THE B.V.I., CAYMAN ISLANDS, AND BERMUDA – CURRENT PRACTICE, ENFORCEMENT, AND EMERGING TRENDS

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INTRODUCTION

This article surveys selected recent developments in regulatory and tax-related law and practice in the British Virgin Islands ("B.V.I."), Cayman Islands and Bermuda that are relevant to end-clients, advisors and intermediaries.

OVERVIEW

The three leading Caribbean international financial centers – namely, Bermuda and the B.V.I. and Cayman Islands (together, the "I.F.C.'s") – are members of the Caribbean Financial Action Task Force (C.F.T.F.) and have consistently implemented O.E.C.D. initiatives and similar E.U. requirements. As such, these I.F.C.'s participate in C.F.T.F. and O.E.C.D. peer review and monitoring and continue to develop their legal systems and enforcement mechanisms to reflect international best practices.

As mentioned in the introductory remarks to this edition of *Insights*, the past decade has seen significant changes in law and regulatory enforcement across the I.F.C.'s. The implementation and periodic review timetables are largely set by the international standards setters. The pace of change does not show any signs of slowing.

The main emphasis is on information exchange and transparency. Prior to the adoption of Bermuda's domestic minimum tax from 2025 onwards on certain constituent entities in large M.N.E. groups (broadly, groups with annual consolidated revenues of €750 million or more) in response to O.E.C.D. Pillar 2, which is beyond the scope of this article, these I.F.C.'s were largely "tax neutral" and did not impose any corporate income or similar taxes on companies. This article also does not consider O.E.C.D. Country-by-Country Reporting ("C-b-C Reporting"), as that is again limited to large M.N.E. groups, which do not account for a very significant proportion of the corporate registry in the I.F.C.'s, when measured by number.

None of the regimes discussed below are taxing regimes, as such. Rather, they are concerned with information exchange and increased transparency or, in the case of the economic substance requirements, a *sui generis* compliance and reporting regime for no-tax or nominal-tax jurisdictions" ("N.T.J.'s"). The goal is to ensure a level playing field regarding tax competition, as perceived by the E.U. or O.E.C.D., in order to avoid tax results that are harmful to the interest of member states.

For the ultimate client, its advisors, and intermediaries, keeping abreast of regulatory changes is essential to ensure that entities remain compliant and prepared for regulatory inspection. Although many of the compliance regimes are not new, revisiting them is important as we are seeing or anticipating increased investigation

and enforcement action in these areas. It is not uncommon to find that entities have misunderstood their classification, or the level of compliance and reporting requirements, only to discover this when an inquiry or notice is received from the regulator.

This article surveys some common themes and key developments across the I.F.C.'s, particularly regarding

- beneficial ownership transparency initiatives,
- C.R.S./F.A.T.C.A. and the Crypto Asset Reporting Framework ("C.A.R.F."),
- economic substance requirements,
- tax information requests, and
- general trends in investigation and enforcement action in relation to these areas.

As well as current market trends and future regulatory trajectories, we will consider some key practical points to consider for advisors or other persons responsible for ensuring ongoing compliance.

This is a high-level survey rather than a detailed comparison. There are important differences between the laws of the three jurisdictions. For simplicity, this article deals in general terms, and except where otherwise stated, focuses on companies limited by shares, since that is the most popular form of corporate entity in each I.F.C. jurisdiction. Readers considering their specific obligations should seek appropriate advice from competent legal counsel.

BENEFICIAL OWNERSHIP TRANSPARENCY INITIATIVES

As readers will be familiar from similar developments in the E.U. (now under the 6th Anti-Money Laundering Directive) and U.S. (under the Corporate Transparency Act), there has been sustained focus by governments and international organizations on beneficial ownership ("B.O.") information on a global basis and what are loosely described as public beneficial ownership registers ("P.B.O.R.'s").

All three I.F.C.'s already has in place robust regulatory regimes requiring covered entities to keep records of their B.O.'s and provide information confidentially under their respective domestic anti-money laundering or B.O. reporting regimes. An example is the Beneficial Ownership Secure Search ("B.O.S.S") database in the B.V.I., which has been widely praised by regulatory officials working in financial investigation units.

Very broadly, the I.F.C.'s previously committed only to the introduction of P.B.O.R.'s once adopted as the international standard. That commitment was made in response to evolving standards and the I.F.C.'s' relationship with the U.K. In particular, it responded to a draft Order in Council published by the U.K. Secretary of State to comply with a requirement under the U.K.'s Sanctions and Anti-Money Laundering Act 2018. On November 22, 2022, the European Court of Justice issued a key

judgment declaring that public access to B.O. information in Luxembourg (and other E.U. member states) was a disproportionate interference with the rights guaranteed by the E.U. Charter of Fundamental Rights. Given that judgment and data protection concerns, it is expected that the I.F.C.'s and other U.K. Crown Dependencies will allow access to B.O. information only to competent law enforcement authorities and to those members of the public who can demonstrate a legitimate interest in the information. The I.F.C.'s have subsequently undertaken various formal and informal consultations and discussions regarding P.B.O.R.'s, including with the U.K.

At the time of writing, which was just around the time of the U.K. Overseas Territories Joint Ministerial Conference ("J.M.C.") in November 2024, this area remains in flux, particularly with regard to (i) the right of access to members of the public having a legitimate interest and (ii) the scope of appropriate protections for B.O.'s or at-risk persons. In the B.V.I., a framework regime has been introduced via amendments to the B.V.I. Business Companies Act to require companies to keep and maintain prescribed B.O. information and report it to the B.V.I. Registrar of Companies. It is expected that the detail of the regime – and any provisions dealing with P.B.O.R.'s – will be published in regulations.

Similar changes were adopted in the Cayman Islands in July 2024 via the Beneficial Ownership Transparency Act and related regulations and followed up by public consultation in October 2024. Bermuda has only recently launched a consultation process and has not yet implemented its precise framework, but responsibility for central B.O. registers will shift to the Registrar of Companies. A timeline for implementation is expected before the end of 2024. Further updates and public statements may be expected following the J.M.C.

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This is a fast-moving and technical area. It would be prudent taking advice early in 2025, after the law is settled and further guidance and regulations have been published. It is expected that there will be transitional periods for pre-existing companies and that there will be mechanisms for B.O.'s to object to or restrict access rights in circumstances where there is a disproportionate risk of harm in the event of public access.

It would be prudent to ensure that ultimate beneficial owners of relevant entities are aware of the requirements. On a global basis, authorities have begun conducting more frequent audits of B.O. data to ensure compliance and accuracy. In practice, we find that market participants are now accustomed to B.O. identification and reporting requirements, although privacy and safety concerns remain a critical issue for a limited number of B.O.'s.

ECONOMIC SUBSTANCE ("E.S.")

The B.V.I.'s E.S. requirements implementing Action 5 of the B.E.P.S. action and equivalent E.U. criteria were introduced in the author's previous article for *Insights*.[1] Similar requirements were also introduced in 2019 in Bermuda, the Cayman Islands, and the other nine N.T.J.'s.

[1] "British Virgin Islands Economic Substance Requirements," Volume 10 No 5 *Insights* p. 11.

Scope of E.S. Rules

Broadly, the E.S. laws apply to legal entities that are registered in the relevant I.F.C., including foreign registered entities, carrying on any of nine relevant activities or passively receiving relevant income or gains. Compliance is assessed over defined financial periods.

There is no requirement that such entities be tax resident, or deemed tax resident, in the relevant I.F.C. to be in scope, since none of the I.F.C.'s generally impose corporate income or other taxes on companies. However, there are exemptions from the E.S. requirements for entities qualifying as deemed nonresident. Broadly this is (i) an entity resident abroad, (ii) an entity that qualifies as tax "transparent" or (iii) an entity that is otherwise liable to corporate income tax on the relevant income, provided that the jurisdiction in which the status is claimed is not on Annex I of the E.U. list of non-cooperative jurisdiction for tax purposes.

There are broad exemptions for investment funds. The exemption does not extend to an entity engaged in fund management business, which is a relevant activity. There is also a simplified E.S. compliance requirement for pure equity holding entities ("P.E.H.E.'s"). A P.E.H.E. is an entity that only holds equity participations in other entities and only earns dividends and gains from those participations. This is a very narrow category of entity. Entities falling outside the narrow definition should consider the other eight relevant activity definitions, and whether they fall within any of them.

Requirements

Entities subject to E.S. requirements must meet the following requirements in order to be compliant:

- Direction and management must take place in the I.F.C.
- Core income generating activity ("C.I.G.A.") must be undertaken in the I.F.C.
- Adequate employees, operating expenditures and physical premises must be situated or be incurred in the I.F.C.
- Limitations on outsourcing of C.I.G.A., which importantly cannot be performed by another entity outside the I.F.C. must be followed

There is a further extremely onerous regime applicable to companies engaged in an intellectual property business. In particular, any special equipment used in the business must be physically located within the I.F.C. Certain legal presumptions of noncompliance exist, and enhanced penalties may be imposed for noncompliance where an entity fails to carry on qualifying C.I.G.A. within the I.F.C. or is a high risk intellectual property legal entity.

Effect of E.S. Rules

As a result, the I.F.C.'s have seen a discernible trend of intellectual property rights ("I.P.R.") being repatriated. In some instances, the I.P.R. has been moved to jurisdictions with a favorable regime for I.P.R. In other instances, activities that are dependent on personnel or premises outside the I.F.C. have been restructured, except

where the entity is able to claim the nonresident exemption. This trend has been amplified by international tax changes aimed at traditional I.P.R. holding structures and the digital economy.

On the other hand, the practical impact has generally been more manageable for traditional private wealth structures such as (i) personal investment companies, (ii) trust and estate planning structures, (iii) transactional special purpose vehicles used in mergers and acquisitions or capital markets work, and (iv) investment funds. There has also been a significant growth of businesses providing professional outsourcing solutions to assist with E.S. requirements, although these should be carefully tailored to each relevant activity. A one-size-fits-all approach is discouraged.

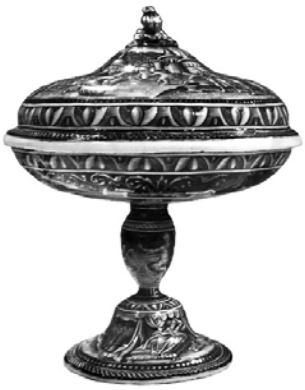
Even if entities do not carry on any relevant activity, an E.S. notification or report is required. Note, there are some important technical differences between the I.F.C.'s in the format and manner of reporting. In the early years, limited guidance existed, and inevitably, some variations existed in the interpretation of certain defined terms. That was not surprising as no precedent existed under domestic law or common law. Each I.F.C. has published and updated detailed guidance notes to assist with understanding the compliance obligations. Changes to guidance notes should be monitored. It is expected that improvements and modifications to the B.V.I.'s E.S. reporting system will take place during 2025.

We have also seen a significant increase in the number of investigations and enforcement actions by the competent authorities in each I.F.C. in relation to E.S. Typically, this may take the form of a formal information request followed by further enforcement action in cases where the authority determines non-compliance.

Path Forward

In practical terms, we recommend that entities maintain proper records and take steps to ensure they remain on top of any compliance obligations and the reporting deadlines. The impact of any proposed changes to the entity's financial position or tax status should be assessed in advance, as compliance obligations may change considerably partway through a financial period.

Individuals completing reports should ensure they fully understand the regime and the civil and criminal penalties that may arise for insufficient information or late filing. Management must understand that spontaneous information exchanges may occur with overseas tax authorities under the E.S. regime. It may be prudent to revisit historic classifications or reports if there is any uncertainty whether the position taken initially was correct or whether facts may have changed.



Penalties for breaches or regulatory enforcement may also have a knock-on impact on commercial arrangements, such as contractual representations, which may not be governed by the law of the I.F.C. To illustrate, if a company is not compliant for E.S. purposes because it is not directed and managed in the I.F.C., that information may be exchanged with tax authorities of the country where a B.O. resides. In turn, this could trigger tax issues for the B.O. in its country of residence.

Entities should also ensure that the position presented in their E.S. reporting is consistent with other data reported, such as annual returns. The B.V.I. introduced annual return requirement for most B.V.I. companies commencing with 2023 onward.

Looking ahead, the proper interaction between E.S. and Pillar 2 may present some interesting questions for multinational groups with revenues at or above the €750 million threshold. This is a topic for discussion between the standards setters. Under the current rules, any responses require analysis that is extremely fact-specific and technical. Coordination between specialist E.S. and tax advisors in each relevant jurisdiction is imperative.

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F.A.T.C.A., C.R.S. AND THE C.A.R.F.

F.A.T.C.A. and C.R.S. Reporting

All three I.F.C.'s have established frameworks to require domestic financial institutions to comply with U.S. F.A.T.C.A. and the similar O.E.C.D. C.R.S. requirements. In addition to the legislative requirements, the competent authorities in each jurisdiction have published and updated extensive domestic guidance notes that must be considered along with the Treasury Regulations under F.A.T.C.A. or the O.E.C.D. guidance and implementation handbook for C.R.S.

Again, we are seeing increased investigation and enforcement actions in relation C.R.S. and F.A.T.C.A. Local authorities have strengthened their enforcement actions and compliance checks pursuant to data audits. There is an increased focus on risk-based reviews, particularly targeting sectors with increased potential for non-compliance or shortfalls in reporting. In practice, it is the investment entity category that raised most queries, many going beyond the usual technical questions regarding financial account identification and due diligence ("D.D.") procedures.

We are seeing reporting financial institutions ("R.F.I.'s") increasingly turn to specialized compliance services providers to ensure timely and accurate reporting. Outsourcing does not allow R.F.I.'s to shift their compliance obligations or potential liability for breach, so providers should be carefully selected. R.F.I.'s are also adopting data security technologies to meet reporting requirements and ensure safe transmission of sensitive information in compliance with data protection laws. As the C.R.S. and F.A.T.C.A. regimes have now been in place for nearly a decade, and with the recent growth of artificial intelligence tools, digital technology solutions will likely be used universally. Equally, the O.E.C.D. and other global tax authorities have enhanced the quality of data sharing in order to streamline cross-jurisdictional investigation and enforcement.

The C.A.R.F.

Continuing with the theme of new technologies, the C.R.S. was updated in March 2022 to cover digital assets, such as certain cryptocurrencies and related financial products. The updates brought certain providers within the scope of C.R.S., requiring them to conduct D.D. and report on financial accounts.

As a related development, the C.A.R.F. was proposed by the O.E.C.D. in October 2022. The C.A.R.F. outlines the scope of covered crypto assets, entities, and individuals subject to reporting and data collection requirements, transaction reporting criteria, D.D. procedures and relevant tax jurisdictions for exchange of information and reporting. Much like C.R.S., the C.A.R.F. will facilitate automatic exchanges of tax-related information among tax authorities in a manner aligned with the O.E.C.D. tax information exchange standards. The C.A.R.F. will focus on decentralized crypto

assets, including stablecoins, certain non-fungible tokens, derivatives and digital representations of value that rely on a secured distributed ledger technology.

The Cayman Islands has actively joined the group of 47 jurisdictions committed to implement the C.A.R.F. by 2027. The C.A.R.F. provides for the automatic exchange of tax-relevant information on crypto-assets between tax authorities and is part of the automatic tax information exchange standards developed by the O.E.C.D. under a G-20 mandate. Bermuda and B.V.I. have shown support for the C.A.R.F. but were not among the early adopters.

It is expected that any legislative adoption would likely follow a phased approach, as was the case with C.R.S. and F.A.T.C.A. Market participants, especially in fintech, may need to seek specialized guidance and services to navigate their C.A.R.F. compliance obligations in future. The I.F.C.'s' regulatory regimes for virtual asset service providers implementing the recommendations of the Financial Action Task Force ("F.A.T.F.") are beyond the scope of this article but should be considered in parallel.

In practical terms, entities and persons operating in the crypto-assets and virtual-assets space should continue to monitor regulatory developments and ensure that they are aware of any existing obligations under C.R.S. or F.A.T.C.A.

TAX INFORMATION EXCHANGE AND INFORMATION REQUESTS BY OVERSEAS AUTHORITIES

This article has largely focused on domestic compliance and reporting obligations. However, all three I.F.C.'s participate in numerous bilateral tax information exchange agreements ("T.I.E.A.'s") and participate (via extension from the U.K.) in the O.E.C.D.'s Multilateral Convention on Mutual Administrative Assistance in Tax Matters (the "Multilateral Convention"), facilitating exchanges of tax information on request. There are nearly 150 jurisdictions participating in the Multilateral Convention.

Whereas the regimes summarized above require reporting of data that, in practice, may be of limited interest to anyone, the two on-request regimes under the Multilateral Convention or T.I.E.A.'s usually relate to in-depth investigations into the affairs of specific taxpayers and their offshore holding entities. This may occur where there is a data leak involving the I.F.C. It may also occur in situations where there is a contentious tax controversy or investigation taking place in an onshore jurisdiction.

Authorities globally are reporting an uptick in information requests under T.I.E.A.'s, especially concerning high-net-worth individuals and complex cross-border structures or transactions reported under disclosure regimes. As global regulatory and tax enforcement strengthens, this is expected to increase. The increase in cross-border investigations underscores the need to ensure that entities have robust records and are prepared for any enquiries.

In practice, entities or persons receiving an information request should ensure that they understand their legal obligations. In most cases, it will be advisable to retain a competent attorney who can advise under the attorney-client privilege. The assignment is to check that the request is valid and complies with legislative and procedural requirements and to consider any other relevant obligations, such as director responsibilities or other fiduciary duties that are subject to confidentiality obligations.

Many requirements are not set out in the E.S. legislation itself but instead apply under common law principles of procedural propriety. It is vital to consider the recipient's legal obligations. Failure to comply with those obligations, or divulging the existence or contents of a request can result in significant criminal liability. However, common law rules of fairness and due process do exist to guard against fishing expeditions and to ensure that the recipient of a request is able to determine the basis on which it has been issued and whether it is valid and in conformity with the legislative requirements.

CONCLUSION

The three leading Caribbean I.F.C.'s (B.V.I. and the Cayman Islands, and Bermuda) continue to attract international business and high-net-worth individuals due to their corporate advantages, including (i) flexible and modern company laws, (ii) efficiency of doing business, (ii) sophisticated financial services industries, (iv) robust court and other legal systems rooted in English and common law principles, and (v) generally "tax neutral" environments for cross-border inbound and outbound investment.

In line with international standards and trends, there has been a significant increase in regulatory and tax-related information exchange and transparency initiatives in the past decade or so. As domestic and overseas authorities continue to increase these requirements and exercise their investigative powers, it is important to ensure that structures remain compliant, fit-for-purpose and adequately prepared for any audits or investigations.