Economic Substance Regulations

cBrain's F2 Solution for Managing and Enforcing Compliance
with the Economic Substance Regulations (ESR)

cBRAIN
The Process Company

ESR - Background

- **Regulations** to ensure corporations have an adequate 'economic presence' in-country, i.e., not just a 'shell company'.
- Intended to **combat base erosion and profit shifting** (BEPS).
- Applies to about **40,000 companies** in 11 relevant industries.
- Two-step annual filing process: **Notification and full Report.**
- Some companies are exempt from full Report.
- High-risk companies are selected for audit.
- **Companies** that meet certain criteria or fail to demonstrate economic substance are reported back to their home country's tax authorities.

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Key Accomplishments on the Project

- Only **3 months** from contract award to system go-live.
- **39 different government agencies** with different domains and directories needed to access 1 unified solution to review cases.
- **Enforcing ESR** is shared responsibility across multiple stakeholders.
- **New digital identity system for corporations**, e.g., no CVR number or federal tax ID number was in place.
- Large number of reports would overwhelm auditors, without some tools to help them prioritize high-risk cases.
- **OECD reporting** schema for nominal tax jurisdictions (NTJ) was quite new and complex but now **significantly simplified.**

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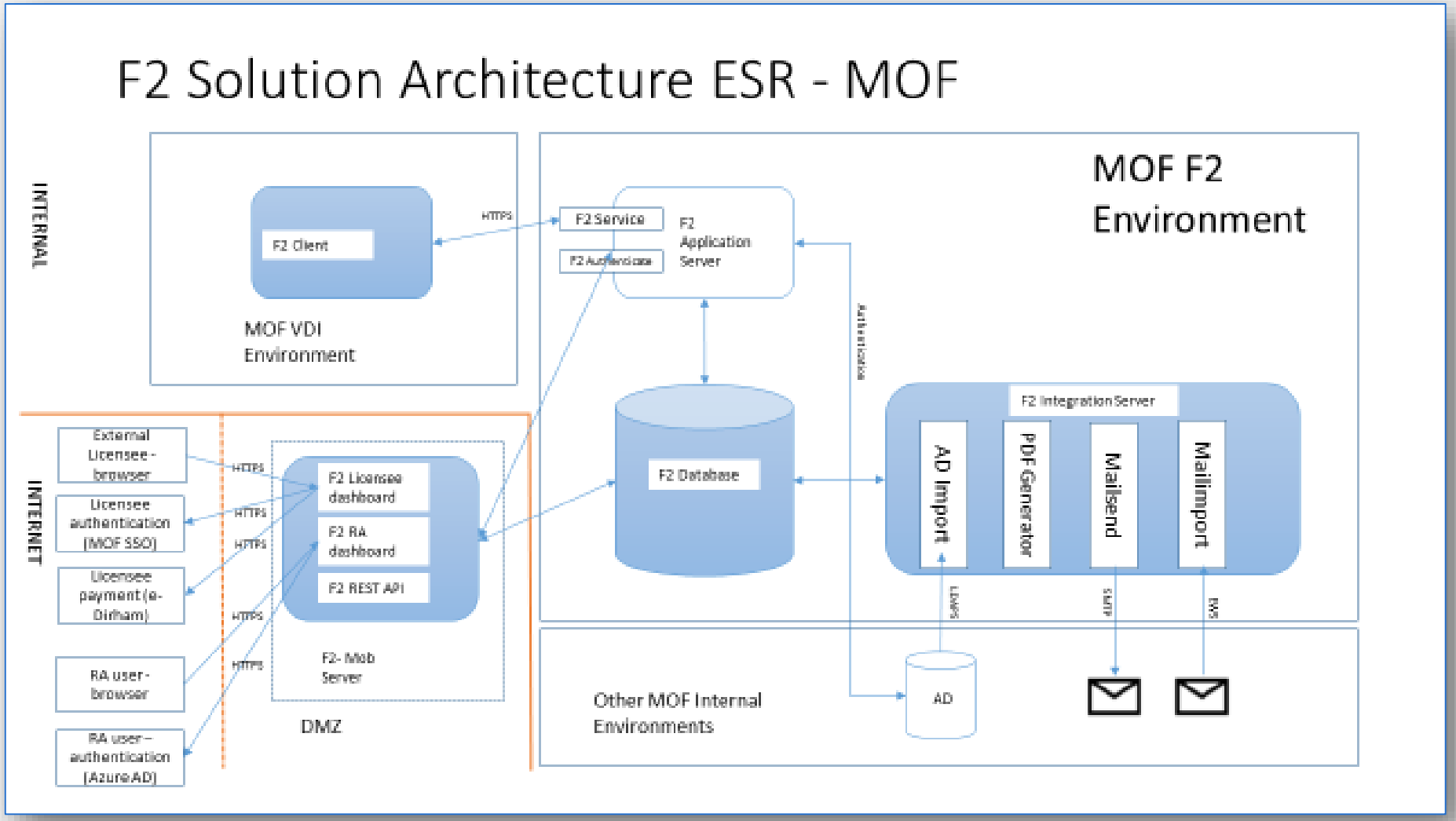
Infrastructure Architecture



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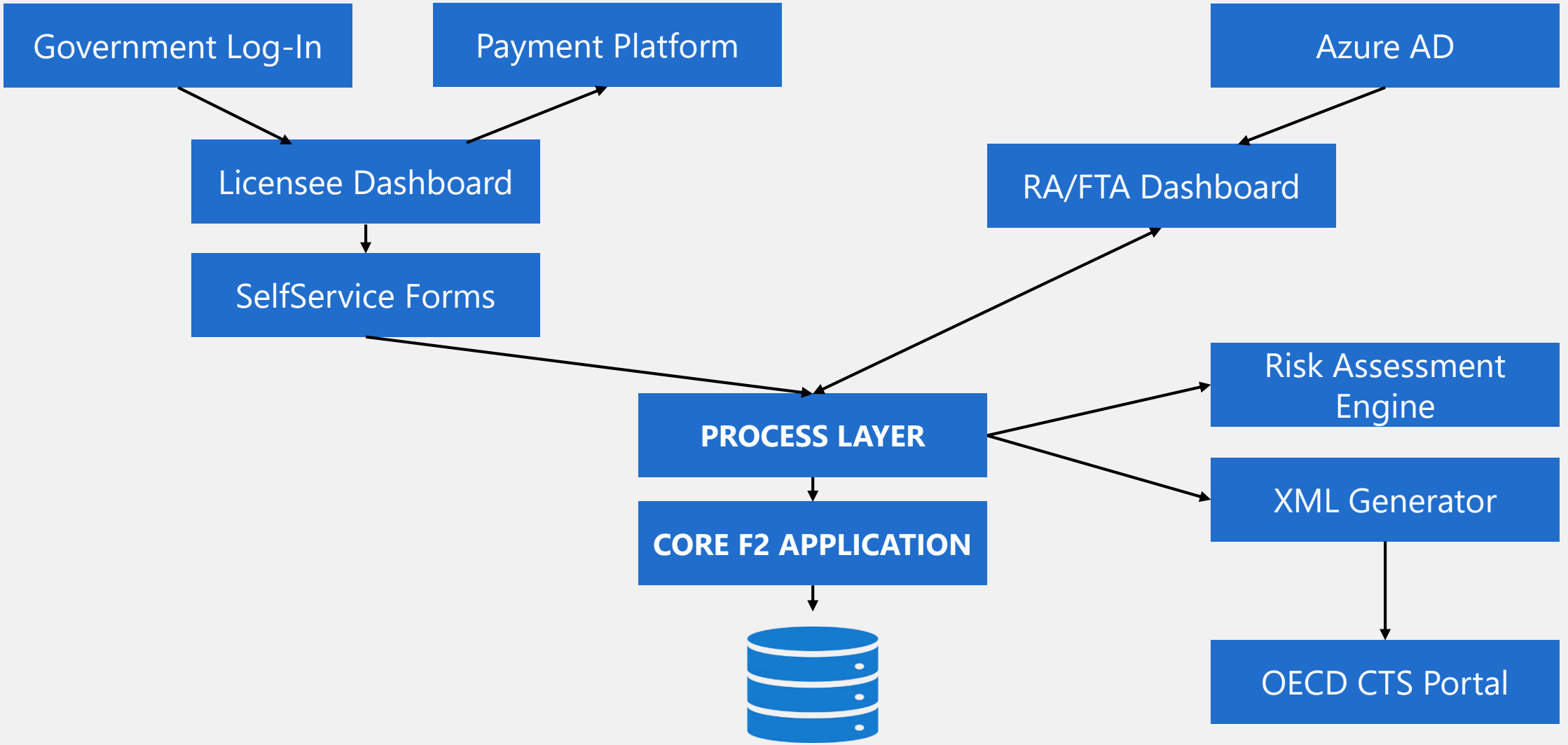
Map of Services and Interfaces



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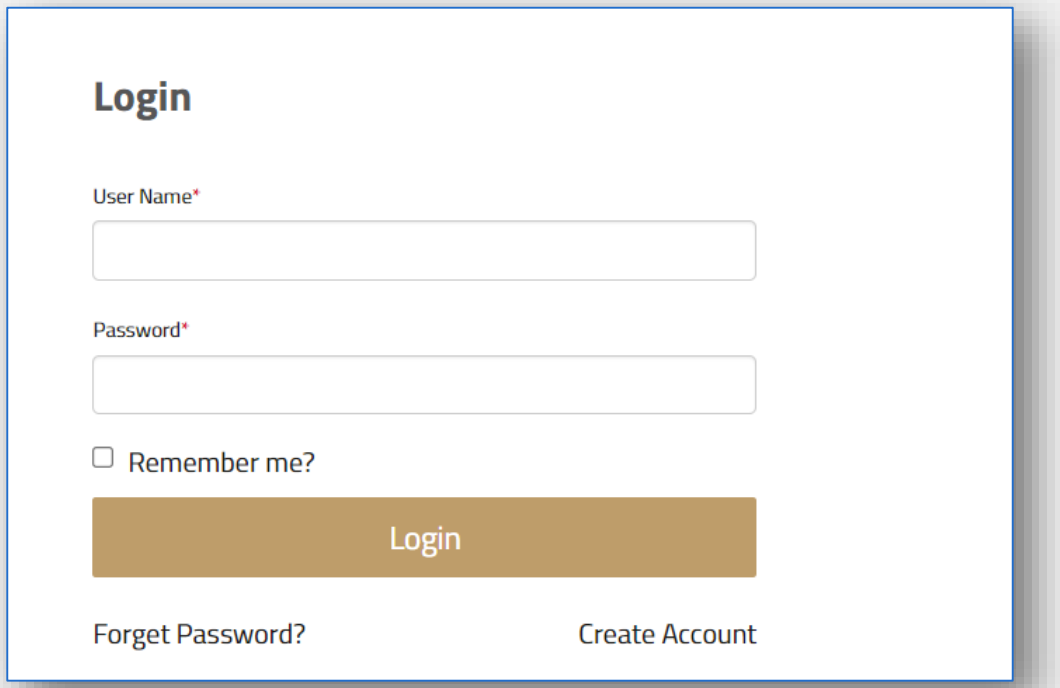
Company (Licensee) Perspective

Log in from Ministry of Finance webpage with government account.



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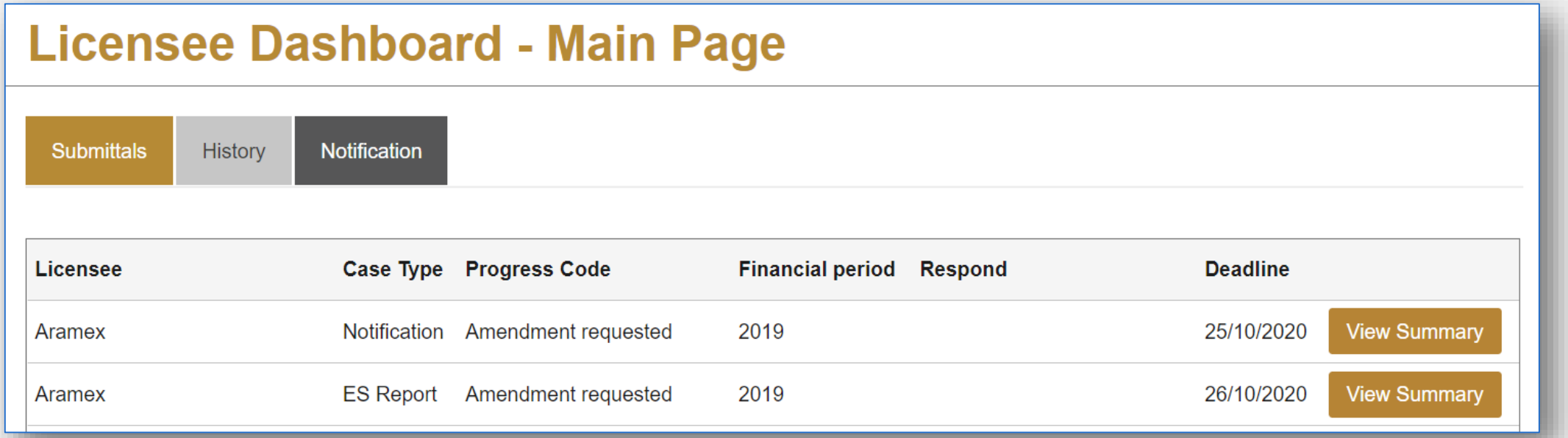
Company (Licensee) Perspective

Access dashboard to:

- Start a new Notification
- Manage existing filings



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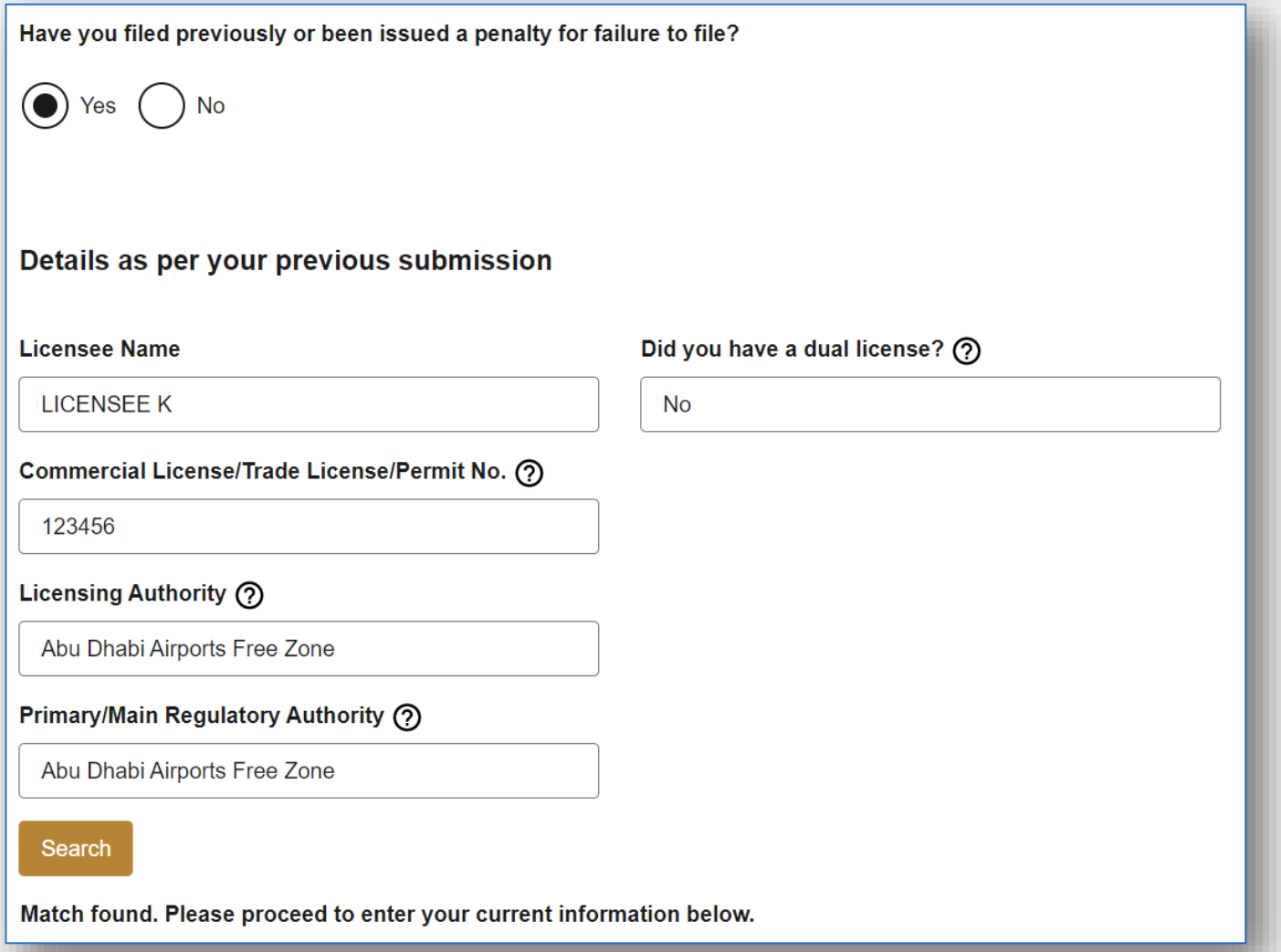
Company (Licensee) Perspective

- **User** is guided through intuitive forms to fill and submit the Notification and Report.
- **Notification** begins with questions that ensure the filing is linked to the company's previous filings.
- **System** builds a picture of the company's compliance history year after year – even if a different consultant or accountant is filing on their behalf.



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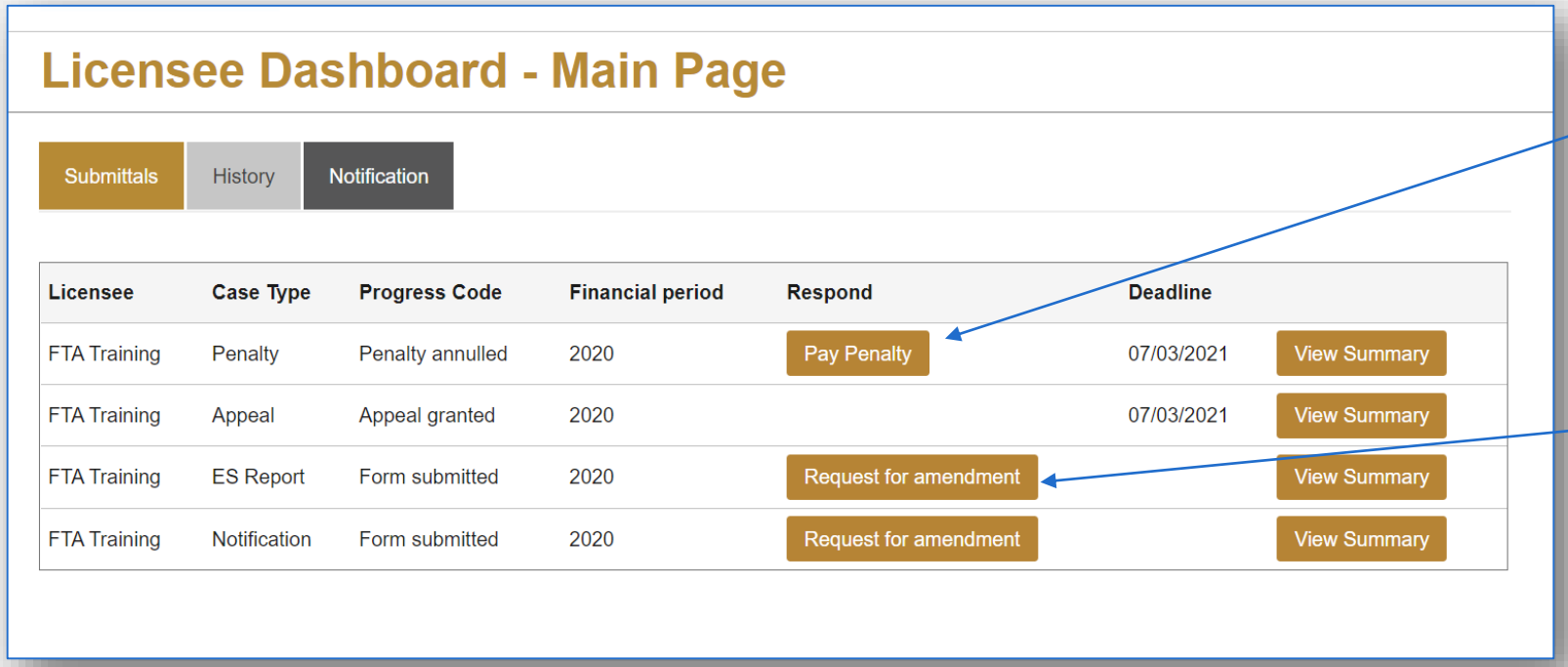
Company (Licensee) Perspective



Company can also use the dashboard to:

- Pay penalties levied against them, via a link to a third-party payment platform.
- Respond to official information requests.
- File appeals of penalties they dispute.
- Request to amend their previous filings.

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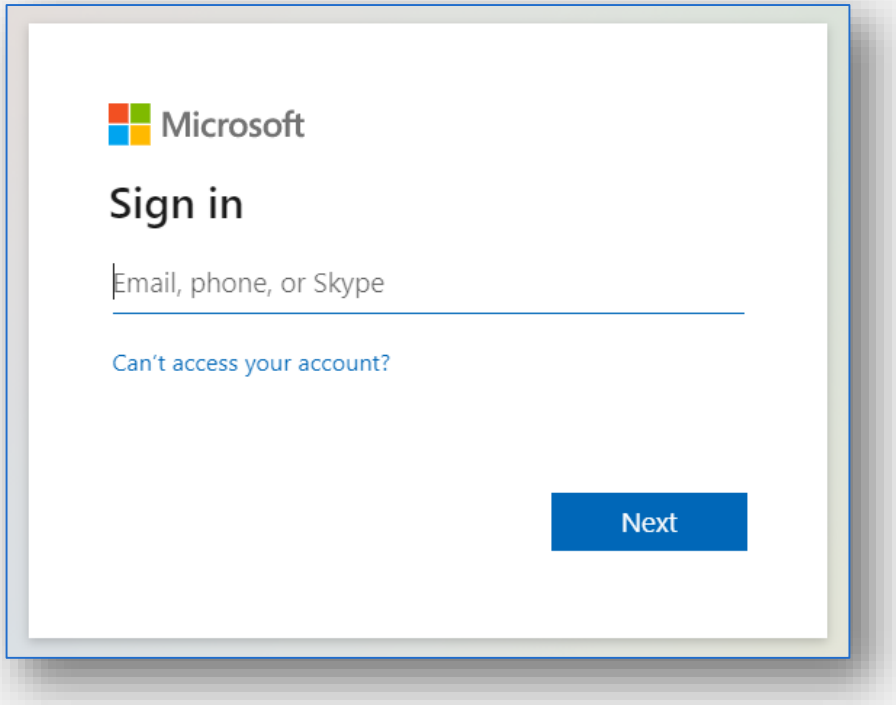
Regulatory Authority (RA) Perspective

Log in with government email address and password.
Multi-factor authentication enforced.



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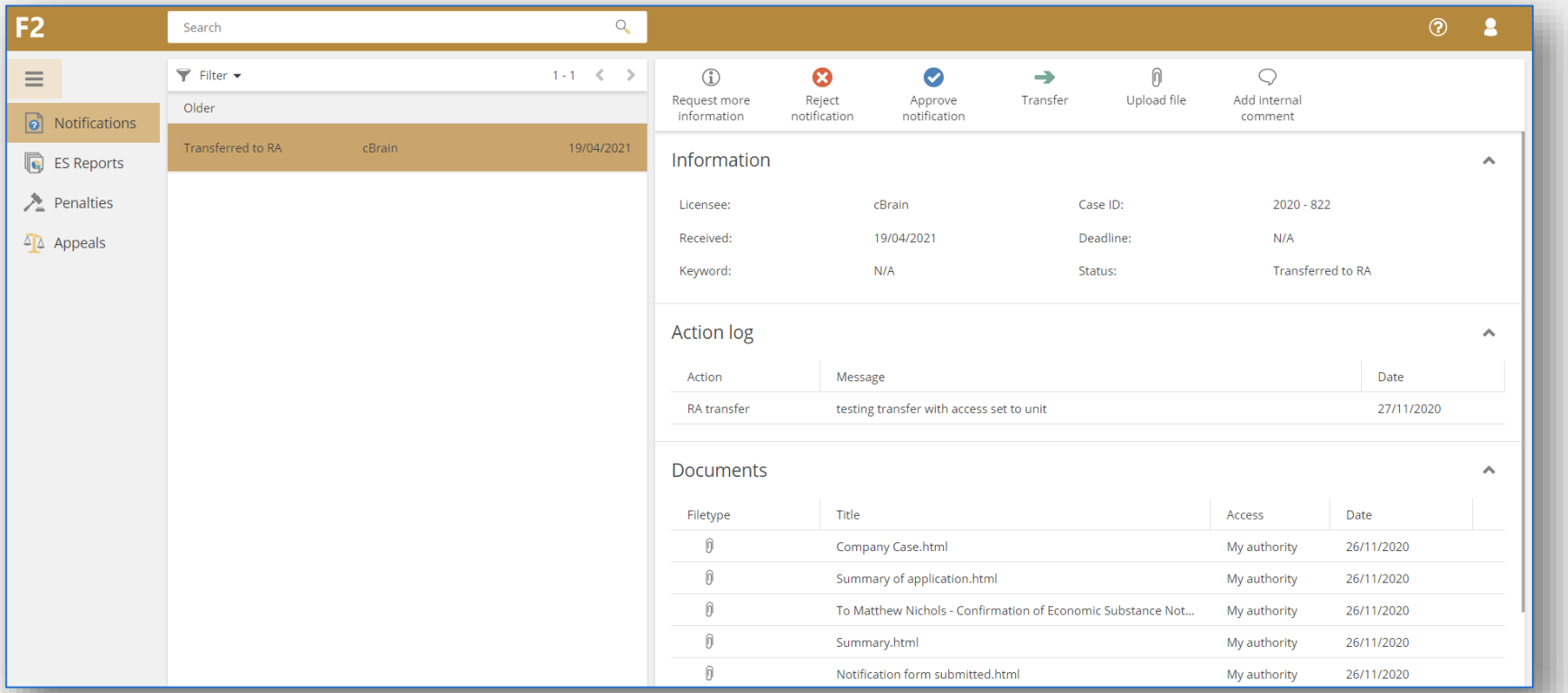
Regulatory Authority (RA) Perspective

- Each of **37 authorities** sees a list of only filings from companies under their jurisdiction.
- **Case manager** can review the company's filing and accept, reject, transfer, or request more information.
- **All actions are logged and fully auditable.** Cases can be searched and filtered by status and keywords.
- **Users** in each authority with special permissions can cancel cases and generate overview reports.



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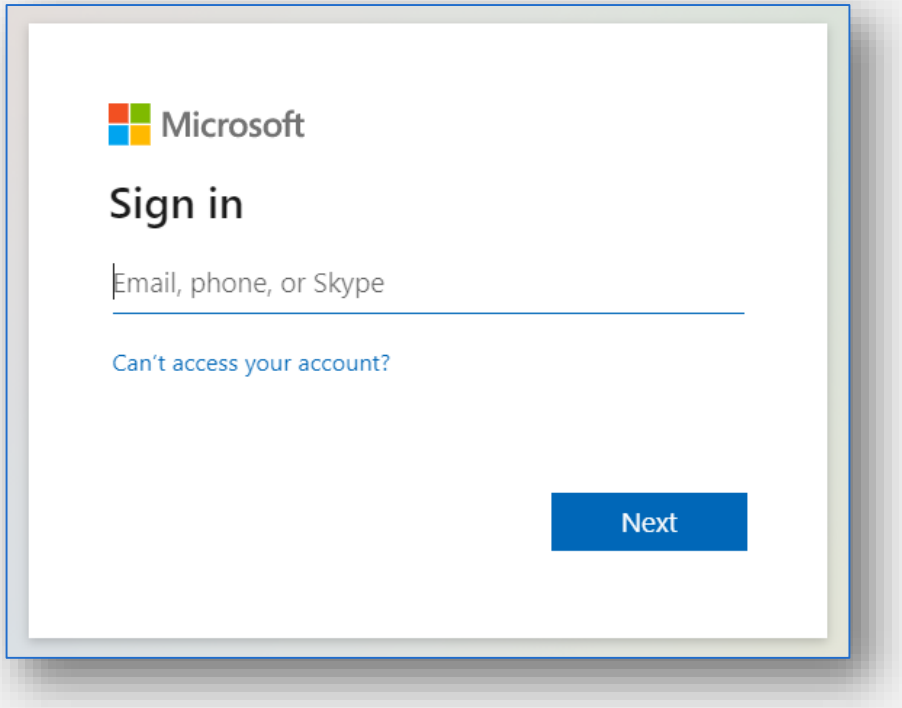
Federal Tax Authority (FTA) Perspective

Log in with government email address and password.
Multi-factor authentication enforced.



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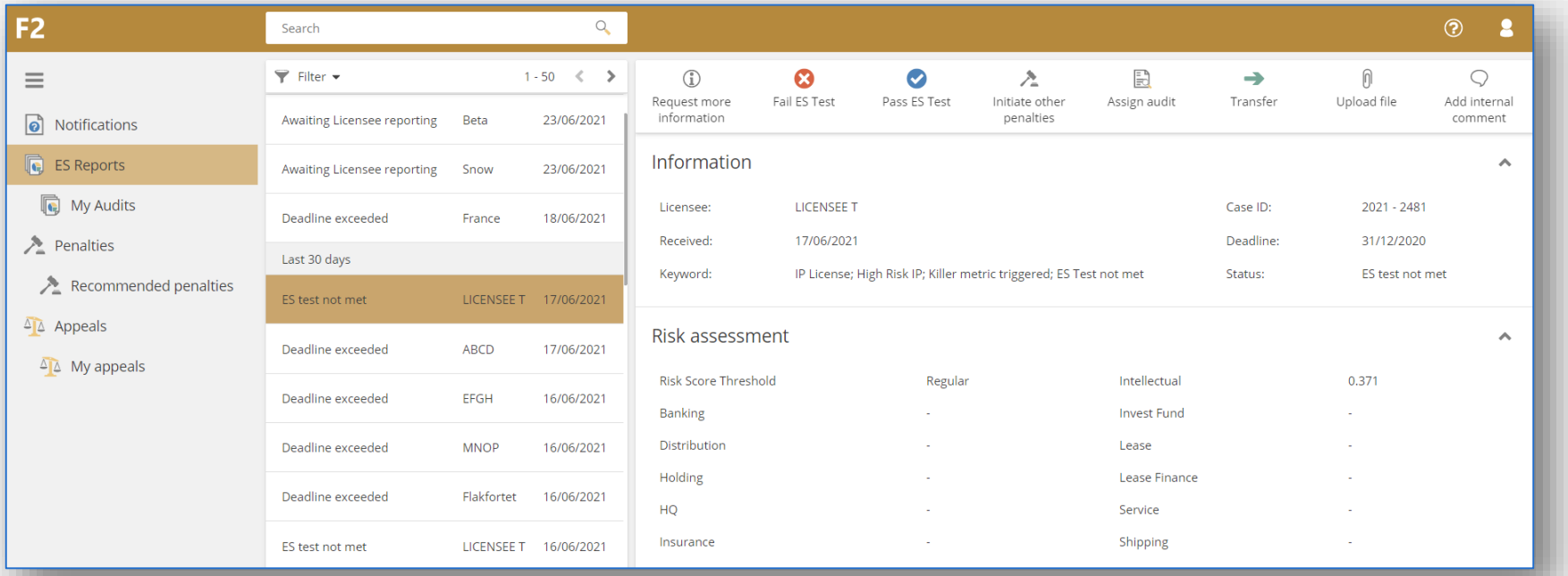
Federal Tax Authority (FTA) Perspective

FTA HAS ACCESS TO ALL FILINGS FROM ALL 37 AUTHORITIES.

Specific job roles within the FTA can perform distinct functions:

- **Auditors:** review high-risk ES Reports and provide a recommendation about their economic substance.
- **Senior Auditors:** review the Auditor's decision and make a final determination on the case.
- **Appeal Managers:** review appeals submitted by companies against their penalties and grant or deny them.
- **FTA** can also request more information from the company at any point in the process.



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Risk Assessment Engine

As shown below, a decision-support tool – the Risk Assessment Engine – helps prioritize companies for the FTA to audit.

- Companies that fail any of **13 key criteria** (*below right*) are flagged as **'Killer metric triggered'** for mandatory audit.
- **The engine also calculates a detailed Risk Scorecard** (*below left*) with the normalized risk level (scale of 0 to 1) for each company compared to its peers in that industry, plus an overall threshold (Regular, Substandard, or Critical).

	A	B	C	D	E	G	H	I	J	K	L	M
1	Dimensi	Rul	Activatio n Flag	Criteria/Ratio	Calculation Method	Outp ut	le Compar ed to	Weigh	Absolu te Score	Weight ed Score	Minimum Theoretical Score	Maximum Theoretical Score
2	1	1	N	Income to expense ratio	Relevant gross income from the Relevant Activity / Relevant gross expenditure from the relevant activity	1,167	22	0,00%	1	0,000	0,000	0,000
3	1	2	N	Income to FTE ratio	Activity / Avg. number of FTE employee (incl. outsourced)	514,66	77	0,00%	4	0,000	0,000	0,000
4	1	3	Y	Expense to FTE ratio	Relevant Activity / Avg. number of FTE employee (incl. outsourced)	441,14	77	10,00%	4			
5	1	4	Y	Outsourced FTE to total FTE ratio	Sum of avg. number of outsourced FTE employee across outsourcing providers /Avg. number of FTE employee (incl. outsourced)	0	11	10,00%	1			
6	1	5	Y	Outsourcing expenses to total expenses ratio	Expenditure incurred on Outsourcing Providers / Relevant gross expenditure from the Relevant Activity	0	11	10,00%	1			
7	2	6	N	Percentage change in Income to Expense ratio	Percentage change of Relevant Gross Operating Income / Relevant Gross Operating Expenditure (Current period vis-à-vis Last reportable period)							
8	2	7	N	Percentage change in Income to FTE ratio	Income / Avg. number of FTE employee (incl. outsourced) (Current period vis-à-vis Last reportable period)							
9	2	8	N	Percentage change in Expense to FTE ratio	Expenditure / Avg. number of FTE employee (incl. outsourced) (Current period vis-à-vis Last reportable period)							
10	2	9	N	Percentage change in Outsourced FTE to total FTE ratio	FTE employee / Avg. number of FTE employee (incl. outsourced) (Current period vis-à-vis Last reportable period)							
11	2	10	N	Percentage change in Outsourcing expenses to total expenses ratio	Outsourcing Providers / Relevant Gross Operating Expenditure (Current period vis-à-vis Last reportable period)							
12	3	11	Y	Claimed false exemption status in last five years	Licensee claimed exemption status but the claim was not accepted by a Regulatory Authority	N	-	10,00%	1			
13	3	12	Y	Missed Notification filing in current	Licensee failed to file a Notification on time	Y	-	10,00%	4			
14	3	13	Y	No: of times missed Notification filing in last five years	No. of times licensee failed to file a Notification on time in the last five years	1	-	10,00%	2			
15	3	14	Y	Late ESR Report filing in current	Licensee failed to file an ESR Report on time	Y	-	10,00%	4			
16	3	15	Y	No: of times missed ESR Report filing in last five years	No. of times licensee failed to file an ESR Report on time in the last five years	1	-	10,00%	2	0,200	0,100	0,500
17	3	16	Y	pass the verification by RAs - in last five years	Average number of resubmissions to finalize ESR Report in last five years	0	-	10,00%	1	0,100	0,100	0,500
18	3	17	Y	If current year reporting is the first reporting	If current ESR Report is the first ESR Report submitted by the Licensee	Y	-	10,00%	3	0,300	0,100	0,300
19	ABSOLUTE RISK SCORE									2,300		
20	NORMALIZED RISK SCORE									0,3714	1,000	4,500

	A	B	C
1	Dimension	Rule Description	Determination
2	IP Business	Licensee carried out Intellectual Property business during the reportable period	Yes
3	High Risk IP Business	Licensee self certifies it is a High Risk IP Licensee and elects to rebut the presumption it has failed	Yes
4	Core Income Generating Activity (CIGA)	Licensee does not conduct any Core Income-Generating Activity (CIGA) in the UAE	No
5	Directed and Managed	No board meetings held in the UAE during the Reportable Period	No
6		No directors physically present in the UAE for the board meetings held in the UAE	No
7		No strategic decisions were made during the board meetings held in the UAE	No
8		Board meetings minutes and company records are not maintained in the UAE	No
9		Board of directors do not have necessary knowledge and expertise to discharge their duties	No
10	Outsourcing	Licensee does not have adequate supervision of the CIGA carried out by the Outsourcing Provider	No
11		The CIGA was not carried out exclusively in the UAE by the Outsourcing Provider	No
12	Adequate Qualified Employees	No employee (incl. outsourced and contractual) in the UAE, but Licensee generates revenue	No
13	Adequate Operating Expenditure	No operating expenditure in the UAE, but Licensee generates revenue	No
14	Compliance History	Failed ESR test in last reportable period	No
15	**Audit Required?**		Yes

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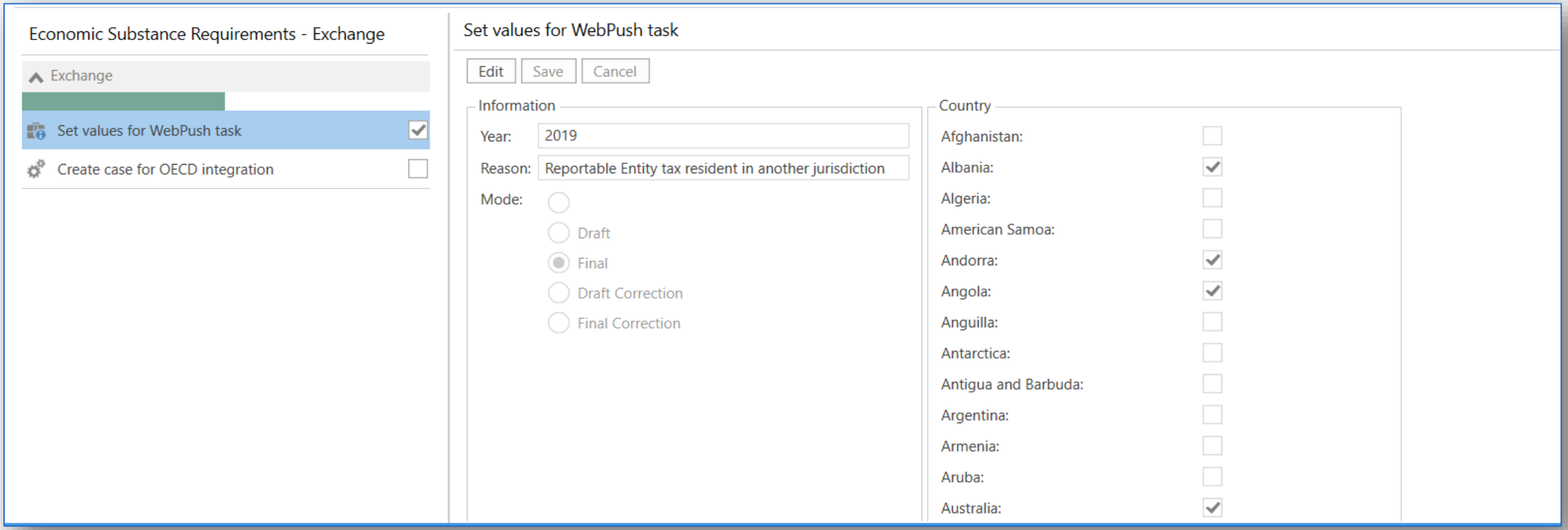
Ministry of Finance (MOF) Perspective

IN THE F2 DESKTOP CLIENT, **MOF CAN ACCESS ALL CASES**, ADMINISTER THE SYSTEM, AND GENERATE DATA EXCHANGES VIA THE OECD CTS PORTAL.

MOF uses the case guide feature to **select parameters for the data exchange,** including the tax year, 1 of 7 reporting reasons under the NTJ schema, and one or more participating countries to receive the data.



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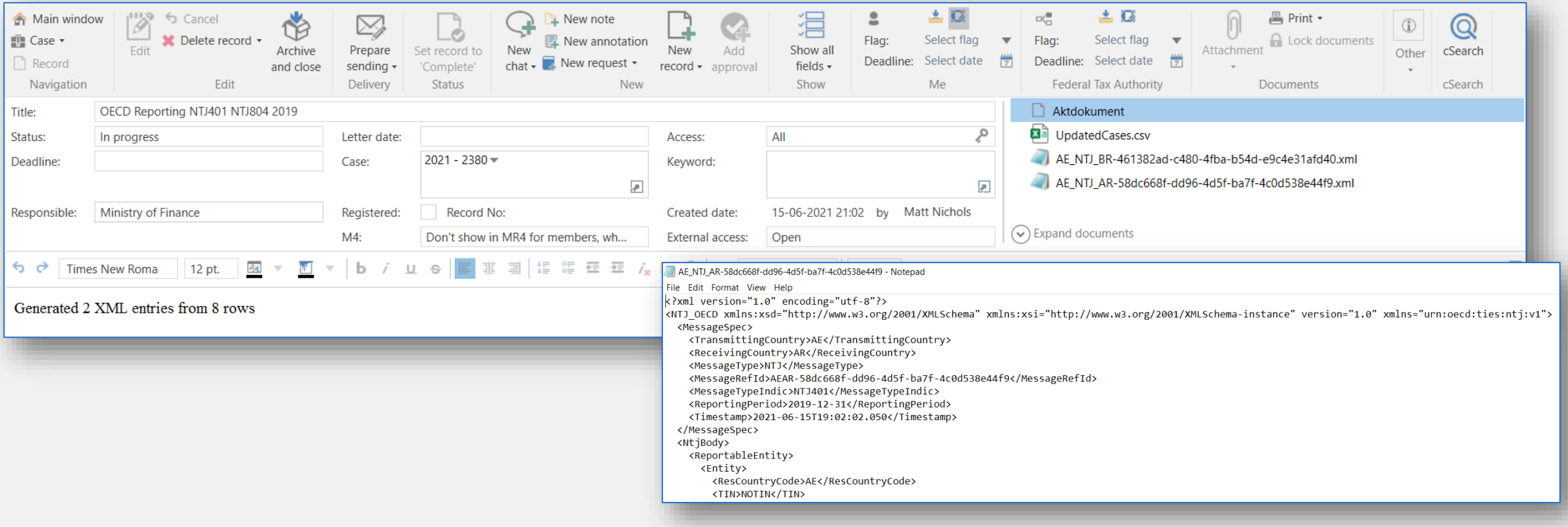
Ministry of Finance (MOF) Perspective

F2 QUERIES THE DATABASE OF FILINGS, RETURNS THOSE THAT MATCH THE PARAMETERS, AND GENERATES XML FILES TO PACKAGE, ENCRYPT, AND UPLOAD TO THE OECD CTS PORTAL FOR EACH COUNTRY.

The system also includes **tools to correct previously sent XML files** – either automatically or upon request from the receiving country.



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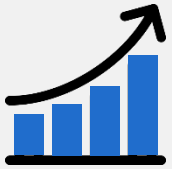

Summary and Project Benefits

- Ensured the client remained in **compliance with OECD requirements** on a very tight timeline – 3 months from kick-off to go-live.
- **Enabled +30,000 companies to file within 1 month of launch.**
- Brought together **39 government agencies on 1 unified platform** – no information silos, 1 common source of truth.
- Onboarded **more than 200 government users** to manage cases.
- Staffed a level 1 help desk that provided timely **(< 1 day response time**) support in multiple languages.
- By linking filings using a 'company case', **built a first-of-its-kind register of all companies in the country.**

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