

# **ECONOMIC SUBSTANCE VIRTUAL COURSE**

## **QUESTION BANK**

### **(PURE EQUITY) HOLDING COMPANY**

#### **1 MIDCO LTD**

Midco Ltd is an intermediary (pure equity) holding company in a group structure, it holds 100% of the shares in three other companies and receives dividends annually. This is Midco Ltd's only activity. Is Midco Ltd a (pure equity) holding company?

#### **2 RESTAURANT LTD**

Restaurant Ltd runs 2 restaurants, it also acquired all the shares in another company Bistro Ltd which is constructing a new restaurant. Is Restaurant Ltd a (pure equity) holding company?

#### **3 TRUST SERVICES LTD**

Trust Services Ltd acts as trustee to a number of unconnected trusts, holding assets in its capacity as trustee. Is Trust Services Ltd a (pure equity) holding company?

### **BANKING**

#### **4 HIGH STREET SAVINGS LTD**

High Street Savings Ltd has a number of branches from which it offers current or savings accounts and other banking services. Is High Street Savings Ltd a bank?

#### **5 BANKING SERVICES LTD**

Banking Services Ltd is part of a banking group, however it does not take deposits, it only provides advisory and other services to clients of the banking group. Is Banking Services Ltd a bank?

## **FINANCE AND LEASING**

### **6 ABC LTD**

ABC Ltd lends £1,000,000 to its subsidiary, CDE Ltd, at a 5% interest rate. Would ABC Ltd's activities come within the definition of finance and leasing?

The loan of £1,000,000 to CDE Ltd, is transferred by ABC Ltd to another company 123 plc. Does this change the decision in relation to ABC Ltd?

### **7 FGH LTD**

FGH Ltd is a trading company that provides its customers with 45 days trade credit on invoices. If the customers have not paid their invoice in the 45 days, FGH Ltd will charge late payment interest. Would FGH Ltd's activities come within the definition of finance and leasing?

### **8 ABC LTD**

ABC Ltd is considering the CIGA it performs in relation to its loan of £100,000,000 to its subsidiary CDE Ltd.

ABC Ltd had agreed its funding for the loan from a third party bank; its finance director and his deputy, had compiled the data required, met with a number of banks and negotiated a long term facility with one.

ABC Ltd's Board of Directors in setting the terms of the financing had set the amount it could lend to CDE Ltd, and the rate based on CDE Ltd's assets and expected income streams and ABC Ltd's own financial commitments and requirements for a return.

In order to do this, ABC Ltd had engaged the services of a professional to model different cashflow scenarios from the lending and the borrowing, so that ABC Ltd's Board could better understand the potential risks and rewards, enabling the Board to then ultimately make the final strategic decision.

ABC Ltd has set up a system in which a member of office staff on the Island ensures the information required to undertake the monitoring of both the payments of interest, and the financial data from CDE Ltd are provided in accordance with the agreement, with a process to escalate issues to the finance director.

The finance director takes the information provided and discusses with the Board of ABC Ltd the loan, and its own and CDE Ltd's performance, and ensures they take steps to manage any risks emerging.

Will ABC Ltd be regarded, for the purposes of the substance requirements, as conducting the CIGA in the Island?

## **9 XYZ LTD**

XYZ Ltd is a finance leasing company, it has one crane which it leases to an overseas connected company, and is considering the CIGA it performs for this finance leasing.

XYZ Ltd was funded by capital for its initial shares, which it used to acquire the crane, and has determined that it requires no additional funding.

XYZ Ltd had been introduced to the previous crane owners to acquire the crane. XYZ Ltd's Board of Directors approved the proposal to purchase the crane, however, the asset had been identified prior to XYZ Ltd's incorporation and no alternatives were considered once XYZ Ltd had been incorporated.

Whilst the Board of directors of XYZ Ltd considered the finance lease agreement that had been drawn up prior to the incorporation, they did not have the necessary knowledge and expertise to understand the terms of that lease agreement, and they did not seek appropriate specialist advice. Ultimately the Board of directors accepted the agreement as drafted and did not properly consider the terms.

XYZ Ltd outsource their monitoring to a professional adviser, who has a member of staff who spends up to half an hour a week reconciling the monies received as well as sending invoices etc. XYZ Ltd relies on the professional adviser to raise any issues, it does not monitor the professional advisor at all.

XYZ Ltd did not include clauses within the lease agreement to mitigate the risk of the lessee not making the lease payments, or the risk of the crane not being properly maintained or improperly used throughout the duration of the lease.

Will XYZ Ltd be regarded, for the purposes of the substance requirements, as conducting the CIGA in the Island?

## **FUND MANAGEMENT**

### **10 BLACK LTD**

Black Ltd is a company which undertakes fund management activities in relation to a number of funds which requires it to be licensed, as a fund manager, with the regulator. Is Black Ltd subject to the substance requirements?

### **11 WHITE LTD**

White Ltd is a fund in the Island, it has an administrator in the Island, Red Ltd. Are either of these companies subject to the substance requirements?

## **12 XYZ LTD**

A fund is established as a limited partnership in the Island and appoints a general partner (XYZ Ltd) who takes on the fund management role. XYZ Ltd outsources administrative activities to an administrator company, Service Ltd, which is also based on the Island. However, XYZ Ltd monitors and retains the ability to control the activities of Service Ltd. It is clear XYZ Ltd's directors collectively have the ability and knowledge to understand the fund and its investments, also to judge the activities of Service Ltd.

XYZ Ltd's Board takes the overarching strategic decisions as to the fund's investments, including such considerations as the mix of investment types, the markets and sector to be invested in. XYZ Ltd sets out these investment parameters and decides within these parameters how to implement these decisions. Two companies Euro GmbH (in the EU) and USA Inc (in the US) are appointed to acquire the investments in their regions, XYZ Ltd giving them limited discretion to act within the overall parameters it decided. The performance of Euro GmbH and USA Inc, including how they use this discretion, is carefully monitored by XYZ Ltd supported by Service Ltd.

XYZ Ltd requests frequent returns and reports to be provided to it from Service Ltd, Euro GmbH and USA Inc. These returns and reports assess the risks of the fund and also the reserves position. Service Ltd has to reassure XYZ Ltd that the processes and systems it has in place mean that the reports are accurate and comprehensive. Service Ltd collates these returns and reports so they give the overall risk position and overall reserves and provides to XYZ Ltd for incorporation in the Board's decision making, monitoring and control.

XYZ Ltd has taken the strategic view at the outset that hedging in respect of currency or interest rates was not appropriate based on the overarching strategy of the fund. This decision is however kept under review periodically by the Board.

Will XYZ Ltd be regarded, for the purposes of the substance requirements, as conducting the CIGA in the Island?

### **13 WHISP LTD**

A fund is set up in the Island and a company tax resident in the Island, Whisp Ltd, is appointed as the fund manager.

Whisp Ltd in turn appoints an investment manager company in the US, FMB Inc. Whisp Ltd's Board has sufficient knowledge and experience of the fund management business. Whisp Ltd provides FMB Inc with the prospectus of the fund, with full discretion for FMB Inc to make investment decisions for the fund within the scope of the prospectus. Despite having an adequately comprised board of directors, Whisp Ltd does not take any strategic decisions regarding the execution of the fund's investment strategy, including such considerations as the mix of investment types and the markets and sectors to be invested in, and does not set out the parameters of investment to FMB Inc. Instead, Whisp Ltd leaves all such strategic decisions to FMB Inc. Whisp Ltd also does not oversee FMB Inc's activities. In such circumstances it will not be possible to say that Whisp Ltd is carrying out the CIGA of taking decisions on the holding and selling of investments.

FMB Inc provides commentary and content for the reports which are then collated and sent to investors and regulatory authorities without further reference to, or review by, Whisp Ltd.

FMB Inc also calculates the risks and reserves and makes any decisions on currency/interest rate hedging. Again, Whisp Ltd has not taken any strategic decision in relation to these activities, and has not set out any parameters within which FMB Inc must operate.

Will Whisp Ltd be regarded, for the purposes of the substance requirements, as conducting the CIGA in the Island?

## **INSURANCE**

### **14 INSURANCE EXAMPLE CO LTD**

Insurance Example Co Ltd provides life insurance in and from the Island. Insurance Example Co Ltd undertakes all of its business in the Island and is regulated as an “insurer” for its own insurance business. Is Insurance Example Co Ltd subject to the substance requirements?

### **15 INTERMEDIARY EXAMPLE CO LTD**

Intermediary Example Co Ltd is an insurance intermediary providing services to the public via telephone and internet. Intermediary Example Co Ltd undertakes all of its business in the Island and is regulated as an insurance broker, but is not required to be regulated as an “insurer”. Is Intermediary Example Co Ltd subject to the substance requirements?

### **16 NON-LIFE INSURER EXAMPLE LTD**

Non-Life Insurer Example Ltd is a non-life insurer that provides policies to clients to insure against the risk of building damage. Non-Life Insurer Example Ltd outsources some of its CIGA to an insurance manager, PQR Ltd, which is also based on the Island.

However, Non-Life Insurer Example Ltd monitors and retains the ability to control the activities of PQR Ltd.

PQR Ltd employs specialist staff members in the Island to predict and calculate the risk associated with the policies that Non-Life Insurer Example Ltd provides. The board of directors of Non-Life Insurer Example Ltd meets regularly on the Island to consider the results and recommendations of this specialist analysis undertaken by PQR Ltd and make the decisions in relation to increases to premiums and changes to conditions of cover, etc.

Non-Life Insurer Example Ltd also outsources other non CIGA activities outside of the Island, in the location of the assets insured. Global1 Ltd is appointed to handle overseas claims up to specific limits and is the loss adjuster appointed to investigate large, complex or contentious claims on overseas buildings. Global2 Ltd is appointed to provide some aspects of treasury functions. The performance of Global1 Ltd and Global2 Ltd, including ensuring they comply with the specific limits, is carefully monitored by Non-Life Insurer Example Ltd, supported by PQR Ltd.

Will Non-Life Insurer Example Ltd be regarded, for the purposes of the substance requirements, as conducting the CIGA in the Island?

## **17 THIN NON-LIFE EXAMPLE LTD**

Thin Non-Life Example Ltd is a non-life insurer which outsources some of its activities to another group company, GroupCo Ltd, which is based in the UK.

GroupCo Ltd predicts and calculates the risks associated with the policies Thin NonLife Example Ltd provides. GroupCo Ltd also advises on the risks of insuring particular customers, preparing regular reports for the Board of Thin Non-Life Example Ltd. The reports, recommendations and commentary are collated by staff working for Thin NonLife Example Ltd and are regularly implemented without amendment by the Board of Thin Non-Life Example Ltd and without evidence of due consideration.

Will Non-Life Example Ltd be regarded, for the purposes of the substance requirements, as conducting the CIGA in the Island?

## **18 LIFE INSURER EXAMPLE LTD**

Life Insurer Example Ltd is an insurer in the life sector, providing single premium life insurance. The insurance provides a guaranteed death benefit for the policyholder.

Life Insurer Example Limited employs a team of staff to maintain and service the client accounts from the company's offices in the Island.

The maintenance and servicing of client accounts undertaken by the employees includes setting up the client accounts, ensuring that the premiums are invested, monitoring the performance of the investments, preparing annual statements on policy performance, dealing with client transactions related to the policy, such as permitted terminal illness claims and processing claims made on the death of a policyholder.

In line with the terms of the regulatory framework in the Island, the regulator in the Island is satisfied that the senior management are fit and proper to undertake/supervise the work that they have been employed to do/have oversight of.

Life Insurer Example Ltd outsources the CIGA to another company within the same group. That company is also located in the Island and has a team of specialist qualified employees who provide these services to Life Insurer Example Ltd and other life insurers in the group. That company performs underwriting functions (i.e. choosing who Life Insurer Example Ltd will insure) and manages the prediction and calculation of risk (i.e. oversees the calculation of the likelihood of the insured event occurring and the likely costs).

Life Insurance Example Ltd outsources HR and IT services, which are not CIGA, to other group companies both in and outside of the Island.

Will Life Insurer Example Ltd be regarded, for the purposes of the substance requirements, as conducting the CIGA in the Island?

### **19 THIN LIFE EXAMPLE LTD**

Thin Life Example Ltd is a self-managed life insurer which offers the same single premium life policies as Life Insurer Example Ltd. However, only the board of directors of Thin Life Example Ltd are present in the Island. The board of directors have sufficient knowledge and experience of the insurance market for the company to be regulated as an insurer.

The underwriting and client account management functions are outsourced to another group company UK Group Service Example Ltd which is based in the UK. Suitably qualified employees of UK Group Service Example Ltd provide all services at its premises in the UK.

UK Group Service Example Ltd predicts and calculates the risks associated with the policies Thin Life Example Ltd provides, also advising on the risks of insuring particular customers, preparing regular reports for the Board. The reports, recommendations and commentary are regularly implemented without amendment by the Board of Thin Life Example Ltd and without evidence of due consideration.

Will Thin Life Example Ltd be regarded, for the purposes of the substance requirements, as conducting the CIGA in the Island?

### **DISTRIBUTION AND SERVICE CENTRE**

#### **20 ABC LTD**

ABC Ltd buys CDs from other group companies based in Asia and re-sells them to other group companies and customers in Europe. Is ABC Ltd subject to the substance requirements?

#### **21 DEF LTD**

DEF Ltd's main activity is to provide administration services to another group company based in the UK, which are recharged at cost. Is DEF Ltd subject to the substance requirements?

#### **22 FGH LTD**

FGH Ltd is the service company for an audit and accountancy partnership that's main activity is to provide services to customers on the Island. FGH Ltd employs the staff and also owns the premises used for the business of the partnership. Another group company based in the UK requires specialist IT skills which sit within FGH Ltd and requests those skills for a period of 3 months, agreeing to reimburse costs. Is FGH Ltd subject to the substance requirements?



### **23 ABC LTD**

ABC Ltd provides administrative services to other non-resident group companies. It employs qualified individuals in the Island who record how their time is spent, in order that this can be billed to the relevant company at the agreed rate. The directors of ABC Ltd will recruit and train employees according to the anticipated needs of other group companies. Will ABC Ltd be regarded, for the purposes of the substance requirements, as conducting the CIGA in the Island?

### **24 XYZ LTD**

XYZ Ltd is a distribution company based on the Island, responsible for the distribution of raw materials purchased from group entities in Asia, to other group entities based in Europe. XYZ Ltd contract transportation of goods to another non-resident company LMN Ltd based off island. Goods are then stored in a UK warehouse by a third party company STO Ltd, who liaise directly with LMN Ltd over deliveries. The board of XYZ Ltd do not oversee the activities of LMN Ltd nor STO Ltd. Will XYZ Ltd be regarded, for the purposes of the substance requirements, as conducting the CIGA in the Island?

## **HEADQUARTERING**

### **25 ABC LTD**

ABC Ltd based on Island, is part of a group, with subsidiaries around the world. The senior management team each have responsibility for a different region, and will regularly spend time at the subsidiaries with the senior management teams providing strategic direction and helping manage material risks. Is ABC Ltd subject to the substance requirements?

### **26 FGH LTD**

FGH Ltd is a trading company based on Island that has subsidiaries in the UK. Whilst the senior management team of FGH Ltd have regular dialogue with staff at the subsidiaries, the senior management team of each subsidiary set their strategic direction and manage risks in line with the corporate policy set by the headquarters based in the USA. Is FGH Ltd subject to the substance requirements?

## **27 ABC LTD**

ABC Ltd based on Island, is the regional headquarters for a global group.

The directors of ABC Ltd are responsible for the success of the region, setting the strategic direction and managing risk. The senior management team of ABC Ltd each have responsibility for a different area within the region, and regularly spend time with the leadership teams of the subsidiaries providing strategic direction and helping manage material risks.

ABC Ltd takes specialist advice on matters of compliance relevant to the region, with staff disseminating that advice and co-ordinating activities to ensure compliance by all subsidiaries.

Each quarter the directors will review the regional performance and risk profile, ensuring they take steps to manage any risks.

Will ABC Ltd be regarded, for the purposes of the substance requirements, as conducting the CIGA in the Island?

## **28 ZYX Limited**

ZYX Ltd based in the Island is the headquarters for a small group of non-Island companies. ZYX provides the senior management team, assumes and controls risks for the activities and assets of the group companies and provides advice to the group companies on the control of risk.

The board of directors of ZYX Ltd act as the senior management team for the group companies. All members are resident outside the Island.

Although they hold an annual board meeting in the Island, all the relevant management decisions are taken outside the Island.

All meetings, deliberations and decisions in relation to the incurring of expenditures on behalf of group entities take place outside the Island.

Will ZYX Ltd be regarded, for the purposes of the substance requirements, as conducting the CIGA in the Island?

## **SHIPPING**

### **29 FERRYBOAT LIMITED**

FerryBoat Limited owns a passenger ship and its business is to operate that ship in international traffic to carry passengers from port A in Spain to port B in Greece. Is FerryBoat Limited subject to the substance requirements?

### **30 CREWMANCO LIMITED**

CrewManCo Limited provides and manages the crew of FerryBoat Limited's ship as part of its crew management business, but it does not operate ships. Is CrewManCo Limited subject to the substance requirements?

### **31 SHIPOWNCO LIMITED**

ShipOwnCo Limited owns a ship and charters it on a bareboat charter basis to CharterCo Limited. ShipOwn Co Limited does not operate that ship, or any other ship. Is ABC Ltd subject to the substance requirements? Is ShipOwnCo Limited subject to the substance requirements?

### **32 CHARTERCO LIMITED**

CharterCo Limited uses the ship it has chartered on a bareboat charter basis in its own ship operation business, to carry cargo from a port in country A to a ports in a number of other countries. Is ABC Ltd subject to the substance requirements? Is CharterCo Limited subject to the substance requirements?

### **33 COMPANY G**

Company G operates a fleet of three ships transporting passengers from Port A in Spain to Port B in Greece.

It *manages the crew* of all three vessels from its leased offices in the Island.

6 staff members in the Island are responsible for ensuring that there is sufficient crew available at all times, that the crew members hold all necessary certificates, for coordinating renewals of appropriate crew certifications etc., for overseeing the wage claims and the payment of crew, although physical payments are made to the crew via a third party paying agent.

The company undertakes the technical management of its ships from the Island, employing specialist staff members to organise and oversee the voyages.

The board of directors of Company G hold relevant technical qualifications and meet regularly with the specialist staff members to consider the strategic direction of the business and to make the necessary financial decisions to support the continued operations.

The maintenance of the vessels is undertaken in specialist shipyards outside the Island, operated by independent third parties.

Will Company G be regarded, for the purposes of the substance requirements, as conducting the CIGA in the Island?

### **34 COMPANY H**

Company H operates a fleet of three ships transporting passengers from Port A in Spain to Port B in Greece.

It outsources the technical management of the vessels and the management of crew to parties outside the Island, who make all of the decisions in relation to the operation of the ship.

The board of directors of Company H are not technically qualified and meet only twice a year to review the company's operating position and rely completely on the services and advice of the parties that the technical and crew management is outsourced to in order to make decisions.

Will Company H be regarded, for the purposes of the substance requirements, as conducting the CIGA in the Island?

## **IP COMPANY**

### **35 BRANDCO**

BrandCo holds a brand, the rights for which are licensed to others in return for a licence fee. Is BrandCo subject to the substance requirements?

### **36 DRINKCO**

DrinkCo has a trademarked range of fizzy beverages, which it manufactures and markets to unrelated third parties. Is DrinkCo subject to the substance requirements?

### **37 KNOWHOWCO**

KnowHowCo developed a unique IT software platform for accepting, processing and tracking online orders that it holds and uses within its own business of online marketing and also licences to others to use within their online marketing businesses. Is KnowHowCo subject to the substance requirements?

### **38 SUBLICENCECO**

SubLicenceCo has a licence to use or exploit copyrighted software developed by fellow group company DevelopCo, both companies are resident in the Island. SubLicenceCo sub-licences the right to use or exploit the copyrighted software to two unrelated companies outside the Island. The unrelated companies pay SubLicenceCo a licence fee in order to use the copyrighted software, and SubLicenceCo pays a fee to DevelopCO for its licence to use the copyrighted software. Is SubLicenceCo subject to the substance requirements?

### **39 PATCO**

PatCo holds a patent which it licences to foreign related parties around the world. The directors of PatCo are resident in the Island and make all of the strategic decisions in relation to the development, maintenance and enhancement of the patent in the Island.

All of the “research and development” activities required to create the patent were undertaken in the Island by PatCo employees. Employees involved hold technical qualifications relevant to the work undertaken.

PatCo employees in the Island undertake all necessary maintenance and enhancement work to retain the value of the patent it holds.

Will PatCo be regarded, for the purposes of the substance requirements, as conducting the CIGA in the Island?

#### **40 PATOFFISLANDCO**

PatOffIslandCo holds a patent which it licences to unrelated foreign parties around the world.

Some of the directors of PatOffIslandCo are resident in the Island but the majority are resident where the activities take place, and all the strategic decisions in relation to the development, maintenance and enhancement of the patent actually take place outside the Island, at the locations where the company's activities take place.

All of the "research and development" activities required to create the patent were undertaken in various locations outside the Island. Employees involved hold technical qualifications relevant to the work undertaken.

PatOffIslandCo does not undertake maintenance and enhancement work to retain the value of the patent.

Will PatOffIslandCoCo be regarded, for the purposes of the substance requirements, as conducting the CIGA in the Island?

