



IN THE GRAND COURT OF THE CAYMAN ISLANDS
FINANCIAL SERVICES DIVISION

CAUSE NO. FSD OF 2023 ()

**IN THE MATTER OF THE INTERNATIONAL TAX CO-OPERATION (ECONOMIC
SUBSTANCE) ACT (2021 REVISION)**

CHINA CONSTRUCTION BANK (BRASIL) BANCO MULTIPLO S/A

APPLICANT

THE CAYMAN ISLANDS TAX INFORMATION AUTHORITY

RESPONDENT

NOTICE OF ORIGINATING MOTION

TAKE NOTICE that the Court at the Law Courts, George Town, Grand Cayman will be moved on the day of 2023 , at o'clock, or as soon thereafter as counsel can be heard, by counsel on behalf of China Construction Bank (Brasil) Banco Multiplo S/A (the "**Applicant**") for:

- 1 An order under section 9 of the International Tax Co-operation (Economic Substance) Act (2021 Revision) (the "**Act**") that the determination made by the Cayman Islands Tax Information Authority (the "**Authority**") on 25 September 2023 to: (a) issue a penalty of US\$12,202.62 on the Applicant pursuant to section 8(4) of

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the Act; and (b) issue direction as to the actions to be taken by the Applicant "to satisfy the ES Test in the subsequent financial year" (together, the "**Penalty**") be reversed.

- 2 An order under section 9(3) of the Act for a declaration that the liability to the Penalty does not arise.
- 3 The Applicant's costs of and incidental to this appeal be paid by the Authority.

Background

- 4 The Applicant is a company incorporated in Brazil on 27 July 1981 with its head office and principal place of business situated at Av. Brigadeiro Faria Lima, 4.440 2nd floor - Itaim Bibi 04538-132, São Paulo SP, Brazil.
- 5 The Applicant was registered as a foreign company in the Cayman Islands pursuant to Part IX of the Companies Act on 3 January 2002 (registration number 115096) with its agent listed as Cainvest Bank and Trust Limited, 5th Floor, 103 South Church Street, George Town, Cayman Islands (the "**Agent**").
- 6 The Applicant operates 8 branches in Brazil and provides a range of banking services, mainly to corporate clients
- 7 On 15 August 2001, the Brazilian Central Bank authorised the constitution of a branch of the Applicant in the Cayman Islands, which was approved at the administrative council meeting held on 18 May 2001 (the "**Cayman Islands Branch**").
- 8 On 21 January 2002, the Cayman Islands Monetary Authority granted the Applicant a "category B" licence authorising the Applicant to carry on a banking business through the Cayman Islands Branch pursuant to the Banks and Trust Companies Act (Revised).
- 9 The Cayman Islands Branch officially commenced its operations in the Cayman Islands on 4 February 2002 with its principal activities focussed on loan operations.
- 10 The Applicant is registered with the Special Department of Federal Revenue of Brazil. Its registration number which is issued by the Brazilian National Registry of Legal Entities (Cadastro Nacional de Pessoas Jurídicas) ("**CNPJ**") is 07.450.604/0001-89.

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- 11 The Cayman Islands Branch continues to be regulated by and under the supervision of the Brazilian Central Bank. In accordance with regulations issued by the Brazilian Central Bank, the financial statements of the Cayman Islands Branch are prepared on the basis of Brazilian Corporate Law 6,404/76, amended by Law 11,638/07 and the regulations of both the Brazilian Central Bank and the National Monetary Council (“CMN”) of Brazil, such as Resolution n. 4.868 of the CMN. These regulations require the Applicant to prepare consolidated financial statements in respect of both itself and all of its branches (whether local or foreign).
- 12 The Applicant's consolidated financial statements are then provided to the Special Department of Federal Revenue of Brazil, at which point the amount of tax payable by the Applicant (on the basis of the revenue generated by all of its branches; including the Cayman Islands Branch) is calculated and subsequently paid by the Applicant, in Brazil, on behalf of all of its branches. On this basis, although the Applicant is carrying on a relevant activity (through the Cayman Islands Branch) it is tax resident outside of the Cayman Islands and therefore does not fall within the definition of "relevant entity" under the Act.
- 13 In the premises, as pleaded below, the Applicant was therefore not required to file an economic substance return and, any failure to do so was not a breach of the Act. Further, as the Applicant has not breached the Act, the Penalty should not have been issued and, as a result, should be reversed.

The Legal Framework

Economic substance

- 14 Section 3 of the Act states that the Authority shall have the following functions (emphasis added):
 - (a) *"to administer this Act;*
 - (b) *to determine whether a relevant entity that is required to satisfy the economic substance test in relation to a relevant activity satisfies such test;*
 - (c) *to monitor compliance with this Act; and*
 - (d) *any other function specified in this Act".*

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- 15 Section 4(1) of the Act states that (emphasis added): "*(1) Subject to subsections (5), (6) and (7) and to regulations made under section 15, a relevant entity that carries on a relevant activity is required to satisfy the economic substance test in relation to that relevant activity*". Section 4(2) of the Act goes on to set out the relevant elements required of a relevant entity in order for it to satisfy the "economic substance test" as set out under the Act (the "**ES Test**").
- 16 Under the Act:
- (a) "relevant activity" includes "banking business" (as defined under the Act); and
 - (b) "relevant entity" means (emphasis added):
 - (a) *"a company, other than a domestic company, that is —*
 - (i) *incorporated under the Companies Act (2021 Revision); or*
 - (ii) *a limited liability company registered under the Limited Liability Companies Act (2021 Revision)*
 - (b) *a limited liability partnership that is registered in accordance with the Limited Liability Partnership Act (2021 Revision);*
 - (c) *a company that is incorporated outside of the Islands and registered under the Companies Act (2021 Revision),*
but does not include —
 - (i) *an investment fund; or*
 - (ii) *an entity that is tax resident outside the Islands*
- 17 An entity that is a tax resident outside of the Cayman Islands is accordingly not a "relevant entity" under or for the purposes of the Act; and is not required to satisfy the ES Test.
- 18 The exception to the satisfaction of the ES Test for entities that are tax resident outside of the Cayman Islands is confirmed in the Authority's Guidance on *Economic*

Substance for Geographically Mobile Activities (Version 3.2), issued by the Authority in July 2022 (the "**ES Guidance**") which states as follows with respect to banks operating in the Cayman Islands under a class B licence (as is the case for the Applicant) (emphasis added):

"A bank with a Class "B" Licence or a Restricted Class "B" Licence that would otherwise be in scope for the ES Act will be out of scope, on the basis that it is not a relevant entity for the purposes of the ES Act, if it establishes to the Authority that it is tax resident outside the Islands. For example, a bank with a Class "B" Licence would be out of scope for the ES Act on this basis if it is the Cayman Islands branch of a foreign bank which is subject to corporate income tax on all of the entity's income in a jurisdiction outside the Islands. The DITC will require any entity which claims that it is tax resident outside the Islands to produce satisfactory evidence to substantiate this claim. Further information on this exemption is outlined in Section II.B.2.c) above".

- 19 The ES Guidance also states that "*the Authority will also regard any branch of a relevant entity as tax resident outside the Islands if the branch is subject to corporate income tax on all of that branch's income in another jurisdiction by reason of its domicile, residence or any other criteria of a similar nature. The Authority will require any relevant entity which claims that its branch is tax resident outside the Islands to produce, with respect to its branch, satisfactory evidence of the type described in the previous paragraph. In this context, a "branch" refers to a business unit or division of the relevant entity that is not a separate legal person from the relevant entity*".

The provision of information

- 20 Section 6(1) of the Act states:

"The Authority shall have the power, in accordance with this Act, regulations made under this Act and the guidance issued under section 5, to make a determination as to whether a relevant entity that is required to satisfy the economic substance test in relation to a relevant activity satisfies such economic substance test for any financial year of the relevant entity commencing on or after the date prescribed under section 4(6), except that such a determination shall not be made later than six years after the end of such financial year".

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21 Section 7(1) of the Act requires an entity to provide the Authority with the following information, the nature of which depends on whether it is a "relevant entity":

"An entity shall annually notify the Authority of the following —

- (a) *whether or not it is carrying on a relevant activity;*
- (b) *if it is carrying on a relevant activity, whether or not it is a relevant entity;*
- (c) *in the case of an entity that is carrying on a relevant activity and is tax resident in a jurisdiction outside the Islands —*
 - (i) *the name and address of its immediate parent, ultimate parent and ultimate beneficial owner and any other information reasonably required to identify its immediate parent, ultimate parent and ultimate beneficial owner;*
 - (ii) *the date of the end of its financial year; and*
 - (iii) *the jurisdiction in which the entity is claiming to be tax resident and any other information as may reasonably be required to support that claim;*
- (d) *in the case of a relevant entity that is carrying on a relevant activity —*
 - (i) *the date of the end of its financial year; and*
 - (ii) *the name and address of the officer who is responsible for providing information to the Authority,*

and shall provide appropriate evidence to support the information provided in the notification as may reasonably be required by the Authority.

22 Sections 7(2) states that a notification under sub-section 1 "*shall be made at the time specified by the Authority and in the form and manner approved by the Authority*".

23 Section 7(3) states that "*Subject to subsection (4), a relevant entity that is carrying on a relevant activity and is required to satisfy the economic substance test shall, no later than twelve months after the last day of the end of each financial year of the relevant*

entity commencing on or after the prescribed date, prepare and submit to the Authority a report for the purpose of the Authority's determination under section 6". Sub-section 4 lists the information that is required to be listed in a relevant entity that is carrying on a relevant activity's economic substance return ("**ES Return**").

- 24 Section 8(1) of the Act states that: "*If the Authority determines under section 6 that a relevant entity that is required to satisfy the economic substance test in relation to a relevant activity has failed to satisfy such economic substance test for a financial year, the Authority shall issue a notice to the relevant entity notifying the relevant entity of —*

The Authority's determination that the relevant entity has failed to satisfy the economic substance test in relation to the relevant activity for that financial year;

- (a) *the reasons for the determination;*
- (b) *the amount of any penalty imposed under subsection (2);*
- (c) *the date on which the penalty under subsection (2) is due being not less than twenty-eight days after the date of issue of the notice;*
- (d) *the Authority's direction as to the action to be taken by the relevant entity to satisfy the economic substance test in relation to the relevant activity*

..."

Applicant's TRO Form and ES Returns

- 25 On 29 December 2021, the Applicant submitted an "*economic substance – entity tax resident in another jurisdiction form*" with respect to its 2020 financial year in accordance with section 7(1)(c) of the Act (the "**TRO Form**") through the Department of International Tax Co-operation's online reporting portal (the "**DITC Portal**"). The Applicant selected the following fields on the TRO Form (with the responses underlined):

- (a) Relevant Activity: Banking Business;
- (b) Jurisdiction of Tax Residence: KY;

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- (c) Ultimate Parent Details:
- (i) Does the Entity have an Ultimate Parent? Yes
 - (ii) Jurisdiction of tax Residence: CN (being a reference to the People's Republic of China).
- (d) Confirmations:
- (i) The Entity is subject to corporate income tax on all of its income from the relevant activity by virtue of its tax residence, domicile, or other criteria of a similar nature in the jurisdiction of tax residence? Yes
 - (ii) The Applicant does not have an immediate parent or ultimate beneficial owners and those fields were accordingly left blank.

26 On 29 December 2021, the Applicant also completed and submitted an ES Return with respect to its 2020 financial year to the Authority via the DITC Portal pursuant to section 7(3) of the Act. This was done by the Applicant in error.

27 On 27 July 2022, the Applicant received an ES compliance letter from the Authority (the "**Compliance Letter**") which stated that, following a review of the TRO Form, the Authority "*has decided to reject the [Applicant's] claim that it is a tax resident in the Cayman Islands*" because (emphasis added):

"For the entity to claim the TRO exception it must be tax resident and subject to the corporate income tax system (other than withholding tax) in another jurisdiction. Given that Cayman Islands does not have a corporate income tax system, the entity cannot claim tax residence in this jurisdiction... As the entity's claim for the TRO exception has been rejected, the entity must prepare and submit an ES Return for the 2020 financial year by 29 August 2022.

If the entity fails to submit the ES Return by the above deadline, it will be deemed to have failed the ES Test and an ES Penalty Notice will be issued to the entity pursuant to section 8(1) of the ES Act".

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- 28 A reasonable person acting in the position of the Authority would have appreciated, prior to issuing the Compliance Letter, that a plain and obvious error had been made by the Applicant, in that:
- (a) The Applicant would have been required to complete and submit either a TRO Form or an ES Return with respect to its 2020 financial year to the Authority (these two different types of filings being mutually exclusive). The fact that the Applicant completed and submitted both the TRO Form and an ES Return (both with respect to the Applicant's 2020 financial year) to the Authority, on the same date, indicates, at a minimum, that one of these filings had been made in error;
 - (b) In completing the TRO Form, the Applicant had clearly indicated that it was a tax resident in another jurisdiction (i.e. outside of the Cayman Islands). The Applicant's selection, in the TRO Form, of the Cayman Islands as its jurisdiction of tax residence directly contradicted the very completion and submission of a TRO Form and was, on its face, a clear and manifest error;
 - (c) This error on the TRO Form was facilitated by the DITC Portal which allowed the Applicant to select the Cayman Islands as its jurisdiction of tax residence in the relevant drop down options in relation to the relevant field of the TRO Form, notwithstanding that: (a) the Cayman Islands does not have a corporate income tax system (as is explicitly referred to in the Compliance Letter); and (b) the TRO Form that the Applicant completed was specifically designed and provided by the Authority for entities that consider themselves to be tax resident in another jurisdiction (i.e. outside of the Cayman Islands).
- 29 Notwithstanding the clear and manifest error made by the Applicant in the TRO Form, which was subsequently carried through in the Applicant's economic substance notifications and ES Return as filed by the Applicant with the Authority with respect to the Applicant's 2021 financial year, the Authority issued the Compliance Letter.
- 30 The Compliance Letter was misleading and/or incorrect in a number of material respects, including:

- (a) It failed to properly explain the purpose of an ES Return or explain that an ES Return was only required to be made under section 7(3) of the Act by an entity that is a "relevant entity" which the Applicant was not; and
 - (b) It wrongly asserted that: (i) the completion and submission of an ES Return in respect of the Applicant's 2020 financial year was a compulsory next step required of the Applicant given that the TRO Form had been rejected by the Authority; and (ii) that a penalty would be automatically imposed on the Applicant by the Authority if such an ES Return was not completed and submitted to the Authority by the Applicant within the timeframe prescribed in the Compliance Letter.
- 31 On 29 July 2022, the Applicant sent an email to the Authority querying whether it was required to re-submit an ES Return with respect to its 2020 financial year when the Applicant had already submitted one to the Authority via the DITC Portal (albeit, in error) on 29 December 2021. The Applicant did not receive any response.
- 32 On 10 August 2022, the Applicant, reliant on the Compliance Letter, completed and submitted a further ES Return with respect to its 2020 financial year to the Authority via the DITC Portal.
- 33 On 28 April 2023, the Authority sent a letter to the Applicant which noted that the Authority considered that Applicant had not satisfied the ES Test for its 2020 financial year and the reasons for the Authority's determination in this respect. This letter afforded the Applicant the opportunity to "*provide the Authority with any relevant information or clarification which the entity believes would demonstrate that it did not fail the ES Test for the financial year*" by no later than 28 May 2023 (the "**Second Compliance Letter**").
- 34 The Second Compliance Letter was only sent to the email address of Mr Carlos Roque who was listed on TRO Form and the Applicant's ES Returns with respect to its 2020 financial year as the "Responsible Person" as required under section 7(1)(d) of the Act being "*the officer who is responsible for providing information to the Authority*". Mr Roque had however ceased to be an employee of the Applicant on 25 August 2022 and the Second Compliance Letter accordingly did not come to the attention of any persons who were employed by the Applicant at the material time; nor was the Applicant aware that the Second Compliance Letter had been issued by the Authority until it was later referred

to, by the Authority, in the ES penalty notice issued by the Authority to the Agent on 25 September 2023 and searches were done by the Applicant in order to retrieve a copy of the Second Compliance Letter from the Applicant's server.

AND FURTHER TAKE NOTICE that the grounds of this appeal are that, in issuing the Penalty and the direction set out therein, the Authority behaved unlawfully, unreasonably, procedurally improperly and/or in breach of the Applicant's legitimate expectation as:

- 1 It incorrectly and/or unreasonably determined that the Applicant was a relevant entity that was required to satisfy the ES Test in relation to a relevant activity, contrary to its functions under section 3 of the Act. In that connection, the relevant facts are as follows:
 - (a) The Applicant is an entity that is a tax resident outside the Cayman Islands and is assessed for, and liable to pay, corporate income tax in Brazil. The Applicant is accordingly not a relevant person to whom the ES Test applies;
 - (b) The Cayman Islands Branch is out of scope of the Act on the basis that it is a branch of the Applicant (a foreign bank) who is subject to corporate income tax on its income in Brazil;
 - (c) The Applicant completed and submitted the TRO Form to the Authority and, as such, indicated to the Authority that it was an entity that is tax resident outside the Cayman Islands.
- 2 It therefore has no power to issue the Penalty (including the direction) to the Applicant under section 8 of the Act in circumstances where the Applicant is not a relevant entity on whom a penalty may be imposed or to whom directions may be issued.
- 3 The manner in which the Authority required the Applicant to provide information under section 7(1)(c) of the Act, namely through the DITC Portal, was confusing and facilitated the series of errors:
 - (a) The DITC Portal allowed the Applicant to submit both the TRO Form and an ES Return with respect to its 2020 financial year, notwithstanding that these two different types of filing are mutually exclusive;

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- (b) The TRO Form that the Applicant completed and submitted via the DITC Portal allowed the Applicant to select the Cayman Islands as its jurisdiction of tax residence notwithstanding that:
 - (i) the Cayman Islands does not have a corporate income tax regime; and
 - (ii) the TRO Form that the Applicant completed was specifically designed and provided by the Authority for entities that consider themselves to be tax resident in another jurisdiction (i.e. outside the Cayman Islands).
- 4 It failed to seek any clarification regarding why the Applicant had completed and submitted the TRO Form to the Authority if the Applicant believed itself to be tax resident in the Cayman Islands, or to request any further information to clarify the Applicant's position, in circumstances where:
- (a) Paragraph 3.1 of the *Enforcement Guidelines: Economic Substance (ES)* issued by the Authority (the "**Enforcement Guidelines**") state: "*In cases where, in the opinion of the Authority, a clarification of the information provided or additional documentary evidence is required, the Authority will contact the designated responsible person ("RP")*". In other words, the Authority had expressly represented that, in circumstances where there was any error and/or ambiguity surrounding an applicant's return, it would investigate this by contacting the applicant's designated responsible person; and
 - (b) The Authority is expressly empowered under section 7(5) of the Act to request such additional information as shall be reasonably required by it to make a determination under section 6 of the Act, which would include such information as may be necessary in order for the Authority to clarify any inconsistency in the application process, including any inconsistency of the kind inherent in the Applicant's TRO Form and ES Return.
- 5 It failed to request any of the information listed in either the Enforcement Guidelines or the ES Guidance as evidence that the Authority requires from an entity claiming to be tax resident in another jurisdiction.

- 6 It failed to give the Applicant the opportunity to amend the TRO Form notwithstanding the clear and manifest error that the Applicant had made in completing and submitting it.
- 7 It acted unreasonably in issuing the Compliance Letter in circumstances where its contents were misleading and led the Applicant to believe that it was mandatorily required to complete and submit an ES Return to the Authority in order to avoid incurring a financial penalty.

Dated this 23rd day of October 2023



Ogier (Cayman) LLP

TO: The Clerk of the Court

AND TO: The Cayman Islands Tax Information Authority

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