consultation, and in order to explain how the draft Law would operate in practice, the Comptroller of Taxes issued [guidance notes](#) on 7th November 2018. It is expected that more comprehensive guidance notes will be published should the draft Law be approved by the Assembly.

The Panel notes that the Corporate Services Scrutiny Panel requested submissions in order to inform its review of the Budget 2019 and some respondents for that review commented positively on the draft Law:

John Shenton, Director, Grant Thornton

“One must applaud the efforts of the States, its civil servants and co-opted members in reaching potential agreement in relation to the challenges posed by the EU Code of Conduct Group within the short time frame laid down.

⁵ P.132/2018 – Article 5

⁶ [Key aspects](#) in relation to proposed economic substance requirements, as issued by Guernsey, Isle of Man and Jersey

Although I await for the detailed guidance to be published, the draft law is welcomed⁷”.

Alex Ohlsson, Chairman, Fiscal Strategy Group, Jersey Finance

“It is appropriate to take this opportunity to applaud Government for the significant progress made in 2018 to address the concerns raised by the EU Code of Conduct Group in December 2017⁸”.

Conclusion

Whilst the need for this draft Law is acknowledged, the Panel was concerned about the powers of entry provided to the Comptroller of Taxes in Article 16. The fact that these powers mirror those available under the Income Tax Law should not deter the Assembly from monitoring the use of such powers in the years following the Law’s adoption.

The Panel also notes that in a recent Public Hearing with the Minister for External Relations he explained that this draft Law, as presented to the States of Jersey, will become the international standard, initially for other third countries to follow and subsequently for EU Member States to also adopt.

Overall, the Panel supports the adoption of this draft Law and acknowledges the urgent timescale for its implementation. It is noted that if Jersey does not meet its commitment to address the concerns raised by the EU Code Group it is highly likely Jersey will be listed as a non-cooperative jurisdiction. The Panel may consider reviewing the Law in the future, should it be approved by the States Assembly.

⁷ Grant Thornton [submission](#), received by the Corporate Services Scrutiny Panel in relation to the Budget 2019 review

⁸ Jersey Finance [submission](#), received by the Corporate Services Scrutiny Panel in relation to the Budget 2019 review

1 – Panel questions to Department

1. **Article 6 makes provision for the Comptroller of Taxes to determine that a resident company has not met the economic substance test for a financial period of the company starting after 1st January 2019.** Please could you provide further information on this process? Does the Comptroller need to liaise with any other individuals? What are the checks and balances? Is there any consultation with others?

The draft Law provides the Comptroller authority to make a determination.

The full process is still being developed but a broad outline is as follows:

- a) All companies will provide some information through their tax return to the Taxes Office.
- b) The Taxes Office will then identify those companies of concern from both the information in returns, as well as other information in its possession.
- c) It will then contact these companies of concern and obtain much more detailed information, to be able to judge the test in the context of their specific activities (See Article 7).
- d) The Comptroller will make the determination on the facts.
- e) A company can appeal under Article 12.
- f) There are appeal rights up to the Royal Court if required.

As appropriate, the Taxes Office will seek an open dialogue with the company concerned.

In due course the Comptroller will publish guidance on the substance test under Article 5(4). Companies will be able to consult this guidance in demonstrating how they meet the economic substance test.

Note there is a duty of confidentiality owed by the Comptroller and his staff to these companies, as such there is no *vires* to consult more widely.

2. **Article 16 makes provision for persons authorised by the Comptroller to enter business premises for the purpose of investigating compliance with any provision of this Law.** Is the Comptroller able to authorise any person to enter premises? Is this normal practice or should there be a more robust description of who can enter premises? What safeguards will be put in place?

This power mirrors those available under Part 22A of the [Income Tax \(Jersey\) Law 1961](#), and similar powers are available under Schedule 8 to the [Goods and Service Tax \(Jersey\) Law 2007](#); in each case the Comptroller may specifically authorise persons, who need not be Taxes Office staff.

In practice this power to enter premises is generally effective not because it is utilised but because it exists, and it therefore encourages voluntary compliance with the Taxes Office.

In practice Taxes Office staff would likely be acting together with investigators from the JFSC, the police or other bodies, and the Comptroller would authorize all such persons entering the premises, to ensure any documents/information they obtained could be used for the purposes of this Law.

3. Has this legislation been compared to any other jurisdictions? Did the Department take any advice from other jurisdictions who already have the Law in place? If so what were the findings?

The EU Code of Conduct group set this task to a number of jurisdictions at the same time, so no jurisdiction has implemented this yet.

Jersey's Government has worked together with the other Crown Dependencies to ensure a joint approach and to ensure we benefit from the differing perspectives across our Islands.

Together with the other Crown Dependencies we have drawn on work by the OECD's Forum for Harmful Tax Practices (FHTP), which has begun to consider economic substance in the context of preferential tax regimes, and who the EU Code of Conduct Group have indicated they will follow. Importantly the FHTP has deliberated on, and specifically approved the use of the term 'adequate' in the context of substance legislation (initially in a Mauritius tax regime), which is a rejection of more prescriptive approach used in some jurisdictions.

4. The Panel understands that the Law needs to be in place by January 2019 – what are the reasons for this urgent timeline?

The timeline has been imposed by the EU Code of Conduct Group. In response to Code Group concerns on economic substance, Jersey made a political commitment to address these concerns by the end of December 2018. The (then) Chief Minister made a statement to the States Assembly in December 2017 updating States Members and providing a copy of the letter sent to the Chair of the COCG containing the commitment made by the Government of Jersey.

If Jersey does not meet its commitment, there is a high likelihood Jersey will be listed by the EU as a non-cooperative jurisdictions for tax purposes.

Statement under Standing Order 37A [Presentation of comment relating to a proposition]

The Panel wishes to apologise for submitting late comments. Due to a high volume workload in recent weeks, including review work and public hearings, the Panel met on 29th November 2018 to discuss a final draft of the Comments paper relating to P.132/2018. Furthermore, out of courtesy, the Panel wanted to give the Minister for External Relations and his team the opportunity to review the Comments before they were formally presented to the States.