



## **ECONOMIC SUBSTANCE RULES**

### **Enforcement and Penalties**

The ITA is responsible for assessing and enforcing compliance with the requirements imposed by ESA.

The penalties imposed by the ESA are twofold.

- (1)** Where there has been a failure to provide information, or information provided is inaccurate; and
- (2)** Where there has been a failure to comply with economic substance requirements.

#### **Failure to provide accurate information**

A failure to provide information without reasonable excuse and the intentional provision of false information incurs a penalty. The persons who may be liable for penalties include not only the relevant entities to whom the information relates and their registered agents but any person on whom the ITA serves a notice under [ESA section 11](#).

#### **Penalty**

- (1)** A person who fails to provide information without reasonable excuse or who intentionally provides false information in response to a request under ESA section 11 is liable: (i) on summary conviction, to a fine not exceeding forty thousand dollars or to imprisonment for a term not exceeding two years, or both; or (ii) on conviction on indictment, to a fine not exceeding seventy five thousand dollars or to imprisonment for a term not exceeding five years, or both [ESA section 11\(3\)](#).
- (2)** The same penalties apply where a registered agent intentionally provides false information relating to an entity on its RA database or where the entity intentionally provides false information under [section 9\(2\) or 12\(1\) of the BOSS Act \(BOSS Act section 16\)](#).
- (3)** Where an entity fails to comply with a requirement of section 9 of the BOSS Act without reasonable excuse, it commits an offence and is liable: (i) on summary conviction to a fine not exceeding forty thousand dollars or to imprisonment for a term not exceeding six months, or both; or (ii) on conviction on indictment, to a fine not exceeding two hundred and fifty thousand dollars or to imprisonment for a term not exceeding five years, or both [BOSS Act section 9\(6\)](#).

**(4)** Where a registered agent fails to comply with a requirement of section 9 without reasonable cause, it commits an offence and is liable: (i) on summary conviction to a fine not exceeding twenty thousand dollars; or (ii) on conviction on indictment, to a fine not exceeding forty thousand dollars [BOSS Act section 9\(7\)](#).

As can be seen, save where there has been an intentional provision of false information, there is a defence of 'reasonable excuse' (see [ESA section 11\(3\)](#); [BOSS Act sections 9\(6\), 9\(7\) and 10\(4\)](#)).

### **Failure to comply with the economic substance requirements**

If an entity fails to comply with the Economic Substance requirements the entity and the persons responsible will be penalized and compelled to take corrective action. If the latter purpose cannot be achieved, then the entity risks being struck from the register.

**In the majority of cases there will be a three-stage regime for sanctions:**

**(1)** On a first determination of non-compliance, the ITA will issue a first determination, explaining the reasons for the determination, the amount of the penalty and the date from which the penalty is due and the action which the ITA considers should be taken by the entity and the date by which such action needs to be taken. It will also notify the entity of its right of appeal under section 13 ([ESA section 12\(1\)](#)).

**(2)** If the entity fails to take the action demanded of it in the first determination within the prescribed time, or within such longer period as the ITA may allow, the ITA will issue a second determination. That notice will have the same elements as that issued on a first determination of non-compliance, save that it will also notify the entity that the ITA may make a report to the Financial Services Commission ([ESA section 12\(4\)](#)).

**(3)** Following the issue of a second determination of non-compliance, the ITA may, if it considers it appropriate to do so having regard to all the circumstances of the case, request that the legal entity be struck off the register.

In exceptional cases, the ITA may leapfrog this three-stage regime, and go straight to striking off. It may exercise this power at any time following the service of a first determination of non-compliance where it decides that there is no realistic possibility of the entity meeting the economic substance requirements ([ESA section 12\(8\)](#)).

Once it has determined that an entity is in breach of the economic substance requirements, the ITA has no discretion as to whether to impose a financial penalty, but must impose a minimum penalty of five thousand dollars on a first determination of non-compliance and ten thousand dollars on a second determination of non-compliance ([ESA section 12\(2\) and 12\(4\)](#)). If an entity wishes to challenge the imposition of the minimum penalty on the grounds that it is too high, it must submit an appeal under [ESA section 13](#).

Subject to the requirement that the ITA must impose a minimum penalty on a determination of non-compliance, the ITA has a broad discretion as to the amount of any penalty, provided that it does not exceed the maximum penalty which: on a first determination of non-compliance, is fifty thousand dollars in the case of a high risk IP legal entity and twenty thousand dollars in all other cases ([ESA section 12\(2\)](#)); and, on a second determination of non-compliance, is four hundred thousand dollars in the case of a high risk IP legal entity and two hundred thousand dollars in all other cases ([ESA section 12\(5\)](#)).

In determining the amount of the penalty, the ITA will take into account the following factors:

**(1)** The nature and seriousness of the non-compliance;

- (2) The reason for the breach;
- (3) Whether this is the first financial period in which the entity has failed to comply with the economic substance requirements, or whether it has previously been deemed non-compliant;
- (4) The total turnover of the entity;
- (5) The entity's conduct during the assessment process and (where relevant) following the first determination of non-compliance, and in particular whether it has been cooperative with the ITA;
- (6) What steps (if any) the entity has taken to prevent a recurrence of the breach.

### **Appeal**

An entity who has been served with a notice of non-compliance by the ITA under ESA section 12 has a right of appeal against both the determination of non-compliance and against the amount of any penalty imposed, including where the amount of the penalty is the minimum prescribed ([ESA section 13](#)).

However, notice of the appeal stating the ground of appeal must be filed at the Court within 30 days of the date of the notice of non-compliance ([ESA section 14\(1\)](#)).

The ITA, on whom the notice of appeal must be served, is entitled to appear and be heard at the hearing of the appeal ([ESA section 14\(2\)](#)).

The powers of the court on an appeal comprise the power to confirm, vary or revoke the determination of non-compliance, and to confirm, vary or cancel the penalty ([ESA section 14\(3\)](#)).

Where notice of appeal has been lodged, the time for complying with the requirements specified in the notice of non-compliance only starts to run from the date on which the appeal is finally determined or withdrawn ([ESA section 15](#)).