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INDIA
BUDGET 2018

The Finance Bill presented by Indian Finance Minister on 1 February 2018 has been passed by both Houses of Parliament and received Presidential assent on 29 March 2018. Tax amendments have been introduced to support the larger agenda of easing doing business, widening the tax base, etc. Some of the key amendments relevant for foreign investors are summarised below:

1. **Corporate tax rates**
   In line with the roadmap announced to reduce corporate tax rates from 30% to 25%, the headline tax rate for fiscal year 2018-19 for domestic companies with turnover of INR 2.50 billion in the fiscal year 2016-17 is reduced to 25%. This seeks to cover almost all small and medium sized enterprises in India.

2. **Capital gains tax**
   Since 2004, long-term capital gains arising from transfers of listed equity shares or units of equity-oriented funds (specified assets) have not been taxable.

The Finance Act now introduces a tax of 10% on capital gains in excess of INR 0.1 million on transfers of specified assets after 31 March 2018. Grandfathering is provided for gains accruing up to 31 January 2018. Similar provisions are applicable for capital gains in the hands of foreign institutional investors.

Acquisition cost will be determined as follows:

(a) For existing holdings of specified assets (i.e. acquired before 1 February 2018) – Higher of:
- Actual cost; and
- Lower of fair market value or sale consideration;

(b) For bonus and rights shares acquired before 1 February 2018 – Fair market value as on 31 January 2018;

(c) For equity shares not listed on 31 January 2018 but listed at the time of transfer – Fair market value mentioned in (a) above, determined as the indexed cost of acquisition, adjusted for inflation up to the fiscal year 2017-18.

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EDITOR'S LETTER

Welcome to this issue of *BDO World Wide Tax News*. This newsletter summarises recent tax developments of international interest across the world. If you would like more information on any of the items featured, or would like to discuss their implications for you or your business, please contact the person named under the item(s). The material discussed in this newsletter is meant to provide general information only and should not be acted upon without first obtaining professional advice tailored to your particular needs. *BDO World Wide Tax News* is published quarterly by Brussels Worldwide Services BVBA. If you have any comments or suggestions concerning *BDO World Wide Tax News*, please contact the Editor via the BDO Global Office by e-mail at mireille.derouane@bdo.global or by telephone on +32 2 778 0130.

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3. Digital economy taxation

To tackle tax challenges of the digital economy, India introduced an Equalisation Levy in 2016 on online advertisement services rendered by non-residents not having a Permanent Establishment (PE) in India. To capture businesses operating remotely through a digital medium without creating a physical presence in India, a new nexus rule in domestic law has been introduced by the Finance Act, in line with options suggested in the BEPS Action Plan 1. To this effect, the test of a business connection to tax income accruing or arising to a non-resident in India, is expanded to include a significant economic presence concept. Significant economic presence is defined to mean:

- Carrying out transactions in respect of goods, services or property in India, including provision of or download of data or software in India in excess of certain amounts to be notified; or
- Systematic and continuous soliciting of business activities or engaging in interaction with a certain number of users in India through digital means.

The above amendment will enable India to negotiate for inclusion of a similar nexus rule in its tax treaties. Pending corresponding amendments in the PE rule in tax treaties, cross-border business profits will continue to be taxed under existing provisions of tax treaties.

4. Business connection through agency

The business connection test hitherto covered only cases where contracts were concluded in India by an agent of the non-resident. Aligning with Multilateral Instrument provisions dealing with artificial avoidance of a PE, the Finance Act has widened this test to include business activities carried out through a person who habitually plays the principal role leading to conclusion of contracts by a non-resident. The conditions are that the contract should be:

- In the name of the non-resident;
- For transfer of ownership of, or for granting of right to use, property owned by the non-resident or that the non-resident has right to use; or
- For provision of services by the non-resident.

5. Dividend distribution tax on deemed dividend

A loan or advance given by a closely held company to a shareholder holding 10% or more voting power or to a concern in which the shareholder has a substantial interest is treated as a dividend. Such a deemed dividend was taxable in the hand of recipient. The Finance Act has now levied a dividend distribution tax on such deemed dividend at the rate of 30% to be payable by the company as opposed to the recipient.

6. International Financial Services Centre (IFSC)

(a) Capital gains

The Finance Act has provided a relaxation in the transfer provisions by excluding transactions in Bonds or Global Depository Receipts or rupee-denominated bonds of an Indian company or derivatives by a non-resident on a recognised stock exchange located in the IFSC;

(b) Alternate Minimum Tax (AMT)

The Finance Act has reduced the AMT rate for units located in the IFSC deriving income in convertible foreign exchange to 9%.

7. Start-ups

Start-ups are eligible for a 100% deduction of profits in three out of seven years from the date of incorporation. The Finance Act has expanded the definition of start-ups eligible for this incentive. While the earlier definition only covered start-ups driven by technology or intellectual property, the Finance Act has revised the definition to include even scalable business models with a high potential of employment generation or wealth creation.

To obtain the profit-linked deduction, the earlier condition stipulated that turnover should not exceed INR 250 million up to the fiscal year ended 31 March 2021. The condition is now relaxed by providing that the turnover should not exceed the specified limit in the year in which the deduction is claimed.

8. Country-by-Country Reporting (CbCR)

With retrospective effect from the fiscal year 2016-17, the Finance Act has made certain amendments to the CbCR regime:

- The constituent entity, other than the parent entity or alternate reporting entity of the international group (where the Consolidated Group Revenue threshold was crossed), resident in India will now be required to file a CbCR in India, where there is no filing obligation for the ultimate parent entity in its home jurisdiction. The due date for such filing will be prescribed later;
- The Finance Act has provided an exemption to the constituent entity resident in India from filing a CbCR in India, if the alternate reporting entity files the CbCR within the due date of filing CbCR in its country of residence, provided India has signed a tax treaty and an agreement with the country of alternate reporting entity for sharing of CbCR reports;
- The Finance Act has extended the time limit for filing a CbCR by the ultimate parent entity or alternate reporting entity resident in India to twelve months from the end of the reporting accounting year.

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AUSTRALIA

INTERNATIONAL TAX DEVELOPMENTS IN AUSTRALIA SIGNAL FOCUS ON CROSS BORDER ACTIVITY

Many international tax developments have unfolded in Australia during the last few months including the following issues that are summarised in this article:

- Australian Taxation Office (ATO) guidance on cross-border financing;
- ATO guidance on Diverted Profits Tax;
- Legislation on Multinational Anti Avoidance Law (MAAL) that closes loopholes involving trusts and partnerships;
- Legislation to implement the Multinational Convention to Implement Tax Treaty Related Measures to Prevent BEPS;
- Draft law to implement Australia's adoption of the OECD hybrid mismatch rules; and
- The first round of Country-by-Country Reporting files in Australia that were lodged for the 2016 year.

ATO guidance on cross-border financing following the Chevron case

Building on the ATO's Transfer Pricing success in the 2017 Chevron Australia decision, the ATO continues its scrutiny on cross-border financing arrangements. The Practical Compliance Guideline (PCG), PCG 2017/4, finalised on 5 February 2018, sets out the framework used by the ATO to assess risk in relation to certain related party financing arrangements having regard to a combination of quantitative and qualitative indicators. The ATO uses this risk assessment to tailor its engagement with taxpayers according to the features of its related party financing arrangements, the profile of parties to the arrangements, and behaviour of taxpayers.

The PCG, which applies from 1 July 2017 to both existing and newly created financing arrangements, is not a public ruling, but rather provides guidance to taxpayers to understand where the ATO will allocate compliance resources to test the tax outcomes of related party financing arrangements. The ATO has been clear that the PCG does not constitute a 'safe harbour', nor alter or affect in any way its interpretation of the relevant law.

ATO guidance on Diverted Profits Tax

On 18 December 2017, the ATO released an important draft ruling on the application of the Diverted Profits Tax (DPT). Draft Law Companion Ruling, LCR 2017/D7 explains how the ATO will apply the new DPT law and, in particular, clarifies new concepts introduced by the measure to provide taxpayers with greater certainty on the application of the new law. On the same date the ATO also released Practice Statement Law Administration, PS LA 2017/2, which provides specific direction to ATO staff on the internal administrative oversight framework for the DPT, with an emphasis on the processes leading to the issue of a DPT assessment, which will provide assurance to taxpayers that the new rules will be applied with the appropriate levels of internal review.

This was followed by PCG 2018/D2 issued on 7 February 2018, which contains scenarios with examples illustrating 'high risk' and 'low risk' cases that can be used in determining whether sufficient economic substance exists to support the allocation of profit or prices set between international related parties. This highlights the far-reaching nature of the DPT law and the extent of analysis and evidence expected to prove that the DPT provisions do not apply in the taxpayer's circumstances. It will be of particular use to taxpayers in self-assessing their level of DPT risk, and indicating what, if any, further work is required to support their position and avoid the application of the DPT.

The DPT only applies to 'significant global entities', i.e. entities with either annual global income of AUD 1 billion or more or that are part of a group of entities that have annual global income of AUD 1 billion or more.

Legislation on MAAL and closing loopholes involving trusts and partnerships

On 28 March 2018, the Australian Government introduced legislation to Parliament to extend its Multinational Anti Avoidance Law (MAAL) to prevent taxpayers from using trusts and partnerships in corporate structures to avoid the application of the MAAL. The MAAL, which took effect in Australia on 1 January 2016 and applies to 'significant global entities' (SGEs), is designed to prevent large multinationals from avoiding Australian tax by using artificial or contrived arrangements to avoid having a taxable permanent establishment (PE) in Australia.

The changes address concerns that companies can avoid Australia's anti-avoidance rules targeting global companies through the use of arrangements that would insert Australian partnerships or trusts in their structures to facilitate avoidance of the law when supplies and income are passed between the trust or partnership, and the global company. The amendments seek to ensure that when deciding whether the MAAL applies to a tax arrangement, supplies made and income received by a closely related trust or partnership would be treated as being made or received by the foreign company.

The MAAL effectively deems the foreign SGE to have a PE in Australia, and overrides the business profits article in the relevant double tax agreement, thus making the Australian-sourced profits subject to Australian income tax.

Legislation to implement the Multilateral Convention to Implement Tax Treaty Related Measures to prevent BEPS

On 28 March 2018 the Australian Government introduced legislation to Parliament for the implementation of the Multilateral Convention to Implement Tax Treaty Related Measures to Prevent Base Erosion and Profit Shifting (Multilateral Instrument or MLI), which incorporates into Australia's existing bilateral tax treaties new provisions that seek to curtail tax avoidance by multinational enterprises and improve cross-border tax dispute resolution. The Australian Government signed the MLI on 7 June 2017.

Pending the ratification of the Convention by Australia and its bilateral tax treaty partners, the Convention will modify almost all of Australia's bilateral tax treaties (except the treaty with Germany) to implement the relevant BEPS outcomes aimed to prevent their exploitation for tax avoidance purposes and improve tax treaty-based dispute resolution mechanisms. These provisions concern hybrid mismatches, tax treaty abuse, avoidance of PE status, and improvements to tax dispute resolution, including mandatory binding arbitration.

Draft law to implement the OECD hybrid mismatch rules

On 24 November 2017, the Government released draft law to implement the OECD hybrid mismatch rules to prevent multinational groups from exploiting tax differences across jurisdictions. The draft law broadly applies to payments between related parties, and structured arrangements. Generally, these rules apply to transactions that result in a deduction in the country of payment but the receipt is not taxed in the country of the recipient, or where there are deductions in both Australia and another country for the single payment. The draft law also included imported hybrid mismatch rules which, in essence, seek to reduce or eliminate tax deductions for payments made by an Australian company which directly or indirectly fund a hybrid mismatch outcome in any country that has not adopted OECD hybrid mismatch rules.

On 7 March 2018, the Australian Government released a revised draft OECD hybrid mismatch law with new integrity measures to discourage foreign interposed zero or low tax rate entities lending to Australia and address branch mismatch arrangements. The dual inclusion income rule was also expanded to ensure that an amount is not inappropriately taxed twice. The revised draft law also includes measures to deal with branch mismatch arrangements.

Country-by-Country obligations in Australia

The first round of Country-by-Country (CbC) reporting files in Australia were recently lodged for the 2016 year. CbC reporting requirements apply to SGEs or Australian entities (of any size) which are part of an accounting consolidated group with global revenue at or above AUD 1 billion during the preceding income year. The ATO requires the submission of the Master File, along with the Local File, which is a unique Australian requirement. The CbC Local File differs from the OECD standard in form and content. Whilst the 'OECD CbC Local File' is akin to transfer pricing documentation, the 'Australian CbC Local File' is a collation of information transaction-by-transaction and also requires submission of intercompany legal agreements, advance pricing agreements etc.

CbC submissions in Australia also require the input of information and documents using specialised software, which converts the information into the required (machine readable) .xml format. As CbC reporting requirements in Australia differ from the OECD standard and global requirements, this has led to confusion amongst taxpayers' head offices in relation to Australian CbC reporting requirements.

There are also significant potential penalties for late lodgement: (one day late can lead to a potential penalty of AUD 105,000), up to a maximum of AUD 525,000 per document.

It is expected that the ATO will analyse the data collated from CbC reporting compliance to better tackle transfer pricing risks.

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HONG KONG

2018-19 BUDGET HIGHLIGHTS

The Financial Secretary, Mr Paul Chan Mo-po, delivered his second Budget speech on 28 February 2018. The Budget proposals will be subject to review and modification by the Legislative Council prior to the enactment of the legislation. We summarise below the main proposals of interest to international businesses.

Profits Tax

The rate of Profits Tax for 2018-19 remains at 16.5% for corporations and 15% for unincorporated businesses. The first HKD 2 million of assessable profits of eligible taxpayers will be chargeable at half of the tax rate.

A one-off reduction of profits tax for the year of assessment 2017-18 by 75% is proposed, subject to a ceiling of HKD 30,000 per case.

It is proposed to allow a full tax deduction for capital expenditure on eligible energy-efficient building installations and renewable energy devices in one year instead of over five consecutive years.

Salaries Tax

A one-off reduction of salaries tax and tax under personal assessment for the year of assessment 2017-18 by 75% is proposed, subject to a ceiling of HKD 30,000 per case.

Industry-specific proposals

Innovation and technology

It is proposed to introduce an additional tax deduction for domestic expenditure on research & development (R&D) (a 300% tax deduction for the first HKD 2 million qualifying R&D expenditure and a 200% deduction for the remainder).

Financial services industry

(i) Bond market
- A three-year Pilot Bond Grant Scheme will be launched, to attract local, Mainland and overseas enterprises to issue bonds in Hong Kong for the first time. Each enterprise can apply for a grant for up to two bond issues, to cover half of the issue expenses, capped at HKD 2.5 million each.
- The qualifying debt instrument scheme will be amended to include debt securities listed on the Hong Kong Stock Exchange and extend the scope of tax exemption from debt instruments with an original maturity of not less than seven years to instruments of any duration.

(ii) Asset and wealth management
- The existing tax concessionary treatment applicable to the fund industry with regard to international requirements on tax co-operation will be reviewed.
- An open-ended fund tax exemption regime will be introduced later in 2018.
- The feasibility of introducing a limited partnership regime for private equity funds and the related tax arrangements will be examined.

(iii) Corporate treasury centres
It is proposed to extend the coverage of the profits tax concession to specified treasury services provided by qualifying corporate treasury centres to all their onshore associated corporations.

(iv) Insurance industry
Tax arrangements and other regulatory requirements to enhance Hong Kong as an insurance hub will be explored.

BDO comment

In 2017-18, profits tax, salaries tax, stamp duties and land premium account for about 74% of total Government revenue. Mr Chan recognises that Hong Kong's tax base is narrow and not rooted in recurrent revenue. While Mr Chan vows to be proactive, innovative and bold in investing for the future of Hong Kong, the Budget speech would have been more encouraging had it proposed more creative and tangible approaches to incentivise different businesses in Hong Kong and more sustainable measures to broaden the Government's source of revenue.

Although the two-tiered profits tax rates regime will no doubt lower the tax burden of enterprises, in particular small and medium ones, the attractiveness of Hong Kong's once low tax regime will continue to diminish in the wake of global trends to reduce income tax rates. Further reductions in tax rates and enhancement in tax certainty by reducing the general statute of limitation (currently six years) would help foster Hong Kong's international competitiveness.

While the Budget speech did not mention the Tax Policy Unit (TPU) set up after Mr Chan's maiden Budget speech last year, we look forward to the Government's update on the progress of the TPU's work in respect of long term measures to address Hong Kong's narrow tax base. We hope to see concrete proposals with details and specific implementation timelines soon.

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SINGAPORE

INNOVATION TAX INCENTIVES ENHANCED

In the Singapore Budget announcements on 19 February 2018, the Singapore Government placed special emphasis on developing the nation into a hub of enterprise, innovation and technology. Faced with an ever-changing global landscape, one of the key areas of focus is to make innovation paramount in the region to ensure that local companies remain relevant in today's competitive economy.

In order to encourage taxpayers to innovate and create digital solutions through collaboration, the Singapore Government has made enhancements to three existing schemes:

- Enhanced deduction for intellectual property (IP) registration costs;
- Enhanced deduction for IP in-licensing costs;
- Enhanced deduction for qualifying research and development (R&D) projects performed in Singapore.

(a) Enhanced deduction for intellectual property (IP) registration costs

Currently, IP registration costs qualify for a 100% deduction under Section 14A of the Singapore Income Tax Act (SITA), and this scheme will lapse after Year of Assessment (YA) 2020. In the recent Budget announcement, the scheme has been extended until YA 2025.

In addition, with effect from YA 2019, the deduction will be enhanced to 200% on the first SGD 100,000 of qualifying IP registration costs incurred for each YA. This may encourage some small and medium enterprises in the South East Asian region to move their operations to Singapore and register their IPs here to take advantage of the favourable tax treatment.

(b) Enhanced deduction for IP in-licensing costs

Expenditure incurred on IP licensing currently qualifies for a 100% deduction. For qualifying licensing costs incurred between YA 2019 to YA 2025, the deduction will be enhanced from 100% to 200% for the first SGD 100,000 per YA. Costs incurred in excess of SGD 100,000 will continue to enjoy a 100% deduction.

It has been clarified that this enhancement will not apply to all related party licensing arrangements and any IP rights where writing down allowances under Section 19B of the SITA have been previously granted. Costs incurred on the transfer of ownership of IP rights, legal fees and expenditure that has been subsidised by the Singapore Government have been specifically excluded from the definition of qualifying expenditure. Payments made for the use of trademarks are also excluded as this does not serve to promote innovation.

(c) Enhanced deduction for qualifying R&D projects performed in Singapore

R&D forms the foundation of innovation and the Singapore Government has introduced multiple tax incentives to encourage R&D activity in Singapore. Previously under the popular Productivity and Innovation Credit (PIC) scheme, companies could enjoy up to 400% tax deductions on qualifying R&D expenditure. However, the PIC scheme is scheduled to expire after YA 2018, and companies can only enjoy deductions of up to 150%. In view of this, it was announced in the Budget that the deduction amount will be enhanced to 250% for R&D projects performed locally so as to continually spur R&D efforts.

The above enhancements should boost Singapore's position as an innovation hub and, together with the other existing tax incentives, the nation is well placed to receive foreign investments and expand local businesses.

If you are considering expanding your business to Asia and would like to explore the option of creating a business presence in Singapore, please feel free to contact us.

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SRI LANKA

CHANGES TO WITHHOLDING TAX ON CROSS BORDER PAYMENTS

The concept of tax deduction at source, i.e. withholding tax (WHT), is adopted by most countries to ensure that the fair share of tax is retained in the source country. Usually, when the withholding is made in advance, the withholding tax is treated as a payment on account of the recipient's final tax liability. It may be refunded when the liability is determined, when a tax return is filed.

With regard to cross-border payments, treaty provisions override comes into effect if a Double Tax Agreement (DTA) has been entered into between the host and home country. Sri Lanka has over 44 DTAs with various treaty partners. The applicable rates in these Agreements tend to vary, but they generally provide for reduced rates.

In the absence of a DTA with the home country, WHT on cross-border payments are imposed at the rates specified in the domestic statute. Taxation in Sri Lanka will change significantly with the new Inland Revenue Act No. 24 of 2017 coming into effect from 1 April 2018. Key changes include the WHT applicable on cross-border payments. The sources and key changes are tabulated below in accordance with the First Schedule Section (10):

Source of income	Rate/Treatment up to 31 March 2018	Rate/Treatment from 1 April 2018
Interest on foreign loans	Exempt	5% or Rate specified in the DTA
Dividends	10% or rate specified in the DTA	14% or rate specified in the DTA
Royalties	20% or Rate specified in the DTA	14% or Rate specified in the DTA
Management fees, technical fees and service fees	20% or Rate specified in the DTA	14% or Rate specified in the DTA
Specified fees	Not applicable under previous law	14%
Rent	20%	14%

CHANGES TO OUTWARD REMITTANCES MADE BY COMMERCIAL BANKS AND AUTHORISED DEALERS

The Department of Inland Revenue, by a circular issued on 16 November 2017, instructed banks and authorised dealers to ensure that they effect outward remittances only upon the furnishing of a tax clearance certificate by the remitter. This mechanism serves to ensure that the recipient non-resident has duly discharged its tax obligations in Sri Lanka. However, clearance is not required for the following types of payment:

1. Remittances of sale proceeds on quoted shares owned by non-residents in companies resident in Sri Lanka;
2. Remittances of dividends paid to non-resident shareholders if withholding tax on dividends has been paid;
3. Foreign investments made by companies resident in Sri Lanka, in accordance with the guideline issued by the Central Bank of Sri Lanka;
4. Transportation expenses in relation to freight forwarding, courier services and airline services involving the carriage of passengers and goods, subject to submission of an annual clearance certificate obtained from the Commissioner General;
5. Payments to expatriate employees including wages, salaries and other benefits which have been subjected to tax under the PAYE Scheme;
6. Remittances by export companies in respect of services in relation to advertising and marketing performed outside Sri Lanka;
7. Remittances by export companies in respect of registration of trademarks outside Sri Lanka;
8. Remittances in relation to annual subscriptions for membership of professional bodies, or periodical subscriptions for journals, magazines and other publications;
9. Remittances made in relation to student fees, examination fees, enrolment fees and payments of a similar nature;
10. Remittances in respect of visa expenses, medical expenses and hotel accommodation abroad;
11. Capital repayments of foreign loans obtained by resident companies;
12. Payments made from one country to another other than Sri Lanka.

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THE EUROPEAN UNION

AGREEMENT ON MANDATORY DISCLOSURE OF TAX INFORMATION ABOUT POTENTIALLY AGGRESSIVE TAX PLANNING ARRANGEMENTS WITH CROSS-BORDER IMPLICATIONS

On 13 March 2018, the council of Economy and Finance Ministers (ECOFIN) agreed on the **Proposal for a Council Directive amending Directive 2011/16/EU** ('the proposal') as regards mandatory automatic exchange of information in the field of taxation in relation to reportable cross-border arrangements).

The proposal was published on 21 June 2017, and foresees new transparency rules for advisers and intermediaries who facilitate potentially 'aggressive tax planning schemes'. If advisers or intermediaries are involved in such tax planning arrangements, they should report this to the relevant tax authorities. The tax authorities will subsequently automatically exchange this information with the tax authorities in the other jurisdictions involved, every quarter of a year. We summarise below the most relevant aspects of the proposal.

The proposal

Which arrangements should be disclosed?
On the basis of the proposal, reportable cross-border arrangements should be subject to mandatory disclosure. A cross-border arrangement exists if an arrangement involves an EU Member State and another country (also if this is a non-EU country) and meets at least one of the following conditions:

– The parties to the arrangements are tax residents of different jurisdictions;

– One (or more of) the parties is considered dual resident for tax purposes;

– One (or more of) the parties carries on a business in another jurisdiction through a permanent establishment (PE) located in that other jurisdiction;

– One (or more of) the parties carries on a business in another jurisdiction through a PE which is not located in that other jurisdiction;

– The arrangement has a tax-related impact in at least two jurisdictions.

A cross-border arrangement is considered 'reportable' if it satisfies one of the specific characteristics ('hallmarks') as mentioned in annex IV of the proposal.

Who should disclose?
The mandatory disclosure rules apply to qualifying intermediaries and, if there is no intermediary, the taxpayer. Intermediaries should disclose the information to the tax authorities within five days beginning on the day after such arrangements become available to a taxpayer for implementation. Taxpayers have to disclose the information to the tax authorities within five days beginning on the day after the reportable cross-border arrangement or the first step in a series of such arrangements has been implemented.

Which information should be exchanged?
The tax authorities of a member state should exchange the following information:

– The identification of taxpayers (including associated parties) and intermediaries;

– Details of the hallmarks on which the reporting obligation is based;

– A summary of the arrangement, including the business activities, start date, value of the transactions and the national tax provisions;

– Identification of other member states involved;

– Identification of any person in the other member state (if any) likely to be affected by the reportable cross-border arrangement.

When will the new regulations enter into force?

Member States must ensure implementation of this Directive in national legislation by 31 December 2019 at the latest. The reporting obligation will apply from 1 July 2020 and the first automatic exchange with other Member States is expected to take place before 31 October 2020. The obligation to notify these structures has a certain retroactive force. All advice for which a first step of implementation is executed in the time frame between the date on which the directive formally enters into force and 1 July 2020 also has to be notified. It is expected that the directive will formally enter into force on a date in June or July 2018. If the first step in implementation is executed before that date, the advice is not to be notified.

EUROPEAN COMMISSION PUBLISHES THE NON-CONFIDENTIAL DECISION IN THE AMAZON STATE AID CASE

On 26 February 2018, the European Commission (EC) published the non-confidential decision in the Amazon State aid case after concluding in October 2017 that Luxembourg gave illegal tax benefits to Amazon. The investigation and the EC decision concerned a ruling between the Luxembourg Tax Authorities and the Amazon operating company in Luxembourg (Lux OpCo).

Amazon's structure in Europe

Lux OpCo functioned as the headquarters of the Amazon group in Europe and recorded all European sales from Amazon's European online retail and service business as carried out through the EU websites. On the basis of the ruling, Lux OpCo is taxed on the basis of a profit of between 0.45% and 0.55% of the turnover in the EU. This is achieved by paying a royalty to the Amazon holding company in Luxembourg (Lux HoldCo), a Luxembourg limited partnership, which is not subject to Luxembourg tax because of tax transparency. Lux HoldCo had no employees, no offices and no business activities and only held the shares in Lux OpCo and certain Amazon intellectual property rights for Europe. Lux HoldCo granted an exclusive license to this intellectual property to Lux OpCo, which used it to run Amazon's European retail business. The ruling indirectly entailed a method to calculate the royalties from Lux OpCo to Lux HoldCo for the rights to the Amazon intellectual property, which were used only by the operating company.

Assessment of the contested ruling

A measure can be considered State aid if it:

(1) Confers an advantage;

(2) That is selective;

(3) Which is granted by a State or through state resources; and

(4) Which (threatens to) distort competition and affects trade.

In its assessment of the contested ruling, the EC mainly focused on the presence of an advantage for Amazon as a consequence of the ruling. To establish that the contested tax ruling confers an economic advantage, the EC argues that the underlying transfer pricing arrangement is not a reliable approximation of an arm's length outcome which consequently results in a reduction of Lux OpCo's corporate income tax basis.

First and foremost, the EC believes that in view of the functions of Lux HoldCo in relation to the intellectual property rights the level of the royalty payment does not reflect economic reality. In addition, even if Lux HoldCo could be considered to perform unique and valuable functions in relation to the intellectual property rights, the EC believes that the contested ruling is based on an incorrect transfer pricing methodology which produces an outcome which is not in line with the arm's length principle. To substantiate its arguments the EC set out an in-depth examination of the functions performed, the assets used, and the risks assumed by Lux HoldCo and Lux OpCo, and of the appropriate transfer pricing method to be used.

Building on its reasoning on the presence of an advantage for Amazon, the EC concluded that the ruling was selective and was granted by the Luxembourg Tax Authorities, thus by a State or through state resources. As the ruling was selective, this (threatens to) distort competition and affect trade.

Impact

As the decision only concerns the Amazon ruling, it does not directly affect other taxpayers. Nevertheless, the decision (again) shows that the EC is seriously pushing its policy towards fair taxation and greater transparency. Transfer pricing documentation, whether underlying a ruling or not, should be in line with the functions performed, assets used and the risk assumed, and should reflect economic reality. Multinational groups with intragroup transactions should review whether their transfer pricing policy and/or group structure (still) complies with economic reality.

Follow-up

The Amazon State aid case wasn't the first such case involving a large company targeted by the EC. Following the previous decisions by the EC in the Apple, Starbucks and Fiat State aid cases, and the subsequent appeals to the Court of Justice of the European Union (CJEU), it remains to be seen whether the CJEU confirms the approach taken by the EC.

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HUNGARY

HUNGARY'S REACTIONS TO THE BEPS PROVISION

1. **Hybrid instruments (BEPS 2)**
Hungarian legislation in connection with hybrid instruments was modified even before BEPS, from 1 January 2015. The Act on Rules of Taxation provides that in the case of income affected by international treaties where in consequences of different interpretations neither of the involved States consider this income taxable in its territory, Hungary should not exempt such income from taxation.

2. **CFC regulations (BEPS 3)**
Regarding controlled foreign companies (CFC) Hungarian legislation introduced some related changes in January 2017 (earlier than the implementation deadline provided by BEPS). In simplified terms the main features are:
   - An entity should be considered a CFC only where it has over 50% of control;
   - CFC rules are applied if the foreign corporate tax (or similar type tax) actually paid is less than the difference between the corporate tax that should have been paid under Hungarian regulations and the foreign corporate tax actually paid;
   - Exceptions regarding location in EU/OECD/DTT countries no longer exist;
   - Hungarian taxation of CFC profits should be based on special kinds of activities – Not in the ratio of all profits, as previously.

3. **Royalties (BEPS 5)**
In relation to royalties, Hungary has already implemented BEPS recommendations: since July 2016, the definition of royalties has been significantly narrowed, and a new calculation method (in line with the modified nexus approach) should be applied for tax allowances, i.e.:
   i. Profit instead of income should be taken into account when determining the base of the deduction;
   ii. Only a proportionate deduction is allowed – Acquisition costs and expenditure for outsourcing to related parties are excluded; and
   iii. A 30% up-lift is allowed for qualified expenses. However, under transitional rules, former advantages may be applied in some cases until 2021.

4. **Transparency (BEPS 5)**
Higher transparency requirements and international exchange of information are also part of BEPS Action 5. In this regard, on 1 January 2017 Hungary introduced automatic data exchange on binding rulings and advanced price arrangement (APA) decisions in relation to transfer prices with tax authorities of relevant EU Member States.

5. **General Anti Avoidance Rules (BEPS 6)**
In Hungarian legislation the principle of exercising rights within their intent was already effective before recent EU initiatives against tax evasive behaviour: 'All rights and tax-related matters should be exercised within their meaning and intent. In the application of tax laws, contracts and other transactions contrived with the intent to evade the provisions of tax laws should not be construed as exercised within their specific intent'.

   (In any case, since 1 January 2018 this principle has been formally extended to the provisions of municipal tax decrees.) In relation to corporate income tax there is a further restriction: 'If the nature or substance of the transaction suggests that the main purpose of the transaction is to obtain a tax advantage in favour of any or all parties concerned, the costs and expenditure charged on the basis of such transaction should not be treated as ordinary business expenses (...) and no tax allowance may be claimed'. Before 1 January 2017 this latter rule was more permissive, only restricting those transactions whose sole purpose was to obtain a tax advantage.

   Regarding tax planning opportunities of 'preferential transformation', 'preferential transfer of assets' and 'preferential exchange of shares', the above principle occurs in a more direct way: preferential rules can only be applied provided that the transaction is based on economic reality and genuine commercial reason, which in addition should be proved in most cases by the taxpayer (in relation to preferential exchange of shares this took effect from 2012, in the other two cases from 1 January 2017.)

6. **CbC Reporting (BEPS 13)**
With an effective date of 31 May 2017, Hungary introduced legislation related to Country-by-Country Reporting (CbCR), which prescribes reporting obligations for MNEs with consolidated revenue exceeding EUR 750 million. The aim of CbCR is to strengthen the international exchange of information (e.g. detailed financial data per country).

   The liability is mainly that of ultimate parents, however, please note that all relevant Hungarian entities are responsible for submitting notifications. These obligations for financial years 2016 and 2017 had to be fulfilled electronically, by filling in the forms issued by the Hungarian Tax Authority before 31 December 2017.

   Failing to submit the report, late submission, or providing incorrect, false or incomplete information may be subject to a default penalty of up to HUF 20 million. Furthermore, as an effect of BEPS, most of the OECD Member Countries have amended their transfer pricing legislation. Thus, Hungary has also introduced new rules on transfer pricing, that present a new three pillar (Master File, Local File, CBCR) transfer pricing documentation structure.

7. **MLI (BEPS 15)**
The Multilateral Instrument (MLI) is set up to modify the application of thousands of bilateral tax treaties concluded to eliminate double taxation. It also implements agreed minimum standards to counter treaty abuse and to improve dispute resolution mechanisms while providing flexibility to accommodate specific tax treaty policies. On 7 June 2017 over 70 countries – including Hungary – signed the Multilateral Convention to Implement Tax Treaty Related Measures to Prevent Base Erosion and Profit Shifting (MLI); however, it is still not in force.

8. **Anti-tax avoidance directive (ATAD)**
Each EU Member State must implement ATAD regulations by 31 December 2018. Therefore, further modifications are expected in Hungarian regulations – mostly in connection with thin capitalisation rules (deductibility of interest expenses), exit taxes and other anti-tax avoidance rules. However, the exact details still cannot be anticipated.

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ISRAEL

TAXATION OF CRYPTOCURRENCIES

The Israeli Tax Authority (ITA) recently issued Circular 5/2018 ('The Circular') which discusses the ITA's position regarding the taxation of cryptocurrencies. The ITA examined whether these currencies would be:

- Defined as a 'currency' as set out in the Israel Bank Law (the Israel Tax Ordinance – ITO – does not define currency and makes reference to the Israel Bank Law), with the profits generated deemed as foreign exchange income and consequently exempt from tax in accordance with Israeli domestic tax law; or
- Deemed to be an asset in accordance with Section 88 of the ITO and taxed at the relevant capital gains tax rates.

Following long deliberations, the ITA took the stance that cryptocurrencies will be defined as an asset and not a currency, which coincides with the approach taken by the country's central bank. The Circular also mentions that cryptocurrency is also not a financial security, which may result in a number of legal ramifications.

As such, profits generated from the sale of cryptocurrencies will be subject to capital gains tax at a rate of 25% for individual investors (and the exemption for foreign exchange income will not be applicable) and at the corporate tax rate of 23% (for the year 2018) for corporate investors. To the extent that the activity of the taxpayer is deemed an active business activity, capital gains will be taxed at the marginal tax rates for individuals of up to 50% (including a 3% surtax, if relevant), whereas corporations will be taxed at the corporate tax rate mentioned above. The ITA also requires investors to report their profits derived from cryptocurrencies within 30 days of a transaction and to arrange prepayment for taxes due.

In addition, any taxpayer marketing, mining or trading cryptocurrencies that the ITA has deemed a business activity will also be liable to VAT at a rate of 17% in addition to the capital gains tax levied. Individual investors that are active in the field for investment purposes only and are not deemed to have a business activity will not be subject to VAT, since cryptocurrency is considered an 'intangible asset'. Notwithstanding the above, the Circular does not mention levying VAT on Initial Coin Offerings (ICO), but it should be noted that the ITA did release a draft circular which discusses the issue.

The Circular also noted that from an accounting perspective, in order to be able to present relevant evidence in the case of an audit, the taxpayer must maintain documents evidencing the trade using cryptocurrency, and verify the existence of the transaction and its monetary volume. In addition, the seller must provide details of the bank accounts through which the purchase and sale funds were transferred, and/or a computer screen capture showing the sale and purchase of the money supply and the date/time it was held by the seller.

It should be noted that while the circular sets a precedent with respect to digital currencies, the ITA is still working on initiatives that may continue to impact the industry at large, and we should mention that since 2017 the Israeli Government has been considering releasing its own cryptocurrency as one possible means of limiting black market transactions. As such, we would recommend that any individual or corporation involved with cryptocurrencies examine their activity and the tax issues that may be applicable.

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ITALY

RESTYLING OF THE ITALIAN PERMANENT ESTABLISHMENT CONCEPT

The Budget Law for 2018 No. 205 (the Law), approved by the Italian Parliament and in force since 1 January 2018, introduces new measures reflecting a broader definition of 'permanent establishment' (PE) for Italian tax law.

As provided by the Law, the Italian PE definition has been amended in respect of both 'agency PEs' and 'material PEs':

- The agency PE definition has been extended, focusing on the notion of 'conclusion of contracts' of business, just as this assumes relevance with respect to the identification of an agency PE;
- An anti-fragmentation rule has been introduced, aimed at preventing the use of the material PE exemptions to artificially avoid PE status by fragmenting a cohesive operating business into several small operations in order to argue that each part is merely engaged in preparatory or auxiliary activities.

The aim of the Law, amongst others, is to make the definition of PE more consistent with how the term is defined in the final report under the OECD's base erosion and profit shifting (BEPS) Action 7, in order to prevent the artificial avoidance of PE status in relation to BEPS, through the use of commissionaire arrangements and the specific activity exemptions.

In detail

The Law, approved by the Italian Parliament on 23 December 2017, was subsequently published in the Italian *Official Gazette* on 29 December 2017 and came in force on 1 January 2018.

The reform of the tax rules on PEs is contained in Paragraph 1010 of the Law, which amends the Italian PE definition laid down under Article 162 of the Italian Tax Income Code. The previous Italian PE definition is replaced by the PE provisions set out in the BEPS Action 7 report and transposed within the Multilateral Convention (MLI), signed on 7 June 2017 by more than 70 countries, including Italy. The implementation of the BEPS PE provisions at the level of the internal Italian standard may therefore require some multinational companies doing business in Italy to revise their business model in order to reduce the risk of disputes concerning the alleged incorporation of an Italian PE.

Redefinition of the Italian PE rules

Firstly, the Law introduces an additional assumption to the Italian material PE concept. In particular, a significant and continuous economic presence in Italy, built in such a way that it will not result in a physical presence in Italy, is deemed to constitute an Italian material PE. It should be noted that this amendment is aimed at addressing the PE concerns of foreign digital multinational groups doing business in Italy.

In addition, the Law integrates the circumstances that are deemed not to constitute a material PE and the assumptions that give rise to an agency PE, amending respectively Paragraphs 4 and 7 of Article 162 of the Italian Income Tax Code.

Material PE

According to the Law, the material PE definition does not include:

a) The use of facilities solely for the purpose of storage, display or delivery of goods or merchandise belonging to the enterprise;

b) The maintenance of a stock of goods or merchandise belonging to the company solely for the purpose of storage, display or delivery;

c) The maintenance of a stock of goods or merchandise belonging to the company solely for the purpose of processing by another company;

d) The maintenance of a fixed place of business solely for the purpose of purchasing goods or merchandise or collecting information;

e) The maintenance of a fixed place of business solely for the purpose of carrying on, for the enterprise, any activity not described in the previous points;

f) The maintenance of a fixed place of business solely for any combination of activities mentioned in the previous points;

provided that such activity or, in the case of subparagraph f), the overall activity of the fixed place of business, is of a preparatory or auxiliary character.

The Law also provides that the preparatory or auxiliary exemption list does not apply to a fixed place of business that is used or maintained by an enterprise if that enterprise or a closely related enterprise carries on business activities at the same place or at another place within Italy and:

- That place or other place constitutes a PE for the enterprise or the closely related enterprise under the provisions of the Law; or
- The overall activity resulting from the combination of the activities carried on by the two enterprises at the same place, or by the same enterprise or closely related enterprises at the two places, is not of a preparatory or auxiliary character;

provided that the business activities carried on by the two enterprises at the same place, or by the same enterprise or closely related enterprises at the two places, constitute complementary functions that are part of a cohesive business operation.

Agency PE

The Law sets out the agency PE definition where a person is acting in Italy on behalf of an enterprise and in doing so, habitually concludes contracts, or habitually plays the principal role leading to the conclusion of contracts that are routinely concluded without material modification by the enterprise, and these contracts are:

- In the name of the enterprise; or
- For the transfer of the ownership of, or for the granting of the right to use, property owned by that enterprise or that the enterprise has the right to use; or
- For the provision of services by that enterprise.

That enterprise is deemed to have an agency PE in Italy in respect of any activities which that person undertakes for the enterprise unless these activities, if they were exercised by the enterprise through a fixed place of business of that enterprise situated in Italy, fall within the preparatory or auxiliary exemptions cases, that do not cause that fixed place of business to be deemed to constitute a PE, as provided by the new Italian PE rules.

In accordance with the Law, this agency PE provision does not apply where the person, acting in Italy on behalf of a foreign enterprise, carries on business in Italy as an independent agent and acts for the enterprise in the ordinary course of that business. Where, however, a person acts exclusively or almost exclusively on behalf of one or more enterprises to which it is closely related, that person is not to be considered an independent agent with respect to any such enterprise. In particular, a person is closely related to an enterprise if, based on all the relevant facts and circumstances, one has control of the other or both are under the control of the same persons or enterprises.

In any case, a person is considered closely related to an enterprise if:

- One directly or indirectly possesses more than 50% of the beneficial interest in the other (or, in the case of a company, more than 50% of the aggregate vote and value of the company's shares or of the beneficial equity interest in the company); or
- Another person directly or indirectly possesses more than 50% of the beneficial interest (or, in the case of a company, more than 50% of the aggregate vote and value of the company's shares or of the beneficial equity interest in the company) in the person and the enterprise.

Misalignment between the domestic and the tax treaty network provisions

Upon submitting its provisional list of expected reservations to the OECD MLI, Italy reserved the right not to apply the provisions regarding the artificial avoidance of PE status through commissionaire arrangements and similar strategies contained in Article 12 of the MLI.

In practice, there is a misalignment between the amended domestic PE rules and the PE provisions laid down in the tax treaty network that should be amended by the MLI at the time of ratification.

Regarding this concern, Article 169 of the Italian Income Tax Code provides that domestic provisions prevail over those of double tax conventions only if they are more favourable to taxpayers. Consequently, the provisions of the double tax conventions in force with Italy should prevail over the stricter rules introduced in the domestic tax law. Therefore, Italy should review its MLI position in order to ensure the correct implementation of the amended PE definition under its tax treaty network.

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COOPERATIVE COMPLIANCE PROGRAMME

The cooperative compliance programme is aimed at promoting enhanced cooperation between the Italian Tax Administration and taxpayers in order to increase the level of certainty on relevant tax issues and, consequently, to prevent tax litigation.

Who can access the programme?

The following entities can participate in the programme:

1. Resident and non-resident entities having a permanent establishment (PE) in Italy, with a total turnover or operating revenues exceeding EUR 10 billion;
2. Resident and non-resident entities having a PE in Italy, with a total turnover or operating revenues equal to at least EUR 1 billion, which applied for the pilot project launched in 2013;
3. Entities acting on the opinion of the Italian Revenue Agency in response to the advance ruling on new investments, notwithstanding the threshold of turnover or revenues.

In addition, resident and non-resident companies who have the requirements set out in points 1. and 2. can, when submitting the application form, ask for admission to the cooperative compliance programme even for their resident and non-resident entities with a PE in Italy, performing strategic direction functions in relation to the tax control framework, regardless of the amount of turnover or revenues.

How to adhere to the programme

Eligible taxpayers must file an application including fundamental information on the enterprise, with particular regard to the adopted tax control framework (TCF). A TCF is the part of the system of internal control that assures the accuracy and completeness of the tax returns and disclosures made by an enterprise. The TCF plays a central part in bringing rigour to the cooperative compliance concept. It is important that within multi-national enterprises participating in cooperative compliance programme, senior managers, up to and including board-level executives, understand:

- The purpose and importance of the TCF;
- Their responsibility to be in control of tax risks; and
- The agreement to be transparent with the Revenue Agency.

The essential features of a tax control framework

The importance of the TCF lies in its ability to provide a verifiable assurance that the information and returns submitted by the taxpayer are both accurate and complete. However, cooperative compliance places an additional emphasis on disclosure and transparency:

- Disclosure signifies the willingness of the taxpayer to make the Revenue Agency aware of any tax positions taken in the return that may be uncertain or controversial, and being ready to go beyond their statutory obligations to disclose;
- Transparency refers to sharing information about the internal control system, including the design, implementation and effectiveness of the TCF that enables the taxpayer to be fully aware and 'in control' of all the positions and issues that need to be disclosed. The integrity and robustness of a well-designed and effective TCF that has been tested by the Italian Revenue agency is empirical evidence that underpins the 'justified' trust in the taxpayer, and in return the Revenue Agency can provide certainty on the disclosed tax positions.

Six principles or essential building blocks were identified. They are consistent with existing enterprise-wide models of internal control such as COSO[1], and can be summarised as follows:

1. **Tax Strategy Established** – This should be clearly documented and owned by the senior management of the enterprise, i.e. at Board level;
2. **Applied Comprehensively** – All transactions entered into by an enterprise are capable of affecting its tax position in one way or another, which means that the TCF needs to be able to govern the full range of the enterprise's activities and ideally should be embedded in day-to-day management of business operations;
3. **Responsibility Assigned** – The board of an enterprise is accountable for the design, implementation and effectiveness of the tax control framework of that enterprise. The role of the enterprise's tax department and its responsibility for the implementation of the TCF should be clearly recognised and properly resourced;
4. **Governance Documented** – There needs to be a system of rules and reporting that ensures transactions and events are compared with the expected norms and potential risks of non-compliance identified and managed. This governance process should be explicitly documented and sufficient resources deployed to implement the TCF and review its effectiveness periodically;
5. **Testing Performed** – Compliance with the policies and processes embodied in the TCF should be the subject of regular monitoring, testing and maintenance;
6. **Assurance Provided** – The tax control framework should be capable of providing assurance to tax administrations that tax risks are subject to proper control and that outputs such as tax returns can be relied upon. This is accomplished by establishing the entity's 'risk appetite' and then by ensuring that their Risk Management Framework is capable of identifying departures from that with mechanisms for mitigating/eliminating the additional risk.

These building blocks are generic in nature. In certain specific industry sectors, they may need to be supplemented with some additional features that reflect the particular risks associated with those industries.

Benefits

Admission to the cooperative compliance programme allows taxpayers to benefit from several advantages:

- Fast track ruling (no more than 45 days after receipt of the request or the integration of documents) regarding the application of tax provisions;
- Tax penalties reduced by 50% and, in any case, applied to an amount not exceeding the minimum provided by law;
- No guarantees required to obtain refunds of direct and indirect taxes.

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[1] In 1992, the *Committee of Sponsoring Organizations of the Treadway Commission* (COSO) developed a model for evaluating internal controls. This model has been adopted as the generally accepted framework for internal control and is widely recognised as the definitive standard against which organisations measure the effectiveness of their systems of internal control.

MOLDOVA

NEW SINGLE TAX FOR RESIDENTS OF MOLDOVAN IT PARKS

New amendments to the Tax Code of the Republic of Moldova have been completed, with the title X 'Other Tax Regimes', containing a dedicated tax regime for residents of virtual Moldovan information technology (IT) parks.

The main activities carried out in Moldova IT Parks are: customised software development, computer game editing, web portal activities, editing other software products, and other IT services activities. An important aspect of the virtual IT parks regime is that it offers the opportunity for residents to carry out their activities and benefit from the facilities granted, even from their own offices or residence, after properly registering.

A single tax will apply to IT park residents who meet all the conditions stipulated in the Law on IT parks.

The single tax applies to income obtained from the sale of products, provision of services and work carried out, as recorded monthly in the accounts. The single tax is 7% of sales revenue, covering corporate income tax, personal income tax, social security contributions, health insurance contributions, and local and real estate taxes.

The single tax cannot be less than a minimum amount per employee, which is 30% of the forecast national average monthly salary, multiplied by the number of employees in the current month. For example, for the 2018 year it will be approximately EUR 92/USD 115.

The fiscal period for the single tax is the calendar month.

Other tax obligations such as VAT or customs duties will be accounted for under the legislation in force.

IT companies will become virtual residents in the IT parks after registering in the Register of residents and undertaking all the obligations stipulated by the law.

The state will provide a five-year guarantee on the treatment under the preferential legislative regime.

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THE NETHERLANDS

COURT OF JUSTICE OF THE EUROPEAN UNION DECIDES THAT THE NETHERLANDS SHOULD ALLOW THE 'PER ELEMENT APPROACH' IN RELATION TO THE DUTCH FISCAL UNITY REGIME

On 22 February 2018, the Court of Justice of the European Union (CJEU) decided that the 'per element approach' applies to the Dutch fiscal unity regime. On the basis of the per element approach, certain benefits of the Dutch fiscal unity regime, which were first only granted to domestic parent companies and its domestic subsidiaries, should also be granted to foreign EU-subsidiaries of the domestic parent company, even though the foreign subsidiaries are not allowed to be part of the fiscal unity.

The decision of the CJEU may have a substantial impact on taxpayers which are part of a fiscal unity for Dutch corporate income tax purposes. As a result of this decision, the emergency repair measures, which were published by the Dutch Ministry of Finance on 25 October 2017 to prevent taxpayers from having the possibility to 'cherry pick' certain elements of the fiscal unity regime, have now entered into effect. The emergency repair measures have retroactivity to Wednesday 25 October 2017, 11:00 A.M. (Dutch time).

On the basis of these emergency repair measures, the fiscal unity regime will no longer apply to certain articles of the Dutch corporate income tax act (DCIT) and the Dutch dividend withholding tax act. For Dutch corporate income tax purposes, these articles concern interest deduction limitation rules (Article 10a and 13l DCIT), the participation exemption and the loss compensation rules in the event of a change in beneficial ownership. For dividend withholding tax purposes, the remittance deduction rule will be affected by the emergency repair measures.

As the emergency repair measures are retroactive, it might be possible to apply certain beneficial elements of the fiscal unity regime to the foreign EU-subsidiaries of a domestic parent company. Please note that this only applies for the financial years ending ultimately 24 October 2017 and for which no final corporate income tax assessment has yet been issued by the Dutch tax authorities.

For more information, we also refer to our **Update** – published in February 2018 – in which the above is outlined in more detail.

FURTHER DUTCH GOVERNMENT EXPLANATION ON FUTURE DUTCH WITHHOLDING TAX ON DIVIDENDS, ROYALTIES AND INTEREST

As already briefly mentioned in the Dutch coalition agreement 2017-2021 published on 10 October 2017, the Dutch Government is planning to abolish the Dutch dividend withholding tax for non-abuse situations. To counterbalance this abolition, the Dutch Government is looking to amend the Dutch dividend withholding tax so that it will only apply in abuse situations (i.e. payment to low tax jurisdictions) and to introduce a withholding tax on royalties and interest, also paid to low tax jurisdictions.

By letter dated 23 February 2018, the Dutch State Secretary of Finance, elaborated on the Dutch approach to counteract tax avoidance and tax evasion. As part of his explanation, the State Secretary also provided more insights on the future Dutch withholding tax on dividends, royalties and interest. The most important insights provided by the Dutch State Secretary are:

- The group of recipient countries for which payments will be subject to the new withholding tax consists of low tax jurisdictions (there is still no guidance on what exactly will be the minimum statutory tax rate to be considered low taxed or not) and countries on the EU list of non-cooperative tax jurisdictions;
- Anti-abuse legislation will ensure that dividends, royalties and/or interest – indirectly paid from The Netherlands to a low tax and/or non-cooperative tax jurisdictions by means of an artificial group structure – will be subject to the new withholding tax;
- If a tax treaty prohibits or limits the Netherlands from levying the new withholding tax on dividends, royalties and/or interest, the new withholding tax will be less effective. Because of the impact of tax treaties, the Dutch State Secretary of Finance mentioned that he will investigate if he can revise the Dutch tax treaty policy (which will only impact new tax treaties) and if he can contact the relevant tax treaty partners to prevent these situations as much as possible.

The introduction of the amended withholding tax on dividends and general abolition of the Dutch withholding tax in non-abuse situations, is scheduled for 1 January 2020. The Dutch State Secretary of Finance will publish the draft bill for the new withholding tax on royalties and interest in 2019. These withholding taxes are scheduled to be introduced in 2021.

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POLAND

THE MOST IMPORTANT CORPORATE INCOME TAX AND VAT CHANGES IN POLAND IN 2018

Many corporate income tax and VAT regulations entered into effect in Poland at the beginning of 2018. Furthermore, other changes will come into force in the coming months. In this article we summarise the most important features of those changes which may influence the application of the amended tax law in the current year.

Corporate income tax

The bill amending Polish Corporate Income Tax act was published on 27 November 2017 in the official Journal of Laws. This regulation entered into force in the beginning of 2018. The most important amendments are:

- As of 1 January 2019, tax deductibility of interest will be limited to 30% of the amount corresponding to the excess of the total revenues from all revenue sources (less interest income) over the total of tax-deductible costs (less depreciation charges recognised in the tax year under tax-deductible costs) and debt financing costs (30% of EBITDA). However, it will be possible to deduct the allowable amount within the next five tax years.
- Income will be classed by revenue sources, i.e. capital gains will be separated from income derived from other sources. It should also be pointed out that the set off of capital gains or losses against other sources of income is not allowed.
- New provisions apply to 'tax capital groups'. The legal regime for those entities has been relaxed in certain ways, including lowering the average share capital which must be held by each company to PLN 500,000 and the percentage of share capital for companies to 75%.
- The controlled foreign company (CFC) rules have been amended, including the definition and scope of a CFC. The CFC rules will only apply when the taxpayer has – directly or indirectly – 50% of the foreign company's capital (rather than 25%).
- A minimum tax on commercial real estate is introduced. The tax is obligatory for taxable persons owning commercial real properties worth more than PLN 10,000,000, based on the initial value of the assets. The minimum tax will apply to commercial buildings classified as shopping centres, shopping malls, independent shops and boutiques, other commercial real properties and office buildings.
- Tax deductibility of intangible and legal services is restricted. This services to which this applies include: advisory services, market research, advertising services, management and control, data processing, insurance, guarantees and any similar services. The limit of 5% of tax EBITDA of cost deductibility is applicable to costs from related parties.
- Deductibility of interest from debt-push-down structures is excluded.

Value added tax

In 2018 several VAT changes will enter into force, including:

- Micro-enterprises are obliged to send the JPK_VAT file by the 25th day of the month following the month the settlement relates to. Furthermore, from 1 July 2018, it is required to provide access to other JPK files in the case of e-control of the tax office.
- Regardless of turnover there will be an obligation to record sales of certain types of services on cash registers, including admission to circus performances and amusement parks, theme parks, discos, dance halls, and currency exchange services, excluding services provided by banks and cooperative savings and credit unions.
- The tax rate for medical devices made of rubber will be reduced. The scope of this amendment includes such products as contraceptives, coils, syringes, spreaders, pacifiers and oxygen bags. Those products will benefit from a reduced rate of 8%, but only if they are medical devices. Otherwise, they will be subject to a rate of 23%.

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SERBIA

NEWLY PUBLISHED RULEBOOKS ON ARM'S LENGTH INTEREST RATES AND SERVICES SUBJECT TO SERBIAN WITHHOLDING TAX

The Serbian Ministry of Finance recently published a Rulebook which defines 'arm's length' interest rates for inter-company loans for corporate income tax purposes for 2018, and a Rulebook which defines types of service revenues which are subject to Serbian withholding tax when received by non-resident legal entities.

Rulebook on 'arm's length' interest rates for 2018

The newly published Rulebook defines the following interest rates as the ones which are considered to be at arm's length for corporate income tax purposes in 2018:

1. **For Banks and finance leasing companies**
   - 3.10% for short-term loans in RSD;
   - 4.10% for long-term loans in RSD;
   - 3.19% for loans in EUR and RSD loans denominated in EUR;
   - 2.45% for loans in USD and RSD loans denominated in USD;
   - 3.12% for loans in CHF and RSD loans denominated in CHF;
   - 3.70% for loans in SEK and RSD loans denominated in SEK;
   - 1.15% for loans in GBP and RSD loans denominated in GBP;
   - 3.33% for loans in RUB and RSD loans denominated in RUB.
2. **For other legal entities:**
   - 5.84% for short-term loans in RSD;
   - 5.58% for long-term loans in RSD;
   - 3.10% for short-term loans in EUR and RSD loans denominated in EUR;
   - 3.42% for long-term loans in EUR and RSD loans denominated in EUR;
   - 12.97% short-term loans in CHF and RSD loans denominated in CHF;
   - 8.21% for long-term loans in CHF and RSD loans denominated in CHF;
   - 4.41% for short-term loans in USD and RSD loans denominated in USD;
   - 4.16% for long-term loans in USD and RSD loans denominated in USD.

Rulebook on services which are subject to Serbian withholding tax

Unless otherwise stipulated by the applicable Double Tax Treaty (DTT), starting from 1 April 2018 income from the following services is subject to 20% Serbian withholding tax if received by a non-resident legal entity:

1. Market research which comprises: collection of market information related to providing data to resident legal entities for planning purposes, organisation and control of the business of resident legal entities; processing and analysis of data; determination of characteristics and measurement of market potential; analysis of market share; analysis of sales; analysis of competition; and testing new and potential products on the market. These services do not include marketing services, including advertising services.
2. Accounting, audit and assurance services which comprise: preparation of financial statements, and audit of financial statements, i.e. checking financial statements based on which independent expert opinion about the statements is issued which confirms whether they present a fair and true picture of the business operations of the entity according to relevant regulations.
3. Other legal and business advisory services comprising: all forms of legal and business advice, in particular tax advice, lawyer services, management services for resident legal entities, and all other advisory and consultation services in connection with the business operations of resident legal entities. These services do not include holding seminars, workshops, courses and intermediation.

Notwithstanding the above, income of non-resident legal entities received in respect of dividends, interest, royalties and rent fees is also subject to 20% Serbian withholding tax, unless otherwise stipulated by the applicable DTT or the income recipient is located in a country which under Serbian legislation is on the list of tax havens.

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SPAIN
RECENT DEVELOPMENTS

Permanent establishment exposure – Server located in Spain

On 17 January 2018, the General Directorate of Taxes issued a binding tax ruling that a server of an Irish company can be considered a permanent establishment (PE) in Spain, according to the PE definition included in Paragraph 1 of Article 5 of the Double Tax Treaty signed with Ireland, even if no personnel is assigned to that server. The decisive factors were that the server is located in Spain and also that the server automatically executes trading transactions, which is the core business of the entity that exploits the server.

The Spanish General Directorate of Taxes based its argument on the provisions set out in the OECD's Commentaries on the Model Tax Convention regarding electronic commerce.

In particular, it considers that although the intellectual property, the management of risks or the financing remains in Ireland, the server meets, per se, the fixed place of business requirement for being considered a PE based on the following facts:

(i) It can be considered as a 'place': the server is located in electronic equipment physically located in Spain;

(ii) It can be considered as 'fixed': it is always located in the same place;

(iii) The company carries out part of its business activity through that server, not requiring the presence of personnel to carry out such activity;

(iv) The server is available to the company (i.e. it is owned or leased by the company); and

(v) The activity carried out is not deemed to be considered purely preparatory or auxiliary.

Although the concept of the server PE is not new at international tax level, according to our information, this is the first time that the Spanish General Directorate of Taxes has stated in a binding ruling the possibility of a server triggering a PE. Nevertheless, it is worth mentioning that this is based on the definition of a fixed place of business rather than of a server PE, which is not included in the tax treaty.

Urban Land Value Increase Tax draft bill published in the Spanish Parliament Official Gazette

On 11 May 2017, the Spanish Constitutional Court ruled that the Urban Land Value Increase Tax (ULVIT), commonly known as *'plusvalía municipal'*, was contrary to the Spanish Constitution, as it was in breach of the principle of economic capacity.

ULVIT is levied upon ownership of urban land and the tax is triggered at the moment the property right over such land is transferred by any type of arrangement (i.e. sale and purchase, gift, inheritance, contribution in kind, etc.). Under the prior wording of the law the main characteristic of this tax was that it was assessed by taking into consideration a theoretical value increase rather than the actual increase in value of the land that may have occurred during ownership.

The tax was not assessed on the basis of the difference between the sale price and the acquisition cost, but based on the evolution of the cadastral value of the land at the date of its transfer.

On 9 March 2018, in response to the judgement of the Spanish Constitutional Court, a new draft bill modifying the text of the Law that regulates the ULVIT at State level was published in the Official Gazette of the Spanish Congress. According to this draft, cases where the taxpayer can prove that no increase in the value of the land has been realised will not be subject to tax. Although the bill proposes no changes to the calculation of the taxable base, it gives the taxpayer the possibility of proving a decrease in value.

Further attention should be paid to the final wording of the law once it is finally approved by the Congress.

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UNITED KINGDOM

NEW WITHHOLDING TAX FOR CERTAIN INTANGIBLES RELATED PAYMENTS

There is ongoing debate at a UK, EU and OECD level regarding the taxation of intangible related value. There is particular focus on the taxation of digital businesses, but some of the identified issues and proposed measures could be relevant more widely than for typical digital businesses.

The UK Government is looking to lead the debate at an international level, and has recently issued a number of consultation and position papers. Amongst these, the UK Government has stated that it intends to implement a new withholding tax on certain intangibles related payments with effect from April 2019. These rules are capable of applying to both digital businesses and more traditional business models.

HMRC issued a consultation document regarding the design of the new rules in December 2017, and the consultation period closed on 23 February 2018. Whilst there is the possibility that the design of the rules will be refined as a consequence of the consultation period, the UK Government appears committed to moving forward with the concept, and therefore it will be important for businesses to review the potential impact of these measures.

Scope

The rules are proposed to apply where a **non-UK resident** person makes a **payment for the right to use or exploit intangible property in the UK** (not yet precisely defined, but intended to be broad), and the recipient is resident in a territory with which the UK does not have a double tax treaty with a non-discrimination clause. Territories without a relevant treaty include Bermuda, BVI, Cayman Islands, Gibraltar, Guernsey, Jersey, Isle of Man and Brazil.

Targets

The measures purport to target intra group arrangements that achieve an 'artificially low' rate of tax. However, the approach proposed in the consultation document makes no mention of any intention to test the motive or commerciality of an arrangement. As such, entirely commercially driven structures could be affected.

The proposed approach to implementation of the provisions suggests that the UK Government wants to apply the rules in much wider circumstances than just situations where royalty payments achieve nil or low effective tax rates for groups (the narrow objective stated in the consultation). Reading between the lines, there appears to be a broader desire to apply UK tax to income arising from the exploitation of intangibles in the UK (unless treaty obligations override such an approach). This overlaps with the UK Government's activity on the reform of the taxation of digital businesses.

US tax reform

The consultation document was issued before the recent US tax reforms were finalised and, therefore, does not reflect their impact on the international tax landscape. Among many changes, the US tax reforms have introduced a mandatory tax on accumulated offshore earnings, as well as significantly tightened controlled foreign company (CFC) provisions that will tax low taxed intangible related income on an arising basis. There is no provision in the consultation document of a credit being made available where a CFC charge has been levied on the profits of the recipient entity, so there is a risk of multiple taxation arising.

Reporting

The proposed measures could introduce onerous reporting requirements on businesses, even where no withholding tax is ultimately levied. Further, the nature of the tax (a tax imposed at source on payments by non-UK tax residents) will make enforcement of both reporting obligations and the collection of tax due practically challenging.

There is also a risk of the new measures resulting in a proliferation of similar measures in other jurisdictions. Some territories already have an established approach of applying an effective minimum taxation in considering the deductibility of payments: they could look to extend such provisions to withholding tax obligations. In such circumstances, a challenging debate could arise regarding what is an 'appropriate' level of tax in setting these rules, and to what extent should the commercial 'substance' of the arrangements be taken into account.

Overall, as we highlighted in our response to the consultation, there is a need for further clarity about the arrangements that are being targeted to ensure an appropriate balance is struck between commercial motives, structural risk and the burden of tax collection and enforcement. We await further developments in these proposals. In the meantime, please contact us if you would like to discuss the potential implications in more detail.

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CORPORATE CRIMINAL OFFENCE: NEW UK ANTI-EVASION LEGISLATION THAT AFFECTS COMPANIES AND PARTNERSHIPS WORLDWIDE

The Criminal Finances Act was enacted on 27 April 2017 and entered into force on 30 September 2017. Amongst other measures, this legislation introduced two new Corporate Criminal Offences (CCOs) of failure to prevent criminal facilitation of tax evasion. The Government has also published accompanying guidance. The legislation does not change what constitutes tax evasion; rather, it extends the scope of those persons who can be prosecuted if evasion occurs.

The new offences have a global reach and address the perceived gap in the law which makes it difficult to prosecute a 'relevant body' when its employees, contractors and other 'associated persons' are seen to be facilitating tax evasion by a taxpayer who could include a customer or a supplier.

Investigation of the offences will be undertaken by the UK tax authorities (HMRC) and the decision to prosecute will be made by the Director of Public Prosecutions. A successful prosecution would lead to an unlimited financial penalty, potential regulatory sanctions and reputational damage.

Definitions and scope of CCO legislation

A '**relevant body**' is defined as a body corporate or a partnership, wherever incorporated or formed. An '**associated person**' is a person (an individual or a corporate body) including an employee, agent or other person who performs services for or on behalf of the relevant person. In other words, a person acting on behalf of a company or partnership and knowingly aiding, abetting, counselling or procuring tax evasion by a taxpayer could result in that relevant body being found guilty of committing these new offences.

Despite its UK nature, **the legislation has a wide geographic scope and applies to the failure by a relevant body to prevent the facilitation of both UK and overseas tax evasion**.

What are the new offences and how could they apply to non-UK entities?

The domestic (UK) offence

This occurs where there is criminal tax evasion under UK law, facilitated by an associated person acting on behalf of a company/partnership and this relevant body has failed to put in place reasonable procedures to prevent the tax facilitation procedures.

It is important to appreciate that **the UK offence can be committed by any relevant body, regardless of whether it is established under UK law or the law of a foreign jurisdiction, e.g. France, US, Australia or any other country**.

> **Example 1**
>
> *A German car parts manufacturer [the relevant body] enters into a contract with an EU-based distributor [the associated person]. The distributor creates a false invoicing scheme with the assistance of a UK purchaser allowing the purchaser to evade UK taxes due on the purchase of the parts.*
>
> *Unless the German company can demonstrate it has undertaken an appropriate tax evasion facilitation risk assessment including a due diligence assessment of its distributor, then it may be found guilty of this offence.* ***This is notwithstanding the fact that the German company itself has no nexus with the UK****.* *The offence will be subject to the jurisdiction of the UK courts.*

Arguably, this may be difficult for HMRC to pursue, and we will have to wait to see how any future prosecutions operate in reality. The question as to whether the distributor is acting 'for or on behalf of' an organisation is also potentially problematic. The UK guidance indicates that this is to be determined 'by reference to all relevant circumstances', and indeed the definition of associated person specifically includes 'agents'. This might suggest, with regard to the above example, that the tax authorities would consider the exact nature of the principal-distributor relationship and the extent to which the distributor was acting as a dependent agent or entirely independent third party. In other words, was the distributor providing services to *or* for and on behalf of the German manufacturer? What was the proximity of the relationship?

The Foreign Tax (overseas) offence

The foreign tax offence operates in a similar way to the domestic offence. However, in contrast to the UK offence, it can only be committed by a relevant body which has a **UK nexus** and where the prosecution can demonstrate '**dual criminality**'.

A UK nexus occurs where a relevant body is incorporated or has part of its business (e.g. via a branch) in the UK, or in respect of which the relevant associated person was located within the UK at the time of the criminal act of facilitation of overseas tax. Dual criminality arises where, under UK law, both the tax evasion and the act of facilitation would be a tax evasion offence *and* the overseas jurisdiction has equivalent offences at both the taxpayer and facilitator level.

> **Example 2**
>
> *A Hong Kong bank has a UK branch. An employee of the bank commits a tax evasion facilitation offence while working in Singapore. The offence is caught in the UK simply by virtue of the company having a UK branch.*

Demonstrating a Defence: Reasonable Procedures

Under both the UK and Foreign Tax offences, a defence exists where the relevant body has prevention procedures in place such as are reasonable to be expected in the circumstances, or alternatively where it is not reasonable for the relevant body to have any prevention procedures in place. Relevant factors include proximity or level of control that a relevant body has over the associated person in question. Ultimately, however, the UK Government is seeking to overcome current difficulties in attributing criminal liability to corporates and partnerships for the criminal acts of associated persons who may often be their own employees.

Similar to the Bribery Act 2010, the guidance issued by HMRC focuses on the six key principles of defence set out below. The quoted sections are from HMRC guidance.

1. **Risk Assessment** – HMRC makes clear that a first step is to undertake a Risk Assessment of where associated persons could be facilitating tax evasion 'focusing on the major risks and priorities, with a clear timeframe [to mitigate these risks] and implementation plan'.
2. **Top Level Commitment** – The board and senior management should 'foster a culture within the relevant body in which activity intended to facilitate tax evasion is never acceptable'.
3. **Due diligence** – Organisations should strengthen their 'due diligence procedures … in respect of persons who perform or will perform services on behalf of the organisation, in order to mitigate identified risks'.
4. **Proportionality of risk-based prevention procedures** – Are an organisation's existing processes and control environment sufficiently robust to meet the requirements of the new legislation? HMRC 'demand more than mere lip-service to preventing the criminal facilitation of tax evasion'.
5. **Communication and Training** – The organisation should 'seek to ensure that its prevention policies and procedures are communicated, embedded and understood throughout the organisation, through internal and external communication, including training'. Details of the eLearning training we can provide to organisations can be viewed **here**.
6. **Monitoring and Review** – In the longer term, 'an organisation [will need to] monitor and review its preventative procedures and make improvements where necessary'.

Determine potential exposure

HMRC is looking to focus heavily in the coming years on the 'facilitators and enablers' of 'non-compliance' (a blanket term which encompasses both avoidance and evasion). The CCO legislation is seen as a key element of this wider response. Moreover, it is no mere paper tiger and is expected to have real teeth. Significant additional revenue is being focused in this area by HMRC, with anticipated additional revenues generated of some GBP 650 million by April 2023.

As such, we recommend organisations should take immediate steps to determine the extent of potential exposure and put in place a plan to implement prevention measures. As above, the key first step required specifically by HMRC is to evidence that the organisation has undertaken a Risk Assessment to determine where it may be vulnerable to associated persons facilitating tax evasion.

In practical terms, this means documenting where the organisation could be at risk and identifying any gaps in existing controls to manage these risks. Organisations are also developing policies and contractual terms referring to the Criminal Finances Act 2017, updating due diligence procedures and rolling out CCO training across their business.

All companies or partnerships, in particular those with a UK nexus, should ensure they are up to speed with the potential impact, especially as the legislation has now been in force since September 2017.

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ARGENTINA

TAX REFORM REGARDING DIRECT TAXES AND TAX PROCEDURAL LAW

The recent tax reform established numerous and significant changes in direct taxes and in the Tax Procedural Law, as summarised below.

Income tax

Scope of the tax extended

Income arising from the disposal of rights over trusts and similar contracts, digital currencies, and income arising from the transfer of real estate and the rights thereof have been included as taxable operations.

Income of Argentine source

Income arising from the holding and transfer of shares, equity interests, digital currencies, securities, bonds and other securities, will be considered of Argentine source when the issuer is domiciled, established or settled in the Republic of Argentina. Securities, share deposit certificates and other securities will receive the same treatment regardless of the entity issuing the certificates, the place of issue of the latter or the deposit of such shares or securities.

Specific losses

Based on the existence of new kinds of income, new specific losses have been defined – by source and category – which must, therefore, be offset exclusively against future income from the same source and class.

Exemptions

The reform eliminated some income exemptions for Argentine individuals, including:

i. Interest on fixed term deposits;

ii. Government bonds – Bonds issued by the National, Provincial or Municipal Government and the Autonomous City of Buenos Aires;

iii. Convertible bonds – Article 36 Law 23576;

iv. Debt Securities of a Financial Trust incorporated in the country in accordance with the provisions of the National Civil and Commercial Code, placed by public offering;

v. Shares in Mutual investment funds incorporated in the country – Article 1 Law 24083, placed by public offering.

This will also apply to foreign beneficiaries as long as they do not reside in non-cooperating jurisdictions, or the funds invested in do not come from non-cooperating jurisdictions (countries or jurisdictions that do not have an exchange agreement regarding information on tax matters or a treaty to avoid international double taxation with an ample clause of exchange of information in force with the Republic of Argentina).

Exporters – SMEs

With regard to exporters developing their activity in the category of micro, small and medium enterprises, a new exemption is added for amounts corresponding to refunds or reimbursements agreed by the Executive Power on those taxes paid in the domestic market which affect certain products, their raw materials and services.

Deduction of interest for financial debts

In the case of corporate entities, interest on financial debts entered into with related parties, resident or not in the Republic of Argentina, will be deductible from the tax balance corresponding to such allocation. The deduction cannot exceed the annual amount established by the National Executive Power or the equivalent of 30% of EBITDA, whichever is greater.

New assumptions

New assumptions include an assumption that any provision of funds or assets in favour of third parties by companies, not relating to operations performed for their own interest, will (unless proof is provided to the contrary) result in a taxable profit that will be assessed:

i. For the provision of funds, annual interest as specified in the regulation, considering the type of currency (local or foreign);

ii. For the provision of assets, a profit equivalent to 8% per annum of the market value for real estate, and 20% per annum of the market value for other assets.

Allocation of foreign source profits

Profits obtained through trusts, foundations of private interest and other similar foreign structures, as well as all contracts or arrangements entered into abroad or under a foreign legal regime, whose main purpose is the administration of assets, will be allocated to the resident that controls them in the financial or fiscal year in which the annual financial year ends for such entities, contracts or arrangements.

Profits of residents of the Republic of Argentina obtained from interests in companies or entities of any kind, incorporated, domiciled or located abroad or under a foreign legal regime, provided that the entity realising the profits has not been granted with a tax status, will be allocated to the shareholders, partners, owners, controllers or beneficiaries resident in the country, in the financial or fiscal year in which the annual financial year ends for the companies or entities, considering the interest held.

Profits of residents in the Republic of Argentina obtained from direct or indirect interests in companies or other entities of any kind incorporated, domiciled or located abroad or under a foreign legal regime, will be allocated to the shareholders, partners, owners, controllers or beneficiaries resident in the country, in the financial or fiscal year in which the annual financial year of the former ends, as long as certain requirements are met concurrently.

Equalisation Tax

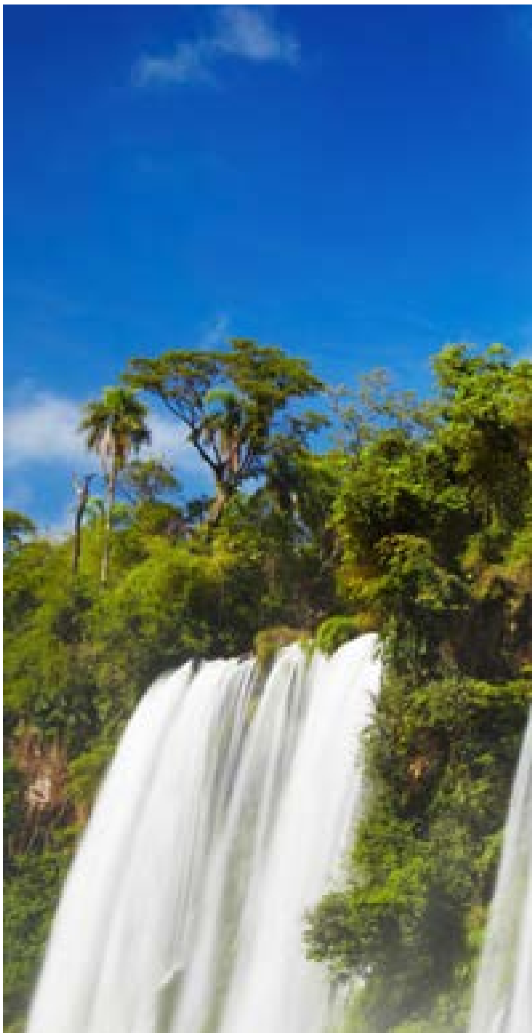
This tax will not apply to dividends distributed in respect of income generated in financial years starting from 1 January 2018.

Transfer Prices

New guidelines have been established to prevent manipulation in import and export goods transactions, in which the participation of an international intermediary is used.

Updates

The procedure of 'Adjustment for Tax Inflation' is renewed for financial years starting from 1 January 2018, applicable in the fiscal year in which a percentage variation of the Internal Wholesale Price Index (IPIM) higher than 100% is verified and accumulated in the 36 months prior to the closing of the fiscal year in which it is settled.



Tax procedural law

Rectification of tax returns

Amounts reported in tax returns can be reduced by subsequent statements, if the errors are recognised within five days of the expiry of the obligation, provided that the rectification does not exceed 5% of the taxable base originally stated.

Voluntary conclusive agreement

A new mechanism is established to conclude the processes in which the Tax Authority reviews a tax return submitted by a taxpayer and consequently, intends to assess a higher amount of tax than originally stated. This mechanism has the purpose of reducing existing litigation in the Argentine tax system.

Preventive closure

The conditions that enable the Tax Authority to preventively close an establishment have been modified. They will apply when it is proven that two (previously, one) or more of the events or omissions provided in Article 40 of the law have occurred, and when there is serious damage or the person in charge has a record of committing the same offence in a period no longer than two years (previously, one year) since the previous one was detected.

Reduction of penalties

The reduction of penalties scheme is modified, with the most relevant change being the elimination of penalties where a taxpayer voluntarily rectifies their submitted tax return.

Excusable Error

The definition of excusable error in tax matters is given the status of law. There is an excusable error when the standard applicable to the case – due to its complexity, obscurity or novelty – admits diverse interpretations that prevent the taxpayer or responsible person, even acting with due diligence, to understand its true meaning.

Mutual Agreement Procedure provided in treaties to avoid international double taxation (DTT)

The mutual agreement procedure provided in DTTs concluded by the Republic of Argentina has been regulated, in terms of taxation on income and equity, by a mechanism that tends to provide a solution to controversies arising in cases in which there is, or could be, taxation which is not in accordance with a certain agreement. The Ministry of Finance is empowered to request all the documentation they may deem necessary, without using, among others, the figure of fiscal secrecy.

Joint transfer pricing determinations in international operations

A regime has been created in which taxpayers or those responsible can request the execution of a 'Joint pricing determination in international operations' (DCPOI) with the Tax Authority, in which they establish the applicable criteria and methodologies to determine prices, amounts of consideration or profit margins of transactions, etc. If relevant in the application of international agreements or treaties, the information in the agreement may be exchanged with third parties.

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PANAMA

COURT RULING ON APPLICATION OF DOUBLE TAX TREATY PROVISIONS ON DIVIDEND DISTRIBUTIONS AND THE CONCEPT OF BENEFICIAL OWNERS

On 24 November 2017 the Administrative Tax Court of the Republic of Panama ('the Tax Court') issued a ruling (Resolution No. TAT-RF-087) by means of which it addressed the application of Clause 10 (2) of the Double Tax Treaty (DTT) signed between Panama and Luxembourg.

The case originated in a tax assessment issued by the General Directorate of the Revenue (DGI) (Resolution No. 201-4221 dated 26 November 2014) by means of which the Tax Administration denied the application of the cited provision based on its understanding that the dividends distributed by Banco Bilbao Vizcaya Argentaria (Panamá), S.A. ('BBVA Panama') a Panamanian tax resident entity, to its shareholder BBVA Luxinvest, S.A. ('BBVA Luxembourg') did not qualify for the reduced tax rate provided in the DTT because the latter was not the 'beneficial owner' of such dividends, as required under the DTT.

This precedent is interesting because it constitutes the first ruling of the Tax Court addressing the determination of the 'beneficial owner' status to apply a provision of a DTT. The Tax Court, contrary to the position of the DGI, in our opinion, regarded the treaty concept of 'beneficial ownership' as an international rule for income allocation rather than a local Panamanian anti-abuse rule.

Background – Denial of DTT tax benefits

According to the DGI, the DTT required the dividend recipient not only to demonstrate its legal status as shareholder (or 'legal owner') of the dividends, but also to produce evidence that BBVA Luxembourg was not a conduit company and that it was the final recipient of the dividend payments made by BBVA Panama.

Originally, BBVA submitted its tax treaty application form including:

(i) The tax residence certificate of BBVA Luxembourg;

(ii) A certificate issued by the Secretary of the board of directors of BBVA Panama confirming the dividend distribution disbursed to BBVA Luxembourg;

(iii) A certificate issued by the Secretary of the board of directors of BBVA Panama confirming that that BBVA Luxembourg was the owner of 44.81% of its share capital;

(iv) A withholding dividend tax form under the relevant DTT; and

(v) The corresponding tax payment receipt.

According to the DGI, the documents submitted with the DTT application were not sufficient evidence to demonstrate that BBVA Luxembourg was indeed the beneficial owner of the dividend payments.

BBVA Panama filed an administrative appeal at the DGI level challenging the tax assessment, and submitted additional documents to support its position as to the applicability of the DTT in the dividend payments made to BBVA Luxembourg. These additional documents included:

(i) A copy of the shareholder certificate issued by BBVA Panama to BBVA Luxembourg, reflecting the total amount of shares owned by the latter;

(ii) A certificate confirming the registration of BBVA Luxembourg in the Commercial Registry of Corporations of Luxembourg;

(iii) A copy of the shareholder´s registry book of BBVA Panama; and

(iv) A copy of the financial statements of BBVA Luxembourg.

The DGI confirmed its original tax assessment (see Resolution No. 201-0845 dated 19 January 2015) and concluded that BBVA Panama should have provided evidence that the dividends distributed to BBVA Luxembourg were not subsequently transferred or distributed to a third party, to demonstrate that BBVA Luxembourg was the beneficial owner of the dividends.

Ruling of the Tax Court – Beneficial owner qualification

The Tax Court issued a ruling confirming the application of the DTT benefits to the dividends distributed by BBVA Panama to BBVA Luxembourg, concluding that the latter was neither a conduit company nor an intermediary in the transaction.

To reach this conclusion, the Tax Court considered the following:

(i) (BBVA Luxembourg was a tax resident in Luxembourg;

(ii) BBVA Luxembourg was incorporated back in 1983 (i.e. it was not incorporated with the sole or main purpose of receiving the dividend distribution from BBVA Panama);

(iii) BBVA Luxembourg was the owner of more than 25% of the shares issued by BBVA Panama;

(iv) The dividend distribution was made between a subsidiary and its holding company (i.e. between related parties);

(v) BBVA Luxembourg had full rights to receive and dispose of the dividends received from BBVA Panama (i.e. there was no evidence or indication that BBVA Luxembourg was not in control of the dividends received);

(vi) BBVA Luxembourg was the legal owner of the shares to which the dividends distributed corresponded (i.e. again there was no evidence that a third party had economic control of the dividends); and

(vii) There was no evidence that BBVA acted as an intermediary for the purposes of the dividend distribution.

Interestingly, the Tax Court recognised the applicability of the OECD Commentaries on the Model Tax Convention (the OECD Commentaries) for the purposes of determining the meaning of the beneficial owner concept, even though domestic tax law does not recognise such commentaries as guidance when applying DTTs. This criterion is welcomed, given the complexities and technicalities that always surround the interpretation and application of International Conventions in general and DTTs in particular.

The Tax Court cited Sub-Paragraphs (8) (9) and (10) of Paragraph I of the Preliminary Comments of the OECD Commentaries. Basically, in our opinion, the Tax Court concluded that for a tax resident of a treaty partner not to benefit from the application of a reduced withholding treaty rate on dividends, it would be necessary to determine that the recipient is an agent or a representative of a third party, hence concluding that such recipient is a 'conduit company'. In the case at bar, there was no evidence available that BBVA Luxembourg acted as an agent or intermediary. The Tax Court also cited foreign landmark judicial precedents: Aiken Industries (1971), Royal Dutch Oil (1994) and Prevost (2008) to support its findings.

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CANADA

VOLUNTARY DISCLOSURES PROGRAM CONDITIONS TIGHTENED

On 1 March 2018, the Canadian Government narrowed the eligibility criteria for its Voluntary Disclosures Program (VDP) and imposed additional conditions to make it more difficult for those who intentionally avoid their tax obligations to benefit from it.

The VDP is available for disclosures in relation to income tax, GST/HST, excise tax, excise duty, softwood lumber products export charge and air travellers security charge.

Income tax disclosures

From 1 March 2018, two tracks are available:

- **Limited program** (providing limited relief for non-compliance where the facts suggest that there is an element of intentional conduct by the taxpayer or a closely related party):
  - Taxpayers will not be referred for criminal prosecution or charged gross negligence penalties;
  - Other penalties and interest will be charged as applicable;
  - Applicants must waive their right to object and appeal in relation to the matter disclosed.
- **General program** (for most other disclosures):
  - Taxpayers will not be referred for criminal prosecution or charged penalties;
  - Penalties will not be charged;
  - Partial interest relief is available for years preceding the three most recent years of returns required to be filed.

Disclosures in relation to GST/HST, excise tax, excise duty, softwood lumber products export charge and air travellers security charge

From 1 March 2018, three tracks are available:

- **Wash transactions** (where a supplier has failed to charge and collect GST/HST from a registrant entitled to a full input tax credit):
  - Applicants must disclose information on any non-compliance during the previous four years;
  - Taxpayers will not be referred for criminal prosecution or charged penalties;
  - Full relief of wash transaction penalties while other interest may apply.
- **Limited program** (providing limited relief for non-compliance where the facts suggest that there is an element of intentional conduct by the taxpayer or a closely related party):
  - Taxpayers will not be referred for criminal prosecution or charged gross negligence penalties;
  - Other penalties and interest will be charged as applicable;
  - Applicants must waive their right to object and appeal in relation to the matter disclosed.
- **General program** (for most other disclosures):
  - Applicants must disclose information on any non-compliance during the previous four years;
  - Taxpayers will not be referred for criminal prosecution or charged penalties;
  - Penalties will not be charged and partial interest relief is available.

Deciding whether a disclosure will be processed under the General or Limited Program

The decision on which Program will apply to a disclosure will be made on a case-by-case basis. The relevant factors will include:

- Dollar amounts involved;
- Number of years of non-compliance;
- Sophistication of the taxpayer.

Generally, applications by corporations with a gross revenue in excess of CAD 250 million in at least two of their last five tax years, and any related entities, will be considered under the Limited Program. However, acceptance into the GST/HST wash transaction and general programs may be available on a case-by-case basis.

Other significant changes

- Payment of the estimated taxes due is required. A payment arrangement can be requested if the taxpayer cannot pay the full amount when making the application;
- Disclosures can no longer be made on a no-names basis, although a pre-disclosure discussion on an anonymous basis is available;
- The name of any adviser who assisted with the non-compliance should generally be disclosed;
- Applications involving complex issues or large amounts of tax will be reviewed by a specialist before being accepted;
- Transfer pricing disclosure applications will be referred to the Transfer Pricing Review Committee.

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UNITED STATES

US TAX REFORM – IMPLICATIONS FOR FOREIGN ENTITIES WITH A US FOOTPRINT

On 22 December 2017, President Trump signed broad tax reform legislation into law that will have significant implications for US investments. But what does it really mean for foreign multinational entities with existing US operations or for those exploring opportunities in the US market?

1. **Federal taxation of US operations**
   Among some of the changes are a reduction of the corporate tax rate to 21%, elimination of net operation loss (NOL) carry backs (replaced by a generous indefinite carry forward period), and a general limitation on NOL deductions of 80% of adjusted taxable income. In addition, the corporate alternative minimum tax, which added much complexity to the Internal Revenue Code (IRC), has been eliminated. The domestic production activities deduction has been repealed. New rules permitting 100% bonus depreciation and capital expensing provide large benefits for those making domestic capital investments.

2. **State tax consequences**
   Tax reform creates additional tax complexities for foreign investment in the United States from a state tax perspective. Not all states follow the IRC in the same manner, and how a state adopts the impending changes will impact a state's taxable income computation. Some states will need to pass additional legislation in 2018 if they wish to adopt the federal rules, or conversely, to prevent the rules from taking effect. C corporations will continue to benefit from the state and local tax deductions that have been repealed with respect to other taxpayers.

3. **Cross-border payments**
   Tax reform adds new rules impacting certain corporations that make cross-border payments to related foreign parties. If certain threshold conditions are satisfied, one such measure imposes a Base Erosion and Anti-Abuse Tax (BEAT) as a minimum tax on certain US corporations and foreign corporations with US branches that take US tax deductions giving rise to 'base erosion tax benefits'. In addition, tax reform generally limits certain interest expense deductions to 30% of modified adjustable taxable income, including certain cross-border interest payments.

4. **Anti-hybrid rules**
   Tax reform adds a new rule which may disallow deductions for interest and royalties paid or accrued to a related party pursuant to a hybrid transaction or by, or to, a hybrid entity in certain situations. This rule bears some resemblance to the Organisation for Economic Co-operation and Development's proposals in BEPS Action 2 applicable to hybrid instruments and hybrid entities.

5. **Controlled foreign corporations**
   Tax reform modifies certain constructive stock attribution rules used to determine whether a foreign corporation is treated as a controlled foreign corporation (CFC) for US tax purposes. As a result, stock of a foreign corporation owned by a foreign shareholder of a US corporation may be attributed to a US subsidiary of that foreign shareholder for the purposes of determining whether such a foreign corporation is a CFC and whether the US subsidiary is a US shareholder in the foreign corporation. This will increase the number of foreign corporations treated as CFCs. US shareholders of CFCs are generally required to file certain information returns to report their ownership interests in the CFCs along with certain other information. The IRS recently provided guidance in Notice 2018-13 on information reporting for certain foreign corporations that are CFCs due to the modification in constructive stock attribution rules.

6. **Intangibles**
   Tax reform provides US corporations with a reduced tax rate on foreign-derived intangible income (FDII). Further, US shareholders of CFCs must now include their portion of global intangible low-taxed income (GILTI) of such CFCs into taxable income. In many cases, a detailed review of a group's ownership of intangibles and business model will be needed. While GILTI and FDII generally target intangible income, given the broad scope of these provisions, multinational groups should review their structures and supply chains to determine the implications of these new rules even in situations where they do not otherwise generate income from intangible property.

7. **Partnership interests**
   The tax reform provisions provide that a gain or loss from the sale or exchange of a partnership interest is effectively connected with a US trade or business to the extent that the transferor partner (as opposed to the partnership) would have had an effectively connected gain or loss had the partnership sold all of its assets at fair market value as of the date of the sale or exchange. In addition, the purchaser/transferee is generally required to withhold tax under new withholding tax rules that apply in these instances.

Tax reform will have profound effects on the way foreign entities with a US footprint are structured

The federal tax changes will have an impact on tax planning for foreign investment and it will be necessary to model these changes to understand how to best position US operations going forward.

Foreign entities also have to understand and layer on how tax reform will impact their cost of doing business in the United States from a state tax perspective.

The new rules that apply to cross-border payments may require foreign entities with US investments to re-examine their related party arrangements, capital investment and financing structures for existing or future US operations.

As a result of new anti-hybrid rules, foreign entities will need to understand the local characterisation of royalty and interest payments among related parties and may need assistance as this is not always easy to determine.

Changes to the CFC attribution rules may result in an increased compliance burden to the US members of foreign multinational groups in certain situations.

As always, foreign entities with US operations should not undertake any radical action or restructuring of their businesses without careful consideration of all implications, for both the US and other territories.

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SOUTH AFRICA

BUDGET 2018 – TAX PROPOSALS

The South African Minister of Finance delivered the 2018 Budget Speech, incorporating the tax proposals, on 21 February 2018. We highlight below the more important proposals which are relevant to international business.

Tax

- The corporate tax rate remains unchanged at 28%;
- The value-added tax (VAT) rate is increased from 14% to 15%, effective from 1 April 2018;
- In the light of the global trend to reduced corporate tax rates, the current exemption for controlled foreign companies (CFCs) operating in countries with a tax rate of higher than 75% of the South African corporate tax rate, will be reconsidered with a view to potentially reducing the 75% threshold;
- In order to ensure that companies pay their fair share of tax in South Africa, the South African Revenue Service (SARS) intends to increase the number of transfer pricing audits to mitigate the risk of companies shifting profits to low tax jurisdictions where there is no underlying substance;
- Tax provisions which currently apply only to resident short-term insurers will be extended to apply to non-residents;
- Legislation will be introduced to prevent foreign shareholders from reducing dividends tax in respect of listed shares acquired in terms of a collateral lending arrangement;
- The anti-avoidance rules relating to share buybacks and dividend stripping will be reviewed;
- Six special economic zones, which entitle qualifying companies to a reduced corporate tax rate and an enhanced employment tax incentive, have been approved;
- The industrial policy project incentive has been extended from 31 December 2017 to 31 March 2020;
- The current research and development tax incentive will be reviewed to ensure that applications are considered and reviewed expeditiously.

Exchange control

- The South African Reserve Bank (SARB), together with other domestic financial sector regulators, will publish a new position paper on the evolving use of cryptocurrencies;
- South African companies, on application to an authorised dealer, may obtain approval to acquire between 10% and 20% of the participation rights in a foreign entity which in turn holds investments in a company located in the Common Monetary Area (CMA), which includes South Africa. This so-called 'loop structure' concession is now increased from 20% to a maximum of 40% for bona fide business investment, growth and expansion transactions and the current minimum requirement of 10% is abolished. Loop structures in excess of this threshold will still require SARB approval;
- South African companies may, subject to certain conditions, establish one domestic subsidiary as a holding company for their offshore operations. Transfers to such a holding company will be increased from ZAR 2 billion to ZAR 3 billion for listed companies and from ZAR 1 billion to ZAR 2 billion for unlisted companies, subject to SARB reporting requirements;
- The National Treasury intends to release, later this year, a paper on a proposed policy framework to facilitate the review and approval of complex cross-border transactions, as well as a comprehensive inward listings review paper.

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CURRENCY COMPARISON TABLE

The table below shows comparative exchange rates against the euro and the US dollar for the currencies mentioned in this issue, as at 16 April 2018.

Currency unit	Value in euros (EUR)	Value in US dollars (USD)
Indian Rupee (INR)	0.01242	0.01532
Australian Dollar (AUD)	0.62930	0.77607
Hong Kong Dollar (HKD)	0.10329	0.12738
Singapore Dollar (SGD)	0.61748	0.76156
Euro (EUR)	1.00000	1.23278
Hungarian Forint (HUF)	0.00321	0.00396
US Dollar (USD)	0.81081	1.00000
Polish Zloty (PLN)	0.23951	0.29530
Serbian Dinar (RSD)	0.00844	0.01041
Swiss Franc (CHF)	0.84233	1.03855
Swedish Krona (SEK)	0.09563	0.11784
British Pound (GBP)	1.15403	1.42326
Russian Rouble (RUB)	0.01305	0.01609
Canadian Dollar (CAD)	0.64252	0.79245
South African Rand (ZAR)	0.06694	0.08256

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