

# Economic Substance - Application & Requirements for Jersey Companies

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*This briefing note is designed to cover the basic principles of Economic Substance and for the requirements for a Jersey company to be caught by the provisions in various circumstances.*

## Overview

Economic Substance was introduced into Jersey law by the Taxation (Companies - Economic Substance) (Jersey) Law 2019 (the “Law”) on the 1st of January 2019. It applies to Jersey tax resident companies that carry on certain activities, which are defined under the Law as “relevant activities” in respect of financial periods commencing on or after 1 January 2019.

The Law was introduced to meet the requirements of the EU Code of Conduct Group in order to show that such companies that generate profits in Jersey are within their economic activities and presence in Jersey.

Guidance notes on economic substance were subsequently produced by the Jersey Comptroller of Taxes in order to help clarify those seeking clarification on whether the substance rules apply.

The following briefing note is designed to show the various requirements under the Law which a Jersey company can be caught by conducting a relevant activity as defined under the Law.

## Substance Requirements

The Law includes three key tests which must be met to demonstrate compliance.

1. Relevant companies must be directed and managed in Jersey, meaning:
  - Board Meetings - meetings of the board of directors must be held in Jersey at regular periods, depending on the requirement for various levels of decision making for different companies;
  - Quorum of Board Meetings - all quorums of board meetings depend on the minimum requirement of number of directors to attend a board meeting in order for the meeting to be validly held, must be physically present in Jersey, particularly when the meeting is held to consider a “core income generating activity” (i.e. authorising entry into a sale and purchase agreement);
  - Minutes of a Board Meeting - any strategic decisions made in these board meetings are to be documented by minutes made at the relevant meeting; and
  - Company Records - all company records and minutes relating to the board meetings (including any supporting documents relevant to the strategic decision-making process of that meeting) are to be retained.

Although the Law does not stipulate that all board meetings of a company need to be held in Jersey, there will be an expectation that the majority of board meetings will take place in Jersey, so that it may be evidenced that the decisions taken and the Core Income Generating Activities (CIGA) undertaken in Jersey are of a quality and quantity to clearly outweigh the question that the CIGA involving the decisions is undertaken outside of Jersey.

2. Relevant companies must be able to demonstrate adequate activity in Jersey, meaning that a company must have:

- An adequate number of employees;
- Demonstrate an adequate expenditure in Jersey; and
- Access to adequate 'physical assets' or premises in Jersey.

In the above requirement, the definition of employees (although very broad) are deemed not only to be persons who are directly employed by the company, but also persons that fall under the definition of employee under Jersey law, whether that be the owner/managers or directors.

In addition, in order for the company to demonstrate 'adequate' facilities and requirements, adequacy will be assessed by reference to its ordinary dictionary meaning being 'enough or satisfactory for a particular purpose', being purely dependant on the company's specific business activities.

Examples of adequacy for a company's general business activities might be the appropriate levels of staff with the correct qualifications for the business activities conducted, the length of time employees are required to work as required by the company's business activities, and the employees' competence and experience of the relevant work that the company conducts.

3. Relevant companies must conduct CIGA's in Jersey. If this is in the context of a company that could be considered as being a 'finance and leasing business' (as defined in the Law) then this would include:

- Agreeing funding terms under an agreement, together with setting the terms and duration of any financing or leasing of assets;
- Revising and monitoring any agreements made previously; and
- Managing any risks

If the company in question is considered as a "holding company business", the CIGA's will be all activities that the company conducts. It must be noted that sufficient CIGA's must be carried out in Jersey in order to demonstrate compliance with the Law.

Should a company have no gross income in the financial year then it will not be subject to the substance test in the year of assessment for when the financial period ends.

In addition to the requirements for a company to be conducting a relevant activity, the following points should be noted in addition to these requirements:

- a company may undertake or outsource all or part of an activity outside of Jersey only if it does not generate income for the company;
- it is not necessary for a company to perform all of the CIGA listed for a relevant activity in order to demonstrate substance but all the CIGA that is undertaken, should be undertaken in Jersey;
- the CIGA requirements do not preclude companies seeking expert professional advice or engaging the services of specialists in other jurisdictions;
- a company undertaking financing and leasing business will need to evidence decision making by its board in relation to decisions to lend, setting the terms of loans and monitoring and managing the risk of loans;
- whether a company will be undertaking headquarters business will depend on the extent to which management and responsibility for subsidiaries by the company is in fact taking place;
- where CIGA is undertaken for the company by another entity in Jersey (e.g. by an administrator or another group company) the company must be able to demonstrate that it supervises the carrying on of that activity by the other entity and, to meet the substance test, that it undertakes such supervision in Jersey.

## Self Assessment & Reporting

A Jersey company will be required to submit any information reasonably required by the Comptroller to assist in determining whether the substance test has been met. This information would include (but is not limited to):

- a statement of each relevant activity that the company conducts;
- the gross income received from each individual relevant activity;
- number of board meetings where the quorum of directors was present in Jersey;
- all types of CIGA's which form a part of a company's relevant activity;
- number of employees in Jersey (together with those of reportable qualifications);
- premises address in Jersey;
- declaration by the company based on its own analysis whether the substance test in respect of each relevant activity is met;
- copy the company's financial accounts;
- total expenditure incurred in Jersey on a relevant activity less expenditure by or attributed to an overseas permanent establishment; and
- total expenditure on outsourcing providers in Jersey, whether the activities outsourced are CIGA and, if so, the name, address and TIN of the providers, the total expenditure and confirmation if the figures in the return for employees and premises include the outsourcing providers employees or premises.

## Penalties

If the Comptroller decides that a company has failed to meet the substance test for a financial period, a notice will be issued to the company in question, notifying it of the decision and the reasoning behind it. A penalty can be imposed of up to £10,000, depending on the seriousness of the breach.

If the company in question fails the substance test for a second year, the Comptroller can impose further penalties of up to £100,000, depending on the seriousness of the breach, which can ultimately lead to the breaching company being struck off.

## Summary

If a company is subject to the substance test, it must start preparing all necessary documentation as may be required by the Comptroller to show that they have satisfied the test. Should a company be unable to satisfy the criteria as laid out above, the penalties for not being in compliance can be severe.

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