

## Bermuda corporate and finance update Q2 2024

**Briefing Summary:** Our corporate team outline the latest developments within the corporate and finance market in Bermuda including Bermuda's Corporate Income Tax Act 2023, Cyber risk management and The Bermuda Monetary Authority's enhancements to its Insurance Regulatory Regime.

**Service Area:** Corporate

**Sector:** Banking

**Location:** Bermuda

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### Introduction to Bermuda's Corporate Income Tax Act 2023

On 27 December 2023, the Corporate Income Tax Act 2023 ("CITA") received governor's assent in Bermuda. The operating provisions of this legislation come into effect on 1 January 2025, and, at such time and for the first time in Bermuda's history, corporate income tax will be chargeable to certain Bermuda-based entities (referred to in CITA as "**Bermuda Constituent Entities**") for fiscal years beginning on or after 1 January 2025.

### The OECD's Pillar Two GloBE Rules

CITA was enacted in response to the OECD's Global Anti-Base Erosion Model Rules (Pillar Two) (the "**GloBE Rules**"). The GloBE Rules endeavour to ensure that large multinational enterprise ("MNE") groups pay a minimum level of tax (15%) on income that arises in each jurisdiction in which the group operates. The GloBE Rules endeavour to achieve this through the inclusion of a "top-up tax" framework. Pursuant to such framework, if profits arise in a jurisdiction where the effective tax rate is below the global minimum tax rate, top-up tax may be payable to other GloBE Rule adhering jurisdictions applicable to the MNE group.

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## Bermuda's new domestic corporate income tax

Although generally aligning with the GloBE Rules, CITA is not Bermuda's domestic enactment of the global minimum tax framework described above. Rather, CITA is a new domestic corporate income tax regime implemented, according to the Government of Bermuda, to protect Bermuda from being a non-adhering jurisdiction under the GloBE Rules and from being penalized through the GloBE Rules' top-up tax framework in the home jurisdictions of other MNE group entities (including through the application of the income inclusion rule ("IIR") and the under-taxed profits rule ("UTPR"), each as defined in the GloBE Rules).

### Scope and applicability of CITA

#### In Scope MNE Groups

From 1 January 2025, CITA will apply to any Bermuda Constituent Entity incorporated or formed in Bermuda (unless that entity is a tax resident in another jurisdiction) or that has a permanent place of business in Bermuda if such entity is a member of an "In Scope MNE Group." An In Scope MNE Group is defined as a group of entities related through ownership and control that has an annual revenue of 750 million euros or more in a fiscal year, pursuant to the consolidated financial statements of the ultimate parent entity, in at least two of the four fiscal years immediately preceding the fiscal year beginning on or after 1 January 2025, and such group includes at least one entity located in a jurisdiction that is not the parent entity's jurisdiction.

#### Bermuda Constituent Entities and Bermuda Constituent Entity Groups

For all Bermuda Constituent Entities that form part of an In Scope MNE Group (referred to as a Bermuda Constituent Entity Group), corporate income tax will be chargeable at a rate of 15% of net taxable income less applicable tax credits that may be available.

Each Bermuda Constituent Entity of the Bermuda Constituent Entity Group will be jointly and severally liable for the corporate income tax chargeable to the Bermuda Constituent Entity Group.

Liability for corporate income tax under CITA will apply to all Bermuda Constituent Entities notwithstanding any assurance given pursuant to the Exempted Undertakings Tax Protection Act 1966.

#### Exclusions and exemptions

Governmental entities, international organisations, non-profit organisations, pension funds, an investment fund that is an ultimate parent entity, and any real estate investment vehicle that is an ultimate parent entity (each as defined in CITA) are not to be treated as Bermuda Constituent Entities and, unless they elect otherwise, will be excluded from the income tax charging provisions of CITA. Although corporate income tax will not be charged to such "excluded entities," their annual revenue will be taken into account in determining whether an MNE Group qualifies as an "In Scope MNE Group."

An entity that is less than 80% owned (by value), directly or indirectly, by the ultimate parent entity of the relevant In Scope MNE Group will also not be treated as a Bermuda Constituent Entity and will be excluded from the tax charging provisions of CITA.

In addition to the above, CITA contains other exemptions and exclusions, including for example:

- a five-year exclusion for MNE groups with a limited international footprint;
- a de minimis exemption (if the Bermuda Constituent Entity Groups' average revenue is less than 10 million euros and the average net taxable income or loss is less than 1 million euros); and
- an exclusion for international shipping income.

## Economic transition adjustments

CITA also includes various tax credits as well as adjustments to the taxable income or loss of a Bermuda Constituent Entity including an economic transition adjustment provision ("ETA"). The ETA is understood to be included in CITA as an attempt to ensure a fair and equitable transition into the Bermuda corporate income tax regime for the entities that will be liable for the new income tax. The ETA recognizes a fair value adjustment for the assets and liabilities of a Bermuda entity to 30 September 2023 (except goodwill).

## Further information

The Government of Bermuda has published guidance on CITA in the form of "Frequently Asked Questions." These FAQs addresses various topics including exclusions and exemptions, elections, tax credits, determining tax loss carry forward deductions, changes in accounting principles, adjustments due to IFRS17 and LDTI, ETAs, and transfer pricing adjustments.

## Going forward

Bermuda entities and permanent establishments that form part of MNE groups will want to consider if CITA is applicable to them, the impact CITA may have, whether any elections may be applicable, and whether such entities may benefit from the ETA provisions, among other things.

Please contact us for advice or further information with respect to corporate income tax in Bermuda and CITA's potential effect on your organisation or group.

The Bermuda Monetary Authority (the "BMA") continues to seek ways to enhance its regulatory regime in relation to persons licenced to conduct digital asset business ("DABs").

The BMA has published updates to that regime which establish duties, requirements and procedures for DABs in relation to operational cyber risk management, and asset safekeeping by DAB custodial wallet service providers.

## Cyber risk management

Cyber incidents can cause significant financial losses and/or reputational damage to DABs and their clients. Addressing cyber security risks has become a focus of the BMA in recent years: it considers the confidentiality, integrity and availability of information, in all its forms, to be critical to the daily operations of DABs.

The BMA has updated its regulatory regime relating to cyber risk with the following:

- DAB Operational Cyber Risk Management Code of Practice (the "**Cyber Risk Code**"); and
- Digital Asset Business (Cyber Risk) Rules 2023 (the "**Cyber Risk Rules**").

### The Cyber Risk Code

The Cyber Risk Code came into effect on 1 January 2024 but all existing DABs have until 30 June 2024 to be in compliance.

The Cyber Risk Code applies to all DABs and provides standards and procedures for the stable and secure management of information technology systems of those regulated entities. It is deliberately not exhaustive. DABs must implement their own risk programmes, determine what their top risks are and decide the appropriate risk response. It is crucial that DABs provide evidence that there is adequate Board visibility and governance of cyber risks.

Some key requirements of the Cyber Risk Code include:

- *Board Governance* – the board of directors and senior management must have oversight of cyber risks;
- *Role of the Chief Information Security Officer* – whether outsourced or internal, this officer is to deliver the operational cyber risk management programme;
- *Cyber risk policy* – cyber risk controls and procedures can be covered in a standalone cyber risk policy document or in a section in a broader risk policy document; and
- *Three lines of defence model* – the BMA requires the cyber risk governance to follow a three lines of defence, namely: operational management, risk management and audit.

### The Cyber Risk Rules

The Cyber Risk Rules became operative on 1 January 2024 and introduced rules around the filing of a Cyber Risk Annual Return (a "**Return**").

DABs that hold:

- a Class F (full) digital asset business licence are required to lodge a Return annually and must do so within four months after the end of their financial year.
- a Class M (modified license intended to provide a regulatory sandbox) or Class T (test license for carrying out pilot or beta testing) digital asset business licence, will be required to lodge a Return at such time as determined by the BMA.

## Custody by DABs

The BMA also seeks to provide more clarity and guidance on custody obligations of DABs holding assets of their clients.

### The Custody Code

For those DABs which operate as custodial wallet service providers, the BMA revised the Digital Asset Business Custody Code of Practice (the **"Custody Code"**). This now provides clearer regulatory standards for the safekeeping of digital assets by DABs. This revised Custody Code was published in February 2024.

Key requirements of the Custody Code include:

- **Dedicated Roles** – the BMA requires there to be documented roles and responsibilities for DABs' custody operations and custody operational risk management; and
- **Technology Controls** – DABs are required to implement controls to ensure digital assets are securely created and stored; and
- **Fraud Detection and Prevention Measures** – in addition to procedures for detecting fraud, DABs are required to implement controls for preventing fraud in respect of digital asset transactions.

### Consultation on new Custody of Client Assets Rules

The BMA has also published a draft form of Digital Asset Business (Custody of Client Assets) Rules 2024 for consultation. When they come into effect, these Rules will provide further clarity to DABs that hold client assets (including digital assets and fiat) by addressing matters such as fiduciary duty, segregation, delegation and accounting.

## The Bermuda Monetary Authority enhances its Insurance Regulatory Regime

Changes to the Bermuda Monetary Authority's (**"BMA"**) Regulatory Regime for Commercial Insurers (**"Regulatory Regime"**) came into effect on 31 March 2024, following a consultation last year. These enhancements seek to ensure that the cornerstones of the regulatory regime for commercial insurers continue to be sound, serving the dual goal of protecting policyholders and contributing to financial stability.

The key changes to the Regulatory Regime are split into:

- Technical provisions;
- Bermuda Solvency Capital Requirements (**"BSCR"**);
- Enhancements to Section 6D of the Insurance Act 1978 (the **"IA"**); and
- Regulatory fees, as discussed further below.

## Technical provisions

The BMA changed the calculation of the risk margin for Insurance Groups, the Scenario-Based Approach (“**SBA**”) and the standard discount curve for liabilities denominated in Euros.

### Risk margin calculation

The risk margin calculation for insurance groups is now on an unconsolidated basis. This means that the calculation is aligned with the principles behind the risk margin construction that apply to certain transfers.

### SBA

The BMA’s aim in making changes to the SBA is to ensure that there continues to be a robust regulatory framework review process, which takes into account the evolving industry practices and business models. The changes include enhanced modelling, governance, validation, stress testing and reporting requirements.

### Standard discount curve

The BMA has adjusted the euro-denominated (“**EUR**”) discount curves for the Standard Approach, as covered in depth within the Regulatory Regime. This change aligns EUR rate curves provided by the European Insurance and Occupational Pensions Authority (“**EIOPA**”) and the EUR rate curves which are also provided by the BMA, the results of which had previously been similar. This means that insurers are permitted to use the EIOPA EUR curve for EUR liabilities without first seeking separate approval from the BMA.

### BSCR

#### Increased risk sensitivity

The calculation of the BSCR has increased the risk sensitivity for lapse and expense risks for the other long-term insurance risk capital charge. In implementing this change, the BMA have created a separate identification for lapse and expense risks. The change to the lapse and expense risk charges will have a ten-year transitional period.

#### Changes to Property and Casualty charges

The BMA has also changed its Property and Casualty charges to improve the capture of man-made risks by including a dedicated man-made catastrophe risk submodule. This is to promote closer alignment with the corresponding Solvency II capital requirement for man-made catastrophe risk scenario and better alignment of the prescribed man-made scenarios and insurers’ risk profiles. The submodule will be comprised of catastrophe scenarios for terrorism, credit and surety, marine, and aviation. The charges for the new scenarios will be phased in over the next three years.

## Enhancements to Section 6D of the IA

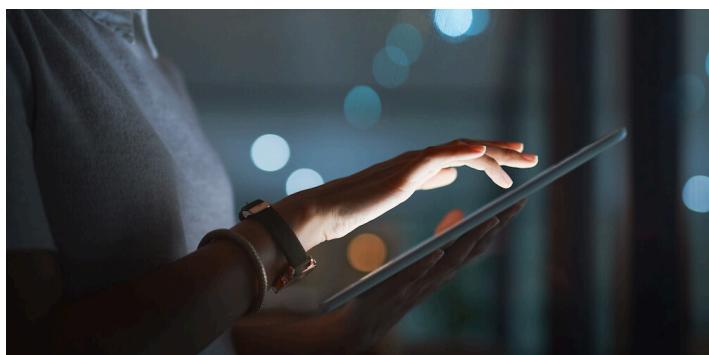
The BMA have clarified the types of adjustments that are permitted, or standards an application is required to meet, within Section 6D of the IA. Following this clarification, insurers can make adjustments to BSCR requirements where the BSCR does not represent the insurer's risk profile. The BMA have created three routes in line with these adjustments which are for simple, simple-complex and complex adjustments, each with their own specific requirements.

## Regulatory fees

The BMA has increased registration and annual business fees for long-term commercial insurers to fund the BMA's supervisory activities. The increased regulatory fees will be phased in over the next three years.

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