

OECD releases additional guidance on spontaneous exchange of information by no or only nominal tax jurisdictions

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Executive summary

On 31 October 2019, the Organisation for Economic Co-operation and Development (OECD) released new guidance titled "Substantial Activities in No or Only Nominal Tax Jurisdictions: Guidance for the Spontaneous Exchange of Information" (the [Guidance](#)).

The Guidance addresses the practical modalities regarding the exchange of information requirements of the "substantial activities requirement" for "no or only nominal tax" jurisdictions (the [Standard](#)) that was agreed by the Inclusive Framework on Base Erosion and Profit Shifting (IF on BEPS) in 2018.¹ It provides guidance on the timelines for the exchanges, the international legal framework under which they may occur and clarifications on the key definitions, in order to ensure that the spontaneous exchanges take place in a coordinated and efficient manner. The guidance also contains a standardized IT format for the spontaneous exchanges, the No or only nominal Tax Jurisdictions (NTJ) XML Schema and the related user guide.

It is expected that exchanges pursuant to the standard will commence in 2020.

Detailed Discussion

Background

On 15 November 2018, the OECD released a standard on substantial activities that would apply to jurisdictions that do not impose a corporate income tax. It would also apply to jurisdictions that are considered to impose only nominal levels of corporate income tax to avoid such requirements. Broadly, the standard looks at whether a regime encourages purely tax-driven operations or arrangements, as many harmful preferential tax regimes are designed in a way that allows taxpayers to derive benefits from the regime while engaging in operations that are purely tax-driven and involve no substantial activities.

No and only nominal tax jurisdictions are therefore expected to have legislation in place requiring entities conducting relevant activities to meet the substantial activities requirement. After agreeing on the substantial activities' standard, in July 2019 the OECD's Forum on Harmful Tax Practices (FHTP) identified 12 jurisdictions as being *No or only nominal tax* jurisdictions, namely Anguilla, the Bahamas, Bahrain, Barbados, Bermuda, British Virgin Islands, Cayman Islands, Guernsey, Isle of Man, Jersey, Turks and Caicos Islands and the United Arab Emirates (UAE).² Based on the FHTP's July review, the domestic legal framework of all of these jurisdictions, except for the UAE, are in line with the substantial activities standard and are therefore "not harmful." Regarding the UAE, the FHTP concluded that its legal framework was generally in line with the standard, with one technical point outstanding. In this respect, the UAE committed to make further legislative changes and the law is now "in the process of being amended."³

In order to ensure compliance with the substantial activity factor, the FHTP agreed that no or only nominal tax jurisdictions should have a mechanism to identify the entities conducting the relevant categories of mobile activities and to detect whether the core income generating activities were indeed being carried out; an enforcement mechanism in the event an entity fails to meet the substantial activities requirement; and enhanced spontaneous exchange of information (SEOI). This implies that jurisdictions must collect specific information from the relevant entities in order to identify whether an entity is conducting relevant activities and whether that entity meets the substantial activity requirement as laid out in the Standard. The Standard requires no or only nominal tax jurisdictions to exchange information in specified situations. The framework for

SEOI consists of two parts. First, for any entities that do not comply with the substantial activities requirement, all no or only nominal tax jurisdictions would be required to spontaneously exchange all relevant information with the jurisdictions of residence of the immediate parent, ultimate parent, and ultimate beneficial owner. Second, in the absence of non-compliant entities, the scope of spontaneous exchange will depend on whether a no or only nominal tax jurisdiction can demonstrate that it has a fully equipped monitoring process.

The content of the information to be exchanged depends on a number of circumstances (i.e., compliance with the substantial activities requirements and whether a no or only nominal tax jurisdiction can demonstrate that it has a fully equipped monitoring process). Some of the information that will be exchanged is, for example, the entity name and address, the name of the immediate parent, ultimate parent, and ultimate beneficial owner, and the type of mobile income. In certain cases, the exchange information will also include the amount and type of expenses incurred, and assets and premises held, in the course of carrying out the business, the number of full-time, qualified employees, and a summary of which elements of the core income generating activities test the entity has failed to meet.

Guidance for the Spontaneous Exchange of Information by no or only nominal tax jurisdictions

Building on the abovementioned work, the OECD released on 31 October 2019 additional guidance for the spontaneous exchange of information which addresses the practical modalities regarding the exchange of information requirements of the Standard and opt-in notification template.

The Guidance has two parts:

- ▶ Part 1 contains guidance on: (i) the applicable timeline for conducting the exchanges; (ii) the legal mechanism to operationalize the exchange process; and (iii) relevant definitions for the exchange framework.
- ▶ Part 2 contains the standardized IT format for the exchanges, i.e., the NTJ XML Schema and the related user guide.

The Guidance also includes six Annexes; in Annex A an extract of the Standard relevant to the issues addressed, in Annexes B - E templates for the exchanges which are the basis for the XML Schema and in Annex F the opt-in notification template for the exchanges under the Standard.

Part 1: Additional guidance for the exchange of information of no or only nominal tax jurisdictions

According to the Guidance, the applicable timeline for conducting the exchanges varies depending on whether the information is exchanged as a result of non-compliance with the substantial activity requirements or in other situations. There are four different scenarios with different timelines:

- (i) All jurisdictions - cases of non-compliance
- (ii) Jurisdiction with fully equipped monitoring mechanism - high risk intellectual property (IP)
- (iii) Jurisdiction with standard monitoring mechanism - high risk IP
- (iv) Jurisdiction with standard monitoring mechanism - all other cases

An entity may be subject to the exchange of information in more than one category, but at different times.

The SEOI can occur under the Multilateral Convention on Mutual Administrative Assistance in Tax Matters (the Convention), or under applicable Tax Information Exchange Agreements or bilateral tax treaties that permit SEOI. In order to operationalize the exchanges, potential recipient jurisdictions have to opt-in to the exchange process in respect of each no or only nominal tax jurisdiction. The opt-in process is by way of notification required to be submitted to the Co-ordinating Body Secretariat of the Convention (or for exchanges pursuant to bilateral tax agreements, to the respective no or only nominal tax jurisdiction). The template for this notification is included in Annex F of the Guidance.

The precondition to opt-in to receive the information from a no or only nominal tax jurisdiction is that the potential recipient jurisdiction notifies, on the basis of its applicable legislation and/or taxation principles, that the information relating to compliance with the substantial activity requirements is foreseeably relevant as it can affect the domestic tax treatment of an entity or person in its jurisdiction which is (1) the immediate parent, (2) the ultimate parent and/or (3) the ultimate beneficial owner. The potential recipient jurisdiction must also notify the no or only nominal tax jurisdiction whether it meets the confidentiality and data safeguards requirements as assessed in connection with the Global Forum on Transparency and Exchange of Information for Tax Purposes (Global Forum) process for the Automatic Exchange of Financial Account Information (AEOI Standard) and also used for the Action 5 minimum standard on exchange of information on rulings and the Action 13 minimum standard on exchange of Country-by-Country (CbC) reports.

No or only nominal tax jurisdictions are only required to exchange information with recipient jurisdictions that have notified the Co-ordinating Body Secretariat of the Convention or the relevant no or only nominal tax jurisdiction no earlier than the time that is the first month beginning at least three months in advance of the next exchange date as set out above, unless the recipient jurisdiction's notification specifies a later date. The Guidance provides an example of this time framework in action as per which, if a potential recipient jurisdiction submits its notification on or before 31 August 2020 and the notification specifies that the recipient jurisdiction is ready to start receiving information immediately, the no or only nominal tax jurisdictions are required to begin exchanging information with the recipient jurisdiction in December 2020 onwards. While this timeline sets out when no or only nominal tax jurisdictions would first be expected to spontaneously exchange information, it does not prevent them from spontaneously exchanging the information earlier, if this is permitted under their law and a relevant international legal instrument is in place.

Lastly, the Guidance includes the definitions used for the exchange framework under the Standard, i.e., jurisdiction of residence, reportable entity, immediate parent, ultimate parent, ultimate beneficial owner, and gross income.

According to the Guidance, and for the purposes of identifying the jurisdiction of residence, the jurisdiction may rely on reporting by the reportable entity and in the absence of such reporting, the jurisdiction may, for legal entities, rely on the place of incorporation/formation of the entity, or, in absence thereof and for natural persons, on the address of the person or entity. Also, for the purposes of identifying the immediate parent, the ultimate parent, and the ultimate beneficial owner of a reportable entity, the Guidance sets out that the jurisdiction may rely on the domestic procedures it has in place in order to implement the relevant Financial Action Task Force⁴ recommendations, the latest terms of reference of the Global Forum Peer Review process with respect to the standard on the exchange of information on request, the exchanges of CbC reports pursuant to the BEPS Action 13 recommendations, or any other domestic procedures that enable the jurisdiction to identify the immediate parent, ultimate parent, and the ultimate beneficial owner of a reportable entity.

Part 2: NTJ XML Schema

The main sections of the NTJ⁵ XML Schema User Guide are:

- I. The Message Header. The information in this section identifies the tax administration that is sending the NTJ message.

- II. The Organization Party type. This section defines the information to be included in the NTJ XML Schema in relation to an entity, in particular the Reportable Entity in the no or only nominal tax jurisdiction, as well as the ultimate and/or immediate parent in a recipient or other jurisdiction as part of the Exchange Nexus element.
- III. The Person Party type. The data elements in this section are used to provide identification information on individuals that are the ultimate beneficial owner of a Reportable Entity.
- IV. The NTJ Body. The NTJ Body contains the information on the Reportable Entity (i.e., the identification and activity-related information on the entity subject to reporting) and on the Exchange Nexus (i.e., the entity or person in the receiving jurisdiction that gives rise to the exchange under the Standard in light of its link with the Reportable Entity).

According to the Guidance, the NTJ XML Schema is designed to be used for the exchange of information by Competent Authorities of no or only nominal tax jurisdictions with the Competent Authorities of jurisdictions interested and legally able to receive information pursuant to the Standard (i.e., those that have opted in to receive information pursuant to the Standard and that have an exchange instrument providing for the spontaneous exchange of information in force with the sending jurisdiction). Where appropriate, the User Guide says, no or only nominal tax jurisdictions could also consider using the schema domestically for the purpose of gathering the required information from their respective reporting entities.

Regarding exchanges with European Union (EU) Member States under the parallel work on criterion 2.2 under the EU list of non-cooperative jurisdictions for tax purposes, the Guidance mentions that exchanges with respect to high-risk

IP cases by jurisdictions with a fully-equipped monitoring mechanism would occur as a one-step process and rely on the template in Annex C rather than the template in Annex D of the Guidance.

Next steps

The OECD's FHTP reviewed for the first time the substantial activities factor for no or only nominal tax jurisdictions in June 2019. The FHTP will now proceed with an annual monitoring process where it will review any changes in the legal framework, as well as the implementation of safeguards and enforcement measures in practice.

Jurisdictions interested in receiving information from no or only nominal tax jurisdictions should submit the opt-in notification form to the Co-ordinating Body Secretariat of the Convention to operationalize the exchanges. Following submission of the opt-in notifications form, the sporadic exchange of information from no or only nominal tax jurisdictions could commence as early as 2020. To ensure the effectiveness of the information collection and exchange mechanism, the OECD will hold a review in 2022. Should particular issues surface in the operation of the exchange mechanism in the interim, however, the FHTP could have an earlier discussion.

Implications

The release of the Guidance provides greater clarity regarding the timelines and mechanism to exchange information, as well as the specific data points that will be exchanged. Multinational enterprises (MNEs) operating in no or only nominal tax jurisdictions should be aware and assess what information will be exchanged, when, and with which jurisdictions. Impacted MNE should monitor developments related to the standard, as exchanges are expected to commence in 2020.

Endnotes

1. See EY Global Tax Alert, [OECD releases updated results on scrutiny of preferential tax regimes and substantial activity requirements for no or only nominal tax jurisdictions](#), dated 20 November 2018.
2. See EY Global Tax Alert, [OECD releases update on peer review of preferential tax regimes and no or only nominal tax jurisdictions](#), dated 24 July 2019.
3. <https://www.oecd.org/tax/beps/harmful-tax-practices-peer-review-results-on-preferential-regimes.pdf>.
4. An intergovernmental organization founded on the initiative of the G7 to develop policies to combat money laundering and financial crime.
5. Non or no tax jurisdiction.

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