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The Impact of Cayman's EU Blacklisting

At the ECOFIN meeting of 18 February 2020 the EU finance ministers added Cayman to the EU list of non-cooperative jurisdictions for tax purposes.

It was reported at that time that the Cayman Islands has been listed because it "does not have appropriate measures in place relating to economic substance in the area of collective investment vehicles". Cayman passed collective investment vehicle legislation, the Private Funds Law, 2020 and the Mutual Funds (Amendment) Law 2020, on 7 February 2020 in order to address the EU's concerns regarding the Cayman Island's collective investment vehicle regulation but these law came into force too late to avoid the EU blacklisting.

There are no automatic sanctions on blacklisted non-cooperative tax jurisdictions but the EU has encouraged its Member States to apply one or more legislative measures on transactions with non-cooperative tax jurisdictions from 1 January 2021. These measures include:

- limiting tax deductions on payments to entities in non-cooperative tax jurisdictions;
- applying controlled foreign company rules where entities in non-cooperative tax jurisdictions are used;
- imposing withholding taxes on payments treated as received in non-cooperative jurisdictions; and
- limiting tax exemptions on revenue treated as received from a non-cooperative jurisdiction.

Luxembourg has recently produced draft legislation which is expected deny tax deductions on interest and royalty payments to related entities located in non-cooperative tax jurisdictions. Luxembourg already applies enhanced

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tax audit requirements for Luxembourg companies with related entities located in non-cooperative tax jurisdictions.

Efforts by the Cayman Islands Government to ensure that the Cayman Islands are removed from the EU list of non-cooperative jurisdictions for tax purposes are ongoing and it is expected that with some minor changes to the Private Funds Law, 2020 and the Mutual Funds (Amendment) Law 2020 the Cayman Islands will be able to ensure its removal from the list by October 2020.

With Luxembourg being a major jurisdiction for collective investment funds and with the key promoters of those funds also being key promoters of collective investment funds established in the Cayman Islands it is hoped that the coming into force of Luxembourg's draft legislation will be set for the 1 January 2021 target date.

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