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GLOBAL TAX WEEKLY
a closer look

ISSUE 108 | DECEMBER 4, 2014

SUBJECTS TRANSFER PRICING INTELLECTUAL PROPERTY VAT, GST AND SALES TAX CORPORATE TAXATION INDIVIDUAL TAXATION REAL ESTATE AND PROPERTY TAXES INTERNATIONAL FISCAL GOVERNANCE BUDGETS COMPLIANCE OFFSHORE

SECTORS MANUFACTURING RETAIL/WHOLESALE INSURANCE BANKS/FINANCIAL INSTITUTIONS RESTAURANTS/FOOD SERVICE CONSTRUCTION AEROSPACE ENERGY AUTOMOTIVE MINING AND MINERALS ENTERTAINMENT AND MEDIA OIL AND GAS

COUNTRIES AND REGIONS EUROPE AUSTRIA BELGIUM BULGARIA CYPRUS CZECH REPUBLIC DENMARK ESTONIA FINLAND FRANCE GERMANY GREECE HUNGARY IRELAND ITALY LATVIA LITHUANIA LUXEMBOURG MALTA NETHERLANDS POLAND PORTUGAL ROMANIA SLOVAKIA SLOVENIA SPAIN SWEDEN SWITZERLAND UNITED KINGDOM EMERGING MARKETS ARGENTINA BRAZIL CHILE CHINA INDIA ISRAEL MEXICO RUSSIA SOUTH AFRICA SOUTH KOREA TAIWAN VIETNAM CENTRAL AND EASTERN EUROPE ARMENIA AZERBAIJAN BOSNIA CROATIA FAROE ISLANDS GEORGIA KAZAKHSTAN MONTENEGRO NORWAY SERBIA TURKEY UKRAINE UZBEKISTAN ASIA-PAC AUSTRALIA BANGLADESH BRUNEI HONG KONG INDONESIA JAPAN MALAYSIA NEW ZEALAND PAKISTAN PHILIPPINES SINGAPORE THAILAND AMERICAS BOLIVIA CANADA COLOMBIA COSTA RICA ECUADOR EL SALVADOR GUATEMALA PANAMA PERU PUERTO RICO URUGUAY UNITED STATES VENEZUELA MIDDLE EAST ALGERIA BAHRAIN BOTSWANA DUBAI EGYPT ETHIOPIA EQUATORIAL GUINEA IRAQ KUWAIT MOROCCO NIGERIA OMAN QATAR SAUDI ARABIA TUNISIA LOW-TAX JURISDICTIONS ANDORRA ARUBA BAHAMAS BARBADOS BELIZE BERMUDA BRITISH VIRGIN ISLANDS CAYMAN ISLANDS COOK ISLANDS CURACAO GIBRALTAR GUERNSEY ISLE OF MAN JERSEY LABUAN LIECHTENSTEIN MAURITIUS MONACO TURKS AND CAICOS ISLANDS VANUATU

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GLOBAL TAX WEEKLY
a closer look

Global Tax Weekly – A Closer Look

Combining expert industry thought leadership and the unrivalled worldwide multi-lingual research capabilities of leading law and tax publisher Wolters Kluwer, CCH publishes Global Tax Weekly — A Closer Look (GTW) as an indispensable up-to-the minute guide to today's shifting tax landscape for all tax practitioners and international finance executives.

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ISSUE 108 | DECEMBER 4, 2014

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The unacceptable face of tax journalism

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Captive Insurance & US Regulatory Competition

by Andrew P. Morriss, and Drew D. Estes

Andrew P. Morriss is Dean & Anthony G. Buzbee Dean's Endowed Chairholder, Texas A&M University School of Law; Drew Estes is a JD/MBA Candidate, Class of 2016, University of Alabama.

Regulatory competition is a key force driving jurisdictions around the world to innovate. Profs Erin O'Hara and Larry Ribstein provided a conceptual framework for understanding the incentives that drive jurisdictions to engage in regulatory competition in *The Law Market* (Oxford University Press, 2009). As they noted at the start of their book, "Parties, in effect, can shop for law, just as they do for other goods. Nations and states must take this 'law market' into account when they create new laws."

One reason jurisdictions compete in the law market is that if they can persuade businesses and individuals to bring legal business to their jurisdiction, the jurisdiction can earn taxes and fees, and local accountants, lawyers, and other professionals can benefit. Jurisdictions can compete in beneficial ways, by innovating and offering more efficient business entities; they can also compete in detrimental ways, by allowing outside interests to pollute the local environment or rob local property owners of rights. In business law, the ability of businesses to choose the law that will govern their organizational structure by choosing the jurisdiction within which they incorporate or locate their corporate seats facilitates this competition.

The competition among US states for captive insurance business began with Colorado's 1972 adoption of a specialized statute. Growth was slow at first, with just nine states following suit between then and 1992. By 2000, the number of domestic captives had doubled and this spurred additional jurisdictions to jump on the bandwagon: 12 more passed captive laws between 2001 and 2008, and four more have entered the market since then. Not all of these jurisdictions have succeeded – some have never licensed even a single captive, while others have almost 600. We examined the history of each captive statute and spoke with regulators in multiple jurisdictions in search of answers. There is no doubt that this is a highly competitive market. Moves by one jurisdiction to enhance its attractiveness lead quickly to responses by other leading competitors. For example, when protected cell companies appeared after 1999 (an innovation copied from Guernsey), US jurisdictions swiftly implemented the concept and 15 US jurisdictions had recognized protective cell captives by 2005.

Similarly, Vermont's creation of branch captives, in 1999, spread to four more jurisdictions within the year and then rapidly to others. Moreover, the top jurisdictions regularly tweak their statutes, which we see as a search for a competitive advantage. Vermont and Hawaii, two of the leading jurisdictions, have amended their statutes more than 30 times. In Hawaii's case, that comes to 1.36 material amendments per year – an astonishing level of legislative attention for a specialist body of law.

Our read of the evidence suggests there are three important factors that contribute to success in the competition. (The table below summarizes some important data.) First, there is a definite first-mover advantage, although this is not enough to explain relative success. Vermont, Delaware and Hawaii have all been leaders in the field and were early adopters. However, Colorado, Florida and Virginia were also early adopters and have not experienced the same degree of success. Second, investment in keeping a statute up to date appears to be important. (Most top jurisdictions average one material amendment per year.) Looking at the number of material amendments to statutes per year, we found a 0.491 correlation between that number and the number of captives registered. This is reinforced if we look at the adoption of the major innovations in captive structures (protected cell, branch, and special purpose captives). All the top jurisdictions recognize at least two and most recognize all three. Finally, having a public fund dedicated to the regulation and/or marketing of the jurisdiction's captive industry is linked to success, with all the most successful jurisdictions doing so as well as all but one of the next most successful group of jurisdictions. While not sufficient, a strategy of reinvesting in the industry appears to be a virtual necessity.

Is this a good thing? The original debate over corporate charter competition in the 1970s began with Prof. William Cary's 1974 *Yale Law Journal* article, "Federalism and Corporate Law: Reflections Upon Delaware" (vol. 83, p. 663) and Ralph Winter's 1977 response, "State Law, Shareholder Protection, and the Theory of the Corporation," *Journal of Legal Studies* (vol. 6, p. 251). Cary and Winter debated whether states would serve the interest of the management at the expense of the shareholders (Cary's view), allowing management to reincorporate into states where the law favored them over the shareholders or provided opportunities for management to increase the value of shares by choosing a regulatory regime that gave shareholders what they want. Winter focused on managers' need to compete for capital by giving shareholders what they wanted in order to get the capital at the lowest possible price, thus putting the competition for corporate charters into a framework in which competition for managers was conducted by showing that a state's laws advanced the interests of shareholders. Forty years later, the empirical evidence tends to support Winter, with most studies showing shareholder value increases (or, at least, does not decrease) with reincorporation into market-leader Delaware.

In the market for captive insurance, a similar dynamic is at work. The New York State Department of

Insurance issued a report, "Shining a Light on Shadow Insurance: A Little-known Loophole That Puts Insurance Policyholders and Taxpayers at Greater Risk," on captives in June 2013, arguing that "Insurance companies use shadow insurance to shift blocks of insurance policy claims to special entities – often in states outside where the companies are based, or else offshore (*e.g.* the Cayman Islands) – in order to take advantage of looser reserve and regulatory requirements." This report took on the role of Prof. Cary's 1974 article, arguing that states (and OFCs) competed for insurance managers' business by allowing them to be undercapitalized or engage in other risky behavior that offered opportunities for greater profits, by shifting risk from the insurers back to the insured and to taxpayers, who would have to pick up the pieces if insurers collapsed. In addition, the New York regulators made a real effort to publicize the term "shadow insurance" to suggest an illicit aspect to the use of captives.

The twist on Cary's original argument is that it is not the shareholders being duped but the insured. Winter's response rested on the efficiency of capital markets: if managers are gaining the ability to shift wealth from shareholders to managers by reincorporating into Delaware, a reasonably efficient capital market would correct the problem. If someone noticed the impact (and since Cary had published an article making the argument in the high profile *Yale Law Journal*, the idea was hardly a secret once his article was out), he could profit by selling short the companies that reincorporated to Delaware as their share prices would drop as managers got busy enriching themselves at shareholder expense. (That the evidence from studies of the impact of reincorporation into Delaware suggests the opposite occurs is a powerful argument against Cary's thesis). In insurance markets, this mechanism was not present. Managers would have ample time to shift wealth to themselves at the expense of policyholders, who would not notice the move until it was too late and their claims went unpaid (or were paid by the public treasury bailing out the insurer). The insureds would not notice because the transactions were being done between the insurers and their captives, and so out of the public eye. For example, the New York study pointed to the use of conditional letters of credit (*i.e.*, letters of credit that provide credit only if certain conditions are met), two-step transactions in which risk was transferred by a New York insurer to another insurer outside New York and then to a captive controlled by the original insurer, reliance on "hollow assets" such as letters of credit with a parental guarantee, and "naked parental guarantees" of the captive's losses.

We find this story implausible in the face of the evidence we found of vigorous competition among states seeking captive business. In particular, we think that the greater success of states investing in maintaining their statutes' up-to-date status by adopting substantive amendments at a rapid rate is an important indicator of quality control. Now, one could tell a story in which Hawaii or Vermont decided it did not care about whether out-of-state insurance companies used entities in Hawaii or Vermont to enrich insurance company managers

and shareholders at the expense of New York policyholders. However, this would require those states' legislatures to adopt such a posture annually, without a member ever letting slip the nefarious plan. This does not appear to us to be a realistic description of the behavior of state legislatures.

Moreover, the importance of investment back into the industry to the success of a state's captive industry is inconsistent with this theory. If all that was needed was to kowtow to the needs of shady operators, taxing the operators to fund the industry's development would be an unlikely strategy for success.

Finally, the Cary-style story makes little sense in the context of a highly regulated industry. Many insurers are major players, whose long-term profits from successful business in multiple states are far more substantial than the short-term gain from underfunding reserves in any particular state. Regulators in other states would have incentives to investigate any company whose captives led to losses elsewhere.

In short, we think the example of captive insurance law among US jurisdictions confirms the O'Hara-Ribstein theory that there is a vibrant market for law across jurisdictions where relocation from one to another is relatively cheap. This market has led to major innovations in business structures, which we think have largely reduced insurance costs for a wide range of businesses and consumers. Competitive pressures prove effective with regulatory markets, as they do in more conventional markets, in inducing innovation.

State	Initial Passage	Amendments Per Year*	Number of Captives*
Hawaii	1986	1.357	179
Utah	2008	1.167	399
Vermont	1981	0.939	588
West Virginia	2004	0.9	1
South Carolina	2000	0.857	147
Arizona	2002	0.667	106
Montana	2001	0.615	150
Oklahoma	2004	0.5	11
Connecticut	2008	0.5	4
Illinois	1999	0.467	1
Rhode Island	1999	0.467	0
Nevada	1999	0.4	150
Arkansas	2001	0.385	1
Tennessee	1978	0.361	30
D.C.	2000	0.357	135
Louisiana	2008	0.333	2
Maine	1997	0.294	3
Missouri	2007	0.286	40
Colorado	1972	0.214	4
Kentucky	2000	0.214	128
Delaware	1984	0.2	550
Alabama	2008	0.167	26
Nebraska	2007	0.143	2
New York	1997	0.118	62
South Dakota	1996	0.111	12
Florida	1982	0.063	0
Georgia	1988	0.038	0
Kansas	1988	0.038	1
Virginia	1986	0	0
Texas	2013	0	3
Oregon	2012	0	7
New Jersey	2011	0	15
North Carolina	2013	0	5
Michigan	2008	0	12

* Data collected between February and July 2014.

United States Taxation Of Income From International Shipping – Section 883

by Stephen Flott and Joseph Siegmann, Flott & Co.

Contact: sflott@flottco.com

This is the fifth in a series of articles on US taxation of income from the transportation of cargo or passengers to or from the United States or from the provision of services on the US Outer Continental Shelf, and the compliance regimes that apply to companies that receive such income.

If a foreign corporation cannot use provisions of a bilateral tax treaty to avoid the 4 percent gross tax imposed by Section 887, as discussed in the last article, it may be able to use Section 883 to exclude US source gross transportation income ("USSGTI") from its US gross income. In effect, Section 883 allows USSGTI to be excluded from a foreign corporation's gross income, thus reducing its US source income to zero. Even though technically an "exclusion from gross income," it is most commonly referred to as the Section 883 "exemption," which is how we will refer to it in these articles.

Section 883 provides a two-step qualification process for the exemption. The first depends upon the country in which the foreign corporation is incorporated. The second depends upon the identity and residence of the individuals who are the ultimate beneficial shareholders of the corporation because more than 50 percent of the value of the shares of the corporation must ultimately be owned, for more than half the days of the corporation's tax year, by shareholders who reside in countries that provide an equivalent exemption to companies organized in the United States.

Determining residence is key to both steps. The first step focuses on the country of incorporation. A corporation that earns USSGTI must be incorporated in a country that extends an equivalent exemption to corporations organized in the United States. Such countries are referred to in the Section 883 Regulations[1] as "qualified countries." If the foreign corporation is not organized in a qualified country, that is the end of the story. It may not use the Section 883 exemption regardless of who owns it.

Countries are "qualified countries" if they extend an "equivalent exemption" within the meaning of Section 883. Essentially, if a country does not tax the international shipping income of companies organized in the United States sourced in that country, it is a qualified country. This can be established in

one of two ways: an exchange of diplomatic notes with the United States explicitly exempting such income – generally called Transportation Agreements – or by its domestic law. Section 883 sets out an objective test in this regard which is not dependent upon approval from the IRS. A company that wants to claim exemption under Section 883 based on the domestic law of the jurisdiction in which it is incorporated need only prove that the domestic law of that country does not tax income from international shipping.

Table I, Part A of Revenue Ruling 2008-17 [2008-12 IRB 626, March 24, 2008] lists countries which have exchanged diplomatic notes with the United States. Table I, Part B lists countries which the IRS has determined extend an equivalent exemption under Section 883 based on their domestic laws. Even if a country is not listed in Part B of Table I, it may qualify based on proof that its domestic law qualifies.

Part A of Table I identifies the year in which each Transportation Agreement became effective and the types of income it covers. The footnotes are important as they contain limitations that may exist in the scope of an exemption. For example, the Belgium and Pakistan Transportation Agreements do not cover bareboat hire. The Chilean, Indian, Malaysian, Peruvian, Swedish and Venezuelan agreements exempt bareboat income only if it is incidental to operating income.

Part B of Table I lists those countries whose domestic law the IRS officially declared meets the "equivalent exemption" test, the date that the foreign law was reviewed, and the scope of the exemption provided by the relevant country's domestic law. Again, footnotes identify limitations. For example, bareboat hire is not within the scope of the British Virgin Islands', Qatar's and Spain's domestic law exemptions. Bareboat, time or voyage hire are not covered by Turkey's and Uruguay's domestic law exemptions.

If the foreign corporation that earns USSGTI is incorporated in a qualified country, it must be able to establish that its controlling ultimate beneficial owners ("UBOs") are also residents of a qualified country. The country of incorporation and the country of residence of the controlling UBOs can be different qualified countries and the basis on which the countries qualify can also be different. We use the term controlling because the UBOs must own more than 50 percent of the shares of the foreign corporation seeking to use the Section 883 exemption.

It is important to understand that, with some exceptions to be discussed in the next article, the controlling UBOs must be physical persons because Section 883 incorporates a "look through" rule to determine whether the foreign corporation qualifies for the exemption. This aptly named rule "looks through" legal persons (corporations, trusts, partnerships, foundations, limited liability companies, *etc.*) to identify the physical persons who ultimately control the legal person seeking to use the exemption. This requirement is often not well understood.

Many think that the Section 883 inquiry ends with a corporate shareholder; it does not. The Section 883 Regulations make it very clear that ownership must be traced to human beings, who, with few exceptions, are the only ones who can be what the regulations call "qualified shareholders."[2]

The Section 883 Regulations use attribution rules to establish "constructive ownership" of legal persons, that is, the regulations specify how ownership of an entity is apportioned among its owners. For example, in the case of a corporation, ownership is attributed *pro-rata* based on ownership of its shares. There are constructive ownership rules for partnerships, trusts and estates, taxable non-stock corporations, mutual insurance companies, non-government pension funds, and non-profit organizations.

The "look through" rule tracks ownership up to the UBOs. When a foreign corporation seeking exemption under Section 883 is wholly owned by a second corporation, the "look through" rule in effect ignores the second corporation, and looks to identify its controlling shareholder and so on up the corporate ownership chain until it reaches the UBOs. If the controlling UBOs at the top of the structure are not qualified shareholders, as defined by the Section 883 Regulations, the foreign corporation does not qualify for exemption under Section 883.

The Section 883 Regulations give particular attention to shares issued to bearer, commonly known as "bearer shares." Essentially, notwithstanding the constructive ownership rules that attribute ownership of a corporation proportionally to the holders of its shares, the Section 883 Regulations specifically prohibit attribution of bearer shares.[3] Without the attribution of its shares, a foreign corporation cannot be controlled by "qualified shareholders" and thus is subject to the tax under Section 887 on its USSGTI.[4]

When the controlling UBO is identified, he or she must be a qualified shareholder as defined in the Section 883 Regulations. To be a qualified shareholder, a UBO must reside in a qualified country, that is, the UBO must "reside" in a country which extends an equivalent exemption to US corporations. Revenue Ruling 2008-17 lists the qualified countries. A UBO qualifies if he or she resides, within the meaning of the Section 883 Regulations, in any of these countries. The basis on which the country qualifies (treaty, diplomatic note or domestic law) does not matter as long as the UBO resides in a qualified country.

The Section 883 Regulations set out two requirements to "reside" in a qualified country. First, the UBO must be "fully liable" to tax in the qualified country. Second, the qualified country must be the UBO's "tax home," defined as the country in which the UBO resides for at least 183 days in the tax year of the corporation seeking exemption under Section 883. The definition of "tax home" also includes a "regular or principal" place of business test. The 183 day minimum applies both to the place of business and the place of abode tests. The Section 883 Regulations specifically disqualify

persons who reside in the United Kingdom as "non-doms" because they are not subject to tax in the United Kingdom on their worldwide income. There are other countries that allow people who reside in them to pay either on money brought into the country or under a special arrangement. In effect, any person who lives in a country and does not pay tax on the same basis as ordinary residents will not be a qualified shareholder.

This article has discussed the rules that apply to qualified shareholders who are individuals. The next article will address qualified shareholders who are not individuals.

Endnotes

1 Treas. Reg. §1.883-1 *et seq.*, 68 Fed. Reg. 51394 *et seq.* (August 26, 2003), as amended. The effective date was postponed by Section 423 of the American Jobs Creation Act of 2004 (Pub.L. 108-357) for one year to tax years beginning on or after September 24, 2004.

2 Qualified shareholders are ultimate beneficial owners ("UBOs") who meet the residency requirements set out in the Section 883 Regulations discussed later in this article.

3 On November 15, 2010, the Treasury finalized rules that allow attribution of bearer shares if they are held in an immobilized or dematerialized book entry system. T.D. 9502, IRB 2010-46. Most jurisdictions that permit bearer shares (*e.g.*, Antigua, Cayman Islands, Liberia, and Marshall Islands) do not have such systems in place. Panama now requires bearer shares be held by designated authorized custodians. *See* Don Winner, Law 47 Passed: Panama Corporation Bearer Shares to be Restricted, *Welcome to Panama Guide*, Aug, 28, 2013, available at http://www.panama-guide.com/article.php/20130828163830289 (last visited November 17, 2014). Thus, the changes to the Section 883 Regulations permitting attribution of bearer shares in such systems are of little, if any, practical use to most companies that issue such shares. Of course, countries that allow bearer shares also authorize companies to issue shares in the names of the shareholders. These are sometimes called "registered" shares.

4 A number of foreign corporations have taken the Section 883 exemption despite that fact that their shares are issued in bearer form. One such corporation is currently engaged in a US Tax Court case challenging the validity of the prohibition on bearer shares. The case has been briefed and argued, but no decision has yet been issued.

An Exploration Of Proposals To Publicize Beneficial Company Ownership Data

by Stuart Gray, Senior Editor, Global Tax Weekly

This article looks at the key developments and issues regarding plans to make information on corporate beneficial ownership easier to access by law enforcement authorities and, more controversially, the public at large, as part of global efforts to increase tax and corporate transparency.

Lough Erne

The establishment of publicly accessible registries of beneficial ownership was one of the main points agreed by the G8 at the Lough Erne Summit in Northern Ireland in June 2013, at which the issue of tax avoidance by companies and wealthy individuals was placed at the top of the agenda by the United Kingdom.

The "Lough Erne declaration"[1] contains ten points, the foremost of which is that: "Tax authorities across the world should automatically share information to fight the scourge of tax evasion." The G8's declaration went on to recommend that multinational corporations should report to the authorities what tax they pay, and where, and that countries amend rules that enable profit shifting for the purposes of tax avoidance.

Emphasis was also placed on company ownership, with the declaration stating that "companies should know who really owns them and tax collectors and law enforcers should be able to obtain this information easily." To that end, the G8 adopted an Action Plan[2] which set out "core principles that are fundamental to the transparency of ownership and control of companies and legal arrangements." It argued that companies should obtain and hold information on their beneficial ownership, and that central registries containing these details should be set up at national or state levels. Likewise, trustees of express trusts ought to acquire such data, and financial institutions and designated non-financial businesses and professions placed under effective obligations to identify and verify the beneficial ownership of their customers.

On the enforcement side, the Action Plan emphasized that "effective, proportionate and dissuasive sanctions" must be "robustly enforced." Countries are warned to be aware of the risks attached to their anti-money laundering and counter-terrorist financing regimes, and make any appropriate reforms. Authorities should be able to act rapidly upon a request for information from a separate

jurisdiction, and, at an international level, should cooperate across borders to combat abuse.

To show their commitment to ever-tougher standards on transparency, the G8 countries published their own "action plans" on beneficial ownership at the conclusion of the Lough Erne Summit informing the world of the steps they intend to take to improve access to this type of information. Action plans were also published by governments in certain offshore jurisdictions, namely the British Overseas Territories with offshore finance industries, including Anguilla, Bermuda, the British Virgin Islands, the Cayman Islands, Gibraltar, the Turks and Caicos Islands, and the three British Crown Dependencies of Guernsey, Jersey and the Isle of Man.

Mostly variations on a theme, these action plans typically committed governments to undertake the following actions within one to two years:

- Review and/or amend national anti-money laundering and anti-terror financing legislative frameworks
- Ensure that national legislation falls into line with new standards set by the Financial Action Task Force in 2012
- Ensure that rules are in place requiring companies to maintain their own records on company ownership
- Consider whether corporate service providers should collect beneficial ownership information upon forming new companies and whether customer due diligence measures should be stronger
- Consider new laws to create a central registry of information on companies' and trusts' beneficial owners, which may or may not be open – *i.e.*, accessible by the public
- Work with other countries and supranational organizations to increase international cooperation in the area of corporate and tax transparency.

The United Kingdom

The UK is waving the corporate transparency flag particularly vigorously, perhaps feeling that it has a certain responsibility for the many offshore – both in the constitutional and economic senses – territories that remain within its sphere of influence. So having placed this issue at the heart of discussions at Lough Erne, the UK has taken an early lead in the exploration of the uncharted territory represented by the publication of beneficial corporate ownership information.

The UK Action Plan committed the Government to the following actions:

- Conduct, and share the findings of, a national assessment of money laundering and terrorist financing risks by 2014, coordinating action by the public and private sectors to assess risks, apply resources, and mitigate those risks.
- Ensure the Companies Act 2006 and UK Money Laundering Regulations oblige companies to know who owns and controls them, by requiring that companies obtain and hold adequate, accurate and current information on their beneficial ownership.
- Amend the Companies Act 2006 to require that this information is accurate and readily available

to the authorities through a central registry of information on companies' beneficial ownership, maintained by Companies House – the UK registry of incorporation – and consult on whether information in the registry should be publicly accessible.

- Ensure that trustees of express trusts are obliged to obtain and hold adequate, accurate and current information on beneficial ownership regarding the trust.
- Put in place mechanisms to ensure that the relevant competent authorities have access to information on trusts and ensure effective mechanisms to share this information with other jurisdictions, in line with bilateral and multilateral agreements.
- Improve the supervision and enforcement of those who facilitate company formation in the UK, to start with a review of supervision and enforcement of trust and company service providers. The review would include consideration of additional measures to ensure company formation agents conduct effective due diligence including the identification and verification of beneficial owners.
- Review of corporate transparency, including bearer shares and nominee directors.
- Support the Overseas Territories and Crown Dependencies to publish Action Plans setting out the concrete steps, where needed, to fully implement the Financial Action Task Force Standards.
- Improve international cooperation including the timely and effective exchange of basic and beneficial ownership information.
- Implement these measures through, and at the same time as, transposition of the 4th EU Money Laundering Directive and UK Money Laundering Regulations, through changes to the Companies Act 2006, as well as through other relevant bilateral and multilateral agreements.

In July 2013, the UK Department for Business, Innovation and Skills announced the launch of a consultation paper entitled "Transparency and trust: enhancing transparency of UK company ownership and increasing trust in UK business,"[3] setting out how the UK will implement its G8 commitment to a central registry of companies' beneficial owners. In addition it proposes the abolition of bearer shares and measures to tackle misuse of corporate directors and nominee directors.

Despite many negative responses from the 314 respondents to the consultation, the UK Government made an early decision to forge ahead with its corporate transparency proposals.

Claiming that "for too long a small minority have hidden their business dealings behind a complicated web of shell companies," and that "this cloak of secrecy has fueled all manners of questionable practice," Prime Minister David Cameron told an audience in October 2013 that not only will plans for a register go ahead, but that the Government intends the register to be open to the public.

According to the Government's own response document to the submissions made during the transparency consultation, published in April

2014,[4] the decision to forge ahead with a public corporate beneficial owner registry was arrived at "on the basis that good corporate behavior and tackling company misuse would be best served by greater transparency."

Under the UK proposals, the existing definition of beneficial ownership, as applied in the anti-money laundering context, will be used as the basis for the statutory definition of "beneficial ownership" in the context of these new requirements. This means that information on individuals who ultimately own or control more than 25 percent of a company's shares or voting rights, or who otherwise exercise control over the company or its management, will need to be obtained and held by the company and provided to the central registry. Where a qualifying beneficial interest in a company is held through a trust arrangement, the trustee(s) or any other natural person(s) exercising effective control over the activities of the trust will be required to be disclosed as the beneficial owner of the company.

It was then confirmed in the 2014 Queen's Speech in June, in which the Government's legislative program for the year ahead was announced, that legislation would be tabled in parliament to create a central public register of beneficial ownership.

Tension Within The European Union

Draft legislation for a Fourth European Union Anti-Money Laundering Directive[5] represents the EU's response to changes made to the FATF Recommendations in 2012[6] and a review by the European Commission of the existing Third Money Laundering Directive, 2005. The draft contains new requirements with regards to recording information of the beneficial owners of companies.

The revised Directive proposes new measures in order to improve access to beneficial ownership information, and it requires legal persons to hold information on their own beneficial ownership. This information should be made available to both competent authorities and obliged entities. For legal arrangements, trustees are required to declare their status when becoming a customer and information on beneficial ownership is similarly required to be made available to competent authorities and obliged entities.

In the case of corporate entities, the draft Directive defines a beneficial owner as any natural person who ultimately owns or controls a legal entity through direct or indirect ownership or control over a sufficient percentage of the shares or voting rights in that legal entity, including through bearer share holdings, other than a company listed on a regulated market that is subject to disclosure requirements consistent with European Union legislation or subject to equivalent international standards. A percentage of 25 percent plus is the threshold set to show evidence of ownership or control through shareholding and applies to every level of direct and indirect ownership.

In the case of legal entities, such as foundations, and legal arrangements, such as trusts, which administer and distribute funds, a beneficial owner is defined as:

- the natural person(s) who exercises control over 25 percent or more of the property of a legal arrangement or entity; and
- where the future beneficiaries have already been determined, the natural person(s) who is the beneficiary of 25 percent or more of the property of a legal arrangement or entity; or
- where the individuals that benefit from the legal arrangement or entity have yet to be determined, the class of persons in whose main interest the legal arrangement or entity is set up or operates. For beneficiaries of trusts that are designated by characteristics or by class, obliged entities shall obtain sufficient information concerning the beneficiary to satisfy itself that it will be able to establish the identity of the beneficiary at the time of the payout or when the beneficiary intends to exercise vested rights.

However, the European Commission, which drafts EU legislation, now finds itself in the middle of a fight between the European Parliament, which wants amendments relating to information on beneficial owners substantially broadened in scope to require member states to maintain public beneficial ownership registries, and the member states themselves, some of which are opposed to the idea of public registries. Initially, it was expected that this "trialogue" process would result in an agreement between the Parliament, the European Council and the Commission by the end of the year, allowing MEPs to then vote on a final version of the legislation. As 2014 draws to a close however, there is a significant risk that this timetable could slip.

A Level Playing Field

Unlike the consensus that has been built towards global automatic exchange of financial information for the purposes of enforcing national tax laws, with dozens of countries having signed up to the OECD's common reporting standard and existing mechanisms such as the Multilateral Convention on Mutual Administrative Assistance, it is clear that there is some degree of hesitation on the part of governments to force the beneficial ownership issue.

A major concern is the likelihood of an uneven playing field in beneficial ownership reporting standards, a particular worry for offshore jurisdictions which have made significant strides in the area of transparency, largely thanks to the OECD's drive to "clean up" offshore, which began around 15 years ago. It is already a legal requirement in many of these territories that information on beneficial owners is recorded, either by corporate service providers or by government agencies. Such information is normally made available to law enforcement authorities on request, although no offshore jurisdiction has yet taken the step of putting it in the public domain. Nevertheless, in this regard, the mainstream offshore territories are already considered in advance of the large countries pushing this agenda, where information about companies' beneficial owners is not held in a systematic way. Indeed, during a debate at the European Competition Forum in Brussels in February 2014, the Secretary General of the OECD, Ángel Gurría, suggested as such when he was heard to praise the Crown Dependencies in particular for the progress they have

made towards increasing tax transparency, while noting that the "big islands – the UK itself and the US" have a lot more to do in this area.

As Fiona Le Poidevin, Chief Executive of Guernsey Finance, the promotional agency for the jurisdiction's finance industry, pointed out in reaction to the announcement that the UK intends to legislate in this area: "Guernsey already regulates its corporate service providers who are required to keep records on beneficial ownership, and so we believe that we are in many ways ahead of the curve. We welcome the moves of other jurisdictions to enhance their regimes, but we and other like-minded territories believe that the most effective route forward is for the development of a truly global level playing field on beneficial ownership."

In its most recent assessment, the IMF concluded that in Guernsey "companies are subject to a wide variety of measures which in summary ensure that accurate and comprehensive beneficial ownership information is obtained for all legal entities."

Jersey's Chief Minister Ian Gorst has also pointed out the presence of similar legal requirements in his jurisdiction. "Jersey already holds a central register of beneficial ownership of companies. In addition we regulate those who form and administer companies and trusts. They are required by statute to maintain up-to-date and accurate information on the ownership of those for whom they act. All the information held in the Island is available to tax authorities and law enforcement agencies on request."

Rules currently in place in Jersey require beneficial ownership to be disclosed to the Jersey Financial Services Commission at the time of incorporation of a company, and the Commission holds this information in a central register. Furthermore, trustees are bound to hold information on the settlors and beneficiaries of trusts under the provisions of Common Law (supported by Case Law), Trusts Law and anti-money laundering requirements. The Commission also actively supervises compliance by trust and company service providers with a requirement that they must collect and hold information on beneficial ownership for all legal persons and arrangements.

"Jersey has access to all the information on beneficial ownership that is required to meet the present international standards and to respond effectively to requests for information from tax authorities or law enforcement agencies as required by statute," the Government states in the preamble to its Action Plan.

It goes on to state that should new international standards on access to beneficial ownership information be agreed, "Jersey will comply with any new international standard in this respect that has global application covering G8, G20, OECD, and EU member jurisdictions plus other major financial centers."

The Isle of Man also has rules in place to ensure the identification of the beneficial ownership of companies and the availability of this information to the

authorities, and has made a commitment to review these in the light of new international efforts to improve access to beneficial ownership information.

"Establishing the ultimate beneficial ownership behind all account relationships conducted in the Isle of Man is a legal requirement backed by on-site supervision to ensure compliance," said Chief Minister Allan Bell. "Legislation is in place to ensure that full and accurate details are maintained on the true ownership and control of every company, trust and fund in the Isle of Man, and that this information is freely available to law enforcement agencies and tax collectors."

However, like Guernsey, the Isle of Man doesn't want to find itself too ahead of the curve. "The outcome of the [review] exercise has to be appropriate for the Isle of Man, of course," said Chief Minister Allan Bell, "which is why we will be engaging in full consultation with the business community before reaching any conclusions."

Collection and maintenance of beneficial ownership information by corporate service providers and trustees of express trusts has been a legal requirement in the Cayman Islands for more than a decade. The obligation on trust and corporate service providers to collect, update and retain such data is enforced through a regime that mandates a licensing process for trust and corporate services and an ongoing program of supervision and enforcement action that involves onsite regulatory inspections.

"As evidenced in our April 2013 Phase 2 Peer Review Report by the OECD Global Forum on Transparency and Exchange of Information for Tax Purposes, information relating to beneficial owners is available in Cayman," stated Cayman Minister for Financial Services, Wayne Panton, in a statement issued in November 2013. "Through our recognized legal and regulatory infrastructure, that information has been collected and updated in the jurisdiction for more than a decade."

"[W]e will continue to monitor the global response to the UK's announcement and any proposals that are made by other G8 countries, the G20 and other relevant international bodies on matters related to transparency. Universal success will be predicated on a fair, and level, playing field in which all jurisdictions adhere to accepted and recognized standards," Panton added.

More recently, Bermuda delivered a more forthright response to UK calls for the introduction of public beneficial ownership registers in its offshore territories, stating that it will introduce such measures only when the UK, the US and Canada do the same for their companies. "Bermuda has for the last 75 years led the way in terms of transparency, having established a legislative framework requiring that persons wishing to incorporate in Bermuda provide central authorities with information on the proposed beneficial owners of the business," commented Bermuda's Minister of Finance, Bob Richards. "If we agree to a public register, while our competitors around the world do not, we will put

ourselves at a distinct disadvantage, severely damaging our economy."

Perhaps the biggest loser, however, is going to be the UK, if it does forge ahead with its plan. Critics of these proposals say that the UK's dash for open beneficial ownership registries is a strange stance for a supposedly pro-business government to take, and warn that the Cameron administration could be about to commit economic suicide.

One organization that is concerned at the implications for UK competitiveness if new legislation is approved is the Law Society of England and Wales, which stated in its response to the Government's consultation[7] on the matter that: "We are concerned that the proposals may damage the attractiveness and competitiveness of the UK as a jurisdiction for the incorporation of companies."

"If the UK is in the vanguard of countries to introduce such requirements, other countries may in due course implement less onerous requirements and this could put the UK at a serious disadvantage in terms of attracting new business to the UK."

The Law Society goes on to warn that even if measures equivalent to those being pushed by the UK are agreed by the EU, "there are numerous jurisdictions outside the EU which could be used for the formation of companies."

"There is mention in the consultation paper of the UK encouraging other members of the G8 to take steps to adopt similar measures but it has been reported that the State of Delaware has announced that it has no intention of introducing a requirement for a beneficial ownership register. We do not wish to see a scenario where the UK loses out as a jurisdiction in which to incorporate."

The United States

Perhaps the largest impediment to a level playing field is the situation in the US, where company formation procedures and requirements are governed by state, rather than federal, legislation. Indeed, the US is often accused of double standards with its attempts to enforce tax transparency around the world, while states maintain corporate laws that are more "secretive" than in most offshore jurisdictions; if confidentiality is high on your list of wants when incorporating a company, then Delaware and Nevada remain hard to beat. It can be no coincidence that despite being one of America's smallest states, Delaware remains the biggest state for the formation of business entities.

The White House released the US beneficial ownership action plan in June 2013 shortly after the conclusion of the Lough Erne Summit. It commits the Government to four broad sets of actions, grouped around themes of risk assessment, legislative initiatives, clarification of customer due-diligence standards, and international cooperation.

Under the Action Plan, the Government will pursue the implementation of legislation which will require the identification and verification of beneficial

ownership information at the time a company is formed. It will explore defining "beneficial ownership" as "a natural person who, directly or indirectly, exercises substantial control over a covered legal entity or has a substantial economic interest in, or receives substantial economic benefit from, such legal entity, subject to several exceptions."

To ensure that the information collected is accessible to the relevant enforcement authorities, the Action Plan recommends that a central registry be set up in each state.

Company formation agents would also be required to collect beneficial ownership information, under reforms to anti-money laundering obligations. In a similar vein, the Government will continue the process of updating its national risk assessment documentation, which involves an investigation of money laundering channels and methods. The aim here would be to address problems associated with the abuse of legal entities. In cases where false information or documentation is knowingly provided, civil and criminal penalties would be enforced.

Another ongoing project referred to in the Action Plan is the Government's planned creation of explicit customer due diligence standards for US financial institutions. Among the options is the introduction of a general requirement to identify the beneficial owners of legal entity customers.

Lastly, the Government will assess the effectiveness of existing means for complying with requests for mutual legal assistance, and other forms of international cooperation related to the beneficial ownership of companies.

It is noteworthy that unlike other G8 countries, such as the UK, the US Action Plan doesn't call for such registries to be open to the public, but available only to relevant enforcement authorities. Perhaps this was a concession to the states, which aren't going to give up their cherished company laws without a fight. But it already suggests that a global level playing field will be difficult, if not impossible, to achieve.

Legislation aimed at making the US incorporation rules more transparent was introduced in the US Senate by anti-offshore hawk Carl Levin (D – Michigan) two years before the beneficial ownership issue was forced up the agenda by the UK in 2013. Levin's Incorporation Transparency and Law Enforcement Assistance Act, which would require the States to obtain the identities of the persons behind the corporations formed under their laws, was introduced in August 2011, then again two years later[8] when the previous legislation died. However, the little attention that the proposals have received – the latest incarnation hasn't even been considered by committee, let alone come up for a vote – demonstrates a certain apathy about this issue in Congress. And Levin's attacks will probably be blunted even more from next year when the Republicans, who are generally more hostile to anti-privacy measures, retake control of the legislature.

The Pros And Cons

Supporters of greater transparency of corporate ownership argue that it will make it much harder for tax evaders and other criminals to hide behind the corporate veil, and in turn much easier for law enforcement authorities to track them down.

"Today, criminals can hide behind anonymously owned corporate structures," Eurodad – the European Network on Debt and Development – said in a statement[9] urging the EU to establish a system of public beneficial ownership registries. It continued: "The fact that banks don't have to know who the real owners of companies and other corporate vehicles are makes it easy to move illegal money around the global banking system and out of the reach of tax collectors. Companies, trusts and foundations can hide the real person – or 'beneficial owner' – behind a bank account. In this way, they can facilitate laundering of proceeds from crimes such as tax evasion, corruption, drugs and arms trade. Tax evaders and avoiders use many of the same mechanisms. Therefore, shedding light on these anonymous structures would make tax avoidance – which is legal, yet morally unacceptable – far more difficult.

Another advantage to central registries, says Eurodad, is that they will make the process of identifying customers much more efficient for banks, lawyers and other professionals than current "know your customer" rules.

Furthermore, public registries of corporate ownership could actually be advantageous to businesses, Eurodad contends, because they will be able to see exactly who they might be going into partnership with, sub-contracting out to, or bidding against for contracts. For example, knowing whether a corrupt politician is the beneficial owner of a potential partner can help companies avoid the risk of violating anti-corruption laws.

The other side to this coin is that public registries of beneficial ownership will at best be yet another nail in the coffin of individual privacy, and at worse be downright dangerous.

Critics of the plans espoused by the G8 say that there are plenty of reasons why a company or an individual might want to keep their details private that don't involve fraud, tax evasion or any number of other nefarious activities that governments are trying to eliminate. As Guernsey Finance's Le Poidevin points out: "The European model has already raised concerns among potential clients around the world who – quite legitimately – want their affairs to remain confidential. Interest groups in the UK have also expressed their fears that a public register might damage business prospects, pose a security issue, raise questions about data privacy, and have human rights implications."

Meanwhile, the Society of Trust and Estate Practitioners has said in response to the European Commission's ongoing attempts to find a compromise position between the EU Parliament and member states that it remains opposed to public registers "on the grounds that they are unnecessarily intrusive

into the financial affairs of families and pose unacceptable risks given that many families create such structures to protect the interests of vulnerable family members."

Ironically, open beneficial ownership registries could also actually encourage financial crime, by allowing criminals to exploit the information contained within them to extort company owners, or target them in other ways. And in all likelihood, determined criminals hiding behind the corporate veil are just going to flout the sorts of rules being advocated by the UK anyway.

Other flaws in the UK plans have been highlighted. One unintended consequence is that, far from simplifying due diligence and beneficial owner checks, public registries could achieve the opposite as those company owners concerned about their privacy reorganize their affairs into ever more complex and hard-to-penetrate structures. Or they could simply relocate their companies to jurisdictions where privacy is protected by law. And, as the UK Government's consultation paper acknowledged, overseas companies operating in the UK cannot be compelled to disclose beneficial ownership information.

Conclusion

So far governments have been keen up to now to pay lip service to the idea of beneficial ownership registries. But given the concerns about a level playing field, competitiveness, data protection and privacy among others, there is a growing sense that the advantages in terms of making it easier to crack down on, as Cameron puts it, a "small minority" of criminal types committing international fraud and tax evasion, are outweighed by the pitfalls. Perhaps this is one global transparency initiative too far.

Endnotes

1 https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/207543/180613_LOUGH_ERNE_DECLARATION.pdf

2 https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/207771/Lough_Erne_2013_G8_Leaders_Communique.pdf

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Topical News Briefing: An Unwritten Pact

by the Global Tax Weekly Editorial Team

It seems somewhat incongruous that as the corporate tax compliance burden continues to fall in many parts of the world, governments are demanding a larger slice of the corporate pie.

The latest PwC/World Bank global report on paying taxes shows that, on average, mid-sized companies have to make fewer tax payments, and spend less time discharging their tax obligations, than they did a decade ago. There are of course wide variations, as is to be expected of a survey involving 178 countries. For example, on average it takes 2,600 hours (108 days) per year for a company to comply with Brazil's complex web of taxes. In the United Arab Emirates, joint top of the paying taxes league table with Qatar, tax compliance takes just 12 hours. Nevertheless, like corporate tax rates, the international trend is towards simpler tax administration, and as the report points out, the gradual introduction of online filing and payment systems is largely to thank for this.

But perhaps there is a price to be paid by multinational companies for lower, simpler taxes, and that is obedience. Even though the vast majority of large companies with operations in more than one country stay within the law when carrying out their tax planning strategies – although mainstream media reports often erroneously suggest otherwise – it is becoming clear that tax avoidance, acceptable or not, immoral or otherwise, is no longer going to be tolerated by governments, especially in the industrialized countries. This is why the OECD enjoys a high level of support for its BEPS initiative, however impossible appears its goal of changing the international tax landscape. The Organisation, with backing from key players like the US Government and the EU, also seems to have won the argument for global automatic exchange of information for the purposes of enforcing national tax laws.

There is perhaps one global compliance initiative that hasn't found its wings yet though, and which will probably struggle to fly like BEPS and information exchange. As also reported in this week's issue, the EU is keen to add wording to European anti-money laundering legislation, currently in the process of being updated, that would require member states to record who ultimately owns companies in some form of central registry, the idea being that tax evaders and other criminals would find it much harder to hide from the authorities behind the corporate veil. This of course sounds laudable. But critics point out that such proposals have deep flaws: determined criminals may merely go deeper to ground to avoid detection; and there are serious privacy implications for the vast majority of people who use companies legitimately. At least the EU isn't going as far as the UK, which is championing these proposals. Under legislation now being drawn up by the UK

Government, beneficial ownership registries will be accessible by the public. The Government has been warned that if this became a reality, then it could expect to see the hard-won confidence of global investors evaporate overnight. Unsurprisingly, few, if any, other countries are seriously pushing this agenda without assurances that there would be a level playing field.

So, trends suggest that while governments are making taxes lower and easier to pay, they are also increasingly anxious to get their share of corporate tax, whatever this share should be. Still, while some taxpayers might overstep the line between "acceptable" and "unacceptable" tax planning, governments, too, can also push the boundaries of acceptability when it comes to compliance.

ISSUE 108 | DECEMBER 4, 2014

Domestic Resource Mobilization And Fiscal Discipline In Africa

by Emmanuel Tem and Theodore Josias, SizweNtsalubaGobodo, South Africa, independent member of Morison International

Contact: emmanuelt@sng.za.com; theoj@sng.za.com

Introduction

There is a common understanding of the central role that taxation plays in development and poverty reduction. A strong tax system is the heart of a country's financial independence. Its revenue is the lifeblood of the state itself. It should be emphasized that taxation is more than just about revenue mobilization. The way in which revenue is collected and spent defines the symbiotic relationship between the state and its citizens, strengthening the former and making it more accountable to the latter.

We accept and welcome the ongoing international initiatives and dialogues and cooperation involving all stakeholders in the field of tax and development and the important role that South–South Cooperation (among developing countries) has to play. We equally welcome and actively support the work program of the African Tax Administration Forum and the Organisation of Economic Co-operation and Development (OECD) on multinational enterprises to improve transparency in the reporting of profits and tax payments.

There is an urgent call for action from the OECD on the Fiscal Affairs and Development assistance committee and the G20 to make progress in the field of tax and development. The United Nations Millennium Declaration decided to create a local and global environment that is conducive to development and to the elimination of poverty. Success in meeting these objectives depends, *inter alia*, on good governance within each country and at the international level, as well as on the transparency in the financial, monetary and trading systems. It is also important to remove the obstacles that developing countries and economies in transition face in mobilizing the resources needed to finance their sustained development.

Ultimately, domestic resource mobilization (DRM) is a path for developing countries to fully fund their development, reducing dependency on foreign assistance. Beyond simply providing a government to pay for vital social services and infrastructure, it will also help to strengthen people's faith in the government's ability to provide accountable and transparent governance.

Conceptual Framework

A set of generally agreed principles is emerging in the DRM literature to guide and follow up action,

including a policy to promote and guide coherence across government and development practitioners in tax, finance and development issues.

Developing countries that have sustained and achieved high rates of growth have typically done so largely through the mobilization of their domestic resources. DRM is crucial to solidify ownership over development strategy and strengthen the bond of accountability between governments and their citizens. In effect, DRM provides the "policy space" for developing countries that is often constrained by the terms and conditions of external resource providers. Foreign aid comes with conditionality or policy strings attached, not to mention procurement restrictions that accompany aid. Aid also tends to be pro-cyclical and volatile. Direct foreign investment typically flows into sectors and projects dictated by the commercial interests of the foreign investors, such as natural resource extraction. Moreover, governments that depend heavily on foreign aid, or on sharing the profits of foreign investors, have less incentive to raise taxes and less reason to pay attention to the demands of tax-paying citizens.

It is in sub-Saharan Africa (SSA) that some of the steepest challenges to DRM are encountered: savings rates are low, dependence on foreign aid is chronically high, and institutional capacity to mobilize domestic resources is weak.

Case For DRM Dependence

It is worth pausing to consider some of the compelling reasons for SSA's overwhelming dependence on DRM – despite evidence that foreign aid and other forms of foreign financial assistance (such as the official development assistance (ODA) component of gross domestic product) has declined significantly in recent years in developing countries, due to a complicated set of exogenous economic factors. According to African Economic Outlook (http://www.africaneconomicoutlook.org/en/), records demonstrate that from 2000 to 2011, total domestic sources of revenue in the 54 SSA countries grew from USD100bn to over USD500bn. Contrast that with the growth of ODA during the same period, which rose from USD20bn to approximately USD60bn. Even with the rapid growth that occurred during those years and increased donor attention on Africa, ODA represents only about 13 percent of all domestic resources in Africa. There has been significant improvement in DRM and, more broadly, public financial management on the continent through efforts such as the collaborative African budget reform initiatives. This has led to the broadening of tax bases. For DRM, the April 2014 high-level meeting (HLM) in Mexico City proved to be a turning point: DRM is a cornerstone of the new global partnership for effective development cooperation. A statement from the Mexico City HLM states:

> *"We recognize the critical challenge of ensuring the adequate mobilization of public and private domestic resources to support development. Adequate mobilization of government revenues is required for direct financing and for leveraging private funds for investments in public services*

and social protection, institutional and human development, basic infrastructure, and strong and inclusive economic growth."

It is therefore important to consider this shift of emphasis in donor funding, foreign aid and financial assistance from other international financial institutions. This has become a point of concern for developing countries as they continue to improve their fiscal regimes and transform their approaches to tax reform, tax policy, and tax administration. The public expects effective and transparent tax administration and budgetary discipline.

The pathway to DRM can be traced to several factors in the different domestic systems, such as:

- The share of trade taxes in total tax revenue. Most low-income countries are heavily dependent on trade taxes as a source of revenue, mainly because they are the easiest taxes to collect. About one-third of non-resource tax revenue in SSA comes from trade taxes; this figure is in decline for several reasons, including tax liberalization and tariff reduction measures. In keeping with global trends, the average tariff rate in the SSA region has declined from over 20 percent in the 1980s to about 10 percent in 2013. Resource-related taxes are responsible for the increase in revenue mobilization in the region;
- Tax legislation in most African countries is complex, and the tax rules often incomprehensible even to well-educated taxpayers. In many tax codes, a large number of exemptions and derogations exist, representing a staggering opportunity cost in terms of foregone revenue. Exemptions complicate tax systems and open the door to political capture. Too often, they are viewed as costless because opportunity costs are not analyzed and because they are offered on an ad-hoc basis. These factors, too, may result in base erosion and minimize revenue optimization;
- The tax systems in SSA countries need to be broadened from their narrow base and compliance must be increased. Typically, taxes are levied at very high rates on a limited number of wealthy taxpayers, inciting widespread tax evasion and fraud. VAT or sales taxes are relatively new to many developing countries, and are likely to be broadened in their coverage and generate more revenue over time. There is scope to contemplate the introduction of further taxes that are currently conspicuous by their absence in developing countries;
- Beyond simplifying and rationalizing tax systems, there is the need to strengthen the capacities of revenue authorities, especially in the area of tax administration. This means elevating the competency of revenue authorities and their officials and rooting out corruption;
- There has been a general decline in aid and donor assistance and other forms of international financial assistance, especially at times of international financial crisis. Revenue mobilization from these sources has become pro-cyclical and unpredictable.

Resource Mobilization Through Taxation

With all the uncertainties and undesirable consequences of aid and other external resource

mobilization strategies for development, taxation is used as the main policy instrument for transferring resources to the public sector. It can also help to create a culture within which the private sector operates in conformity with national objectives.

It is important that in any DRM discourse, the tax system design and implementation issues are taken seriously. It has been argued by multinational institutions, among others, that the tax system should be used only to raise finances that are sufficient for meeting the minimum necessary level of public expenditure – such as to preserve territorial integrity, maintain law and order, provide various public goods, and discourage undesirable activities.

From an efficiency perspective, it can be said that taxes provide the best means of financing the bulk of public expenditure. However, taxes impose on society three types of cost:

- A direct cost or revenue foregone, as taxes reduce their disposable income by paying the amount due;
- An indirect allocative effect, or excess burden, which is the welfare cost associated with the economic distortions induced by taxes as they alter relative prices of goods, services and assets;
- An administrative/compliance cost, since tax forms, tax control payment procedures and tax inspection are costly.

Not all tax systems have the same distortionary effect. For a given amount of tax revenue, the final burden of taxation depends on a number of features of the tax system: the composition of tax revenues (income *versus* consumption), the size of the tax base (affected by tax evasion and tax fraud), tax rates, and other administrative factors. Available evidence for developing countries indicates that corporate and personal income taxes have a negative impact on economic activity, whereas taxes on imports and exports have a significantly negative effect on investment. On the other hand, non-neutralities in taxation and investment severely distort capital markets; this is aggravated when tax evasion is widespread and the informal sector is wide.

Given the disincentive effects of taxes as shown by empirical evidence, efficiency-oriented tax reforms should be characterized by:

- Reliance on a predominantly consumption-oriented set of broad-based taxes;
- Moderate tax rates on labor and capital incomes;
- Simple taxation of profits and returns to financial capital, with few incentive schemes, and as neutral as possible;
- A tax system designed to address issues of equality, neutrality and poverty.

Countries with different economic and demographic characteristics will have varying appetites for tax instruments. A major purpose of fiscal architecture is to provide estimates of the revenue capacity of different taxes given the characteristics of the country. Economic factors include the structure of the economy, the composition of earnings, and resource endowments. Demographic factors include the size of the population, education level, age distribution, the urban/rural population ratio, and family size.

In determining the relative tax mix, it is useful to have estimates of the revenue potential for each tax instrument. Since the design consideration for each instrument greatly affects revenue estimates, calculations are required for different assumptions as to the design and scope of a particular tax instrument – assumptions as to rates, base and coverage of a particular tax.

There are, however, clear challenges to sustaining domestic resources in developing countries. Some points to consider:

- Tax bases are currently limited by the size and persistence of the informal sector;
- Pervasive corruption and lack of transparency in many countries inhibit citizens' willingness to comply with tax laws, suggesting that more attention should be paid to anti-corruption efforts;
- Accountability to taxpayers on how money is spent requires stronger parliamentary control and a strengthened civil society;
- Illicit flows, tax havens, and transfer prices circumscribe the normal tax process;
- Low-income countries that are not resource-rich lag behind resource-rich countries, and DRM may not be an immediate priority;
- Disappearing tax bases;
- Automation and modernization of tax administration. The development and introduction of IT systems must be accompanied by comprehensive reorganizations of administration procedures, as well as intensive training and capacity building for tax officials;
- Measures to strengthen voluntary compliance, including taxpayer services and ensuring consistency and fairness. This will include simplifying the tax system and streamlining compliance procedures to reduce taxpayers' compliance costs. Compliance is also fostered by transparency and integrity of tax administration;
- Putting in place a unified tax administration organized on a functional basis and the introduction of risk management through the adoption of segmentation in taxpayer services and audit programs.

Recommendations

The following recommendations are suggested to enhance the mobilization of financial resources through taxation:

- Developing countries and countries with economies in transition will strive to develop progressive and equitable national taxation systems that are consistent with the country's social and economic framework and generate adequate revenues while minimizing disincentives;
- Developing countries will endeavor to ensure that:
  - the incidence of taxation falls equally on the labor force and owners of financial capital and other assets;
  - the tax base will be extended to cover electronic commerce and innovative financial instruments, but exclude the subsistence sector;
  - indirect taxes will be expanded and made more equitable by targeting the growing service sector and socially undesirable activities, as well as focusing on luxury consumption;
- Developing countries will undertake appropriate administrative and legislative measures to combat

tax evasion and prevent tax avoidance, and reduce the efficacy of tax shelters and tax havens;

- Countries will strive to simplify tax laws and to improve the efficacy and effectiveness of tax administration and enhance enforcement through the strengthening of institutional technical and technological capacities, including the development of a transparent and accountable system;
- Enhancing multilateral cooperation among national tax authorities to encourage tax treaties that aim to eliminate double taxation and promote equitable distribution of taxation among competing jurisdictions;
- Countries will strive to supplement tax revenues by exploring non-tax sources of revenue;
- Developed countries and international financial institutions will provide increasing support to the developing African countries, especially in terms of resources for technical assistance in capacity building.

Topical News Briefing: Trouble In The Family

by the Global Tax Weekly Editorial Team

Prime Minister David Cameron has been praised for his part in convincing the Scots to remain part of a United Kingdom, but that victory has been won at a price.

Unveiled last week were new proposals to allow Scotland greater taxing, spending and borrowing powers, promised in the run-up to the recent referendum on Scottish independence when there was a sudden and alarming – for Westminster that is – shift in support for the pro-independence campaign. For some in Britain, and elsewhere in the world, the constitutional break-up of one of the most stable democracies in recent history was almost unthinkable, leading to questions about how the family silver (or, more accurately, the family debt) would be divided after the divorce, and whether Scotland was really capable of handling the new responsibilities that would have been placed on it. Understandably, that caused a lot of uncertainty, especially for businesses north or the border, and those with operations or investments in Scotland, who wondered what the tax and regulatory framework would look like post-independence. That question is now an academic one, but the new set of powers set to be granted to Holyrood (the seat of the Scottish parliament) can hardly be described as crystal clear. Scotland would be given license to adjust income tax (but only personal income tax, and not as it relates to savings income and dividends) and certain other taxes such as the aggregates levy and air passenger duty (APD), with the UK retaining overall control of the tax system. Scotland will also get to keep the VAT receipts raised from the first 10 percent of the 20 percent VAT. All of which will necessitate the keeping in place of the enigmatic Barnett Formula, which determines what proportion of overall UK tax revenues are transferred to Scotland to fund its local government operations. In fact, the changes being proposed will require the already complex formula to be adjusted to take into account revenues raised in Scotland itself and its new borrowing powers.

While the framework for apportioning tax and spending powers within the UK is becoming ever more complex, the proposals are also bound to throw up anomalies on a day-to-day practical level. For example, what if somebody living in England regularly commutes to Scotland, or vice versa? How will they be taxed? How will company payroll systems cope with such cases? Presumably, HM Revenue & Customs will need to invent yet more tax codes at a time when it is attempting to simplify this problematic tax withholding system. And then what if Scotland decides to scrap the much criticized APD, which can add almost GBP200 (USD300) to the price of a ticket? Will we see boom times at Glasgow Airport as thousands from England take up the opportunity to start their vacations from APD-free Scotland?

And we haven't even mentioned yet the legislation passed by the House of Lords on November 24 that will devolve a range of tax and borrowing powers

to Wales. It is likely that similar sorts of issues will need to be ironed out here too.

Moreover, the independence debate hasn't really gone away with the pro-union referendum victory. The 45 percent of voters wanting independence represents a substantial chunk, and the Scottish National Party is gearing up to make considerable gains at the expense of the traditional parties in the 2015 general election. So there are some interesting, if complicated, times ahead for Britain.

Virtual Currencies: The Modern-Day Equivalent Of Your Father's Offshore Bank Account?

by Mike DeBlis, DeBlis & DeBlis, Bloomfield, New Jersey

In this high tech era of GPS trackers and unmanned drones, new concerns are emerging over the erosion of personal privacy space. A new federal law compels the Federal Aviation Administration to allow drones to be used for all sorts of commercial endeavors – from selling real estate to monitoring oil spills. That same law also makes it easier for local police to send up their own drones. This raises new concerns about how much detail the drones will capture about lives down below. Some advocacy-rights groups are quick to point out that this is nothing more than "routine aerial surveillance of American life."

But as frightening as it might be to think that you could come face-to-face with a drone taking pictures outside of your third-floor fire escape, there is something even more frightening. And that is the piercing stare of an IRS Special Agent standing on the other side of your door. Like the eagle-like eyes of an unmanned drone, the IRS is watching. And what they see might surprise you.

Ever heard of virtual currencies? Virtual currencies, such as Bitcoin, are revolutionizing the payments industry. At the most primitive level, they are a software-based online payment system that does not require fungible bank notes – such as dollars or euro – as its medium of exchange. Instead, payments are recorded in a public ledger using its own unit of account.[1]

With 13 million coins in circulation and an estimated market value of approximately USD7.9bn, Bitcoin dominates the market.[2] If you think that virtual currencies are used only by the most tech savvy and sophisticated computer users, you would be sadly mistaken. On the contrary, they have become as mainstream as pop music and reality television shows.

There is no better example of Bitcoin's mainstream use and acceptance than the fact that large corporations, such as Expedia and the United Way, now accept it.[3] And there is no mystery why: transaction fees are lower than the 2–3 percent typically imposed by credit card processors.[4] In addition, New York leads the nation as the first state to have issued proposed regulations for licensing virtual-currency exchanges.[5]

Does all this hoopla surrounding Bitcoin sound too good to be true? If you worked in the Criminal

Investigation division of the IRS, you'd be viewing this with a healthy amount of skepticism. For all its positive attributes, Bitcoin carries a dark secret. The very same characteristics that make it so desirable – namely speed and secure transfer – make it vulnerable to exploitation by white-collar criminals who seek to use it as a tool to facilitate illicit transactions.[6] And this is precisely the reason why Bitcoin has drawn so much scrutiny by the IRS.

Now you might think of exploitation of Bitcoin in the sense of a grandiose and elaborate scheme to defraud, such as "computer hacking" or the surreptitious planting of malware on a computer server. On the contrary, the most common scheme used by those with sinister motives to exploit Bitcoin is quite simple: they outright steal it,[7] making chargebacks – *i.e.*, a return of funds – next to impossible.[8] And the fact that Bitcoin is a "decentralized virtual currency" – it is "exchanged on a peer-to-peer network *independent* of central control"[9] – makes it that much harder for law enforcement to monitor illicit transactions,[10] thus making it more susceptible to being "hijacked" by criminals.[11] For example, in October of 2013, the FBI shut down the Silk Road online black market and seized 144,000 Bitcoins worth USD28.5m.[12]

But the IRS's fixation with investigating Bitcoin is much broader than just hunting down the "usual suspects" – namely cyber thieves, money launderers, and rogue states. Instead, as so eloquently put by Josh Ungerman in his Forbes article entitled, "Are Virtual Currencies The Next Offshore Bank Account for Tax Evaders?,"[13] it has more to do with what "a potential tax evader who is too young to have hidden money offshore [might] think he can gain by using the cyber currency Bitcoin."

And that harkens back to why an earlier generation parked their money in banks located within offshore tax havens in the first place: to hide it from the government in order to avoid paying tax on the interest. In other words, for a dual purpose: (1) secrecy and (2) "an obtuse trail of funds." Thus, the reason why IRS Criminal Investigation has committed a team of Special Agents to investigate Bitcoin is to prevent a new generation of would-be tax evaders to do with Bitcoin what those in an earlier generation did with foreign financial assets: stash them in offshore bank accounts to hide them from Uncle Sam.

In order to use Bitcoin, the IRS knows that "one needs a virtual wallet along with private keys and public addresses." Unlike most "crypto currencies," however, Bitcoin does not provide complete anonymity. To understand why, it is necessary to have some background information on how Bitcoin transactions are recorded.

Bitcoin transactions are permanently recorded in a public ledger called the "block chain."[14] Approximately six times per hour, a group of accepted transactions, known as "a block," is added to the block chain.[15] These transactions, in turn, are quickly published to all network nodes.[16] This allows Bitcoin software to determine when a particular

Bitcoin amount has been spent, a creative solution for preventing double-spends in an environment that lacks any regulation.[17] Bitcoin software stores its own copy of the block chain, making verification of the chain-of-ownership of any Bitcoin amount "as easy as one two three."[18]

As you might imagine, the block chain is a veritable treasure trove of information for the IRS, allowing it to obtain the identity of Bitcoin users. As Ungerman describes, the IRS does so in three steps:

> "The IRS is simply accessing the block chain to review all Bitcoin transactions (Step One). From that point, the IRS works its way back to the public address that was used in the Bitcoin transaction (Step Two). While the public address itself does not identify the user, the IRS has been very clever in associating the public address with the identity of the Bitcoin user (Step Three)."

The IRS's investigation into the use of virtual currencies is nothing new. For example, it has investigated virtual currencies in connection with money laundering cases in the past. What is new, however, is the purpose that virtual currencies now serve law enforcement: to identify "tax cheats" who are hiding virtual money from Uncle Sam in order to avoid paying taxes. The IRS's recent classification of "convertible virtual currency" as property and not foreign currency (for income tax purposes) proves how serious it regards the threat posed by virtual currency in the tax evasion sphere.[19]

Try as one might to appear non-willful in the wake of failing to disclose his Bitcoin, a tax-dodger might just as well be trying to sell ice to an Eskimo. Regardless of whether it is viewed upside down, right side-up, sideways, or backwards, it is tax evasion. And this is where the wisdom of Shakespeare prevails even in a tax setting. Just as the quote, "A rose by any other name would smell as sweet" is used to imply that the names of things do not affect what they really are, a similar principle prevails in tax law: "substance over form."

The principal of substance over form is used to describe how the economic substance of a transaction transcends its legal form in order to present a true and fair view of the affairs of an entity. Thus, the principal of "substance over form" might just be a "tip of the hat" (or should I say, "beret") to the greatest English poet of all time. And who can forget the famous quote coined by yet another famous English writer that might best describe the inspiration behind the principal of "substance of form:" "imitation is the sincerest form of flattery," by Charles Caleb Colton?

The takeaway is this. Used correctly, Bitcoin is an amazing tool that offers "unparalleled consumer access to a global payment system" in an age where technology is breaking down the geographical barriers of commerce. Used incorrectly, it is a dangerous tool for those with a propensity for engaging in illicit activities, such as tax evasion. The very fate of virtual currency – *i.e.*, whether it will live up to its potential as the most innovative payment system of the twenty-first century and become a legitimate

and trusted medium of exchange or be banished into the ether of cyberspace – depends on "whether law enforcement and private industry succeed or fail in creating innovative safeguards to counter these new threats."[20] And on that note, the IRS has a word of caution for anyone who might be tempted to use virtual currency or Bitcoin for anything other than a lawful purpose: "the taxman cometh!"

Endnotes

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A Global Guide To M&A – Brazil

by Jose Otavio Faloppa, Taxand

Contact: jof@bmatax.com.br, Tel. + 55 11 2179 5234

This article in question and answer format is the latest in a series provided by Taxand from their Global Guide To M&A 2013

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Introduction

Relevant changes in Brazilian tax laws – Law 12,973/14

Law 12,973, enacted on May 13, 2014, created a new Brazilian tax regime based on the International Financial Reporting Standards (IFRS). The legislation contains detailed provisions on the tax effects resulting from taxpayers' adoption of the Brazilian accounting rules, which are aligned with the IFRS.

Law 12,973/14 also made significant changes in the rules governing taxation of legal entities domiciled in Brazil in connection with income earned by the entities' controlled and related foreign companies (CFCs – Controlled Foreign Corporations).

As a general rule, the tax regime introduced by Law 12,973/14 begins on January 1, 2015, although corporate taxpayers can opt for early application of the new regime, starting on January 1, 2014[1].

This article already reflects the changes introduced by Law 12,973/14.

From A Buyer's Perspective

1. What are the main differences among acquisitions made through a share deal versus an asset deal in your country?

Asset deal

From a Brazilian tax liability perspective, if the asset deal involves the acquisition of a complex of assets (that are tangible and intangible) and liabilities that can be organized to be sufficient for operation of a business activity by a legal entity, the buyer would have joint or secondary liability for tax debts due up to the date of sale. The price paid by the buyer in excess of the cost of acquiring the assets (which may be the same as the book value) and attributed to individual assets may be subject to depreciation and amortization costs, which are deductible for corporate income taxes (IRPJ and CSLL) purposes upon reorganization.

Law 12,973/14 allows taxpayers subject to the non-cumulative regime of the social contributions on gross revenues (PIS and COFINS) to record PIS and COFINS credits on amortization charges for intangible assets, as long as the assets were acquired for use in the production of goods intended for sale or in the provision of services (articles 54 and 55, which add item (XI) to article 3 of Law 10,637/02 and Law 10,833/03).

Share deal

The buyer is liable for all tax debts due up to the date of the share sale. If the buyer is a Brazilian entity and the purchase price exceeds the net equity of the acquired entity, the buyer records the difference as goodwill; depending on the economic basis of the goodwill (*i.e.*, expectation of future profits of the acquired entity, difference between the fair market value and book value of tangible assets, or intangibles and other economic factors) upon reorganization, goodwill amortization may be a deductible expense for the purposes of calculating corporate income tax (see section 3 for further information).

2. What strategies are in place, if any, to step up the value of the tangible and intangible assets in case of share deals?

The purchase of shares at a premium (following restructuring) and the direct purchase of tangible and intangible assets may increase such assets' depreciable and amortization value (see sections 1 and 3).

3. What are the particular rules of depreciation of goodwill in your country?

For Brazilian tax purposes, it is essential that goodwill paid by the acquirer is economically justified.

According to the current governing Brazilian tax legislation, the economic grounds for goodwill must be one or any combination of the three types listed below and, upon merger of the acquirer and acquired entities (upstream and downstream), the goodwill has the following treatment:

- **Type A Goodwill:** the market value of underlying assets of the invested, controlled or affiliated entity is higher than the book value of such assets. Upon merger, it is recorded as a counterpart of the accounting entry for the invested entity's relevant underlying asset and could be amortized or depreciated depending on the asset's nature;
- **Type B Goodwill:** expectation of future profits (of the controlled or affiliated entity). Upon merger, it is amortized for corporate income tax purposes by the surviving entity, over the five years following corporate reorganization, at a maximum ratio of 1/60 per month;
- **Type C Goodwill:** the value of the going concern, intangible assets, or other economic factors. Upon merger, it is recorded as a counterpart of the accounting entry for the invested entity's relevant fixed asset (going concern, intangible asset *etc.*), but it is not subject to depreciation or amortization for tax purposes.

In sum, as per the current governing legislation, which applies for the acquisitions carried out until December

31, 2014 with mergers until December 31, 2017, taxpayers are allowed, depending on the factual circumstances of the acquisition, to justify the goodwill paid on the acquisition of investments in one or more of the reasons described in Types A to C above.

Regarding the goodwill, Law 12,973/14 included, in the tax law, provisions are similar to those in IFRS 3. In this sense, Law 12,973/14 sets forth that acquisitions carried out after January 1, 2015, shall have their acquisition cost segregated in:

(a) The proportional net equity value of the investment;
(b) The fair value of the assets and liabilities owned by the invested entity; and
(c) Expectation of future profits of the invested entity (goodwill), being this part the remaining positive difference between the purchase price less (a) and less (b).

Differently from the current governing legislation, whereby taxpayers are allowed, depending on the economic parameters of the transactions, to justify all the purchase price paid over the net equity value in any of the three economic reasons above mentioned, the new tax rules determine the purchase price that exceeds the net equity value shall be first attributed to the fair value of the assets and liabilities and only the remaining amount can be allocated to goodwill (this is rule is similar to IFRS 3).

Upon an upstream or downstream merger, the tax effects will be the same: fair market value of the assets may be considered on the cost of the assets for depreciation/amortization purposes, and goodwill may be amortized within the minimum five-year period.

The purchase price allocation will have to be supported by an appraisal report prepared by independent parties and filed before the Federal Revenue Services, or have its summary filed before the Titles and Documents Registration Office (*Cartório de Registro de Títulos e Documentos*) by the 13th month after the acquisition date.

4. Are there any limitations to the deductibility of interest on borrowings?

According to general tax deductibility rules for corporate income tax, operating expenses are considered to be deductible as long as they are cumulatively:

- Necessary for the company's activity and for the maintenance of the source of income;
- Paid or incurred to carry out transactions or operations required of the company;
- Usual or common to the type of transactions, operations or activities performed by the company.

In respect of payments of interest made by a Brazilian source to a non-Brazilian resident, tax deductibility of the interest payment also will be subject to both thin capitalization and transfer pricing rules.

Thin capitalization rules

Thin capitalization rules apply to interest related to loans obtained from:

- Related parties that are resident or domiciled outside Brazil, according to the definition provided by Brazilian tax law for transfer pricing purposes;
- An individual or legal entity resident or domiciled in a favorable tax jurisdiction or in a jurisdiction under a privileged tax regime.

The following entities are considered related to the Brazilian party in accordance with transfer pricing rules:

- A branch or subsidiary, domiciled abroad;
- Head offices, when domiciled abroad;
- An individual or legal entity, residing or domiciled abroad, whose equity interest in the Brazilian company makes it a controlling shareholder or affiliated company;
- A legal entity domiciled abroad which is a controlling or affiliated company;
- A legal entity domiciled abroad when it and the company domiciled in Brazil are under corporate control or common administration or when at least 10 percent of the capital of each belongs to the same individual or legal entity;
- An individual or legal entity, resident or domiciled abroad, that, together with the legal entity domiciled in Brazil, holds interests in the capital of a third legal entity, which considered jointly makes them a controlling or affiliated company of the third legal entity;
- An individual or legal entity, resident or domiciled abroad, which is the Brazilian party's associate under the legal form of a consortium or co-ownership as defined in Brazilian law in any enterprise;
- An individual resident abroad who is a relative or spouse of any of the Brazilian party's members of management, partners, shareholders or a controlling shareholder directly or indirectly;
- An individual or legal entity, resident or domiciled abroad, that enjoys exclusive rights as the Brazilian party's agent, distributor or concessionaire for buying or selling goods, services or rights;
- An individual or legal entity, resident or domiciled abroad, for which the legal entity domiciled in Brazil enjoys exclusive rights, as its agent, distributor or concessionaire, for buying or selling goods, services or rights.

When the interest is paid to a related party resident or domiciled outside Brazil, the interest will be deductible for corporate income tax purposes only if the debt does not exceed the following limits:

- Twice the equity interest value held by the relevant related company in the Brazilian legal entity, considering each debt separately;
- Twice the net worth value of the Brazilian legal entity, considering each debt separately;
- In both cases mentioned above, twice the total value of equity interest held by all related companies in the Brazilian legal company, considering the sum of debt transactions.

When interest is paid to an individual or legal entity that is resident or domiciled in a favorable tax jurisdiction or in a jurisdiction under a privileged tax regime, that interest will be deductible for corporate income tax purposes only if the debt does not exceed 30 percent of the legal entity's net worth,

considering the sum of debt transactions when the interest becomes due.

In all cases the amounts of debt and net worth of the Brazilian legal entity shall be calculated using a weighted monthly average.

Expenses are not deductible for corporate income tax purposes if they reflect payments made to parties resident or domiciled in a favorable tax jurisdiction or in a jurisdiction under a privileged tax regime, unless the following requirements are cumulatively met:

- The beneficial owner of the proceeds located abroad is identified;
- Operational capacity of the party located abroad is proven;
- Payment for the service and delivery of goods and rights or use of the service is proven.

The requirements related to the operational capacity mentioned above are not applicable to the following transactions:

- Transactions not made for the sole or main purpose of tax savings;
- At the time interest is remitted abroad, the beneficiary is a subsidiary or branch of a controlling entity domiciled in Brazil subject to taxation of its foreign income.

Transfer pricing rules

Parties subject to thin capitalization rules are also subject to transfer pricing rules.

As from January 2013, the following rates apply for the calculation of the deductible amount of interest paid or credited to such parties:

- The market rate for sovereign debt securities issued by the Federal Republic of Brazil in the international market in US dollars, in the case of transactions in US dollars with a prefixed rate;
- The market rate for sovereign debt securities issued by the Federal Republic of Brazil in the international market in Reais, in the case of international transactions in Reais with a pre-fixed rate;
- The six month London Interbank Offered Rate (LIBOR) applies in all other cases. The limits described above are compulsory for contracts made, renewed, or renegotiated after December 31, 2012.

In addition to the pre-established rates, the following annual spreads, based on market averages, may be added by legal entities to above-mentioned rates:

- 3.5 percent rate shall be added to the interest rates to be used for assessment of the deductible interest derived from transactions executed (a) with related parties and (b) with legal entities established in privileged tax regimes jurisdictions; and
- 2.5 percent rate shall be added to the interest rate to be used for assessment of the minimum financial revenues derived from transactions executed (a) with related parties and (b) with legal entities established in privileged tax regimes jurisdictions, regardless of the nature of the transaction.

The Brazilian lender must record, as financial revenue related to the loan granted to a foreign related

party at least, the amount calculated in accordance with the rules mentioned above.

The amount of interest exceeding the limit mentioned above will be added to taxable income subject to corporate income tax.

5. What are usual strategies to push-down the debt on acquisitions?

In most situations where the purchaser intends to push-down debt on acquisitions (*i.e.*, perform leveraged buy-outs), the entity that acts as the borrower is a Brazilian company. Following the purchase, this entity is merged into the acquired entity.

Other structures may involve (i) back-to-back loans on the same terms and conditions, or (ii) obtaining a new loan at the level of the acquired company, transferring the proceeds to the parent company (*e.g.*, *via* dividends, capital reduction or otherwise) so that it can pay off the original loan. These structures may be feasible if all shares of the entity are purchased. Others may also be feasible subject to a case-by-case analysis.

6. Are losses of the target company/ies available after an acquisition is made?

Taxation in Brazil considers each individual entity separately (*i.e.*, there is no consolidation for tax purposes). Tax losses are linked to the entity that generated them. If that entity is merged, tax losses of the merged entity cannot be used by the entity surviving the merger.

In case of a split-off, the split-off company's losses are canceled in the same proportion that the assets and liabilities transferred represent of the total net asset value of the spun-off entity.

If there is a change in control and change in the acquired entity's line of business, its tax losses can no longer be used. There are no percentage thresholds to qualify a change in control. It may be deemed to occur even in situations where the purchaser buys less than 50 percent of the target company's total equity interest. A case-by-case analysis is necessary to ascertain if there is change in control.

7. Is there any indirect tax on transfer of shares (stamp duty, transfer tax etc.)?

There is no Brazilian inheritance or gift tax applicable to the ownership, transfer or disposition of interest, except for gift and inheritance tax imposed by Brazilian states on gifts by individuals or entities not domiciled or residing in Brazil to individuals or entities domiciled or residing within such Brazilian states. There is no Brazilian stamp, issue, registration, or similar tax or duties payable by shareholders.

The conversion into Brazilian *Reais* of proceeds received in foreign currency by a Brazilian entity or the foreign currency conversion of funds held in *Reais* is subject to the tax on foreign exchange transactions (IOF/Fx).

The general IOF/Fx rate is 0.38 percent, which can be increased at any time up to 25 percent by the

Brazilian Government. But this is only with respect to currency exchange transactions carried out after the rule that increases the IOF/Fx rate enters into force.

8. Are there any particular issues to consider in the acquisition of foreign companies?

Current Brazilian CFC Rules

A Brazilian company that acquires foreign companies must comply with Brazilian rules on taxation of CFCs. According to current CFC rules, profits, earnings and capital gains earned abroad through a foreign subsidiary, a foreign controlled or affiliated entity, or a branch establishment of the Brazilian company must be included in calculating corporate income tax owed by the Brazilian entity, which applies at a combined rate of 34 percent.

Such profits must be included in the December 31 financial statements of the Brazilian entity. Therefore they are included in calculating corporate income tax in the year when they were earned or accrued. This foreign income is deemed available to the Brazilian entity as of December 31, regardless of whether it is effectively paid or remitted.

All kinds of income (active and passive) generated by the foreign controlled or affiliated entity must be added to the taxable basis of the Brazilian entity and not just its active earnings.

Losses incurred by the foreign controlled or affiliated company cannot be offset against profits generated by the Brazilian entity in Brazil. Nevertheless Brazilian legislation allows for offsetting of such losses against future profits of the same foreign entity, without quantitative or qualitative limitations. For example, the domestic rule on net operating loss (NOL) limitation, *i.e.*, 30 percent of net profit, does not apply.

In addition, for purposes of determining the foreign taxable income of the Brazilian entity, the CFC must also consolidate the results of entities in which it holds direct or indirect equity interests (second and further tiers).

Brazilian CFC Rules set forth by Law 12,973/14

Law 12,973/14 provides that legal entities domiciled in Brazil must consider in the taxable basis of corporate income taxes (IRPJ and CSLL) the profits or losses of directly and indirectly controlled foreign corporations[2].

Until 2022, the CFCs' profits or losses can be considered on a consolidated basis in calculating Brazilian corporate income taxes (IRPJ and CSLL). The consolidation cannot include net income or loss from CFCs: (i) that are located in countries with which Brazil does not have a treaty or an agreement for exchange of information for tax purposes[3]; (ii) that benefit from a favorable tax regime, or are subject to a low tax regime (see Exhibit I); (iii) that are controlled, directly or indirectly, by a legal entity located in a tax haven or subject to a low-tax regime or a favorable tax regime; or (iv) whose "active

business income" (*renda ativa própria*) is less than 80 percent of their total income[4].

The net income (or loss) of each of the CFCs is considered separately in determining the Brazilian entity's taxable income, if the net income (or loss) of a Brazilian entity's CFCs is not consolidated. If a CFC's net income is positive, the amount must be added to the Brazilian entity's taxable income for the purposes of calculating corporate income taxes in Brazil. If there is a net loss, the amount of the loss may be set off against future profit earned by the relevant CFC, without limitation in time, subject to certain rules.

If a Brazilian legal entity holds a less-than-controlling interest in a foreign company, the income earned by the foreign company will be included in calculating the Brazilian entity's corporate income taxes for the year in which the income was made available to the Brazilian entity.[5]

Income tax paid abroad by the CFC on positive amounts of income included in the Brazilian controlling company's taxable income can be set off, in proportion to the Brazilian entity's equity interest in the CFC, against income tax owed in Brazil on the CFC income.

Until 2022, the controlling shareholder in Brazil can set off, against its taxable income, a presumed credit of 9 percent of positive CFC income from production of beverages and food items, construction of buildings, infrastructure work, general manufacturing industry, exploitation of mines, and exploitation, in the country where the CFC is domiciled, of an asset belonging to the Government under a concession regime.[6]

Law 12,973/14 gives the Brazilian controlling taxpayer the option of deferring payment of corporate income taxes related to the positive adjustment in the CFC investment account or the positive consolidated results of CFC income for up to eight years after the CFC income was first reported, although a minimum payment of 12.5 percent must be made in the first year after the income is reported.[7]

9. Are there any particular issues to consider in the acquisition of foreign companies?

When mergers, consolidations and/or split-offs are carried out at book value, taxable capital gains are not triggered in principle. The main caveat in the context of corporate reorganizations relates to maintenance of NOLs recorded at the level of the acquired company and the transfer of tax credits. (For more information on treatment of NOLs, see section 6.)

It should be noted that corporate reorganizations in Brazil may be performed at book or market value.

10. Is there any particular issue to consider in case of companies whose main assets are real estate?

Assuming that the question refers to companies whose main activities involve the purchase and sale of real estate properties, besides regulatory

and other tax matters, the main tax issues in principle refer to liability for the Municipal Real Estate Transfer Tax (ITBI).

The ITBI is a municipal tax payable by the buyer on the acquisition of real estate. The ITBI rate varies between municipalities, but is usually fixed at a rate of 2 percent. The ITBI is calculated on the basis of the market value of the property or its appraised value, whichever is higher.

It is common practice for real estate companies to structure their holdings in a group of different companies, with each company holding one or more properties for operational and tax efficiency purposes. Therefore each transfer of property held inside the group would be subject to ITBI.

The acquisition and transfer of a company that owns real estate, in contrast, is not subject to ITBI, since it involves only a share deal and not an asset deal. Furthermore the transfer of a real estate property to an entity as a capital contribution is not subject to ITBI if the recipient entity is not a company that has the purchase and sale of real estate as one of its corporate purposes. The recipient entity's operational revenues evidence this for two years preceding and two years following the transfer.

An M&A transaction involving a multi-company real estate group could result in a transfer of tax liabilities (or even potential tax liabilities, if no tax assessment has been issued) to the acquirer.

11. Thinking about payment of dividends out of your country and a potential exit, is there any particular country that provides a tax efficient exit route to invest in your country?

From an income tax perspective, Brazilian legislation provides that payment of dividends (including out of yearly net profits, post-1995 profit reserves, or post-1995 accumulated profits) is neither subject to any withholding tax in Brazil, nor subject to income tax at the beneficiary level, regardless of its nature and domicile.

In addition to dividends on profits, Brazilian legal entities may pay interest on equity (JCP) to their shareholders or *quota* holders. JCP refers to remuneration on the capital contributed by a quota holder or shareholder to the invested company. The amount of JCP that can be paid by a company to its *quota* or shareholders is equal to the balance of that company's net equity accounts (including capital, capital reserve, profits reserve, or retained earnings). This amount is then multiplied by the *pro rata* Long-Term Interest Rate (TJLP), which is normally about 6 percent per year and is limited to (i) 50 percent of current year's net profits, or (ii) 50 percent of the company's total retained earnings accounts. The payment of JCP is subject to withholding income tax (WHT) at a standard rate of 15 percent, or 25 percent if the beneficiary is domiciled in a favorable tax jurisdiction.

It is therefore possible that tax efficiencies would vary according to the tax treatment given to

dividends and JCP by the country. This depends on where the recipient is located and requires analysis by tax experts of that jurisdiction.

12. How is foreign debt usually structured to finance acquisitions in your country?

Typically, an acquisition financed with foreign debt is structured through the incorporation of a company vehicle in Brazil. Alternatively, if the acquiring and acquired entities do not merge, the interest expense payable by the company vehicle may be added to the cost of acquisition of the acquired company, making it possible to reduce capital gain in the event of a sale of the acquired company.

Attention must be paid to the Brazilian thin capitalization and transfer pricing rules when calculating deductible interest paid to related parties abroad or parties located in favorable tax jurisdictions or jurisdictions under a privileged tax regime (see section 4). Brazil recently enacted legislation providing for tax advantages for foreign financing of infrastructure projects in the country.

The tax on financial transactions (IOF) is levied at an increased rate of 6 percent in the case of loans having a term of up to 180 days (six months), as demonstrated by loan registration information lodged with the Brazilian Central Bank. The 6 percent IOF is levied over the amount of the loan in Brazilian Reais. Loans with more than 180 days are not subject to the IOF.

From A Seller's Perspective

13. What are the main differences between share and asset deals?

Asset deals

The sale of individual assets is taxable. At a federal level, the seller's income (including any capital gain from the sale) will be subject to corporate income tax, generally at a combined rate of 34 percent after adjustment for deductible expenses. Sales revenue is subject to the social contributions on gross revenues (PIS and COFINS) unless the sale involves fixed assets that are not subject to PIS and COFINS, generally at combined rates of 9.25 percent, although credits may apply.

The exit of assets from the seller's establishment may be subject to Federal Excise Tax (IPI) levied on manufactured products the moment they leave their point of manufacture or importer's premises. As a value-added tax (VAT), IPI applies to the value of the transaction at rates that vary according to the essential nature of the products. But credits from previous transactions (including acquisitions or importations) can be used to offset the amount of IPI owed.

At the state level, state VAT (ICMS) also applies to transactions for the sale of goods, at rates that vary from 7 percent or 12 percent to 18 percent or 25 percent, depending on the nature of the goods, the state, and whether the transaction occurs within that same state or between states. It should be noted that credits

from previous transactions are generally allowed. Finally at the municipal level, if real estate assets are involved in the sale, ITBI is levied on the property's market value, usually at a 2 percent rate, although it can vary from municipality to municipality.

Share deals

Any capital gain earned on the sale of shares held by a Brazilian seller will be subject to corporate income tax at 34 percent if the seller is a legal entity, and income tax at 15 percent if the seller is an individual.

14. How are capital gains taxed in your country? Is there any participation exemption regime available?

There is no participation exemption regime in Brazil. Capital gain is defined as the positive difference between the purchase price and acquisition cost of a particular asset. That is, when earned by:

- A Brazilian legal entity, the gain is subject to corporate income tax at a combined rate of 34 percent (but in some cases expenses and tax losses carried forward can be considered);
- A Brazilian individual, the gain is subject to income tax at 15 percent.

Non-residents who sell assets located in Brazil are subject to WHT at a standard rate of 15 percent, or 25 percent if they are resident or domiciled in a tax favorable regime (a "black list" is issued by the Brazilian Federal Revenue – see Exhibit I below).

Non-residents who sell shares on the Brazilian stock exchange (including the organized over-the-counter market) are exempt from income tax when it is a portfolio investment (registered under Resolution No. 2,689/01 of the Brazilian Central Bank). If however the non-resident seller is resident in a tax favorable jurisdiction, 25 percent WHT applies.

15. Is there any fiscal advantage if the proceeds from the sale are reinvested?

Brazilian legislation does not provide for any fiscal advantage if the proceeds from sales are reinvested in Brazil.

Exhibit I

According to Brazilian legislation, a favorable tax jurisdiction fulfills one of the following requirements:

- A country or place that does not tax income, or taxes income at a rate lower than 20 percent;
- It imposes restrictions on disclosure of the investment owner's shareholding structure as the ultimate beneficiary of earnings that are attributed to non-residents or of the economic transactions carried out.

A privileged tax regime is one that:

- Does not tax income (that is income in general or specifically income derived from foreign sources), or taxes income at a rate lower than 20 percent;
- Grants tax advantages to non-resident individuals or legal entities, provided these tax advantages either do not require any type of substantial activity in the jurisdiction, or are actually conditional on the absence of economic activity in the jurisdiction;

- Imposes restrictions on disclosure of the shareholding structure of the investment ownership of the ultimate beneficiary of earnings that are attributed to non-residents or of the economic transactions that are carried out.

Instruction No. 1,037/10, issued by the Brazilian Federal Revenue Service, sets out the countries and locations that are deemed to be favorable tax jurisdictions and the regimes that fall under the concept of privileged tax regime.

The low-tax jurisdictions listed in Instruction No. 1,037/10 are as follows:

American Samoa, Andorra, Anguilla, Antigua and Barbuda, Aruba, Ascension Island, Bahamas, Bahrain, Barbados, Belize, Bermuda, British Virgin Islands, Brunei, Campione D'Italia, Cayman Islands, Channel Islands (Jersey, Guernsey, Alderney and Sark), Cook Islands, Costa Rica, Cyprus, Djibouti, Dominica, French Polynesia, Gibraltar, Grenada, Hong Kong, Isle of Man, Kiribati, Labuan, Lebanon, Liberia, Liechtenstein, Macau, Madeira Islands, Maldives, Marshall Islands, Mauritius, Monaco, Montserrat, Nauru, (former) Netherland Antilles, Niue, Norfolk Island, Oman, Panama, Pitcairn Islands, Queshm Island, Saint Helena Island, Saint Kitts and Nevis, Saint Lucia, Saint Pierre and Miquelon, Saint Vincent and The Grenadines, San Marino, Seychelles, Singapore, Solomon Islands, Swaziland, Tonga, Tristan da Cunha, Turks and Caicos Islands, United Arab Emirates, US Virgin Islands, Vanuatu, and Western Samoa.

The countries that have privileged tax regimes and the corresponding regimes deemed privileged by Instruction No. 1,037/10 are as follows:

Exhibit 1

Country or location	Type of regime
Uruguay	Regime applicable to legal entities incorporated in the form of a *Sociedade Financeira de Inversão* (Safi) until December 31, 2010 Olympus Corporation.
Denmark	Regime applicable to legal entities incorporated in the form of a holding company with no substantial activity.
Iceland	Regime applicable to legal entities incorporated in the form of an International Trading Company (ITC).
United States of America	Regime applicable to legal entities incorporated in the form of a state Limited Liability Company (LLC) that is owned by non-residents and not subject to federal income tax.
Malta	Regime applicable to legal entities in the form of an International Trading Company (ITC) and of an International Holding Company (IHC).
Switzerland	Regime applicable to legal entities incorporated (i) in the form of a holding company, domiciliary company, auxiliary company, mixed company and administrative company that taxes income at a rate lower than 20%, according to the federal, cantonal and municipal legislation; and (ii) in other legal forms of corporation, set forth by rulings issued by tax authorities, that taxes income at a rate lower than 20%, according to the federal, cantonal and municipal legislation.

Endnotes

1 The definitive option shall be made in February 2015.

2 Losses realized by a CFC in years prior to Law 12,973/14 can be set off against future profits realized by the same CFC, without limitation in time or on amount, subject to certain rules.

3 Consolidation of results will be permitted, though, if the controlling Brazilian entity makes the CFC's accounting records available in digital format, together with supporting documentation, in accordance with regulations to be issued by the RFB.

4 "Active business income" (*renda ativa própria*) is defined as income obtained directly by the legal entity from its own economic activity. The following income is excluded from "active business income": royalties, interest, dividends, equity interests, rents, capital gains (except those realized on sale of equity interests or permanent assets acquired more than two years ago), financial investments, and financial intermediation.

5 This treatment does not apply, however, to foreign corporations that benefit from a favorable tax regime, or are subject to a low-tax regime (see Exhibit I); or that are controlled, directly or indirectly, by a legal entity located in a tax haven or subject to a low-tax regime or favorable tax regime.

6 This credit does not apply to CFCs (i) that benefit from a favorable tax regime, or are subject to a low tax regime (see Exhibit I); (ii) that are controlled, directly or indirectly, by a legal entity located in a tax haven or subject to a low-tax regime or favorable tax regime; or (iii) whose "active business income" (*renda ativa própria*) is less than 80 percent of their total income. The executive branch of the federal government has powers to include other activities that will entitle Brazilian controlling shareholders to the presumed 9 percent credit.

7 This option is available, however, only to income from CFCs that benefit from a favorable tax regime, or are subject to a low-tax regime (see Exhibit I); or whose "active business income" (*renda ativa própria*) is less than 80 percent of their total income.

Time Extension For 'In Substance' FATCA IGAs

The US Internal Revenue Service (IRS) has provided guidance with respect to jurisdictions that have been treated as if they had a Foreign Account Tax Compliance Act (FATCA) intergovernmental agreement (IGA) in existence, although that agreement has remained unsigned.

Under previous US transitional FATCA rules, IGAs reached in substance before July 1, 2014, can be treated as being in effect through to the end of 2014, as long as the IGA is signed on or before December 31, 2014.

Under the terms of a new announcement, a jurisdiction that has been treated as if it had an IGA in effect, but that has not yet signed it, will also retain such status beyond December 31, 2014, provided that the jurisdiction demonstrates firm resolve to sign the IGA as soon as possible.

However, after December 31, 2014, the US Treasury Department will review the list of jurisdictions having an agreement in substance on a monthly basis to assess whether it continues to be appropriate to treat such a jurisdiction as if it had an IGA in effect, or whether a jurisdiction should be removed from the list.

Congress enacted FATCA in 2010 to target non-compliance by US taxpayers using foreign accounts. It requires US financial institutions to withhold 30 percent of certain payments made to foreign financial institutions (FFIs) that do not agree to identify and report information on US account holders. Foreign governments have two options for complying with FATCA: either they can permit their FFIs to enter into agreements with the IRS, or they can themselves enter into IGAs with the US.

US Treasury has developed two alternative model IGAs. Under Model 1, FFIs report to their respective governments who then relay that information to the IRS. Under Model 2, FFIs report directly to the IRS to the extent that the account holder consents or such reporting is otherwise legally permitted, supplemented by information exchange between governments with respect to non-consenting accounts.

Brussels Moving On Ownership Registries, Says STEP

The Society of Trust and Estate Practitioners (STEP) has noted that a proposal to require EU member states to maintain public registers of information on entities' beneficial owners is progressing quickly in Brussels.

Earlier, the European Commission had produced a draft Directive that closely followed both the Financial Action Task Force recommendations and the recent G20 statement of principles intended to improve the transparency of beneficial ownership of companies and trusts.

The EU Parliament, however, continues to press for the text incorporated in its report, which it adopted earlier this spring, STEP said. This alternative proposal calls for freely accessible public registers of the beneficial owners of companies, trusts, and all other similar legal entities, such as foundations.

STEP reported that the debate in Brussels has now entered the so-called "trialogue" process, where the Commission attempts to find a compromise position between the EU Parliament and member states (who generally remain opposed to public registers). So far, Parliament has refused to shift on its demands for free public access to the trust (and foundation) register and the listing of all beneficiaries, STEP said.

The Society said it remains opposed to a public register, arguing that the proposals are unnecessarily intrusive into the financial affairs of families and pose unacceptable risks given that many families create such structures to protect the interests of vulnerable family members.

The negotiations are scheduled to conclude shortly, with the Directive due to be finalized by the end of the year.

STEP said that if the proposal for publicly accessible registers is adopted, the EU would likely press for similar registers to be introduced in neighboring countries next. Non-EU international financial centers have already been urged to follow the EU's lead.

Tax Compliance Burden Easing For Businesses Globally

Paying taxes has become easier over the past year for medium-size companies around the world, a new report from the World Bank Group and PwC has found.

The average time it takes a company to comply with its tax obligations dropped by four hours last year, according to the study. The average number of payments required from companies also fell to 25.9 each year, and 264 hours were required to achieve tax compliance.

Over the ten years of the study, 78 percent of the 189 economies covered in the report have made significant changes to their tax regimes at least once. Taxes on profits have fallen to 40.9 percent, with the most significant decline seen during the financial crisis, from 2008 to 2010, with an average fall in the total tax burden of 1.8 percent. The rate of decline then started slowing in 2011.

The average time it takes a medium-size company to deal with its tax submissions has fallen by nearly a week and a half over the ten years of the study. This is mainly due to increased use of electronic filing, with 105 of the 379 tax reforms since 2004 relating to electronic filing.

"Taxes provide the sustainable funding needed for social programs and to promote economic growth. Policymakers need to find the right balance between raising revenue and ensuring that tax rates and the

burden of compliance do not deter participation or discourage business activity," said Augusto Lopez-Claros of the World Bank Group. "During economic downturns, this balancing act is intensified; some public spending may increase, putting pressure on deficits, and governments may need to use tax policy as an economic stimulus."

Andrew Packman, leader for Tax Transparency and Total Tax Contribution at PwC, added: "The latest results from the Paying Taxes study show many economies are continuing to make progress in tax reform, but there is still a lot of scope to streamline and simplify tax systems. Tax reform is set to remain an important topic for governments around the world for some years to come, and this will include the need to take on board the proposals from the OECD to modernize the international tax system to cater for today's globalized business."

Changes To HMRC 'Bank Raid' Powers Welcomed

The UK Government has announced that it will strengthen safeguards to prevent the misuse of HM Revenue & Customs' (HMRC's) new Direct Recovery of Debts (DRD) powers.

The introduction of DRD will enable HMRC to recover cash directly from the bank accounts, building society accounts, and Individual Savings Accounts (ISAs) of a small number of debtors who owe the taxman GBP1,000 (USD1,565) or more. HMRC estimates that DRD will apply to around 17,000 cases a year, with the average tax debt expected to be GBP5,800.

Financial Secretary to the Treasury David Gauke said that, following a consultation on DRD, the Government had decided to strengthen the guarantees that it can offer to taxpayers that the use of DRD "will be subject to the toughest scrutiny and oversight possible."

Under the amended proposals, everyone subject to DRD will have the chance to challenge and settle their affairs, either by paying in full or setting up a payment plan. DRD will apply only to those who have chosen not to. A hold will be placed on affected taxpayers' accounts, and they will be given 30 days to contact HMRC and either arrange for payment or object to the use of DRD, before any money is taken.

HMRC officers will visit affected taxpayers to allow the Department to identify vulnerable members of society and provide them with appropriate support. A new specialist unit will deal with cases involving the vulnerable, and a dedicated DRD team and helpline will be established. Appeals to the County Court will also be permitted.

Gauke said: "We already set out robust safeguards to protect vulnerable debtors in our original [DRD] proposals, but feedback from the consultation process told us we could do more to make sure this only catches those who are playing the system. We're strengthening the guarantees we can offer taxpayers that powers will only be used when debtors have consistently refused to talk to HMRC and settle their debts, and their

use will be subject to the toughest scrutiny and oversight possible."

Reacting to the Government's announcement, Chas Roy-Chowdhury, head of taxation at the Association of Chartered Certified Accountants (ACCA), said that while ACCA would have preferred that the scheme was not introduced, the new regime "is light years better than what was originally being proposed."

"There will now be a totally different ethos behind the way the power will be designed and implemented. It will no longer be played out as a remote controlled video game where HMRC remotely takes money out of the taxpayer's account. There will now need to be face-to-face engagement between HMRC and the taxpayer before anything can happen. Vulnerable taxpayers will be identified and taken out of the process entirely and put in touch with a dedicated helpline. In addition we consider it's a good day for taxpayer confidentiality as the new powers will be restricted to only asking the bank or building society for the balance in the account rather than 12 months' information," Roy-Chowdhury said.

Anne Fairpo, President of the Chartered Institute of Taxation, said that DRD legislation will not be included in the Finance Act that is likely to be passed immediately before the 2015 election, due to be held in May next year. Instead, it will probably appear in a post-election Finance Bill. According to Fairpo, this will ensure that there is adequate time for debate on the measure. She added that the revisions "are proof that the Government has listened to, and taken on board, the concerns of interested stakeholders and is evidence of the merit of sustained engagement."

Influential Committee Sets Out New Scottish Tax Powers

UK Prime Minister David Cameron has welcomed recommendations from the Smith Commission on the devolution of additional tax powers to the Scottish Parliament.

Cameron established the Commission in the wake of the "no" vote in September's Scottish independence referendum. He sought to keep Scotland in the UK with promises that Scotland's tax powers would be expanded.

Chaired by Lord Smith of Kelvin, the Commission was tasked with brokering a cross-party deal on devolution. The Commission's report was issued on November 27 and sets out the agreement reached between all five of Scotland's main political parties (Conservative, Green, Labour, Liberal Democrat, and the Scottish National Party).

Under the plans, income tax would remain a shared tax, and both the UK and Scottish Parliaments would share control of the tax. Within this framework, the Scottish Parliament would have the power to set income tax rates and thresholds on the non-savings and non-dividend income of Scottish taxpayers. There would be no restrictions on the thresholds or rates the Scottish Parliament could set.

All other aspects of income tax would remain in the control of the UK Parliament, including the imposition of the annual charge to income tax, the personal allowance, the taxation of savings and dividend income, the ability to introduce and amend tax reliefs, and the definition of income. Westminster would also retain control over all aspects of National Insurance contributions, inheritance tax, capital gains tax, corporation tax, fuel duty and excise duties, and oil and gas receipts.

The Scottish Government would receive all income paid by Scottish taxpayers on their non-savings and non-dividend income. The Scottish Parliament, Holyrood, would also be given increased borrowing powers, to be agreed with the UK Government, and the Barnett Formula will continue to be used to determine the remaining block grant (the portion of revenues provided by the UK Treasury each year to fund Scottish Government operations). The Scottish and UK Governments would agree new rules on how the grant would be adjusted at, and after, the point at which powers are transferred.

The receipts raised in Scotland by the first ten percentage points of the standard rate of value-added tax (VAT), which is currently set at 20 percent, would be assigned to the Scottish Government's budget. These receipts would be calculated on a verified basis, to be agreed between the UK and Scottish Governments. A corresponding adjustment would be made to the block grant. All other aspects of VAT would remain controlled by the UK Parliament.

The power to charge tax on air passengers leaving Scottish airports would be devolved. The Scottish Government would be free to replace or remove the UK's Air Passenger Duty (APD) regime as it sees fit. If a new tax is introduced, the Scottish Government would have to reimburse the UK Government for any costs incurred in "switching off" APD in Scotland. A corresponding adjustment would also be made to the block grant.

Similar rules would apply to the devolution of the Aggregates Levy (AL). Once the current legal issues in relation to the AL have been resolved, the power to charge tax on the commercial exploitation of aggregate in Scotland would be transferred to the Scottish Parliament. If the Scottish Government chooses to replace the AL, it would be required to reimburse the UK Government for any costs incurred, and a corresponding adjustment would be made to the block grant.

The UK and Scottish Governments would work together to avoid double taxation and make administration as simple as possible for taxpayers.

Cameron said: "I'm delighted with what's been announced, we're keeping our promises and our United Kingdom together. I always said that a 'no' vote didn't mean no change, indeed, we made a vow of further devolution to Scotland and today we show how we're keeping that vow to keep that promise. The Scottish Parliament is going to have much more responsibility in terms of spending money but it would also need to be more accountable for how it raises taxes to fund that spending and I think that's a good thing."

Draft clauses to translate Smith's recommendations into legislation will be produced in January 2015.

House Of Lords Passes Welsh Devolution Bill

The UK House of Lords has passed legislation that will devolve a range of tax and borrowing powers to Wales.

The Wales Bill was given its third and final reading in the Lords on November 24, and is expected to receive Royal Assent in early 2015 after it has been debated in the House of Commons.

Welsh Secretary Stephen Crabb described the reading as "an important milestone towards creating a lasting and robust devolution settlement for Wales." He added that the Bill will "provide the Welsh Government with a powerful incentive to grow the Welsh economy and strengthen their financial accountability and transparency."

The Bill proposes the devolution to the Welsh Assembly in Cardiff of powers over landfill tax and stamp duty land tax, and, subject to a referendum, certain income tax powers. The legislation was recently amended to allow the Assembly to determine whether 16- and 17-year-olds should have the right to vote in an income tax referendum.

Crabb said that he wants the Welsh Government to call an income tax referendum after the legislation

has been enacted, to "seize the new powers being offered as soon as possible."

Scotland has already been offered substantial new tax powers as part of a post-independence referendum devolution deal. The Smith Commission, tasked with brokering a cross-party agreement on decentralization, published its proposals on November 27.

As with Scotland, which has already been afforded such powers, the move would involve a *pro rata* change in the Welsh block grant – the portion of revenues provided by the UK Treasury each year to fund government operations.

UK Gambling Tax Regime Rules Overhauled

New rules for the UK's General Betting Duty (GBD), Pool Betting Duty (PBD), and Remote Gambling Duty (RGD) entered into force on December 1, 2014, shifting the place of supply for tax purposes from the place of supply to the place of consumption.

The reforms affect those businesses providing remote betting and gaming to UK consumers from outside the UK, and UK land-based betting businesses, such as high-street betting shops. Land-based gaming sector businesses, such as casinos and bingo halls, are only affected if they offer remote betting or gaming. Those providing premises-based betting and spread betting are largely unaffected, except for some administrative changes.

The change is intended to level the playing field between UK operators, which were subject to tax on all gross gambling profits and also the UK horseracing levy, and overseas operators, who paid no UK gambling taxes.

As a result of the change, anyone who offers remote gambling to a person who usually lives in the UK (a "UK person" under the regulations) will be newly liable to one or more of the relevant taxes (GBD, PBD, or RGD). The change applies regardless of where the supplier is based. Anyone who supplies remote gambling to UK customers from outside the UK will be liable to UK gambling tax for the first time, while UK-based operators who supply remote gambling to customers who do not usually live in the UK are no longer liable to GBD, PBD, or RGD on those transactions.

HMRC is moving to an online registration and return system for these taxes as part of the change. The Department will only issue paper forms for registration and returns if the business in question does not hold – and is not required to hold – a Remote Operating Licence from the Gambling Commission. Anyone who offers remote gambling to UK customers will need to be able to establish which of their customers are "UK people."

The accounting periods for GBD and PBD returns have changed from monthly to quarterly. RGD accounting periods are already quarterly. There is no change to the way GBD is calculated on spread

betting receipts, but quarterly – rather than monthly – returns will be required.

GBD is charged on a bookmaker's profits on specified bets, while PBD is charged on a bookmaker's profits from non-fixed odd bets and are not on horse or dog racing, subject to certain conditions. RGD is charged on a gaming provider's profits from remote gaming played by a UK person.

MEPs Support Juncker Amid Lux Leaks Vote

Most leaders of the European Parliament's political factions expressed support for European Commission President Jean-Claude Juncker in a vote on November 27 on a motion of censure, which had been launched in the aftermath of the leak of Luxembourg's past tax rulings.

The motion called for the removal of Juncker as President of the European Commission, a month into his tenure. It came two weeks after Juncker took part in an extraordinary parliamentary debate on tax avoidance, prompted by the leaked publication by the International Consortium of Investigative Journalists (ICIJ) of more than 500 advance tax decisions issued by the Luxembourg tax authorities between 2002 and 2010.

Juncker served as Prime Minister of Luxembourg between 1995 and 2013, and Finance Minister from 1989 to 2009. He told the European Parliament on November 12 that the rulings were not illegal, but acknowledged that "there probably was a certain amount of tax avoidance in Luxembourg, as in other EU countries." He also said that this is seen "everywhere in Europe because there is insufficient tax harmonization in Europe."

Debate on the motion against Juncker, which was tabled by 76 MEPs, began on November 24. Juncker attended the session, where he told MEPs that his Commission would fight tax evasion and tax fraud and combat unfair tax competition. He has asked Tax Commissioner Pierre Moscovici to draw up proposals for the automatic exchange of information on national tax rulings.

Despite Juncker surviving the vote, and his reassurances that he would press ahead with tackling tax avoidance issues in the EU, the Commission looks set to use the leaked information, with the new Competition Commissioner, Margrethe Vestager, saying that her team regards the documents as "market information." She told a press briefing last week that the Commission will examine the information and "evaluate whether or not this will lead to the opening of new cases."

Priority will, however, be given to completing the existing tax probes into advance rulings provided by Luxembourg, Ireland, and the Netherlands to three multinational companies, Vestager said.

Asia-Pac Tax Agencies Agree Cooperation

At its recent meeting in Sydney, the 44th Study Group on Asian Tax Administration and Research (SGATAR) agreed greater regional cooperation on tax issues.

It will now create a new task force to enable the region to discuss and keep up to date on international developments and issues including base erosion and profit shifting, and tax transparency. Discussions during

the Study Group focused on the latest developments in international taxation, such as the OECD's new global standard for the automatic exchange of information, and discussions were held on how to deal with developments "collaboratively as a region and develop capability, in order to ensure each jurisdiction receives the correct share of taxation."

The members shared their "knowledge and experiences on the key tax administration issues of globalization and the erosion of the tax base; the operation of multinational entities; the seamless exchange of information and the use of bulk data; and opportunities for capability development across all fields of tax administration."

The SGATAR this year brought together almost 200 delegates, including representatives from the Asian Development Bank, the Inter-American Center of Tax Administrations, the International Bureau of Fiscal Documentation, the OECD, and the World Bank Group. The 45th SGATAR conference in 2015 will be held in Singapore.

The SGATAR members are Australia, Cambodia, China, Hong Kong, Indonesia, Japan, South Korea, Macao, Malaysia, Mongolia, New Zealand, Papua New Guinea, Philippines, Singapore, Taiwan, Thailand, and Vietnam.

UK Says Tax On Multinationals To Be Low, But Fair

In a recent speech alongside a new report that recognizes the UK's largest companies' substantial contribution to revenue receipts, the Financial Secretary to the Treasury, David Gauke, has highlighted that the Government aims to establish a fair but competitive tax regime.

Gauke was speaking alongside the release of a new report from PwC that showed that, while corporate income tax is making up a smaller portion of the mix of taxes paid by the UK's biggest businesses, the UK's largest taxpayers are essential to the UK economy's recovery and they pay considerable – and growing – revenues to the UK Government.

Gauke said: "Tax has always been crucial to how our businesses and our economies run. And tax is something people have an opinion on – and they're not afraid to express it! Especially when it is about the eternally fascinating subject of how much other people and organizations pay."

"So, in a time when tax is arguably a higher-profile issue than ever before, it's important that the policy debate is as informed as possible. For example, some people see corporation tax (CT) as a tax on large faceless corporations – abstract and slightly malign entities. And it's very easy to tap into a certain narrative about 'big bad multinationals.' That would be to forget one vital thing. The cost of corporation tax is borne by a combination of shareholders, employees, and the customer."

"Higher corporation tax tends to lead to a combination of higher prices, lower wages, and lower shareholder returns. Everybody is affected in some way. It's for this reason there is a broad consensus

that CT is one of the most distortive and growth damaging taxes."

"The paying taxes survey suggests that globally, cuts in profit taxes have plateaued slightly since 2010. This is unsurprising given the fiscal challenges most Governments have faced since the financial crisis. But on competitiveness, while other countries may have paused, the UK has progressed."

"Since 2010, we have delivered record reductions in corporation tax. The rate has been cut from 28 percent to 21 percent. Next year it will be 20 percent, the lowest rate ever in the UK, the joint lowest rate in the G20. So we have taken great strides to make the UK more competitive and better equipped for the global race. And we are seeing the results. But we know that any competition needs to be fair."

"The UK Government wants an international system with fair rules that ensures all companies pay their share – a system where it isn't possible for a company to play one country off against another so it pays barely any corporation tax at all. Delivering this requires action at an international level."

In comments later in his speech, returning to the findings of PwC's report and its Paying Taxes report, Gauke said: "There are two final points I would like to make: First, we know the burden borne by business goes beyond corporation tax, and differs from sector to sector. The Tax Contribution report illustrates this very well, and it is something we are alive to as a government. But we are committed to listening to businesses, hearing what works, what doesn't, and having a conversation about how we can become even more competitive."

"At Autumn Statement last year, businesses told us their biggest concern was business rates. We listened, and we launched a GBP1bn (USD1.57bn) Business Rates package with particular help for the retail sector. At Budget this year, meanwhile, businesses told us their greatest concern was energy prices. Again, we listened, and launched a GBP7bn package of measures to reduce energy costs for households and businesses, which included specific support for energy intensive industries. We are a listening government – and where necessary we will act."

"The second point I would like to make is this: we still have a long way to go. The report shows how your tax contributions roughly mirror the trajectory of the economy … Your businesses, the jobs and investment you provide, the sales and activity you generate, and the taxes you pay, will have a major role to play in securing this growth."

Gauke's speech came shortly after the publication on November 12, 2014, of a report that explained the efforts from HM Revenue & Customs (HMRC) to work with other countries to amend the international tax rules on multinational companies.

Entitled "Taxing Multinationals: Tackling Aggressive Tax Planning," the HMRC report notes that the UK rules for taxing multinationals are based on

a commonly agreed set of international standards, which have not changed since they were agreed in the 1920s. As a result, the report states, multinationals can plan their tax affairs in a way that separates their profits from the economic activities that generate them.

The report underlines three broad strategies adopted by HMRC to combat tax avoidance, including:

- Working with other countries and tax authorities to combat aggressive tax planning;
- Exchanging information with other tax administrations for greater transparency; and
- Using advance pricing agreements (APAs) to provide certainty on taxable profits.

The report highlights the importance of tax information exchange in meeting HMRC's objectives. It states: "Exchanging information … means there is greater transparency about multinational ownership of assets and the location of their profits … Multinationals based in the UK will have to tell us where they make profits and pay taxes around the world. This information will help us to assess better where there are risks to collecting the tax that is due and where to focus on countering tax avoidance."

Last, on tax rulings, the report states that APAs will only be issued after HMRC has thoroughly assessed the facts and decided if a ruling is appropriate. APAs will also be regularly reviewed to ensure that businesses meet the terms contained in the APA.

WTO Head Says TFA 'Back On Track'

The members of the World Trade Organization (WTO) adopted the Trade Facilitation Agreement (TFA) at a meeting of the General Council on November 27, 2014.

Director-General Roberto Azevêdo congratulated the WTO members for adopting decisions related to the TFA, public stockholding for food security purposes, and the post-Bali work. "By agreeing these three decisions we have put ourselves back in the game," he said. "We have put our negotiating work back on track."

Azevêdo urged the WTO members to begin the process of ratifying the TFA. "Two-thirds of members must deposit their instruments of acceptance for the agreement to come into force," he said.

The Director-General also said that the TFA Facility, which is intended to ensure that least developed countries and developing countries get the help they need to reap the full benefits of the TFA, is now fully operational.

Christine Lagarde, Managing Director of the International Monetary Fund, welcomed the decisions in an official statement on November 29, saying they "reaffirm the commitment of the international community to an open trade system." She added that "they also provide an important opportunity for advancing multilateral trade negotiations in other areas, which is essential to bolster global growth, create jobs, and reduce poverty."

The TFA will create binding commitments across all WTO members to expedite the movement, release and clearance of goods, improve cooperation among WTO members in customs matters, and help developing countries fully implement the Agreement's terms. It is estimated that the agreement can cut trade costs by almost 14.5 percent for low-income countries, and by 10 percent for high-income countries, adding to reforms – and in particular the proposed Doha Round – to cut tax barriers to trade on a global basis.

Chile–Hong Kong FTA Enters Into Force

A free trade agreement between Chile and Hong Kong entered into force on December 1, 2014, according to an announcement in Chile's Official Journal.

The agreement, originally signed on September 7, 2012, provides both sides with preferential access to their respective markets.

On trade in goods, for goods originating from Hong Kong, Chile will abolish import tariffs on around 88 percent of its tariff lines, and will phase out the tariffs on an additional 10 percent of tariff lines over three years.

Hong Kong, on the other hand, has committed to offer tariff-free access for all products originating from Chile from the date that the agreement entered into force.

The agreement also contains provisions to promote competition, open access to government projects, enhance cooperation in customs procedures, and protect the environment.

Obama Threatens To Veto Tax Extenders Deal

Statements from US Treasury Secretary Jack Lew and White House Press Secretary Josh Earnest have indicated that the reported bipartisan deal being put together in Congress on an extension of the "tax extenders" measures would not be supported by President Barack Obama.

The more than 50 provisions for individuals that expired at the end of 2013 include mortgage tax relief; the deduction for state and local sales taxes; and education tax deductions. There has also been talk of extending the provisions of the Child Tax Credit (CTC) and Earned Income Tax Credit (EITC), which improved their benefits for low-income households and are to expire at the end of 2016.

For businesses, the package of measures usually rolled over on an annual basis includes increased expensing under Section 179; 50 percent bonus depreciation; the work opportunity tax credit; the credit for research and development (R&D) expenses; and tax breaks promoting renewable energy, such as the production tax credit that is relied upon by the wind industry.

It has been reported that the deal being put together by Republican and Democrat lawmakers for a renewal of the tax extenders during the current lame-duck congressional session could, for example, permanently renew selected business measures, the most expensive of which would be the R&D credit, at a total ten-year unfunded cost of over USD400bn, but would leave untouched the expiry date of the additional CTC and EITC provisions.

Lew said that such a deal would be "fiscally irresponsible," adding that "an extender package that makes permanent expiring business provisions without addressing tax credits for working families is the wrong approach. … Any deal on tax extenders must ensure that the economic benefits are broadly shared."

In a separate statement, Earnest stressed that the Administration "would not be supportive" if the reports that "some in Congress who want to provide [permanent] tax relief to businesses and to corporate insiders, but not ensuring that those benefits are shared by middle-class families," become reality.

That attitude was also supported by the House of Representatives Ways and Means Committee Ranking Member, Sander Levin (D – Michigan), who called it "fiscally irresponsible to use expiring tax provisions to make permanent changes to our tax code at a cost of more than USD400bn. The President's veto message is very clear in the priorities it sets forth, and we should go back to the drawing board."

However, the current difficulty in reaching some kind of agreement before the end of 2014 harks

back to the gap that has existed throughout this year between Republican and Democrat lawmakers on how to treat the tax extenders.

While Republicans have so far supported a permanent extension of those provisions (including the R&D tax credit) that they see as important to economic growth, Senate Democrats have been looking to renew virtually all of the tax extenders, but for only two years.

Wyden Calls for IRS Action On 'Mega IRAs'

US Senate Finance Committee Chairman Ron Wyden (D – Oregon) has insisted that the Internal Revenue Service (IRS) should implement the recommendations of a new Government Accountability Office (GAO) report on independent retirement accounts (IRAs) with very large account balances, also known as "mega IRAs."

The GAO found that, in the 2011 tax year (the most recent year available), an estimated 43 million taxpayers had IRAs with a total reported fair market value of USD5.2 trillion. While most Americans had a median IRA account balance of about USD21,000, approximately 600,000 taxpayers had accounts worth more than USD1m, and about 9,000 taxpayers had IRAs worth more than USD5m.

In its report, the GAO said that these more affluent taxpayers have the opportunity to invest in assets unavailable to most, such as non-listed shares of their newly formed companies, which are often initially valued very low and offer very high potential investment returns if successful. The GAO noted that these individuals investing in these assets using certain types of IRAs can escape taxation on investment gains.

In 2014, the GAO calculated that the federal government will forgo an estimated USD17.45bn in tax revenue from IRAs, "which Congress created to ensure equitable tax treatment for those not covered by employer-sponsored retirement plans." It suggested that "the accumulation of these large IRA balances by a small number of investors stands in contrast to Congress's aim to prevent the tax-favored accumulation of balances exceeding what is needed for retirement."

The GAO pointed out that the IRS has enforcement programs covering specific aspects of IRA non-compliance, such as excess contributions and undervalued assets. It noted plans to collect data identifying non-publicly traded assets in IRA investments to help identify potential IRA non-compliance. IRS officials said, however, that IRA valuation cases are audit-intensive and difficult to litigate because of the subjective nature of valuation. It said the success of its efforts will depend on the resources available to it.

The IRS also noted that the three-year statute of limitations for assessing taxes owed can pose an obstacle to pursuing non-compliant activity over years of IRA investment.

The GAO has recommended that Congress should consider revisiting the legislation over the use of IRAs. It recommended that the IRS compile and digitize data on non-publicly traded IRA assets and seek an extension of the statute of limitations for IRA non-compliance.

In a statement, Wyden concluded: "The state of retirement savings in the US is completely out of whack. On one hand you've got people sheltering millions of dollars in mega IRAs, while at the same time nearly a third of Americans have nothing set aside for retirement. It's abundantly clear that America needs a better system and tax code that supports retirement planning for all Americans."

In a letter to the Treasury Department and the IRS on November 19, he encouraged the IRS to adopt the GAO's recommendations, which the agency had already largely accepted, and "requested the assistance of the IRS and Treasury in developing legislation to address valuation and compliance concerns."

During a previous hearing of the Committee in September this year, however, Orrin Hatch (R – Utah), who is currently its Ranking Member (but is expected to be its next Chairman), had expressed his concern that the Committee's discussions "would turn retirement policy into another front in the class warfare that consumes so much energy on some of the other committees in Congress."

Witness testimonies at the hearing had suggested that the inefficient targeting of retirement tax incentives is not the main problem. They instead called for simplified, lower-cost investment options and easier workplace access to retirement savings plans.

Study Plugs US Carbon-Corporate Tax Swap

In a policy brief for the Tax Policy Center, Donald Marron, Director of Economic Policy Initiatives at the Urban Institute, has recommended a carbon-corporate tax swap, using the revenue from reducing carbon emissions to cut the US's high corporate income taxes, to contribute to a tax reform package.

With President Barack Obama pushing for a US contribution to countering global climate change, Marron noted that a carbon-corporate tax swap would give the US "a bigger, cleaner economy and avoid any need for more costly efforts to reduce emissions."

He noted that "putting a price on carbon is the most efficient way to reduce carbon emissions. In the absence of a national carbon price, as from a carbon tax or a cap-and-trade system, policymakers will likely continue to pursue piecemeal regulations and subsidies. … These regulatory efforts can reduce emissions, but at greater cost per ton than a national carbon price."

On the other hand, the high US corporate tax rate – at more than 39 percent (including federal and state taxes) – is seen to "discourage business investment and weaken economic growth, [while] inspiring substantial wasted effort on tax avoidance."

In particular, it has led to increasing efforts to use complex regulations to deter US multinationals from using corporate tax inversions to move their tax residence abroad.

Marron concluded that the additional revenue that would be provided by a carbon tax to cut corporate tax rates could be substantial. In 2011, the Congressional Budget Office estimated that a USD20 per ton tax, increasing at 5.6 percent annually, would raise USD1.2 trillion in the first ten years, while cutting emissions by 8 percent. With corporate tax revenues forecast to be about USD4.6 trillion over the next decade, such a carbon tax could then offset the cost of reducing the federal corporate tax rate from 35 percent to 25 percent.

He does point out, however, that, as a carbon-corporate tax swap "would be quite regressive," the effect could need to be "moderated by giving rebates to low-income families or reducing payroll taxes." However, using some revenue this way would reduce the level of funds available for corporate tax rate reductions, he said.

The discussion on a carbon-corporate tax swap is also seen to have achieved increasing relevance recently, due to the US Environmental Protection Agency's plans to establish broad state-level goals for reducing emissions per megawatt hour from electricity, instead of regulating power plants directly.

These plans are seen as giving states a push towards pricing mechanisms, such as a carbon tax, rather than more regulations to achieve their targets. However, as states will have differing carbon reduction goals, dependent on their levels of emissions, it is likely each state would impose its own carbon tax rate and there would also be differing approaches to how the additional revenue would then be utilized.

Spain Gazettes Income Tax Reforms

Spain has completed its domestic ratification procedures in respect of a package of tax reform measures that includes a cut to the corporate income tax rate from next year.

From January 1, 2015, the corporate income tax rate will fall from 30 percent to 28 percent. It will be cut further to 25 percent in 2016. A reduced rate of 15 percent will apply to companies formed in 2013 or 2014, for two years.

The number of personal income tax rates will fall from seven to five, reducing the tax burden on low-income taxpayers by about a fifth. Specifically, the minimum personal income tax rate is to fall to 24.75 percent in 2015 and to 19 percent in 2016. The top marginal tax rate, which will be 47 percent next year, will fall to 45 percent in 2016 but will be levied on income in excess of EUR60,000 (USD74,500), down significantly from EUR300,000 currently. The tax-exempt threshold will rise to EUR12,000.

Tax on savings income of up to EUR6,000 will fall from 21 percent to 20 percent in 2015 and to 19 percent in 2016. Savings income of up to EUR50,000 will be taxed at a 22 percent rate in 2015 and a 21 percent rate in 2016. Above this threshold, the applicable rate will fall from 24 percent next year to 23 percent in 2016. These rates are also to newly apply to capital gains, removing rates more than twice as high on gains from short-term holdings.

The changes, which were published in the Official Gazette on November 28, were included in Law 27/2014, on the taxation of companies; Law 26/2014, on the taxation of individuals; and Law 28/2014, which includes miscellaneous and indirect tax measures.

Dividends Tax Proposed In Colombia

The Colombian Government has rejected a proposal to include a tax on dividends in a package of reforms to be debated by Congress.

The proposal from Senator Antonio Navarro of the opposition Green Party, backed by a group of 16 lawmakers, would introduce a 10 percent tax on dividend income received by Colombian individuals or foreign companies of COP42m (USD19,484) per year or more. It has not been included in the latest tax reform bill, but could be reintroduced in separate legislation.

The reform package seeks to boost Government revenue and plug an emerging budget deficit. One of its key measures is the gradual elimination of the corporate wealth tax. This tax, on companies with equity exceeding COP5bn (USD2.3m), will be phased out by 2018, after the rate falls from 1.3 percent next year, to 1 percent in 2015, and to 0.75 percent in 2017.

Meanwhile, the maximum rate of the wealth tax for individuals would be 1.5 percent until 2018. The minimum rate, on wealth of between COP1bn and

COP2bn, would be reduced from 0.25 percent to 0.125 percent.

The Bill will also extend a 0.4 percent tax on financial transactions (the so-called 4x1000 levy) until 2018. Additionally, it proposes to introduce a tax on large companies with a turnover of COP800m or more, to be known as CREE, which will rise by 1 percent each year, from 4 percent in 2015 to 9 percent in 2018, supplementing the corporate income tax rate paid by these companies.

Peruvian Congress Supports New Tax Proposals

Peru's Congress endorsed a proposed package of tax reforms during an initial debate held on November 26, 2014.

The reforms, which are aimed at reviving Peru's slowing economy, include a reduction to the corporate tax rate from 30 percent to 28 percent in 2015. The rate would fall to 26 percent by 2019. Reforms are proposed also for Peru's personal income tax regime, which would lower the tax burden on low-income persons' fourth and fifth category income (income from independent professional services, and labor income, respectively).

The Bill was approved with 54 votes in favor and 10 votes against, with 36 abstentions, despite calls for the individual income tax reforms to be ditched in favor of a 3 percent reduction to the value-added tax (VAT) rate. Lawmakers, however, approved a proposal to refund micro businesses VAT incurred on the purchase of capital goods, which would be offered for three years.

Noting that Peru's economy is to grow by just 3 percent this year, Fitch Ratings said that Peru is in a unique position in Latin America to deploy revenues from fiscal surpluses racked up over the past three years. In addition, Peru has saved USD9bn in its fiscal stabilization fund. Fitch has estimated that the tax package could be worth 2 percent of gross domestic product (GDP) next year, and could support a recovery in the economic growth rate to 5 percent next year and to 5.4 percent the year after.

Italian Lower House Approves 2015 Budget

Unlike in recent years, the Government's 2015 Budget Bill (*legge di stabilità*) has succeeded in passing through Italy's lower house, the Chamber of Deputies, without substantial amendments, and will now immediately progress for further discussion in the Senate.

Those measures approved by the Chamber include that the EUR80 (USD100) per month income tax deduction, which was first paid on a temporary basis in May this year, will be maintained next year; the tax credits for home restructuring and energy saving expenses will remain unchanged for a further year; and a buy-to-let income tax credit will be introduced for purchases of energy-efficient new or renovated residential properties rented out at a locally subsidized rent for at least eight years.

In addition, businesses who take on new full-time employees (not on fixed-term contracts) during 2015 will receive both an exemption from payment of social security contributions, subject to a cap of EUR6,200 per employee, and also the inclusion of their labor costs in the calculation of the regional tax on production (IRAP).

The Government's plans to expand the list of goods that would be subject to a reverse charge for value-added tax (VAT) purposes from 2015 has also been passed, but is subject to approval from the European Commission.

In an addition to the Bill, which had earlier proposed a reverse charge on real estate and construction services, the Chamber approved (subject to EU agreement) that the reverse charge should also cover the retail sector. The reverse charge shifts the obligation to account for VAT to the recipient, instead of the supplier, to counteract fraud.

After the Chamber's approval, Economy Minister Pier Carlo Padoan professed that he "is convinced that the Budget Bill will allow Italy to begin a reversal in fortune, in terms of economic growth and employment, that has been awaited for years, and to confront 2015 with increasing confidence."

PwC Singapore Suggests Budget 2015 Measures

PwC Singapore has released its annual tax policy recommendations, which have been compiled in response to an ongoing Ministry of Finance pre-Budget consultation on tax and spending measures.

PwC Singapore's Budget 2015 wish list includes various recommendations that aim to provide additional support for small and medium-sized enterprises (SMEs) through the city-state's tax code.

For example, it suggests changes to the partial tax exemption that "was introduced to reduce the effective tax rates of [SMEs], but also benefits all corporate taxpayers, which may not need assistance."

Instead of the partial tax exemption, PwC suggests that an exemption on the first SGD300,000 (USD230,000) of an SME's chargeable income would maximize the tax benefit for such businesses. It said eligibility limitations, such as a turnover threshold and number of employees, could be imposed to target the tax break only at SMEs.

It recommends promoting bank lending to SMEs by allowing banks a double deduction for losses on loans to SMEs, while the Ministry could consider reintroducing an incentive for employee share option schemes and could restrict it to employees of start-up companies or SMEs.

PwC said that, as "international tax rules are being rewritten as part of the [OECD's] base erosion and profit shifting project, measures that have served Singapore well will need to be re-examined in the light of today's environment." While "Singapore tweaks its tax policies to enhance international competitiveness, … we will have to ensure that our rules are consistent with the changing global norms," PwC Singapore said.

In that respect, the firm included a recommendation that the Ministry should streamline Singapore's corporate tax incentives. In particular, a single tax incentive rate should be established, and "core requirements could be legislated for specified concessionary tax rates."

The firm's wish list also includes an enhancement to Singapore's mergers and acquisitions (M&A) rules. It has proposed "allowing a waiver of the condition that the ultimate holding company must either be incorporated in Singapore or a company that qualifies for the international headquarters incentive. This would encourage acquiring groups that have trading operations in Singapore to conduct their M&A from Singapore."

BELARUS - AUSTRIA

Signature

Belarus signed a protocol to amend its DTA with Austria on November 24, 2014.

CZECH REPUBLIC - KAZAKHSTAN

Signature

The Czech Republic signed a protocol to amend its DTA with Kazakhstan on November 24, 2014.

FRANCE - CHINA

Ratified

The French President, Francois Hollande signed a law to ratify the country's DTA with China on November 26, 2014.

GAMBIA - QATAR

Signature

According to preliminary media reports, Gambia signed a DTA with Qatar on November 18, 2014.

HUNGARY - UZBEKISTAN

Signature

Hungary signed a protocol to amend its DTA with Uzbekistan on November 27, 2014.

SWEDEN - HONG KONG

Ratified

Sweden ratified its TIEA with Hong Kong on November 19, 2014.

A guide to the next few weeks of international tax gab-fests (we're just jealous - stuck in the office).

THE AMERICAS

TAX FOR SHIPPING BRAZIL

Lloyd's Maritime Academy

Venue: Pestana Rio Atlantica, Avenida Atlântica, 2964, Rio de Janeiro - RJ, 22070000, Copacabana, Brazil

Key Speakers: Luis Wolf Trzcina (KPMG), André de Souza Carvalho (Veirano Advogados), Werner Braun Rizk (Zouain, Rizk, Colodetti e Advogados Associados), among numerous others.

12/4/2014 - 12/5/2014

http://www.lloydsmaritimeacademy.com/event/taxbrazil

US TAX ASPECTS OF INTERNATIONAL ACQUISITIONS & REORGANIZATIONS

Bloomberg BNA

Venue: Morgan Lewis Conference Center, 1 Market Street, San Francisco, CA 94105, USA

Chair: Bart Bassett (Morgan Lewis)

12/10/2014 - 12/11/2014

http://www.bna.com/uploadedFiles/Content/Events_and_Training/Live_Conferences/Tax_and_Accounting/Conferences_-_Seminars/IPAcqReorgDec2014.pdf

US INTERNATIONAL TAX REPORTING AND COMPLIANCE

Bloomberg BNA

Venue: 731 Lexington Avenue, New York, NY 10022, USA

Key Speaker: Kyle Bibb (K. Bibb LLC, TX), Eytan Burstein (McGladrey, NY), Victor Gatti (KPMG, NY), James Hemelt (Bloomberg BNA, VA), Marcellin Mbwa-Mboma (Ernst & Young LLP, NY), Mitchell Siegel (McGladrey, NY)

12/15/2014 - 12/16/2014

http://www.bna.com/reportingandcompliance_newyork2014/

19TH TAXATION OF CORPORATE REORGANIZATION

Federated Press

Venue: Courtyard by Marriott Downtown Toronto, 475 Yonge Street, Toronto, ON, M4Y 1X7, Canada

Key Speakers: Mark Brender (Hoskin & Harcourt LLP), Firoz Ahmed (Hoskin & Harcourt LLP), Eric C Xiao (Ernst & Young LLP), Mitchell J Sherman (Goodmans LLP), among numerous others

1/20/2015 - 1/22/2015

http://www.federatedpress.com/pdf/TCR1501-E.pdf

4TH ANNUAL INSTITUTE ON TAX, ESTATE PLANNING AND THE ECONOMY

STEP

Venue: Newport Beach Marriott Hotel & Spa, 900 Newport Center Drive, Newport Beach, California, 92660, USA

Chair: Mark Silberfarb (Chapter Chair, STEP OC)

1/22/2015 - 1/24/2015

http://www.step.org/sites/default/files/STEP%20OC%20Conference%20Brochure%202015%20SCREEN%2026%20August%202014.pdf

16TH TAX PLANNING FOR THE WEALTHY FAMILY

Federated Press

Venue: Calgary Marriott Hotel, 110 9th Avenue, SE, Calgary, AB, T2G 5A6, Canada

Key Speakers: James Meadow (MNP LLP), Melanie McDonald (Borden Ladner Gervais LLP), Doris C.E. Bonora (Dentons Canada LLP), David N. Beavis (Counsel Financial), Michael J. Beninger (Bennett Jones LLP), among numerous others

1/27/2015 - 1/28/2015

http://www.federatedpress.com/pdf/TPWF1501-E.pdf

INTERNATIONAL TAX ISSUES 2015

Practising Law Institute

Venue: PLI New York Center, 1177 Avenue of the Americas, New York, New York 10036, USA

Chair: Michael A. DiFronzo (PwC)

2/11/2015 - 2/11/2015

http://www.pli.edu/Content/Seminar/International_Tax_Issues_2015/_/N-4kZ1z12a24?ID=223914

AMERICAS TRANSFER PRICING SUMMIT 2015

TP Minds

Venue: TBC, Miami, Florida, USA

Key Speakers: Samuel Maruca (IRS), Michael Lennard (United Nations), Mayra Lucas (OECD),

David Ernick (PwC), Sergio Luis Pérez (SAT Mexico), among numerous others

2/19/2015 - 2/20/2015

http://www.iiribcfinance.com/event/Americas-Transfer-Pricing-Conference

THE 4TH OFFSHORE INVESTMENT CONFERENCE PANAMA 2015

Offshore Investment

Venue: Hilton Panama, Esquina de Avenida Balboa y Aquilino de la Guardia, Av Balboa, Panama

Chair: Derek R. Sambrook (Trust Services)

3/11/2015 - 3/12/2015

http://www.offshoreinvestment.com/media/uploads/Panama%20Brochure-%20Final.pdf

ASIA PACIFIC

THE 3RD OFFSHORE INVESTMENT CONFERENCE SINGAPORE 2015

Offshore Investment

Venue: Raffles, 1 Beach Rd, 189673, Singapore

Chair: Nicholas Jacob (Wragge Lawrence Graham & Co)

1/21/2015 - 1/22/2015

http://www.offshoreinvestment.com/media/uploads/The%203rd%20OI%20Conference%20Singapore%202015%20pgs%207-10%20(2).pdf

INTERNATIONAL CORPORATE TAX PLANNING ASPECTS

IBFD

Venue: Conrad Centennial Singapore, Two Temasek Boulevard, 038982 Singapore

Key Speakers: Chris Finnerty (ITS), Julian Wong (Ernst & Young), Tom Toryanik (RBS)

4/20/2015 - 4/22/2015

http://www.ibfd.org/Training/International-Corporate-Tax-Planning-Aspects-0

CENTRAL AND EASTERN EUROPE

CIS WEALTH MOSCOW 2015

CIS Wealth

Venue: Renaissance Moscow, Monarch Centre Hotel, 31A bld.1 Leningradsky prospect Moscow 125284, Russia

Key speakers: TBC

2/16/2015 - 2/17/2015

http://cis-wealth.com/files/1411641516.pdf

WESTERN EUROPE

TREASURY FOR TAX PEOPLE

IBC

Venue: London, UK, TBC

Co-Chairs: David Hill (Grant Thornton), Edward Brown (Grant Thornton)

12/9/2014 - 12/9/2014

http://www.iiribcfinance.com/event/treasury-for-tax-people-event

TAX & ACCOUNTING FOR OIL & GAS COMPANIES

IIR & IBC Financial Events

Venue: The Hatton, 51-53 Hatton Garden, London, EC1N 8HN, UK

Key Speakers: Alan Teixeira (IASB), Lars Ragnar Vigdel (Statoil), Michael Karaiskos (Deloitte), Jane Stevensen (Grant Thornton), Adrian Wild (Smith & Williamson), Paul Watts (Baker Tilly), among numerous others

12/9/2014 - 12/12/2014

http://www.iiribcfinance.com/event/Tax-Accounting-and-IFRS-for-Oil-and-Gas-Companies

PRIVATE CLIENT PROPERTY TAXATION 2014

IBC

Venue: Radisson Blu Portman Hotel London, 22 Portman Square, London W1H 7BG, UK

Key Speakers: Robert Smeath (Clarke Wilmott LLP), Michael Thomas (Gray's Inn Tax Chambers), Emma Chamberlain (Pump Court Tax Chambers), Marilyn McKeever (Berwin Leighton Paisner LLP), among numerous others.

1/22/2015 - 1/22/2015

http://www.iiribcfinance.com/event/private-client-property-taxation-conference

EMPLOYMENT TAX PLANNING CONFERENCE 2015

IIR & IBC Financial Events

Venue: etc. Venues, The Hatton, 51-53 Hatton Garden, London, EC1N 8HN, UK

Key Speakers: Patrick Way QC (Field Court Tax Chambers), Teresa Payne (BDO), Nick Wallis

(Smith & Williamson), Rosemary Martin (Deloitte), Jenny Wheater (Duane Morris), among numerous others.

1/28/2015 - 1/28/2015

http://www.iiribcfinance.com/event/Employment-Tax-Planning-Conference

4TH IBA/CIOT CONFERENCE: CURRENT INTERNATIONAL TAX ISSUES IN CROSS-BORDER CORPORATE FINANCE AND CAPITAL MARKETS

International Bar Association

Venue: Holborn Bars, 138-142 Holborn, London, EC1N 2NQ, UK

Key Speakers: TBA

2/9/2015 - 2/10/2015

http://www.ibanet.org/Article/Detail.aspx?ArticleUid=39e22db5-3c06-4228-a829-ccb351190d1e

20TH INTERNATIONAL WEALTH TRANSFER PRACTICE LAW CONFERENCE

International Bar Association

Venue: Claridges Hotel, 49 Brook St, London, W1K 4HR, UK

Chairs: Leigh-Alexandra Basha (Holland & Knight), Gerd Kostrzewa (Heuking Kühn Lüer Wojtek), Christopher Potter (Sete), Rashad Wareh (Kozusko Harris Duncan)

3/2/2015 - 3/3/2015

http://www.int-bar.org/conferences/conf603/binary/London%20IWTP%202015%20programme.pdf

INTERNATIONAL TRANSFER PRICING SUMMIT 2015

TP Minds

Venue: Millennium Gloucester Hotel, 4-18 Harringdon Gardens, Kensington, London, SW7 4LH, UK

Key Speakers: Samuel Maruca (IRS), Joseph Andrus (OECD), Michael Lennard (United Nations), Peter Steeds (HMRC), Ian Cremer (WCO), among numerous others

3/10/2015 - 3/11/2015

http://www.iiribcfinance.com/event/International-Transfer-Pricing-Summit/speakers

INTERNATIONAL TAX ASPECTS OF CORPORATE TAX PLANNING

IBFD

Venue: IBFD head office, Rietlandpark 301, 1019 DW Amsterdam, The Netherlands

Key Speakers: Jeroen Kuppens (KPMG), Boyke Baldewsing (IBFD), Frank Schwarte (Abel Advisory), Luis Nouel (IBFD)

3/18/2015 - 3/20/2015

http://www.ibfd.org/Training/International-Tax-Aspects-Corporate-Tax-Planning-0

SPRING RESIDENTIAL CONFERENCE 2015

Chartered Institute of Taxation

Venue: Queens' College, Silver Street, Cambridge CB3 9ET, UK

Chair: Chris Jones (Chartered Institute of Taxation)

3/27/2015 - 3/29/2015

http://www.tax.org.uk/Resources/CIOT/Documents/2014/11/v4Spring%20Conference%202015%20-%20brochure.pdf

INTERNATIONAL TAX ASPECTS OF MERGERS, ACQUISITIONS AND CORPORATE FINANCE

IBFD

Venue: IBFD head office, Rietlandpark 301, 1019 DW Amsterdam, The Netherlands

Key Speakers: Jan-Pieter Van Niekerk, Daan Aardse (KPMG), Rens Bondrager (Allen & Overy LLP), Marcello Distaso (Van Campen Liem), Piet Boonstra (Van Campen Liem), Paulus Merks (DLA Piper LLP)

3/30/2015 - 4/1/2015

http://www.ibfd.org/Training/International-Tax-Aspects-Mergers-Acquisitions-and-Corporate-Finance

PRINCIPLES OF INTERNATIONAL TAXATION

IBFD

Venue: IBFD head office, Rietlandpark 301, 1019 DW Amsterdam, The Netherlands

Key Speakers: Laura Ambagtsheer-Pakarinen (IBFD), Roberto Bernales (IBFD), Piet Boonstra (Van Campen Liem), Marcello Distaso (Van Campen Liem), Carlos Gutiérrez (IBFD)

4/20/2015 - 4/24/2015

http://www.ibfd.org/Training/
Principles-International-Taxation-1

PRINCIPLES OF INTERNATIONAL TAX PLANNING

IBFD

Venue: IBFD head office, Rietlandpark 301, 1019 DW Amsterdam, The Netherlands

Chair: Boyke Baldewsing (IBFD)

6/1/2015 - 6/5/2015

http://www.ibfd.org/Training/Principles-International-Tax-Planning-0

INTERNATIONAL TAXATION OF EXPATRIATES

IBFD

Venue: IBFD head office, Rietlandpark 301, 1019 DW Amsterdam, The Netherlands

Key Speakers: TBC

6/10/2015 - 6/12/2015

http://www.ibfd.org/Training/International-Taxation-Expatriates

INTERNATIONAL TAX ASPECTS OF PERMANENT ESTABLISHMENTS

IBFD

Venue: IBFD head office, Rietlandpark 301, 1019 DW Amsterdam, The Netherlands

Key Speakers: Andreas Perdelwitz (IBFD), Bart Kosters (IBFD), Hans Pijl, Roberto Bernales (IBFD), Walter van der Corput (IBFD), Madalina Cotrut (IBFD), Jan de Goede (IBFD)

6/16/2015 - 6/19/2015

http://www.ibfd.org/Training/International-Tax-Aspects-Permanent-Establishments

INTERNATIONAL TAX SUMMER SCHOOL

IIR & IBC Financial Events

Venue: Gonville & Caius College, Trinity St, Cambridge, CB2 1TA, UK

Key Speakers: Timothy Lyons QC (39 Essex Street), Peter Adriaansen (Loyens & Loeff), Julie Hao (EY), Heather Self (Pinsent Masons), Jonathan Schwarz (Temple Tax Chambers), among numerous others

8/18/2015 - 8/20/2015

http://www.iiribcfinance.com/event/
International-Tax-Summer-School-2015

INTERNATIONAL TAXATION OF BANKS AND FINANCIAL INSTITUTIONS

IBFD

Venue: IBFD head office, Rietlandpark 301, 1019 DW Amsterdam, The Netherlands

Key Speakers: TBC

9/16/2015 - 9/18/2015

http://www.ibfd.org/Training/International-Taxation-Banks-and-Financial-Institutions

ASIA PACIFIC

Australia

The Administrative Appeals Tribunal of Australia heard the case of a resident of Vanuatu who visited Australia increasingly frequently, and for longer periods, between 1997 and 2006 (and had familial and other ties there). During an investigation by the Australian Government which eventually led to the conviction of the taxpayer for tax avoidance, under the Project Wickenby anti-avoidance initiative, he was assessed by the income tax authorities as being liable for Australian income tax on the basis that he was earning income in Australia.

The taxpayer objected to both the amounts of tax assessed, the fact that he was assessed as being resident in Australia for tax purposes, and the administrative penalties imposed; the latter were significant, and included an "additional tax for late return" penalty of 50 percent of the primary tax due for the 1997 to 2000 period, and a penalty for "failure to provide a document" for the 2001 to 2006 period, amounting to 75 percent of the primary tax amount.

Although the Commissioner amended its stance on a number of points in the time between the taxable period in question and the matter being brought before the Tribunal, including on the imposition of the administrative penalty for the 1997 to 2000 period, the two main points of contention that

A listing of key international tax cases in the last 30 days

remained were whether the taxpayer was a resident of Australia, and if not how much of his income was earned in Australia.

The Tribunal began by looking at the relevant national legislation and interpreting the provision defining "Australian resident." The taxpayer spent his childhood in Australia but as an adult was employed in Vanuatu and, following the divorce of his first wife who lived in Australia, gave up his Australian citizenry in order to become a citizen of Vanuatu at the beginning of the period of time being considered. He remained in contact with his ex-wife and their children and often visited them in Australia, sometimes staying in property that he owned and sometimes

staying with his mother-in-law; he also conducted business in Australia. The Tribunal, in considering the common meaning of the word "resided," rejected the Commissioner's argument that the taxpayer resided in both Vanuatu and Australia, despite acknowledging that a person can reside in two different places. During his visits the taxpayer was staying in Australia but not living there because his activity "during the relevant years lacks the permanent, long-term or non-transient quality" that one would associate with residing somewhere, and therefore the Tribunal concluded that the taxpayer was not a resident of Australia during the years in question.

Regarding the Commissioner's assessments of the taxpayer's income and how much to allow for Australian tax purposes, the Tribunal heard the reasoning behind the assessments; namely that the taxpayer was meeting clients in Australia and convincing them to invest money in offshore arrangements in Vanuatu, and that the taxpayer earned his employment income through the amount of money transferred to companies in Vanuatu controlled by or connected to the taxpayer less the amount which returned to the Australian client. In order to dismiss the assessments, the Tribunal stated that the burden of proof was on the taxpayer to show that they were excessive, and that according to past court judgments he had to "identify those categories of income (if any) that generated Australian-sourced income, but also to prove that there were no others that did so."

The taxpayer reported that he received income from his employment with one company and as a director of another company in Vanuatu, and claimed that neither was derived from a source in Australia, despite the Tribunal pointing out that the focus for a source of income is where it was earned rather than where it came from. The Tribunal also heard that the taxpayer received dividends from the latter company, but the taxpayer continued to argue that the companies involved were established and rendered services in Vanuatu, and even went so far as to provide detailed worksheets outlining his asserted taxable income.

The Tribunal agreed that money from the Australian clients was paid to and owned by the companies in Vanuatu, and the taxpayer received income from those companies as an employee; however, he was also working in Australia as a partner of other companies in Vanuatu and therefore deriving income from Australian sources himself. Unfortunately the taxpayer was unable to quantify to the satisfaction of the Tribunal the amount of income he received while acting as a partner, and as a result the Tribunal ruled that he had failed to discharge the burden of proof by not providing enough evidence to establish that the Commissioners' assessments were excessive.

The administrative penalty for "failure to provide a document" was also allowed by the Tribunal because the taxpayer had failed to file Australian income tax returns on time, which he was required to do as a result of him earning Australian income as a non-resident, according to notices issued on this during the period in question.

The judgment was delivered on November 17, 2014.

http://www.austlii.edu.au/au/cases/cth/aat/2014/854.html

Administrative Appeals Tribunal: *Robert Agius v. Commissioner of Taxation (AATA 854)*

WESTERN EUROPE

United Kingdom

The European Court of Justice (ECJ) heard the case between the European Commission and the United Kingdom concerning national legislation which the former considered a violation of EU law. Under the national legislation, capital gains tax (CGT) is imposed on participators resident in the UK when a gain is made by the non-resident close company they are participating in, but the same CGT only applies to participators in resident close companies if the gain is distributed to them, and is based on the amount the participators receive rather than the amount the company receives. The Commission approached the UK claiming that the difference in treatment restricts the right to free movement of capital available under EU law, but the UK argued that the relevant national legislation was intended to prevent tax avoidance in the UK and therefore the different treatment was justifiable. When the UK failed to amend its legislation in a timely fashion, despite eventually assenting to the Commission's arguments, the Commission approached the ECJ for a ruling; the national legislation in question was amended with retroactive effect in April 2012, but the Commission had requested that changes in this area be made by April 2011.

The ECJ stated that to restrict free movement of capital means to "discourage non-residents from making investments in a Member State or to discourage that Member State's residents from doing so in other States", and that in the present case UK residents were discouraged from participating in non-resident close companies due to the different tax treatment that they received compared to resident close companies. The ECJ therefore deliberated over whether the different tax treatment could be justified. The reason given by the UK, that it was intended to prevent tax avoidance, has been found by the ECJ in past cases to be a suitable reason, but only if the measures in the relevant legislation are "appropriate for attaining those objectives and not go beyond what is necessary for attaining them". The Commission contended that the legislation went beyond what was necessary to prevent tax avoidance in the UK.

The ECJ pointed out that in order to justifiably prevent tax avoidance, measures prescribed under the legislation in dispute must be able to "identify the existence of a wholly artificial arrangement entered into for tax reasons alone", in addition to providing taxpayers the ability to prove with evidence that their arrangement was not only for the sake of avoiding tax. However, in the present case the legislation applied to gains made by close companies without taking

into account the intent of the participators, or whether their stake in the company was a controlling one, or for the purposes of investment only. Therefore, there was no method to determine whether tax avoidance was involved or for participators to justify their participation in the event of a tax avoidance accusation.

The ECJ concluded that even though the national legislation which imposed CGT on non-resident close companies under different conditions than the CGT imposed on resident close companies may have been for the purpose of preventing tax avoidance in the UK, according to past judgments and EU law, the legislation went beyond what was necessary to achieve the intended purpose because it did not distinguish between legitimate participation and participation for the sake of tax avoidance. The ruling was therefore that the legislation was unjustifiably restricting the right to free movement of capital.

The judgment was delivered on November 13, 2014.

http://curia.europa.eu/juris/document/document.jsf?text=&docid=159558&pageIndex=0&doclang=EN&mode=lst&dir=&occ=first&part=1&cid=4915

European Court of Justice: *Commission v. United Kingdom (C-112/14)*

Dateline December 4, 2014

What is it with Asian countries and consumption taxes? As we saw last week, politicians in Japan look at the consumption tax the way a rabbit looks at onrushing headlights; India has spent the best part of a decade trying to replace a panoply of inefficient taxes with a central/state GST akin to Canada's harmonized sales tax; and despite the fact that Hong Kong's narrow tax base is routinely flagged up as one of its main vulnerabilities, the Government swiftly backed away from a sales tax some years ago. But at least we can now remove Malaysia from the list of consumption tax procrastinators, with the Government all set, ten years after it was proposed in parliament, to introduce the long awaited goods and services tax in 2015, a decision recently endorsed by the International Monetary Fund. No, I haven't gone soft. I know the likes of the IMF usually get execrated here for recommending and/or praising revenue increase after revenue increase. But, God knows, if we must suffer taxation at almost every turn, then it helps if governments tax us in a way that most of us can begin to understand. In Malaysia's case, it will be two taxes out, and one tax in. And the tax coming in is one that multinational businesses will in the main be more familiar with than the two taxes being replaced, especially if they operate in Europe, where VAT is pretty much universal, or in the Americas (other than the USA), where these types of taxes are also common. Furthermore, the Government is also cutting income tax to offset the revenue gain it expects to receive. Also, at 6 percent, Malaysia's GST will be comparatively low. Although cynical old me can't help but feel that this just gives the Government, battling a budget deficit, plenty of scope to hike it in future.

If you own or run a business, the UK Government claims to be your friend. And by and large it is. By April 2015, the Conservative-led coalition administration will have cut corporate tax by a not insubstantial 8 percent since it came to power in 2010. This, in combination with other pro-business tax reforms, including to the foreign profits regime, has turned heads in various parts of the world, most notably in the United States, from where companies have been attempting to make a beeline for the UK, much to the chagrin of President Obama and Congress. And these are policies that appear to have succeeded: economic growth of 3 percent is predicted this year, which, to the euro-skeptics' delight, must be rubbing salt into the wounds of the eurozone, showing it up as the failure it was always destined to be when the single currency was fudged in an epic way 15 years ago. Schadenfreude, yes; a word from an appropriate language given Germany's leading role in cooking up the fudge. Back on topic though, Britain has a long history of being the friend of private enterprise. Let's not forget that the British Empire was originally a private trading venture before it became a prestige project. Just lately though, dear old Blighty has become quite a difficult and demanding friend, prone to serious lapses of judgment. We know you're still a bit short of cash now, Britain, but was giving the

attack dog that is HMRC so much license to roam, including powers to raid people's bank accounts, a sensible thing to be doing? Now the caseload of unresolved tax disputes is at an all-time high. Thankfully, somebody has managed to talk you into watering down HMRC's direct recovery powers. But even more astonishing is your determination to put corporate beneficial ownership information into the public domain. It's a noble sentiment, but one that will lead to almost certain economic suicide if pursued too vigorously. Not even Brussels wants to go that far. And now I hear that instead of having just one tax system, you're going to have three, or maybe even more?

With the tax picture in a newly quasi-federal UK looking increasingly confused, it is reassuring to know that in much of the rest of the world, paying taxes is getting easier, especially when, in some places, penalties for non-compliance, innocently committed or otherwise, are getting quite scary. Special mention goes to Mexico, which climbed 13 places up the new PwC/World Bank "ease of paying taxes" league table. Perhaps this can be taken as a small sign that President Enrique Peña Nieto's Government is serious about modernizing Latin America's second largest economy and encouraging foreign investment. The result still leaves Mexico in 105th place out of 189 countries though. And despite there just being six tax payments to make, these take on average 334 hours to complete – that's practically two solid weeks, give or take a few hours. So there is plenty of room for improvement! Nevertheless, it is a sad state of affairs that in even the "simplest" of tax regimes, some considerable time and effort are still needed to comply with tax obligations. The three payments required of companies in fourth-placed Hong Kong take on average 78 hours a year. That's still the equivalent of more than three whole days. It has to be said though that these league tables throw up some quirky results. Who'd have thought that paying taxes would be easier in the high-tax Nordic economies of Denmark (12th) and Norway (15th) than Switzerland (18th)? Time to comply in Brazil still takes 2,600 hours on average (108 days!), placing it 177th. But strangely, this horrific statistic isn't enough to put Brazil at the foot of the table – that dubious honor goes to Bolivia (42 payments, 1,025 hours to comply, and a total tax rate of 83.7 percent). FDI into Brazil, which continues to dominate regional investment, still seems healthy, although until the Brazilian Government makes dramatic (but highly unlikely) simplifying changes to the tax system, we'll never know how high it could be.

The Jester