



# Global tax newsletter

Welcome to this edition of the Global tax newsletter where we will look at what some of the tax authorities have been up to for the past few months.



You will see in our tax policy tab that the Organisation for Economic Co-operation and Development's (OECD's) Business Advisory Committee (BIAC) issued a document covering suggested best practices for engaging with tax authorities in developing countries, and a statement covering tax principles for international business.

In this edition we also have three different feature articles: recent changes in Belgium for the taxation of Belgian corporate repatriations; a recent decision in the United States (US) concerning software transactions in foreign subsidiaries and the ability to defer such revenue streams; and finally significant new tax proposals in Mexico.

In our regional updates there are a number of cases recently dealing with exit taxation, controlled foreign corporate regimes, and thin capitalisation developments. It is interesting to note that these are also agenda items for the OECD in its Base Erosion Profit Shifting (BEPS) working party.

Our transfer pricing tab has an interesting discussion of a French case dealing with the emigration of a treasury centre which could have widespread applicability to many kinds of captive special purpose corporate vehicles.

The indirect tax tab includes the Finnish supreme court dealing with the question of an input tax credit paid by the taxpayer's parent corporation, a frequent transaction occurring in any multi-national group.

Finally, in our treaty tab there is a discussion of what the Netherlands intends to do with its tax transparency programme in terms of its treaties with developing countries.

I hope you find this edition of the Global tax newsletter to be both enjoyable and informative.

---

**Francesca Lagerberg**  
Global leader – tax services  
Grant Thornton International Ltd

## Go to page...

[2 Belgium featured article](#)[3 Mexico featured article](#)[4 United States featured article](#)[5 EMEA news](#)[14 APAC news](#)[20 Americas news](#)[26 Transfer pricing news](#)[29 Indirect taxes news](#)[32 Treaty news](#)[34 Tax policy](#)[37 Who's who](#)

# Belgium featured article



Belgium recently enacted new changes to the taxation of liquidation proceeds; withholding tax on dividends linked to newly contributed share capital, the notional interest deduction and the patent income deduction.

Belgium has recently enacted new changes to taxation.

A summary of the changes includes:

- liquidation proceeds to be subject to a 25% withholding tax (compared to the actual 10%) in order to bring it in line with the standard withholding tax rate of 25% that applies to dividend payments
- exemptions or reductions based on internal tax law or due to double taxation agreements (DTAs) that remain in place
- an established transitional regime offering the possibility to transform taxed reserves (ie carried forward profits) into share capital whereby a 10% withholding tax will be due immediately
- taxed reserves which are transformed into share capital under this transitional regime can be distributed to the shareholders tax free, by way of a share capital reduction (subject to conditions). Where a share capital reduction would take place before expiry of that period of 8 (or 4) years, an additional withholding tax of 15%, 10% or 5% will apply, depending on the number of years which have already expired since the transformation
- anti-abuse legislation has been put into place for dividend transactions
- a 20% withholding tax will apply to dividends distributed out of the profit allocation of the second financial year following the financial year of contributions
- the rate will be further reduced to 15% for dividends distributed out of the profit allocation as of the third financial year following the financial year of the contribution
- a number of conditions have to be met in order to benefit from the reduced withholding tax rates
- anti-abuse legislation for reductions of share capital
- the notional interest deduction that grants companies a deduction against profits for the cost of equity
- the value of shares held as financial assets should currently be deducted from the 'equity' on which the notional interest is calculated. As of tax year 2013, that provision will be extended to the shares held as an investment of which the dividends benefit from the participation exemption
- the benefit of the patent income deduction (leading to an average tax rate of 6.8%) is currently subject to the requirement that the research and development (R&D) department of the company should be structured as a branch of activity. That condition will be abolished for small- and medium-sized companies as of tax year 2014.

# Mexico featured article



Last September the Mexican President submitted amendments to the tax legislation that could be applicable for the 2014 tax year. In general terms, it includes the issuance of a new income tax law, several modifications to other tax laws and provisions, the repeal of the flat tax law, as well as the repeal of the cash deposits law. Some of the more significant income tax proposals include:

- to repeal the actual Mexican income tax law that has been in force since 2002, and issue a new law that will be in force from 1 January 2014
- to include a new procedure which will allow the tax authorities to request information of residents abroad for double taxation relief under DTAs
- a prohibition for the deduction of payments made to related parties being Mexican residents or residents abroad, where the corresponding income is not taxed to such related parties, or if the income is taxed at a lower rate than the 75% income tax that would be generated in Mexico
- with respect to employees allowances, which are either exempt or partially exempt items, the deduction for these employer expenses would be limited to only 41% over such exempt items
- to eliminate the tax incentive with a possibility to apply an accelerated deduction of new asset investments and eliminate the linear tax depreciation, 100% deductible, over the machinery and special equipment acquisitions for controlling environmental pollution
- to eliminate the tax consolidation regime
- to eliminate the tax incentive of taxpayers dedicated to build and sell real-estate through which they are able to deduct 100% of the acquisition cost of the land
- to establish a 10% income tax rate over dividends distributed to shareholders. The tax will be payable by the entity which issues the dividends payment
- that in order to be able to continue working as a 'maquila entity' it must export at least 90% of the total invoicing of the entity
- entities of residents abroad which operate through a 'maquila shelter' can remain under the terms of such regime for a maximum period of three tax years, counted when such entities start operations in Mexico. After that, it is considered that the resident abroad will have to incorporate a subsidiary in Mexico
- foreign tax credit carry forwards can be used for ten years, although new foreign tax credit limitations will be imposed
- to eliminate the preferential Value Added Tax (VAT) rate of 11% applicable to all transactions and services carried out in the border region
- to repeal the obligation that certain taxpayers have in regard with filing the tax report (dictamen fiscal) before the tax authorities
- to create substance over form provisions concerning invoicing for non-existent goods and services.

Mexico has submitted amendments to the tax legislation that could be applicable for the 2014 tax year.

# United States featured article



The Inland Revenue Service (IRS) issued advice that a controlled

foreign corporation's (CFCs) income from software transfers to customers was foreign personal holding company income (FPHCI) and as such immediately taxable to the US shareholder of the CFC. The advice is important to US based companies in the software industry with offshore subsidiaries.

The taxpayer, a CFC, transferred software to customers under perpetual, nonexclusive and transferable (though only to affiliates of the customer) licenses. Under a license agreement, a customer paid a one-time fee for each user and annual maintenance and support fees based on the total number of users. After one year, a customer could terminate the agreement as well as the maintenance and support fees, provided that the customer certified in writing that it no longer used the software. The taxpayer had seven

customers; two of those customers were acquired by the taxpayer when one of its affiliates closed.

The taxpayer had two employees, a financial controller and a software media production assistant, as well as three directors, one of whom (the executive director) was treated as an employee based on his duties. At different points of time the taxpayer did not employ the production assistant. The employees' backgrounds were in accounting, finance and technology and their job functions were largely administrative (eg bookkeeping, tracking payments, ordering the 'software keys' to transfer to customers and filing tax returns). While there was some indication that the executive director assisted with marketing and worked with an affiliate company to promote sales, the employees did not track time spent on specific activities. The maintenance and support services provided to customers under the license agreements are contracted out to affiliates of the CFC.

The taxpayer and the IRS agreed to characterise the income stream as rental income from the lease of copyrighted articles. This characterisation reflects that copyright rights in the software nor benefits and burdens of owning the software are transferred under the agreements. Unless an exception applies, rents generally constitute FPHCI, which is currently taxable to US shareholders.

Rents derived in the active conduct of a business and received from unrelated persons are excluded from the definition of FPHCI (the 'active leasing exception'). Rents are considered derived in an active business if the CFC leases one of four types of property, only one of which, the 'active marketing exception', is relevant. The active marketing exception applies if property is leased as a result of a CFC lessor's marketing function if the lessor, through its own officers and employees in a foreign country, maintains and operates an organisation in that country that is:

- regularly engaged in the business of marketing (or marketing and servicing) the leased property
- substantial in relation to the amount of rents from leasing the property.

The exception also extends to leases acquired by the CFC if the CFC performs active and substantial management, operational and remarketing functions with respect to the leased property.

The IRS found little evidence that the taxpayer regularly engaged in a marketing business. The taxpayer did not employ anyone with marketing expertise, compensate employees for marketing activity or success, or document the time its personnel spent on marketing. Related entities produced nearly all of the press releases for the parent's website and had even won international marketing awards. The agreement between the taxpayer and its parent company indicated that the taxpayer was not a marketing company, and the taxpayer had signed only one of its customers in the years at issue. The IRS concluded that the taxpayer mainly collected passive rents, especially considering that a huge proportion of its income was funnelled to the parent company. Consequently, the taxpayer's rents constituted FPHCI because no active business was conducted and was therefore immediately taxable to the US shareholder of the CFC.



# EMEA news

## Austria



An Austrian resident joint stock company (company G) acquired via its 100% owned subsidiary (subsidiary E) a 100% participation in a limited liability company resident in the Slovak Republic (company Z). From 2006, all three companies were part of a tax group, where G functioned as parent company of the group. After a legal merger in 2008 between G and E, company G became the legal successor of E, ie the sole shareholder of Z. In the annual tax return for 2006, Z claimed depreciation of goodwill in relation to the acquired participation in Z. When the tax authorities denied the claim for depreciation, G appealed against the decision.

Under the Austrian group taxation regime, write-offs in respect of participations in group members are not deductible for corporate income tax purposes. Instead, the group parent may depreciate the goodwill derived from the acquisition of the participation in an operating resident group subsidiary. Goodwill is determined as the lower of:

- the difference between the acquisition price and the accounting equity of a group subsidiary, increased by unrealised capital gains
- 50% of the acquisition price, spread over 15 years.

Under the Austrian group taxation regime, a non-resident company can also be a group member, provided that it is comparable to a resident stock company, limited liability company or cooperative. The court ruled in favour of the taxpayer.

## Denmark



The Danish corporate income tax act states that any cross-border transfer of assets and liabilities out of the Danish tax jurisdiction will be subject to Danish exit taxation. The transfer of assets out of the Danish tax jurisdiction will be treated as a sale at market value, and any capital gain arising from it will be subject to Danish corporate income tax at a rate of 25%.

The European Court of Justice (ECJ) held that this legislation violates the treaty on the functioning of the European Union (EU) regarding the freedom of establishment. The ECJ deemed the Danish rules to be disproportionate because they impose immediate capital gains taxation on unrealised assets at the time of transfer without any possibility of deferring taxation to a later point in time.

Denmark argued that it is proportionate to impose taxation on unrealised non-financial assets at the time of transfer if the assets are used in a business and are subject to depreciation. If taxation could be deferred to the time of realisation, taxpayers could avoid taxation completely, Denmark argued, because such assets will often not be realised at all.

The ECJ rejected this argument and stated that even though it is proportionate for a member state to determine the tax due on the unrealised gains at the time when its power of taxation regarding the assets in question ceases to exist; taxation at the time of transfer without an option to defer taxation is disproportionate.

## Finland



A Finnish company, (company P), applied to deduct losses, despite a change of ownership. Under Finnish income tax law, the change in ownership would prohibit the carry forward of the losses. However, tax authorities may allow the deductions for special reasons. The change in ownership restriction is very common around the world as a means to limit trafficking in loss companies.

P's application was rejected by the tax authorities and its appeal was rejected by a Helsinki administrative court. P then appealed to the supreme administrative court, which referred questions to the ECJ asking whether the Finnish scheme constituted state aid and would therefore be prohibited.

The ECJ held that the Finnish tax law does not prohibit the Finnish loss carry forward scheme because it constitutes existing aid and may remain in place until the European Commission (EC) finds it to violate EU law and the ECJ supports that finding.

The court wrote that the loss carry forward provision does not violate EU law because it is not new aid, but rather existing aid, having come into force before Finland joined the EU in 1995. Only new aid must be reported to the EC, existing aid, such as the loss carry forward scheme, may be lawfully implemented as long as the EC has not found it to be incompatible with EU law.

If the Finnish loss carry forward scheme had been amended, it could be classified as new aid, in which case the decision would be against Finland.

## France



France is expected to hold hearings based on the 'Council of Ministers' publication on a new set of anti-avoidance measures to fight against tax fraud. The key elements of this publication are summarised below.

- **Reporting obligations** – to harden the fight against tax havens, large companies, banks and wealthy individuals will bear new reporting obligations. French banks and companies will be required to report annually the list of their foreign subsidiaries, including specific details on the nature of their business, transactions, sales, employees, profits, taxes paid and public aid received.
- **Investigative powers** – the government plans to increase the police and judiciary authorities specialising in tax investigation staff and create a new prosecuting office for major corruption and tax fraud.
- **Penalties for tax fraud** – the government will increase criminal penalties for major tax fraud and tax evasion.
- **List of non-cooperative states or territories (NCSTs)** – the government proposes to add countries to the NCSTs list that will not cooperate actively with France. Currently, countries that have signed an exchange of information agreement with France are not included on the list even though in practice assistance is not given. The main consequence for being on the French NCSTs list is that the withholding tax on interest, dividends and royalties paid to residents of an NCST is increased to 75%.

## Germany



The federal ministry of finance in Germany released a draft regulation

on the attribution of permanent establishment (PE) profits in accordance with the OECD guidelines. Given the level of foreign firms operating in Germany with German branches, these draft regulations are important as they will ultimately provide the guidance necessary to calculate German branch taxable profits.

The OECD focuses on function, assets, risks and capital, and Germany's new draft regulation contains provisions relating to the classification of PE income as well as the calculation and attribution of that income. The regulation would be a reliable instrument for investors in connection with the classification and attribution of business profits in general, regardless of whether they choose a German corporation or partnership instead of a PE for investing in Germany.

The regulation would cover:

- how the income of a PE is calculated; there would be an 'auxiliary calculation' that requires documentation relating to the attribution of assets and liabilities, equity (allotted free capital), and relevant business transactions
- the circumstances under which civil law contracts (dealings) would be recognised under German tax law
- details about certain business sectors, such as banking, insurance, construction and mineral exploration.

## Greece



A new Income Tax Code (ITC) was announced in the introductory report

as part of Greek Government's effort to overhaul the Greek fiscal system towards enhancing transparency and combatting tax avoidance and evasion. The new ITC is expected to be complemented with a new framework for the rationalisation of existing (but fragmented) tax incentives and special tax regimes. The ITC becomes effective in respect of revenues and expenses occurring in fiscal years starting on or after 1 January 2014.

The ITC adopts rules and definitions already existing in the EU and international tax materials (eg the OECD model tax convention, the EU merger directive, the EU council resolution regarding CFCs and thin capitalisation rules).

For combatting tax evasion and avoidance, the ITC contains rules on CFC and thin capitalisation, imputation of income, disallowance of payments to non-cooperating jurisdictions and preferential tax regimes.

The new ITC retains the principle of income taxation on the basis of worldwide income in respect of domestic tax residents and Greek source income in respect of non-domestic tax residents.

There are new earnings-stripping rules, including:

- net deductible interest is limited to 25% of Earnings Before Interest, Taxes, Depreciation, and Amortisation (EBITDA) (under Greek accounting principles and the relevant tax adjustments)
- net interest, the amount by which interest expenses exceed interest revenues
- limitation does not apply to business taxpayers that are not part of a group of companies and the net interest does not exceed €1 million per year
- interest expenses disallowed can be carried forward to the following five fiscal years
- credit institutions are exempt from such rules.

In terms of CFC legislation, undistributed profits earned by a CFC are added to the taxable profits of the shareholder, under the following conditions:

- shareholder directly or indirectly controls the foreign corporation
- CFC is a tax resident in a non-cooperative jurisdiction or in a jurisdiction with a preferential tax regime
- more than 30% of the income earned by the CFC is classified as passive income (interest, royalties, dividends etc.)
- CFCs established in EU member states are outside the scope of the rule, provided profits have not been artificially diverted there for tax evasion purposes.

## Hungary



The European Court of Human Rights (ECHR) gave its decision in a case with unusual circumstances. The facts of the case dealt with a Hungarian national and former civil servant.

The ECHR found that the applicant, who was entitled to statutory severance, was subjected to a tax whose rate exceeded about three times the general personal income tax rate of 16%. The ECHR observed that the 98% surtax:

- entailed an excessive and individual burden on the applicant's side
- targeted only a certain group of individuals, who were singled out by the public administration in its capacity as employer
- made the applicant bear an excessive and disproportionate burden, while other civil servants with comparable statutory and other benefits were not required to contribute to a comparable extent to the public burden

- was applied without affording the applicant a transitional period within which to adjust to the new scheme
- was imposed on income related to activities prior to the material tax year and realised in the tax year, on the applicant's dismissal.

The ECHR concluded that the specific measure, as applied to the applicant cannot be justified by the legitimate public interest relied on by the Hungarian Government.

## Ireland



Irish tax authorities issued an anti-avoidance measure designed to combat schemes whereby an employer places funds in trusts or other arrangements (generally offshore) and under such schemes, payments/loans, benefits or assets are provided to a director or employee or to an individual connected to a director or employee. Where loans are involved, they are generally rolled over and not repaid. The new measure imposes a charge to income tax where it was not otherwise chargeable:

- in the case of a current or former director or employee, on the amount of such payment/loan, the cost of providing (or the value of) such benefit, or the value of the asset
- in the case of an individual, though not a director or employee at the time of receipt of the payment/loan, benefit or asset, who subsequently becomes a director or employee, on the amount of such payment/loan, the cost of providing (or the value of) such benefit, or the value of the asset
- in the case of a current or former director or employee, on an amount calculated as if the benefit-in-kind provisions apply as regards a loan or use of an asset.

## Israel



The Israeli Government proposed a number of major changes to the Israeli tax system, including amendments that could be particularly relevant to new immigrants and companies doing business in Israel.

Among the measures proposed are:

- a corporate tax increase from 25% to 26.5%
- increases in all tax brackets for individuals by 1.5% so that the highest marginal tax rate would be 49.5%, plus a potential surcharge of 2%, for a total of 51.5%
- significant changes to the CFC regime
- the cancellation, for new immigrants, of a tax exemption for proceeds from the sale of residential apartments in Israel, and a narrowing of the exemption for Israeli residents
- changes to the 'family company' regime so that Israeli companies that are considered to be transparent under certain conditions could no longer be treated as transparent if they have foreign shareholders
- a narrowing of the tax exemption provided to foreign residents on the sale of Israeli companies and the denial of the exemption if the Israeli company holds natural resources.

In addition to these proposals, the bill calls for significant changes in the taxation of trusts and new immigrants in Israel.



**Italy**

A recent court case involved an Italian company that distributed software produced by a US entity. The Italian subsidiary of a US based multinational was subject to assessment for corporate income tax purposes.

During the assessment the Italian tax authorities challenged the deduction of a significant part of the royalties paid by the Italian subsidiary to its US parent by claiming the substantially higher transfer pricing was not in line with the arm's length standards. The tax inspectors recomputed the transfer pricing for the royalties as 7% of the proceeds, based on the guidelines of the ministry of economy and finance.

The taxpayer successfully argued against the tax assessment before the tax court in the first instance, and the Italian tax authorities then appealed the decision. The second tax court reversed the previous judgment and validated the tax inspectors' action that disallowed the deduction of a substantial portion of the royalties paid.

The court rejected the appeal concerning the transfer pricing applied to the payment of royalties for the license of software. The supreme court upheld the position of the Italian revenue agency.

**Liechtenstein**

Recent activity from the US department of justice has sent a stern pre-Foreign Account Tax Compliance Act (FATCA) warning to US taxpayers holding offshore bank accounts with US tax evasion intentions.

In a US department of justice announcement, the assistant attorney general for the tax division, announced a bank based in Vaduz, Liechtenstein has agreed to pay more than \$23.8 million to the US and entered into a non-prosecution agreement (NPA). The NPA provides that the bank will not be criminally prosecuted for opening and maintaining undeclared US taxpayers' bank accounts from 2001 through 2011, at a time when the bank assisted a significant number of US taxpayers in evading their US tax obligations, by filing false federal tax returns with the IRS and otherwise hiding accounts held at the bank from the IRS. The NPA requires the bank to forfeit \$16,316,000, representing the total gross revenues that it earned in maintaining these undeclared accounts and to pay \$7,525,542 in restitution to the IRS, representing the approximate unpaid taxes arising from the tax evasion by the bank's clients.

The assistant attorney general stated "this non-prosecution agreement addresses the past wrongful conduct of the bank in Vaduz in allowing US taxpayers to evade their legal obligations through the use of undisclosed Liechtenstein bank accounts, while also acknowledging the extraordinary efforts of the bank in bringing about significant changes in Liechtenstein law. As a result of new Liechtenstein legislation, US taxpayers who thought that they had obtained the benefit of Liechtenstein's tax secrecy laws have learned that their bank files were turned over on the request of the department of justice."

**Netherlands**

Stock options continue to be used by employers as a means of non-cash compensation for executives. In a recent case, a Dutch resident individual who was a managing director for a Dutch limited liability company, A B.V. was awarded warrants by A B.V., which gave him the right to buy a specific number of shares in A B.V. at a certain price during selected periods. The taxpayer exercised his warrants from which he derived a net taxable gain of €326,475.36. A B.V. withheld the applicable marginal wage tax rate of 52% on this amount. The shares were transferred into the taxpayer's personal investment account. The price of the shares in A B.V. had, however, dropped since the warrants were exercised. At this point, the net gain was €240,084. In the taxpayer's tax return for 2007, the taxpayer included a negative income of €86,391, ie €326,475.36 (the net gain) – €240,084 (the net gain of the shares).

The tax inspector rejected the deduction of the negative income, assessing a taxable income of €424,373. The taxpayer appealed the assessment to the lower court of The Hague and the appeal was rejected.

## Portugal



The Portuguese Government amended its corporate tax law to

include a withholding tax exemption when the beneficial owner of a royalty or interest payment is a company or PE in another EU member state.

The change completes Portugal's transition of the EU interest and royalties directive, which eliminates withholding tax on interest and royalty payments made between associated companies of different member states.

Also, Portugal will exempt withholding tax on payments to a Swiss company or Swiss PE under the 2004 EU-Switzerland savings tax agreement, which provides for measures equivalent to those on the taxation of savings income in the form of interest payments.

## Romania



The ministry of finance published a draft of an ordinance, introducing

lump-sum taxation for certain companies deriving income from activities specified by the law.

The lump-sum tax, which would replace the current 16% corporate income tax or 3% turnover tax, would be imposed on resident companies that, on 31 December of the preceding tax year:

- carried on, as main activity, services of maintenance and repair of cars, tourism, bars and public alimentation
- derived income from the main activity in an amount exceeding 70% of the total income
- had a net annual turnover of less than €50 million or owned total assets of a maximum value of €43 million
- had less than 250 employees annually, on average
- were not under liquidation.

If, on 31 December of the tax year, the conditions for applying lump-sum taxation are no longer met, the taxpayer must report this to the tax authorities by 31 March of the following year.

The lump-sum tax would be determined based on computation formulas which are different for each type of activity.

Lump-sum tax would be payable on a current year basis, with quarterly declarations and payments, by the 25th day of the month following each quarter.

## Russia



The presidium of the Supreme Arbitration Court (SAC) held in a case involving a Russian telecommunications company, that deductible

interest expenses on controlled loans must be calculated quarterly and cannot be recalculated for subsequent changes in the taxpayer's balance sheet position.

The issue of the litigation was the legitimacy of a taxpayer's recalculation of the thin capitalisation ratio on a cumulative basis in subsequent reporting periods. Profits tax returns are normally filed for the first quarter of a calendar year, the first six months, the first nine months and the year as a whole (unless the taxpayer opts for monthly reporting). The taxpayer had recalculated interest deductions for each period covered by a tax return. This resulted in the recognition of increased deductible interest.

The tax inspector did not accept the recalculation of interest for periods covered by previous tax returns. The lower courts concluded that tax law did not prohibit the adjustment (recalculation) of deductible interest expenses, but the case was referred to the SAC for a supervisory review.

The SAC supported the tax authorities' position, holding that the deductible interest expenses have to be calculated on a quarterly basis and should not be recalculated for every period covered by the tax return.

## South Africa



In a recent ruling issued by the South African Revenue Service (SARS), various wealth transfer tax issues were addressed.

The descendants of a testator are the designated residuary heirs under the will of the deceased. The will also bequeaths certain legacies to the surviving spouse of the deceased. The applicant of the ruling request, who is the executor of a deceased estate, anticipates that estate duty will become leviable on the net value of the estate. The descendants propose to renounce their inheritances.

The SARS ruled that:

- the renunciations will not result in the levying of any donations tax
- the renunciations will not be 'disposals'
- the estate duty act will apply to the inheritances that will accrue by operation of law to the surviving spouse by virtue of the proposed renunciations.

In another ruling, SARS issued a binding private ruling dealing with the question as to whether the cancellation and extinguishment of a right to claim interest on a shareholder loan will trigger a capital gains tax liability.

A listed public company sold its majority shareholding of 74% in a private company (the co-applicant) to another public company (the applicant). The co-applicant and the applicant, which are both incorporated and tax resident in South Africa, were not connected parties prior to this equity acquisition.

As part of the equity acquisition, the applicant acquired a loan claim to the value of ZAR 4.161 billion owed by the co-applicant to a financing company. The applicant paid ZAR 1.1 billion for the loan claim. The co-applicant, however, continues to owe the applicant the total ZAR 4.161 billion amount. Interest is charged at the Johannesburg interbank agreed rate plus 4.9% per annum. The co-applicant is not in a position to service all the interest on the loan claim due to the applicant.

The applicant proposes splitting the loan claim into two parts. Interest will continue being charged on the ZAR 1.1 billion, while interest on ZAR 3.061 billion, reflecting the discounted portion of the loan claim, will be cancelled. The ZAR 3.061 billion amount will subsequently become an 'interest free portion'.

In addition, the loan claim will be subordinated in order to restore the solvency of the co-applicant and to allow them to be in a position to negotiate better credit terms with other financial institutions.

SARS ruled that:

- since the co-applicant and the applicant were not connected parties prior to the equity acquisition, the ZAR 1.1 billion paid for the loan claim will represent an arm's length price
- the cancellation and extinguishment of the applicant's right to interest based on the interest free portion of the loan claim will not trigger any capital gains tax liability

## Sweden



The Swedish parliament has passed a law whereby foreign employers must report to the authorities their employees that are seconded to Sweden. The law requires a contact person in Sweden to be registered and authorised to receive notices on behalf of the employer and provide documents to show that requirements under Swedish law regarding stationed employees are met. The authorities have issued brief regulations detailing the reporting requirements that apply from 1 July 2013 and affect foreign employers inside and outside the EU. The notification must be filed no later than when the employees begin their work in Sweden.

The notification shall include the following information:

- the employer's name, mailing address and residence
- information on an authorised representative of the employer, including their name, Swedish personal identity number if existing (or if not their birth date), mailing address, telephone number, and email address
- the type or types of services to be provided in Sweden
- period during which the services will be provided in Sweden
- the place or places in Sweden at which the services will be provided
- name and Swedish personal identity number if existing, or if not, birth date of the employee(s) that are stationed to work in Sweden.

## Turkey



Turkish tax authorities issued a 'resolution communiqué' providing guidance for incentives in Turkey. The objective of the resolution is to explain the principles and procedures of how to:

- orient savings to investments with high added value
- boost production and employment
- encourage regional, large-scale, and strategic investments with greater content of research and development
- enhance international competitiveness
- attract more foreign direct investment
- deal with regional developmental discrepancies.

Investment incentive certificates need to be obtained by individual investors to activate whatever investment benefits will be granted to them. Thus, this document, issued upon request of investors, specifies which benefits will be granted and utilised in what investment-related circumstances under the relevant provisions of the resolution.

Any investment project to be granted with an investment incentive certificate goes through an elaborate and extensive process carried out by the relevant central/local authority.

The 'General Directorate of Incentive Implementation and Foreign Capital', affiliated with the 'Ministry of Economy', is the central, if not the sole, public body vested with authority to issue investment incentive certificates. But there are also local authorities such as chambers of industry, development agencies, and other chambers that operate as local branches of the Union of Chambers and Commodity Exchanges of Turkey to issue investment incentive certificates pertaining to investments under TRY 10 million and falling within the scope of the general investment incentive scheme. Four principal categories of investment incentives are:

- general investment incentive scheme
- regional investment incentive scheme
- large-scale investment incentive scheme
- strategic investment incentive scheme.

## Ukraine



The Ukrainian ministry of revenue issued a guidance in which it clarified the corporate deductibility of expenses incurred in transactions with interdependent (related) persons. The ministry indicated that the following persons should be qualified as related:

- legal entities, if one of them controls the other(s) or if two or more legal entities are controlled by a third legal entity
- a natural person, his family members, and a legal entity if that natural person or his family members control that legal entity
- managers and other executive officers of a legal entity, as well as their family members, who are authorised to undertake actions on behalf of the legal entity that will create, modify, or terminate the legal entity's legal relations
- members of any association of legal entities carrying on business activities through such association.

For tax purposes, the term 'control' means:

- a direct possession or possession through related natural persons or legal entities of a stake of at least 20% in the taxpayer's capital
- a direct influence or influence through related natural persons or legal entities of a taxpayer's business activities as a result of:
  - obtaining corporate rights permitting the exercise of decisive influence on the formation and decision-making of the taxpayer's managing bodies
  - filling posts in the taxpayer's supervisory and executive bodies with persons who already occupy similar posts in other legal entities
  - obtaining a right to enter into contracts authorising the imposition of conditions for exercising the taxpayer's business activities, to make obligatory instructions for the taxpayer, or to delegate to third persons the powers and functions of the taxpayer's managing bodies.

The ministry held that any expenses incurred by a taxpayer in connection with the sale or exchange of goods, performance of works, or provision of services to persons considered affiliated with the taxpayer may be recognised to the extent they do not exceed the income gained from those transactions. It further held that the taxpayer may not register losses on those transactions in its tax accounting.

## United Kingdom



In the House of Lords, a select committee on economic affairs issued a report 'Tackling corporate tax avoidance in a global economy: is a new approach needed?' In the report, the committee noted that:

is a new approach needed?' In the report, the committee noted that:

1. The UK faces a serious problem of avoidance of corporation tax, due in part to the complexity of the tax regime in the UK, but mainly because the international tax system gives multinational companies opportunities to shift profits between countries in ways that reduce their liabilities in the UK. This damages the economy and undermines trust in the tax system.
2. Under the present international framework of corporate taxation, companies operating globally can make their taxable profits arise in low-rate jurisdictions, such as Ireland and Luxembourg, even when their customers are in the UK or elsewhere. The amount of corporation tax a company pays in any one country, such as the UK, can be determined by how aggressively the company seeks to shift its profits to other lower-taxed countries. The effect is to make corporation tax payments in a given country largely voluntary for multinational companies.
3. The UK faces the prospect of losing much-needed revenue through avoidance of corporation tax. There are also distortions in the market place: there is no level playing field between, say, a UK-based retailer which has to pay corporation tax in the UK and a global rival selling in the UK but paying corporation tax somewhere else at a lower rate.

Therefore the committee recommended:

- Parliament should establish a joint committee made up of Members of Parliament and Peers, to exercise greater parliamentary oversight of Her Majesty's Revenue and Customs (HMRC) and the settlements it reaches with multinationals. Like the Intelligence and Security Committee, the new committee would examine confidential evidence in private
- the treasury should urgently review the UK's corporate taxation regime and report back within a year with proposed changes to be made at home and pursued internationally, especially through the OECD
- the review should re-examine some fundamentals of the UK's corporation tax regime, including differential tax treatment of debt and equity and the scope for introduction of an allowance for corporate equity
- HMRC should be better resourced to deal effectively with the tax affairs of complex and well-resourced multinationals.

## Uzbekistan



The President signed a decree establishing a new Free Industrial and Economic Zone (FIEZ) in the Djizzak region. The decree introduces a special fiscal, customs and administrative regime available for residents of the Djizzak FIEZ, for a period of 30 years.

Legal entities registered in the FIEZ are provided with exemption from corporate income tax, property tax, infrastructure development tax, unified tax payment for small companies and contributions to the Republican Road Fund.

The decree provides a relief for customs payment (with the exception of customs clearance fees) on imported equipment, raw materials and spare parts, not produced in Uzbekistan and imported into the Djizzak FIEZ as part of the projects, which are approved by the cabinet of ministers.

The above-mentioned exemptions are granted for the period of:

- three years, if the investments made in the region equal USD 300,000 to USD 3 million
- five years, if the investments equal USD 3 million to USD 10 million
- seven years, if the investments equal over USD 10 million.



# APAC news

## Australia



A recent decision dealt with foreign currency denominated transactions. The News Corporation Limited (TNCL), incorporated in Australia, was the parent company of the News group; News Finance Pty Ltd (NF), News Limited (NL) and News Publishing Holdings Pty Ltd (NPHP), wholly owned subsidiaries and News Publishing Investments Pty Ltd (NPIP) was a subsidiary of NPHP. NL had built up a large debt (its capital and reserves were negative AUS\$239 million) in funding the foreign expansion of the News Group through its interest in News Publishers Limited (NPL) incorporated in Bermuda. NL was a borrower and guarantor of external debt and its accounts were publicly disclosed. To address this problem, News group undertook a reorganisation with the objective of reducing NL's debt.

NF loaned funds to NPHP which it used to subscribe for shares in NPIP. NF and NPHP accounted for this transaction as three separate loans in AUD, USD and GBP although the cheque was in AUD. NPIP then used the funds to acquire NL's interest in NPL and NL used the proceeds of that sale to retire debt. Other financing transactions were also consummated in the group.

The News Group undertook a global reorganisation of its operations in response to a downturn in the economy and a liquidity crisis. The restructure involved NPIP disposing of its interest in NPL by that company redeeming and buying back the redeemable preference shares and ordinary shares held by NPIP and assigning or endorsing a series of promissory notes to various companies within the News Australia group.

NPHP claimed a forex loss occurred when it endorsed the two USD promissory notes to NPIP and when it presented the promissory note to NPIP in final satisfaction of the loan.

The commissioner had submitted a currency exchange loss that could be realised without a related exchange, being necessarily a payment or outgoing involving exchanges of foreign and Australian currency. The commissioner argued that more was required than an exchange of promissory notes and an extinguishment of liabilities in foreign currencies.

The full court noted that the term 'currency exchange loss' was defined as 'a loss to the extent to which it is attributable to currency exchange rate fluctuations'. Considering the definition, the loss must be attributable to fluctuations in the currency exchange rate; and noted that the explanatory memorandum also supported that interpretation. Had it not been so defined they acknowledged that an argument that an actual exchange of currency was required for the section to be activated might have a plausible basis.

## China



The Shanghai free trade zone, proposed by the ministry of commerce and Shanghai municipal government, contains special liberal rules that will apply to the new zone in respect of:

- setting up foreign investment enterprises (new sectors open to foreign investment and less restriction on participation rates in certain sectors)
- customs clearance
- financial sector (including abolition of foreign exchange control of the Chinese currency on capital accounts, interest rate, overseas portfolio investment and foreign participation in future trading etc.)
- preferential tax rate and other incentives.

The Shanghai Government published its 'Plan for the Guidance of the State Council on Financial Support for Economic Restructuring, Transformation and Upgrading' to launch a financial reform which will be experimented in the new zone. The financial reform will cover cross-border settlements, credit asset securitisation, use of CNY in international trade, investment and insurance, direct foreign investment by Chinese enterprises and individuals.

If the plan is carried out, the new zone is considered to be one of the biggest transformations of the Chinese economy and financial sector in Chinese history.

## Hong Kong



Given the constant flow of executives into and out of Hong Kong, the issue of tax residency becomes important. The 'State Administration of Taxation' issued an announcement regarding the procedure for issuing a Hong Kong tax residence certificate.

The mainland tax authority may determine Hong Kong tax resident status on the basis of the certificate of incorporation/registration issued by the Hong Kong registrar of companies or the business registration certificate when the applicant for the treaty benefit is a legal entity. In cases where the applicant is an individual, the following documents must be presented:

- Hong Kong identity card
- Hong Kong resident travel pass to the mainland
- Hong Kong tax clearance certificate of the preceding tax year.

However, in the following cases, a tax residence certificate issued by the Hong Kong tax authority is required:

- the Chinese tax authority is suspicious about the applicant's resident status

- the documents presented by the applicant are not sufficient to prove the resident status
- the applicant applies for the resident status on the basis of automatic recognition of resident status for listed companies, including higher-tier companies of the listed companies
- the applicant, who is an individual, applies for the application of the tax arrangement on capital gains.

To obtain a Hong Kong tax residence certificate, the following documents must be submitted to the Hong Kong tax authority:

- a letter of request issued by the mainland tax authority (at county or higher level) to the Hong Kong tax authority
- the application form for resident status issued by the Hong Kong tax authority (for legal entities there are two forms available, (i) for companies incorporated in Hong Kong and (ii) for companies incorporated outside Hong Kong. Hong Kong will, as the case may be, issue the respective tax residence certificate).

## India



Generally transfer pricing applies to related party sales, services, leases, licenses and loans. Usually the issuance of shares between related parties and most jurisdictions would not even raise a related party share issuance as a transfer pricing issue, although the Indian tax authorities have been looking into a recent transaction as outlined below.

Shell Oil is an interesting Indian view of transfer pricing legislation. Shell India issued around 870 million shares to its Dutch parent at a price of INR 10 per share. The capital was infused into the Indian company as foreign direct investment (FDI) in compliance with Indian exchange control regulations. In the course of transfer pricing assessment proceedings, Indian tax authorities claimed that Shell India significantly undervalued its shares. According to the tax authority, Shell India's shares should have been valued at around INR 180 per share.

The tax authority contended that capital infusion or a subscription of shares of an Indian company by the foreign parent is well within the scrutiny of transfer pricing regulations. The tax authority claimed that Shell India had issued more shares to its parent than the amount invested. It sought to tax the shortfall of around INR 150 billion which according to the tax authority was receivable by Shell India from its Dutch parent on an arm's length basis.

Shell India has challenged the tax authority's order before the Bombay high court on the basis that the tax authority does not have jurisdiction to invoke transfer pricing regulations for taxing subscription to shares of a company, which is a capital transaction that should not have tax consequences.

## Japan



Permanent residents are now required to annually report on their overseas assets worth more than JPY 50 million in the aggregate for the purposes of income and inheritance taxes. A permanent resident is either a Japanese national or a foreign individual who resided in Japan for more than five years in the preceding ten years.

The overseas assets, regardless of their business or private use, include: real properties, bank accounts, brokerage accounts, securities (shares and bonds), equity rights (stock options) not exercised or disposed, interest in partnerships and trusts, antiques, jewellery and other valuables.

Overseas assets are valued at either fair value or estimated value as of 31 December. The fair value can be the value assessed by a professional appraiser or the price published in the financial market. The estimated value is the value computed according to the reasonable benchmarks, such as the acquisition price or the sale price of the similar asset.

The overseas asset report is subject to inspection by the tax authority, and non-compliance with the reporting requirement may trigger a fine up to JPY 500,000 or, in serious cases, one year imprisonment.

## Korea



Under revised regulations, the foreign exchange that will be exempt from reporting duties are:

- net settlements of less than USD 1,000
- payments to third parties
- all kinds of settlement practices usually used in the global market
- small transactions and transactions that are difficult to report, such as rent payments by individuals working overseas and transfers of investment due to bankruptcy.

The following foreign exchange related transactions must be reported:

- capital increases and sales of overseas subsidiaries as well as their establishments
- investments of holding companies in all their subsidiaries
- tax payments of real estate sales by foreigners when they send revenues from real estate sales in Korea overseas.

In addition, the reporting exemption given to individuals with permanent residence rights overseas will be removed to prevent the avoidance of tax on overseas direct investments.

Information regarding foreign exchange transactions will be shared more extensively among government agencies such as the National Tax Service, the Korea Customs Service and the Financial Supervisory Service. Such cooperation is expected to help prevent overseas tax evasion and illegal foreign exchange transactions.

## Malaysia



Malaysia has published rules on the deductibility of costs for the acquisition of foreign-owned companies. A qualifying locally owned company may deduct as expenses 20% of the costs of acquiring a foreign-owned company in the basis year for a year of assessment. The acquisition must be completed within three years from the date an application for deduction is submitted to the Malaysian investment development authority. The deduction will be withdrawn if the paid-up ordinary shares issued by the acquired foreign-owned company are disposed of within five years following the date of completion of the acquisition.

The new rules cover locally owned companies that:

- have obtained the approval of the Malaysian investment development authority regarding an application for deduction submitted on or after 3 July 2012, but no later than 31 December 2016
- acquire more than 51% of the paid-up ordinary shares issued by a foreign-owned company
- use the high technology transferred from the foreign company in their operational activities in order to create or increase the demand for Malaysian-originated products or services provided in Malaysia (the technology must be used for the production or the improvement of material, devices, products, or processes or for the improvement of processing or quality of services)
- have not been granted any incentives under the promotion of investment acts, except for pioneer status or the investment tax allowance as a high-technology company.

## New Zealand



A white paper, entitled 'R&D tax losses', invited discussion on proposed changes to the tax rules to assist start-up companies undertaking R&D. It will be interesting to see what comes out of the discussion in terms of legislative amendments.

The paper suggests that such companies be allowed a refund in respect of 100% of their eligible tax losses, instead of these losses being carried forward and offset against the company's net income in future years. The eligible losses will be capped at NZD 500,000 initially (equivalent to a tax refund of NZD 140,000, at the 28% corporate tax rate) and rising incrementally each year to a maximum of NZD 2 million (a refund of NZD 560,000).

To qualify for the refund, a company (and also a group, if the company is part of a group) would:

- pay R&D wages and salaries of at least 20% of its total expenditure on wages and salaries
- be in a tax loss position for the income year
- be resident in New Zealand
- not be a look-through company, listed company, qualifying company or special corporate entity.

The paper has proposed that R&D expenditure be based on the definition in the New Zealand equivalent of International Accounting Standard 38, with certain activities excluded, such as expenditure incurred in a post-development phase or related to routine work. It is also proposed to exclude interest expenses related to R&D, the purchase of existing R&D assets, R&D undertaken offshore, lease payments, and any expenditure funded by government or other research grants.

## Philippines



Regulations have been published dealing with a new excise tax and a requirement for the advance payment of VAT and corporate income tax by entities selling gold and other metallic minerals to foreign corporations and to non-resident individuals who are not engaged in business in the Philippines.

The regulation was imposed by the bureau of internal revenue to stop growing revenue leakages resulting from unreported sales of gold, other metallic minerals, and jewellery to foreign individuals and entities that come to the Philippines for a limited period of time for the sole purpose of making cash purchases of those products.

The 2% excise tax will be levied either on the actual market value of the gross output at the time of excavation, in the case of locally extracted gold (and other metallic minerals), or the value established by the bureau of customs in computing tariffs and duties on imports.

The VAT will be 12% if the gross selling price exceeds the threshold set by the tax code and other relevant rules and regulations (currently PHP 1,919,500). Otherwise, the rate will be 3%.

The standard corporate income tax rate will be 30%, and individual income tax will be levied at progressive rates ranging from 5% to 32%. The regulation does not specify when the advance payments of VAT and corporate income tax are to be made.

## Singapore



Singapore's inland revenue authority published new guidance clarifying the tax rules for the productivity and innovation credit (PIC) regime.

PIC is an incentive that allows businesses that invest in specified activities enhanced tax deductions, allowances and deferred tax payments. The regime is available from tax year 2011 through tax year 2015.

PIC grants businesses that invest in specified productivity and innovation activities enhanced deductions and allowances on as much as \$400,000 of qualifying expenditure incurred for each activity. These benefits are in addition to the deductions and allowances provided under the general tax rules. The total deductions and allowances amount, in effect, to 400% per dollar of qualifying expenditure.

Eligible activities are as follows:

- the acquisition or leasing of specific information technology and automation equipment
- the acquisition or licensing of intellectual property rights
- the registration of certain intellectual property rights
- R&D
- training
- design.

## Taiwan



Taiwan's parliament amended the capital gains tax on stock trading. The original capital gains tax, which was passed requiring taxpayers to pay a progressive tax ranging from 0.02% to 0.06% whenever the Taiwan capitalisation weighted stock index hit or exceeded 8,500 points. There is no 8,500 point threshold under the amended capital gains tax. Rather, it is levied at 0.1% on annual sales at or above NT \$1 billion (about \$33.2 million). Taxpayers can choose to pay a 15% capital gains tax on the actual gains/losses if doing so would create a lower overall tax burden.

The capital gains tax on initial public offerings will remain the same. Investors are required to pay a 15% tax on any capital gains from a sale of more than 10,000 shares in an Intellectual Property Office (IPO). The 15% rate also applies to capital gains from a sale of 100,000 (or more) shares of an emerging stock or unlisted company. However, if the shares are retained for more than one year, the taxpayer will receive a 50% discount.



## Thailand



The Thai Minister of Finance announced plans to enhance the country's tax incentives for research and development. Currently, Thai entities performing in-house R&D activities are allowed to deduct double the costs incurred from those activities when computing their income taxes. The corporate tax rate is scheduled to drop from 23% to 20% on 1 January and had been as high as 30% in 2011. This further reduction will reduce the actual savings from the R&D deductions so the government is proposing to allow taxpayers to claim a triple deduction of R&D expenses. The government is also planning to extend the R&D tax incentive to activities performed by external researchers, hired firms, or joint development projects with other businesses.

## Vietnam



The Vietnamese ministry of finance issued a Circular, which clarifies the tax treatment of foreign individuals working in Vietnam and other non-resident individuals with Vietnamese source income.

Under the circular, an individual is considered to be tax resident in Vietnam if he stays in Vietnam for a minimum period of 183 days during a tax year or has a permanent or long-term residence in Vietnam, including a house lease for a minimum period of 183 days in a tax year. Currently, the minimum period for a house lease is 90 days.

An individual with a permanent residence in Vietnam who stays in Vietnam fewer than 183 days during a tax year may be considered non-resident for income tax purposes if the taxpayer can provide sufficient evidence that he is a tax resident in another jurisdiction. Evidence can include a certificate of residence or, if an individual is resident in a country that does not have an income tax treaty with Vietnam, a copy of the individual's passport.

The new circular provides a tax exemption for specific income and benefits in kind granted to expatriates working in Vietnam and to Vietnamese persons working abroad. The exempt items include, for example, a relocation allowance, round-trip airline tickets for annual leave, and education expenses. The circular also specifies details concerning:

- gross-up rules for net income
- treatment of housing benefits
- consequences of benefits-in-kind.

To simplify management of the tax status of foreigners working for foreign contractors and subcontractors in Vietnam, the new circular requires such foreigners to register for tax codes in Vietnam for filing purposes.

Finally, a 10% withholding tax rate will apply to every payment exceeding VND 2 million (about \$94,000) to a resident individual if the payment is not specified in a short-term labour contract (covering a maximum period of three months).

# Americas news

## Argentina



### Tax reform measures

A package of Argentine tax reform measures

announced in August entered into force on 23 September. The reforms will affect both personal and corporate taxpayers, as well as cross-border and domestic transactions. With the repeal of a 20-year-long tax exemption, capital gains derived from the sale of depreciable movable assets, shares, quotas and participations, bonds and other securities will now be subject to income tax in Argentina. If the sale is performed by an individual, the applicable tax rate will generally be 15%, applied on a net basis. If the sale of securities is performed by a foreign legal entity, the withholding tax rate will be 13.5% on the gross sale price (unless the transaction is subject to a different treatment under an applicable income tax treaty).

Dividends paid by Argentine legal entities to Argentine individual residents and non-residents and to non-resident legal entities will now be subject to a 10% tax unless a tax treaty applies, in which case the treaty will govern (previously, dividends generally were tax exempt). Dividends paid by Argentine legal entities to other Argentine legal entities will remain non-taxable.

Once the new change will be in force the effective rate for investors will increase at 41.5% according to the following calculation:

Income type	
Income	100
Corporate income tax	-35
Net income to be distributed	65
Withholding tax on distribution	-6.50
<b>Net Income</b>	<b>58.50</b>

### Recent landmark ruling

In other news the Argentine supreme court of justice recently delivered a landmark ruling. In the case, IESA merged with another company, IMASUR that was part of the same economic group. IESA served notice of the reorganisation to the tax authorities as a merger.

The federal tax agency (AFIP) found that the reorganisation did not qualify as tax-free because IMASUR did not meet the relevant requisites. It also held that reorganisation cannot be characterised as both reorganisation and a goods transfer or sale within the same economic group.

After the national tax court and national chamber of appeals both ruled in favour of IESA, the tax authority brought the case before the supreme court, which also sided with IESA, holding that: the fact that the taxpayer initially filed the reorganisation as a merger, but failed to meet the relevant requirements does not prevent the reorganisation from being analysed under another provision, the requirements of which were fulfilled by the taxpayer.

## Bolivia



A temporary tax on foreign currency transactions (IVME) was approved by the chamber and must now be approved by the senate. Features of the IVME include:

- it will apply for a 36-month period
- only financial institutions and foreign exchange businesses will be subject to tax
- a rate of 0.7% will be applicable on the profits from the sale of foreign currencies
- foreign exchange businesses will pay the tax on only 50% of the tax base
- profits derived from the sale of foreign currencies by the central bank of Bolivia will be tax exempt
- it will not be deductible from the net profit subject to corporate income tax
- it will enter into force on the day following the day on which the decree is published.

In another development a recent resolution passed indicating that the tax authorities may now request the payment of tax debts from directors, managers and legal representatives in the following cases:

- **Enforceable tax obligations** – taxes due that have not been paid or disputed before the tax authorities, as well as tax debts which have been disputed before the tax authorities and the tax courts, where the ruling or decision obtained was not in favour of the corporate taxpayer.
- **Partial payment of tax due** – even though the tax authorities have attempted to collect the tax due directly from the corporate taxpayer (frozen bank accounts, asset forfeiture), the funds available are insufficient to pay the tax debt in full. In this case, the tax authorities may collect the full amount of tax due or the corresponding difference from directors, managers and legal representatives.
- **Reasoned decision** – once the tax authorities have declared that the funds available are insufficient or that the corporate taxpayer is insolvent, it shall issue a reasoned decision including the enforceable tax obligations, wrongful acts performed by the legal representative or person in charge of administering the assets and equity, and the deadline for replying to this decision.

## Brazil



A published ruling held that capital gains realised by non-residents are taxable in Brazil even when both contracting parties are non-resident and the only link to Brazil is the location of the relevant asset. The ruling clarified that a 15% withholding tax applies to capital gains 'arising from the disposition of property and rights located in Brazil by non-resident legal entities, except where otherwise provided in conventions to avoid double taxation signed by Brazil'.

In a disposition involving a Brazilian property where both purchaser and seller are non-resident in Brazil, the ruling cited the statutory authority requiring the Brazilian representative of the foreign purchaser to withhold income tax on the capital gains realised by the foreign seller and to remit it to the government even if no payment has been made within Brazil.

In a transaction where no payment was made within or from Brazil, it could be argued that no Brazilian withholding tax should apply because the source of payment is not Brazilian. However, absent taxpayer challenge, Brazil adopts the 'source of payment' principle for taxing cross-border transactions, so the absence of payment in or from Brazil in a transaction taking place outside the country should not trigger any Brazilian tax on capital gains realised by non-residents. In practice, the foreign purchaser's Brazilian representative may not be aware of, or have access to, details of the transaction, such as the purchase price or, more importantly, the seller's acquisition cost and/or the amount of capital gains realised by the non-resident seller. However, under Brazilian law, he is required to calculate and pay the withholding tax and, is personally liable for tax levied on a transaction in which the representative might not have been directly involved.

## Canada



As taxpayer transparency efforts continue to explode globally, the minister of national revenue announced the launch of a strengthened 'Foreign Income Verification Statement' (form T1135), to crack down on international tax evasion and aggressive tax avoidance. Starting in 2013, Canadians who hold foreign property with a cost of over CAD 100,000 will be required to provide additional information to the Canada Revenue Agency (CRA). The criterion for those who must file form T1135 has not changed, however, the new form has been revised to include more detailed information on foreign property. Increased reporting requirements include:

- the name of the specific foreign institution or other entity holding funds outside Canada
- the specific country to which the foreign property relates
- the income generated from the foreign property.

The CRA will use the additional information to ensure all taxpayers comply with Canadian tax laws, through activities including education and audit. Failure to report income from domestic or foreign sources is illegal, and Canadians should know that the CRA actively pursues cases of non-compliance. Tax evasion and aggressive tax avoidance can lead to significant taxes, interest and penalties.

## Chile



The Chilean IRS confirmed that the indirect transfer rules that were introduced in 2012 will not apply to the trading of Chilean company American Depositary Receipts (ADRs). The Chilean IRS also confirmed that capital gains arising from the disposal of ADRs should not be subject to Chilean income tax provided that both the transferor and the depositary bank for the ADRs are neither domiciled nor tax resident in Chile.

The indirect transfer rules, which apply to the indirect sale or other disposal of Chilean company shares via the transfer of an upper-tier non-resident owner, were introduced as part of last year's tax reform. In accordance with these rules, gain that is realised in connection with certain indirect transfers of Chilean shares may be subject to tax. In the ruling, the Chilean IRS states that the trading of ADRs will not be considered an indirect transfer of a Chilean company for this purpose because an ADR does not constitute an asset representing capital in a foreign entity.

For the indirect transfer rules to apply, the indirect transfer of a Chilean company must be executed via the direct transfer of 'rights, titles, shares, quotas, etc' or similar items representing capital in a foreign entity. Because ADRs do not represent rights or titles in a foreign entity, but rather in a Chilean company, the trading of ADRs should not fall within the indirect transfer tax rules.

The Chilean IRS also confirmed that capital gains derived from the disposal of ADRs should not be subject to income tax in Chile provided that both the transferor and the ADR's depositary bank are neither domiciled nor tax resident in Chile. The reason is that any capital gain arising should be deemed to be derived from foreign sources for Chilean tax purposes and, therefore, not taxable in Chile.

## Colombia



The government clarified the classification of resident individuals into two categories: employees and self-employed and issued a decree that contains definitions of the following terms:

- employee
- self-employed
- individuals subject to ordinary income tax regime
- liberal profession
- technical service.

The government issued decree regulates the withholding tax on employment income and provides the scope of application of the simplified minimum tax for employees and self-employed individuals.

According to the National Tax Code (NTC), individuals must be classified as 'employees' when deriving more than 80% of their income from the provision of personal services or from an economic activity carried out on behalf of an employer or a contractor under a labour contract or any other type of contract.

Individuals must be classified as 'self-employed' when receiving more than 80% of their income from any of the specified economic activities indicated the NTC.

In order to determine if an individual is employed or self-employed, the decree establishes that he must provide the following information to the payer or withholding agent, each year before 31 March:

- whether the income received in the previous year derives from the provision of personal services or an economic activity carried out on behalf of an employer or contractor in more than 80% of the total income received during the year
- whether the income received in the previous year derives from the provision of professional or technical services (that does not require the use of specialised materials, supplies, specialised machinery or equipment) in more than 80% of the total income received during the year
- whether the individual is obliged to file an income tax return for the previous year
- whether the income received in the previous year is higher than specified thresholds.

## Costa Rica



Costa Rica, a popular low tax conduit jurisdiction, has finally succumbed to the passage of transfer pricing rules. The new transfer pricing rules apply to transactions between related parties. A special transfer pricing information form must be included with affected taxpayers income tax returns for the 2013 tax period and thereafter. Tax authorities may make adjustments to taxable income if they determine that the transactions were not conducted at arm's length.

There are several definitions of related parties the more important of which is a 25% ownership threshold. The approved methods for determining the arm's-length price of a transaction are:

- the comparable uncontrolled price (CUP) method
- or, alternatively, the valuation of goods based on international price quotations (which is not an OECD-approved method)
- the cost plus method
- the resale price method
- the profit split method
- the transactional net margin method.

The new regime provides for Advance Pricing Agreements (APAs) that are valid for three years. Transfer pricing documentation should be prepared annually in Spanish and must be submitted to tax authorities upon request.



## Jamaica



The house of representatives approved a bill in order to provide the

tax administration with mechanisms to promote tax compliance, and collect and use the information required to assess taxpayers. The main objectives are to:

- increase and facilitate access to information to allow for an efficient and effective investigation, audit, assessment, collection and enforcement by the tax administration
- improve the quality and usefulness of information supplied to the tax administration on a periodic basis
- provide the commissioner general with power to request information from taxpayers
- extend the definition of taxpayer to include persons who might not be under examination by the tax authorities and persons who may be of interest to a requesting state acting in pursuance of an international agreement, in order to empower the tax authorities to obtain information on these persons

- allow tax authorities to request and obtain information in urgent circumstances without prior notification to the taxpayer
- prescribe a minimum retention period of seven years for books, records and other documents relevant to determine the person's tax liability.

## Panama



The government issued a decree to introduce new rules with respect to

withholding agents for taxes, contributions, and any other kind of levies on commercial and industrial activities derived in Panama.

A withholding agent must meet the following conditions:

- be a taxpayer in Panama
- derive at least PAB 5 million of gross income during the previous fiscal year.

The local treasury office suggests on a monthly basis a list of taxpayers who may be designated as withholding agents by the decision-making administrative body. Withholding agents are subject to the following main mandatory assignments:

- be liable for any deficiency of withholding
- transfer the withholding tax to the tax authorities by the last day of the month following the month of payment. In the case of delay, after a period of 60 days, the withholding agent is subject to legal proceedings.

## Peru



The local tax authorities have published regulations with respect

to the tax incentives created to promote productivity. The tax incentives regulations relate to:

- scientific and technological research expenses
- technological innovation expenses
- credit for employees' training expenses.

The provisions will be in force effective as of 1 January 2014.

## Puerto Rico



The 2013 'Tax Burden Redistribution and Adjustment Act' has

amended the 2011 tax code by disallowing various deductions. The following are now regarded as non-deductible expenses:

- expenses related to the use, maintenance and depreciation of residential property located outside Puerto Rico
- expenses related to the ownership, use, maintenance and depreciation of automobiles (with exceptions)
- a percentage of the following payments made abroad if such expenses are not subject to income tax in Puerto Rico (provided that such income is not exempt under a tax incentive act or any other law granting income tax exemptions):
  - 51% of expenses incurred or paid to related legal entities located outside Puerto Rico. For the purposes of this rule, home offices are deemed related legal entities
  - 100% of expenses incurred or paid to a partner, member or shareholder that holds more than 50% of the interest in the company.

## United States



The US tax court heard a case that involved a US corporation that

repatriated funds from its wholly owned CFC and claimed a dividend received deduction (DRD), which provided a temporary one year DRD to US corporations equal to 85% of cash dividends repatriated from their CFCs and resulted in a maximum tax rate of 5.25% on such dividends.

The US IRS determined that certain royalty payments from the US corporation to the CFC were not at arm's length under internal revenue code section 482, dealing with transfer pricing. The parties made the primary adjustments that reduced the royalty payments, thereby increasing the US corporation's income.

The primary adjustments required the US corporation to make secondary adjustments, which would have been deemed capital contributions from the US corporation to the CFC. Instead, the US corporation elected to establish interest-bearing accounts receivable from the CFC to the US corporation.

Under the DRD provisions, any related party debt reduced the amount of the dividend and thus the low effective rate of taxation.

The IRS determined that the related-party debt rule applied to the two accounts receivable established as a result of the transfer pricing adjustments. The IRS thus disallowed the corresponding amount of the claimed DRD.

The US tax court rejected the US corporation's argument that the related-party debt rule applies only to intentionally abusive transactions. The US tax court explained that congress did not incorporate such an intent requirement.

The US tax court then held that the two accounts receivable qualified as increased related-party indebtedness for the purpose of the related-party debt rule. Accordingly, the US tax court affirmed the IRS's determination and denied the DRD for the amount of the related party debt attributable to the transfer pricing adjustments.

# Transfer pricing news

## France



An interesting case was heard concerning the emigration of a captive treasury centre. Although the courts could have raised the issue of an outbound intangible asset transfer for a captive service provider, the courts bypassed this issue entirely leaving the question open as to whether or not intangible value exists in a captive service provider.

A French entity (SNFF) was in charge of carrying out a cash pooling activity for the exclusive benefit of the entire group in Europe. SNFF transferred this activity to a related Swiss entity, Treasury Centre Europe (TCE). SNFF did not receive any compensation for the transfer of its cash pooling activity to the Swiss entity.

The French tax authorities considered that the transfer of the cash pooling activity of a group out of France to a related party in Switzerland qualifies as an indirect transfer of profits, for an amount equal to the market value of this activity. Consequently, the tax authorities reassessed the taxable income of the French company and also applied a withholding tax on the corresponding deemed distribution.

The administrative courts took a position on the withholding tax and on the corporate income tax, respectively. They ruled that the transfer of a business activity had a value, even if it was an administrative function which was only rendered for the internal benefit of the group (with accordingly a 'captive' clientele) and not vis-a-vis third parties.

The administrative courts reduced the amount of the reassessment and stated that the reassessment should be based on the average gross margins ratio of SNFF.

The administrative court of appeal overturned these decisions, but did not take a position on the existence of an intangible asset transfer. It merely pointed out the lack of reliability of the rates that the tax authorities used to set their reassessment. The tax authorities had not provided any information on the identity of their comparables, nor on the way they operate; moreover, the tax authorities did not consider that the lower rates retained by the administrative courts were relevant.

## India



In a recent case, the assessee, a wholly owned manufacturing and distribution subsidiary of a Dutch parent, imports fully built cars and car kits from its parent company. The assessee entered into an import agreement with its parent company that covered India's responsibilities for the marketing and promotion of the parent company's cars.

The assessee applied the resale price method as the primary method, and the transactional net margin method as the secondary method, to establish that its transactions with the parent company were at arm's length.

The tax officer argued that the assessee had contributed to the brand development of the parent company by incurring high spending, and they asked the Indian subsidiary to show why the parent company had not compensated it for expenses relating to its brand promotion, which resulted in the creation of marketing intangibles for the parent.

The Indian subsidiary argued it had a significantly high profit margin from its distribution operations, and there was no need for further compensation from the parent company. The assessee appealed to the dispute resolution panel, which upheld the tax officer's adjustment. However, the panel directed the tax officer to exclude after-sales support costs and sales bonuses from the assessee's costs in India, thereby bringing the assessee's expenditures closer into line with the spending of the comparables.

The tribunal held that a distributor's profits are generally based on pricing arrangements, although it can be compensated over and above that if it renders additional services and pricing adjustments have not covered the costs of the routine services it renders.

The tribunal held that unlike a routine distributor, the assessee also performed the functions of sales promotion and advertising and had a greater role in the company and more responsibility than the companies that were used as comparables. The tribunal therefore accepted the assessee's argument that its expenditures for warehousing, sales promotion, and advertising were necessary and justified.

The tribunal held that the compensation for additional services provided by the Indian subsidiary were embedded in the contract. After a detailed functional analysis of the Indian subsidiary and the terms of its importation agreement with its parent, the tribunal held that no further compensation was required from the parent for the assessee's extra expenses because that compensation had already been received. The tribunal therefore rejected the tax officer's transfer pricing adjustment.

## Poland



The Polish minister of finance prepared a draft regulation (decree) making several modifications to the transfer pricing regulations to bring the rules in line with the OECD transfer pricing guidelines and the recommendations of the EU joint transfer pricing forum.

One of the changes proposed is to replace the hierarchy of transfer pricing methods and adopt a 'most appropriate method'. To assess income under that method, the tax authorities would first take into account the nature of the transaction, the degree of comparability, as well as the reliability of comparability, and the availability of information on comparables.

The proposal stresses the significance of the comparability analysis. The draft decree also addresses restructuring operations. There will also be proposed new regulations on low value-adding intragroup services. Under the proposed regulations, if the taxpayer provides a description of a transaction involving such services, the tax authorities should examine the transaction based on the description presented.

The draft decree provides a broad outline of the description and lists exemplary services that qualify as low value-adding intragroup services (for example, administrative and management services, technical support, information technology services, marketing, and legal services).

The draft decree defines shareholder costs that should not be charged to related entities as costs relating to shareholding that are of no actual benefit to a related entity (and therefore do not justify charging the costs to subsidiaries). The draft decree lists exemplary shareholders' costs and includes the cost of increases in share capital, the cost of consolidated financial reporting, costs of boards of directors associated with the statutory duties of the directors, and so on.

## Ukraine



The Ukrainian ministry of revenue clarified the corporate deductibility of expenses incurred in transactions with interdependent (related) persons. The ministry said the following persons should be qualified as related:

- legal entities if one of them controls the other(s) or if two or more legal entities are controlled by a third legal entity
- a natural person, his family members, and a legal entity if that natural person or his family members control that legal entity
- managers and other executive officers of a legal entity, as well as their family members, who are authorised to undertake actions on behalf of the legal entity that will create, modify, or terminate the legal entity's legal relations
- members of any association of legal entities carrying on business activities through such association.

For tax purposes, the term 'control' means:

- a direct possession or possession through related natural persons or legal entities of a stake of at least 20% in the taxpayer's capital
- a direct influence or influence through related natural persons or legal entities of a taxpayer's business activities as a result of:
  - obtaining corporate rights permitting the exercise of decisive influence on the formation and decision-making of the taxpayer's managing bodies
  - filling posts in the taxpayer's supervisory and executive bodies with persons who already occupy similar posts in other legal entities
  - obtaining a right to enter into contracts authorising the imposition of conditions for exercising the taxpayer's business activities, to make obligatory instructions for the taxpayer, or to delegate to third persons the powers and functions of the taxpayer's managing bodies.

The ministry held, that any expenses incurred by a taxpayer in connection with the sale or exchange of goods, performance of works, or provision of services to persons considered affiliated with the taxpayer may be recognised to the extent they do not exceed the income gained from those transactions. It further held that the taxpayer may not register losses on those transactions in its tax accounting.

# Indirect taxes news

## Bulgaria



A recent Bulgarian case involves a company incorporated under Bulgarian law (the taxpayer) and their main economic activity is the trade in animals. The taxpayer declared nine invoices concerning the supply of calves for slaughter, in order to obtain, in the form of a tax credit, the deduction of the VAT relating to those invoices.

In addition, the taxpayer declared that it had exported live calves to Albania and provided proof of their purchase by invoices and by producing customs declarations, veterinary certificates indicating the animals' ear tags and veterinary certificates for the transportation of the animals on national territory.

In order to provide proof of the acquisition of the animals, in addition to the nine invoices, the taxpayer produced weight certificates, bank statements relating to payment of those invoices and the contract concluded for the supply of calves.

The taxpayer was subject to a tax investigation and the Bulgarian tax authorities requested the supplier to provide information on the supplies which it had invoiced to the taxpayer.

The taxpayer revealed certain gaps in its accounting and in its compliance with the veterinary formalities relating, in particular, to titles of ownership of the animals and to their ear tags. The tax authorities took the view that it had not been proven that those supplies had in fact been carried out and that, consequently, the taxpayer was not entitled to claim a right to deduction of the VAT relating to those supplies.

Accordingly, the Bulgarian tax authorities denied the taxpayer the right to deduct, in the form of a tax credit, the VAT relating to the invoices issued by supplier.

The taxpayer lodged an administrative appeal against that decision refusing the deduction and then appealed against the tax assessment. In particular, it claimed before that court, that the information which it had communicated was sufficient to prove that the supplies invoiced by supplier had been carried out.

The administrative court for the city of Sofia decided to stay the proceedings and to refer the following questions to the court of justice for a preliminary ruling.

The ECJ held that for purposes of claiming VAT input tax deductions, satisfaction of formal ownership rules is not required to prove the supply of goods was made.

## China



China's state administration of taxation released a bulletin which clarifies the scope of the VAT exemption on exported services under the VAT pilot programme.

The bulletin lists various sub-categories and related requirements for:

- international transportation services
- exported technology services
- technology-related information services
- innovative services
- transportation-related ancillary services
- leasing of tangible-movable property
- certification and consulting services
- radio, film, and television services.



To qualify for the tax exemption, Chinese taxpayers must sign agreements with the foreign recipients of the tax-exempt services. All income from the services must be obtained from outside China. Taxpayers are also required to separate tax-exempt income from other income and to accurately calculate the input VAT paid in connection with the provision of the tax-exempt services. Also, taxpayers must submit documents to the competent tax authority.

### Finland



it anyway?

The Finnish supreme court addressed the issue of whose VAT input is it anyway? A Finnish parent company (FI Oy) had paid an invoice issued by a German consulting firm (DE Co) which did not have a fixed establishment in Finland and which had not voluntarily registered itself to the Finnish VAT register. The invoice was addressed to FI Oy and related to a due diligence investigation which DE Co had performed on a German company, whose shares in a German subsidiary of FI Oy (DE Sub) had been acquired. The tax authorities imposed VAT on FI Oy based on the reverse charge mechanism. The issue was whether services which related to the subsidiary's business activity (ie acquiring another subsidiary), but where paid by a parent company, were deductible for the parent company.

The court held that FI Oy did not have the right to deduct the VAT as the consulting services did not have a direct link to FI Oy's own business but the business activities of its German subsidiary.

The Finnish supreme court addressed the issue of whose VAT input is

### France



In a recent case the ECJ held that a company principally established in a member state may not take into account the turnover of its branches established abroad when determining VAT deductibility.

The taxpayer is a bank which has its principal establishment in France and branches in EU member states and in third states.

Following an examination of the accounts of the taxpayer, the tax administration decided the taxpayer had a tax deficiency for VAT. Those arrears result from the administration's refusal to take account of the interest on loans granted by taxpayer's establishment of its branches established outside France.

The taxpayer objected to the declaration claiming that the amount of the interest in question could be taken into account in calculating the deductible proportion of VAT.

Those complaints were rejected by the tax administration and the taxpayer appealed to the tribunal and then to the French council of state.

In support of its appeal the taxpayer claimed that, in order to determine the deductible proportion of expenses of its principal establishment for VAT purposes, the income of its branches established in other EU member states and in third states should be taken into account as a single taxable person.

The taxpayer maintained that the branches established in an EU member state are themselves subject to VAT and must be taken into account, in determining their own deductible proportions of VAT.

The court held that the fixed establishment situated in a member state and the principal establishment situated in another member state constitute a single taxable person subject to VAT and it follows that a taxpayer is subject, in addition to the system which applies in the state of its principal establishment, to as many national systems of deduction as there are member states in which it has fixed establishments. Under the taxpayer's position there would be over-crediting of input tax. Thus the foreign branches were to be ignored in the calculation of the input tax credit.

## Indonesia



The government issued regulations on the exemption of VAT and sales tax on luxury goods for diplomatic missions and international organisations as well as their officials. The regulation applies to:

- importation of taxable goods
- supply of taxable goods
- rendering of taxable services.

A 'diplomatic mission' includes a consular representative that has been accredited to the Indonesian Government, including permanent representatives and/or diplomatic missions accredited to the association of Southeast Asian nations secretariat. The officials of a diplomatic mission who are eligible for exemption are the head and the staff of the mission. An international organisation refers to the representative of an institution under the United Nations, a foreign diplomatic mission or any foreign organisation domiciled in Indonesia.

The officials eligible for the exemption are the head, staff and experts who have received a permit to work in Indonesia. The exemption is not given to staff of diplomatic missions or international organisations who are Indonesian nationals. The exemption applies (with restrictions) to international organisations that are not subject to income tax and obtain a recommendation from the ministry of state secretariat.

## Netherlands



The ECJ held that a company may be entitled to deductions of input VAT paid on pension fund management fees if it can show a 'direct and immediate link' between the payments and its sales transactions.

The taxpayer established a pension fund for the employees that was separate from taxpayer (from a legal and fiscal point of view). Netherlands law that was in force at the time left it to employers to choose whether to set up such a fund themselves, or to entrust the performance of their obligations to an insurance company to which they would pay their contributions and that would be responsible for paying pensions to retired employees. There was no option, however, for them to retain an internal pension scheme.

A subsidiary of a taxpayer entered into contracts with suppliers of services established in the Netherlands relating to the administration of the pensions and the management of the assets of the pension fund. The costs associated with those contracts were paid by that subsidiary and not passed onto the pension fund. The taxpayer deducted the amounts of VAT relating to those costs as input tax.

The principal issue was whether a taxable person who has established a separate pension fund for the purpose of safeguarding the pension rights of their employees and former employees can deduct the tax paid on the basis of services supplied in respect of the implementation of the pension provision and the operation of the pension fund.

For a taxable person to be accorded the right to deduct input VAT, and in order to determine the extent of that right, the existence of a direct and immediate link between a particular input transaction and an output transaction or transactions giving rise to the right to deduct is, in principle, necessary.

Whether there is a direct and immediate link will depend on whether the cost of the input services is incorporated either in the cost of particular output transactions or in the cost of the goods or services supplied by the taxable person as part of his economic activities.

A taxable person who has set up a pension fund in the form of a legally and fiscally separate entity, such as that at issue in the main proceedings to safeguard the pension rights of their employees and former employees, is entitled to deduct the VAT paid on services relating to the management and operation of that fund, provided that the existence of a direct and immediate link is apparent from all the circumstances of the transactions in question.

# Treaty news

## Korea/India



A South Korean company's income from the offshore supply of goods and services used in a power plant project in India is not attributable to the company's Indian permanent establishment and is therefore not taxable in India the Delhi income tax appellate tribunal has held.

The taxpayer was executing a turnkey power plant project in India that involved the offshore supply of plant and machinery and services such as engineering, fabrication, and so on, as well as onshore supplies of plant and machinery and installation and commissioning services. The Indian client paid for each service in a lump sum. The taxpayer was responsible for all risks associated with the project until the plant was transferred to the Indian client, and the assessee provided a warrant to that effect.

The taxpayer constituted an installation PE in India under the India-Korea income tax treaty. Therefore, in its Indian return, the company divided the total revenue and attributed it separately to offshore supplies and onshore supplies of goods and services. The taxpayer maintained that the income for the offshore supplies were not attributable to the Indian PE and was therefore not taxable in India. The taxpayer computed its taxable income for the onshore supplies after deducting its onshore contractor costs from its onshore revenue. During the audit, the tax officer held that the offshore and onshore supplies and revenue were indivisible and therefore held that taxpayer's income from the project was Indian-source income attributable to the assessee's installation PE in India.

The tribunal disagreed with the tax officer. For income to be considered Indian source, the underlying activities must have a nexus with India. Although the offshore supplies were an essential part of the project, no portion of the income derived from the offshore activities could be attributed to the Indian PE, unless the tax officer was able to show either that the price of the offshore supplies was not at arm's length or that the Indian PE was somehow involved in them. Without that evidence, the revenue from the offshore supplies could not be taxed in India, the tribunal held.

## The Netherlands



The Netherlands will improve tax transparency and update tax treaties with low-income countries and low middle-income countries. Tax treaties with Zambia and 22 other developing countries will be revised to allow the incorporation of anti-abuse clauses where necessary. The government is taking the following measures:

- substantial activity requirements (companies must run genuine risks in the Netherlands and the actual management of the company must be conducted in the Netherlands) will apply to more companies
- the Netherlands will inform its treaty partners spontaneously when, in retrospect, a company turns out not to meet the substantial activity requirements. Thanks to this improved information exchange with the source country, that country will be in a position to deny the treaty benefits to a company
- information exchange will also apply to particular financing companies that have obtained advance certainty
- the tax administration will process requests for a tax ruling from holding companies (these companies receive dividends from non-residents and pay out dividends to non-residents) if the group in which they operate has sufficient ties with the Netherlands.

## Russia



The Russian ministry of finance issued guidance in which it clarified the

corporate tax regime for interest payments that a Russian legal entity makes to a non-resident legal entity located in a jurisdiction that does not have a tax treaty with Russia. The ministry of finance held that the payer must withhold from each payment corporate tax at a 20% rate.

The ministry of finance stated that under the tax code, the corporate tax base for foreign legal entities that do not operate in Russia through a PE consists of income derived from Russian sources. The ministry of finance held that income in the form of interest that a non-resident legal entity receives from a Russian legal entity should be qualified as income gained from the Russian sources for corporate tax purposes.

## US/Belgium



The competent authorities

of the US and Belgium entered into an agreement regarding the application of 'Article 7' (business profits) of the convention between the governments of the US and Belgium for the avoidance of double taxation and the prevention of fiscal evasion with respect to taxes on income. Specifically the agreement authorises:

- the use of the OECD authorised approach to determine the profits of a business enterprise attributable to a PE
- the agreement also authorises double taxation relief is to be applied where the OECD approach results in a tax liability at the PE.

The competent authorities of the US and Belgium agree that paragraph 1, Article 7 of the convention is to be interpreted in a manner entirely consistent with the full OECD approach as set out in the OECD report. This means a transfer pricing profit considering the PEs functions, assets, and risks must be considered.

The provisions of the convention that require a determination of whether an asset or amount is effectively connected or attributable to a PE are also to be interpreted in a manner entirely consistent with the full OECD approach as set out in the report.

Where, in accordance with the full OECD approach a contracting state adjusts the profits that are attributable to a PE of an enterprise of one of the contracting states and taxes accordingly the profits of the enterprise that have been charged tax in the other state, the competent authorities of the US and Belgium agree that the other contracting state shall (to the extent necessary to eliminate double taxation) make an appropriate adjustment if it agrees with the adjustment made by the first-mentioned state. If the other contracting state does not so agree, the contracting states shall eliminate any double taxation resulting therefrom by mutual agreement.

When double taxation arises due to the application of the principles of the full OECD approach, the US will continue to eliminate double taxation by allowing the foreign tax credit provided by the laws of the US, subject to the limitations of those laws. Where a taxpayer can demonstrate to the US competent authority that such double taxation has been left unrelieved after the application of mechanisms under US law such as the utilisation of foreign tax credit limitation created by other transactions, the US will relieve such additional double taxation.

# Tax policy

## OECD

The BIAC to the OECD has released a statement covering various tax best practices for engaging with tax authorities in developing countries.

The tax best practices identified in this statement are intended to support responsible business tax management and to enhance co-operation, trust and confidence between tax authorities in developing countries and international business, understanding that business must comply with the laws and regulations of the jurisdiction in which it operates.

These tax best practices aim to promote stability, certainty and consistency in the application of tax principles as well as to support the capacity building for efficient and effective tax authorities in developing countries. This will foster cross-border trade, investment and sustainable growth for the benefit of all.

## Tax best practices

1. Businesses should be open and transparent with tax authorities about their tax affairs and provide relevant, reasonably requested information that is necessary to enable a balanced assessment of possible tax risks.
2. Businesses should commit to responding to reasonable tax authority enquiries and make payment of their tax liabilities within established due dates, or within a reasonable time-frame where no such due dates are established.
3. Where tax authorities ask reasonable, specific and legitimate questions, businesses should commit to answering those questions in a straight-forward and transparent manner.
4. If questions or assessments from the tax authorities appear not to be legitimate or are based on misunderstandings of the facts or the law, businesses should work with tax authorities where possible to identify the issues and explore options to resolve misunderstandings.
5. Where relevant, reasonably requested information is not available, businesses should inform the tax authorities and explore mutually acceptable alternatives in a timely manner.
6. Businesses should work collaboratively with tax authorities to achieve early agreement on disputed issues and certainty on a real-time basis, wherever possible.
7. Businesses may utilise tax incentives that are transparent, publicly published and endorsed by the host nation legislation.
8. Businesses should refrain from claiming or accepting exemptions not contemplated in the statutory, regulatory, or administrative framework related to taxation, financial incentives, or other issues.
9. Businesses should follow established and agreed upon procedures and channels when dealing with tax authority officials.
10. Businesses should consider how best to explain fully to the public, their economic contribution and taxes paid in the jurisdictions in which they operate, where they determine that such explanation would be helpful in building trust in the tax system.



## OECD

The BIAC to the OECD has released a statement covering tax principles for international business. The statement of tax principles is intended to promote and affirm responsible business tax management by international businesses. These principles are based on five key observations:

1. Public trust in the tax system is a vital part of any flourishing society and growing economy.
2. Most businesses comply fully with all applicable tax laws and regulations, recognising the obligations of governments to protect a sustainable tax base.

3. International businesses contribute significantly to the global economy and pay a substantial amount of tax comprising not only corporation tax, but also labour taxes, social contributions and other taxes such as environmental levies and VAT.
4. Transparency, open dialogue and co-operation between tax authorities and business contributes to greater compliance and a better functioning tax system.
5. Tax is a business expense which needs to be managed, like any other, and therefore businesses may legitimately respond to tax incentives and statutory alternatives offered by governments.

## The objectives

- to enhance co-operation, trust and confidence between tax authorities, business taxpayers and the public in regard to the operation of the global tax system
- to promote the efficient working of the tax system to fund public services and promote sustainable growth
- to support stability, certainty and consistency in global tax principles that will foster cross-border trade and investment.

## Tax planning principles

- international businesses should only engage in tax planning that is aligned with commercial and economic activity and does not lead to an abusive result
- international businesses may respond to tax incentives and exemptions
- international businesses should interpret the relevant tax laws in a reasonable way, consistent with a relationship of 'co-operative compliance' with tax authorities

- in international tax matters, businesses should follow the terms of the applicable DTA and relevant domestic and OECD guidance. Businesses should engage constructively in international dialogue on the review of global tax rules and the need for any changes.

## Transparency and reporting principles

Relationships between international businesses and tax authorities should be transparent, constructive, and based on mutual trust with the result that tax authorities and businesses should treat each other with respect, and with an appropriate focus on areas of risk. International businesses should, therefore:

- be open and transparent about their tax affairs with the tax authority in each jurisdiction and provide the relevant, reasonably requested information (subject to appropriate confidentiality provisions) that is necessary to enable a reasonable review of possible tax risk
- work collaboratively with the tax authorities to achieve early agreement on disputed issues and certainty on a real-time basis, wherever possible
- where necessary seek to increase public understanding of the tax system in order to build trust
- where they determine explanations in order to build public trust in the tax system, they should consider how best to explain to the public their economic contribution and taxes paid in the jurisdictions in which they operate.

The BIAC to the OECD has released a statement covering tax principles for international business.





## South Africa



The minister of finance announced members of the tax review committee

as well as the committee's terms of reference. The committee's appointments give effect to the minister's announcement in February that the government will initiate a tax review this year 'to assess the tax policy framework and its role in supporting the objectives of inclusive growth, employment, development and fiscal sustainability'.

The terms of reference for the tax review committee are to inquire into the role of the tax system in the promotion of inclusive economic growth, employment creation, development and fiscal sustainability. The committee will in its work take into account recent domestic and global developments and, in particular, the long term objectives of the national development plan.

The committee will make recommendations to the minister of finance. Any tax proposals arising from these recommendations will be announced as part of the normal budget and legislative processes. As with all tax policy proposals, such proposals will be subject to the normal consultation and parliamentary oversight.

The committee should evaluate the South African tax system against the international tax trends, principles and practices, as well as recent international initiatives to improve tax compliance and deal with tax base erosion.

The following aspects should receive specific attention from the committee:

- an examination of the overall tax base and tax burden including the appropriate tax mix between: direct taxes, indirect taxes, provincial and local taxes
- the impact of the tax system in the promotion of small and medium size businesses, including analysis of tax compliance costs, the possible further streamlining of tax administration and simplification of tax legislation
- a review of the corporate tax system with special reference to:
  - the efficiency of the corporate income tax structure
  - tax avoidance (eg base erosion, income splitting and profit shifting, including the tax bias in favour of debt financing)
  - tax incentives to promote developmental objectives
  - the average (and marginal) effective corporate income tax rates in the various sectors of the economy.

# Who's who

## Grant Thornton International Ltd

### Francesca Lagerberg

#### Global leader – tax services

T +44 (0)20 7728 3454

E francesca.lagerberg@gti.gt.com

### Claude Ledoux

#### Executive director – tax operations

T +1 312 602 8522

E claudel.ledoux@gti.gt.com

### Bill Zink

#### Executive director – tax quality and training

T +1 312 602 9036

E william.zink@gti.gt.com

### Gunter Spielmann

#### Executive director, EMEA – tax services

T +49 (0) 163 895 2434

E guenter.spielmann@gti.gt.com

### Regional tax resources

#### Winston Romero

Senior tax development manager – Americas

T +1 312 602 8349

E winston.romero@gti.gt.com

#### Mirka Vaicova

Tax development manager – APAC and Middle East

T +852 3987 1403

E mirka.vaicova@gti.gt.com

#### Jessica Maguren

Tax development manager – Europe and Africa

T +44 (0)20 7391 9573

E jessica.maguren@gti.gt.com

### Global coordinators

#### Agata Eysymontt

Coordinator – tax specialist services

T +44 (0)20 7391 9557

E agata.eysymontt@gti.gt.com

#### Francie Kaufman

Global project coordinator – training and quality

T +1 262 646 3060

E francie.kaufman@gti.gt.com

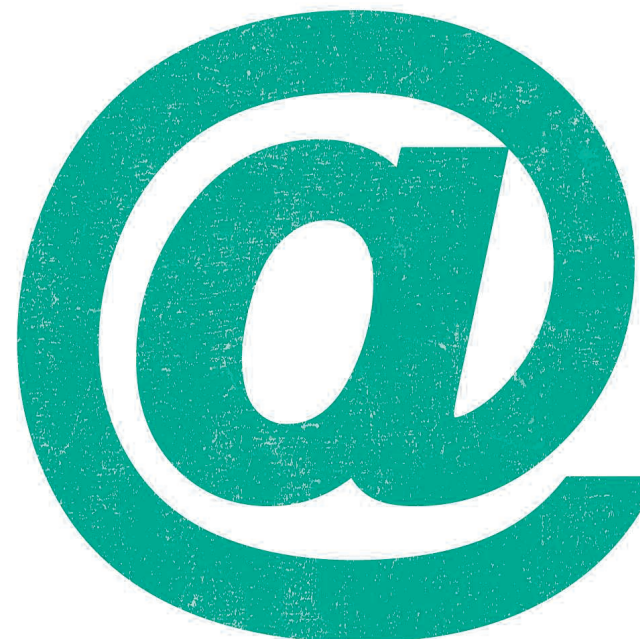
### Marketing

#### Russell Bishop

Senior marketing executive – tax

T +44 (0)20 7391 9549

E russell.bishop@gti.gt.com



© 2013 Grant Thornton International Ltd.  
 "Grant Thornton" refers to the brand under which the Grant Thornton member firms provide assurance, tax and advisory services to their clients and/or refers to one or more member firms, as the context requires. Grant Thornton International Ltd (GTIL) and the member firms are not a worldwide partnership. GTIL and each member firm is a separate legal entity. Services are delivered by the member firms. GTIL does not provide services to clients. GTIL and its member firms are not agents of, and do not obligate, one another and are not liable for one another's acts or omissions.