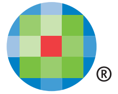

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# GLOBAL TAX WEEKLY
## a closer look

ISSUE 113 | JANUARY 8, 2015

**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

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# GLOBAL TAX WEEKLY
## a closer look

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## The 'Whys And Wherefores' Of FATCA Withholding

by Peter Stafford, DMS Offshore Investment Services

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This article provides some practical insights into FATCA withholding and international tax compliance.

**Introduction**

The IRS wants to know who you are.

If you receive US source withholdable payments or have a financial account with a Foreign Financial Institution ("FFI"), the US Internal Revenue Service ("IRS") really wants to identify and classify you for the purpose of the Foreign Account Tax Compliance Act ("FATCA").

Working in concert, the US Department of the Treasury has now conscripted 114,764 FFIs and 112 foreign governments (as at November 30, 2014) *via* Intergovernmental Agreements ("IGAs"), in addition to US Withholding Agents ("USWAs"), to find out if you are or might be a person of interest, and require you to report your answer to the IRS.

These IGAs, classified as either Model 1 (under which FFIs report *via* their domestic tax authorities) or Model 2 (with direct reporting to the IRS), are helping to propagate FATCA's rapid global growth. An additional 8,117 FFIs from 118 other jurisdictions not subject to an IGA have also recognized that it is in their best interests to register with the IRS and comply with onerous FATCA customer due diligence, withholding and reporting obligations.

Regardless of whether you are US or foreign, it will cost you and your counterparties and financial institutions time and money to document just who you are. If you fail to provide withholding certificates and identification documentation in time, your payor/financial institution is compelled to make a series of unfavorable presumptions about your tax status. The presumptions also apply if your payor/financial institution has "reason to know" that documentation is "unreliable or incorrect." These new international tax compliance rules are designed to help the IRS clamp down on tax evasion by US taxpayers in respect of their undisclosed or under-reported foreign (*i.e.*, non-US) assets.

## Ringing In The FATCA New Year

FATCA was originally scheduled to "go live" on January 1, 2014. Then it was postponed to July 1, 2014[1] and later a "soft-opening" until January 1, 2015 was provided for payees/account holders that are entities (but not individuals). For some time, leading institutions such as Goldman Sachs and Barclays Capital had not banked on any further extensions. Their tax experts, Rasheed Khan and Karen Mosley, made this point at the 3rd Annual FATCA and Global Tax Compliance Forum held on November 4–6 in New York.[2] Khan and Mosley also recommended that USWAs always obtain withholding certificates rather than relying on the "eyeball" test.

From 2015 onwards, USWAs and Participating FFIs ("PFFIs") will be personally liable to the IRS if they fail to pay the IRS any withholding tax due on withholdable payments/credits to certain account holders and payees.[3] Any withholding tax exceeding USD2,000 must be paid to the IRS within three business days after the 7th, 15th, 22nd and last day of each month.

## Agents And Payments

A withholding agent is broadly defined to include "any US or foreign person that has control, receipt, custody, disposal, or payment of any item of income of a foreign person that is subject to withholding … even if there is no requirement to withhold from a payment or even if another person has withheld the required amount from the payment."[4]

USWAs[5] and PFFIs[6] generally have withholding responsibilities, whereas Model 1 Reporting Financial Institutions ("RFIs") do not.[7] As of the December 1, 2014 IRS FFI List, there were: (a) 97,689 FFIs from 88 jurisdictions subject to a Model 1 IGA (*e.g.*, Cayman Islands hedge funds); (b) 17,075 from 13 jurisdictions subject to a Model 2 IGA (*e.g.*, Swiss custodians); and (c) 8,117 PFFIs from 118 jurisdictions not subject to an IGA (*e.g.*, Russian banks). USWAs (*e.g.*, brokers) are not required to register on that list.

The FFI Agreement also generally requires PFFIs to impose FATCA withholding on any withholdable payment made to a payee that is (or is presumed to be) a Non-Participating Financial Institution ("NPFI") with respect to an offshore obligation that is not an account. Withholding on foreign pass-through payments will not start before January 1, 2017, and the IRS guidance is required on that obligation.

Generally, Model 1 IGA FFIs – *e.g.*, Cayman Islands Reporting Financial Institutions – only have withholding responsibilities under Chapters 3 and 4 of the Internal Revenue Code ("IRC") if they elect to be either a qualified intermediary, a foreign withholding partnership, or a foreign withholding trust. A Model 1 IGA FFI will have withholding obligations if the IRS revokes its Global Intermediary Identification Number ("GIIN") for unresolved significant non-compliance.

Chapter 3 of the IRC imposes withholding tax on withholdable payments to "non-resident aliens."

Chapter 4 (*i.e.*, FATCA) also imposes withholding tax on account holders that are "recalcitrant" and NPFIs, and also on NPFIs that are payees of withholdable payments, even if they have no account with the payor. FATCA also extends the definition of withholding agent beyond US financial institutions, non-US Qualified Intermediaries, withholding foreign partnerships and withholding foreign trusts to include PFFIs.

A "withholdable payment" includes any payment of interest (including any original discount), dividends, rents, salaries, wages, premiums, annuities, compensations, remunerations, emoluments, and other fixed or determinable annual or periodical gains, profits, and income, if such payment is from sources within the United States. It also includes (from 2017 onwards) any gross proceeds from the sale or other disposition of any property of a type which can produce interest or dividends from sources within the United States.[8] This does not include income connected with US business. Unlike Chapter 3, FATCA does not provide an exemption for "portfolio interest." This means that FATCA withholding will apply to interest paid by US borrowers to foreign investors outside the US on non-bearer obligations and also on registered bearer bonds that are sold through financial institutions to foreign markets, provided that they are not held by a US citizen.

## The Presumptions

The account holder or other payee of any withholdable payment must provide the withholding agent with "valid documentation" before receiving any withholdable payment in order to avoid 30 percent FATCA withholding and/or reporting.

Any payee or account holder is presumed to be an entity unless it appears to be an individual based on the name or information on the customer file. The person is presumed to be a Specified US Person (*i.e.*, reportable) if there are *indicia* of US status. Conversely, a person presumed to be an entity with *indicia* of foreign status is generally presumed to be a foreign person and not a US person.

Any entity presumed to be foreign will also be presumed to be an NPFI. Similarly, the beneficial owner of an account held by an intermediary is presumed to be an NPFI. The last two presumptions explain why it is insufficient for a USWA or FFI to simply rely on the fact that an account holder appears on the IRS FFI List because the fact that an FFI has a GIIN does not confirm whether the FFI is the beneficial owner of payments from withholding agents or of financial accounts with other financial institutions, and if so, whether the FFI is assuming withholding responsibilities in respect of those beneficial owners.

The presumptions are set to expire on February 28, 2017. In the meantime, the payee can rebut the presumptions by providing valid documentation to the withholding agent or, if applicable, to the IRS.

## Withholding Certificates

"Valid documentation" means an IRS Form W-9 in the case of a US person (individual or entity),

and W-8BEN in the case of a non-US individual. A non-US person should use IRS Form W-8ECI if claiming that the US source income is effectively connected with the conduct of a trade or business in the US.

A non-US entity should use an IRS W-8BEN-E if it is the beneficial owner of the account/payment or W-8IMY if is not. If the entity certifies on the IRS W-8IMY that it does not have FATCA withholding responsibilities in respect of the beneficial owners of the account/payment, it must provide an "IMY allocation" showing the percentage interest of each beneficial owner together with each beneficial owner's withholding certificate.

If the entity confirms that it is a Passive Non-Financial Foreign Entity ("NFFE"), it will also be required to confirm whether it has any Substantial US Owners on its withholding certificate and provide withholding certificates in respect of each Substantial US Owner or – where the FFI is a Model 1 or Model 2 RFI – each Controlling Person. In addition to those withholding certificates, government identification documents are generally required in respect of each account holder, Beneficial Owner, and Substantial US Owner or Controlling Person.

## Unreliable Or Incorrect Documentation

There are detailed "reason to know" rules which invalidate withholding certificates and identification documents and treat them as unreliable or incorrect where a "reasonably prudent person in the position of the withholding agent would question the claim being made." This applies where the document does not reasonably establish the person's identity, is incomplete or inconsistent regarding the person's claim, or inconsistent with other account information. Examples include US *indicia* that have not been "cured" within 90 days of discovery and conflicting information on an entity's financial statements or organizational documents.[9]

## FATCA Presumptions Override Withholding Agent's Knowledge

Without valid documentation, a withholding agent must treat any entity payee as an NPFI and any individual payee as a Specified US Person or recalcitrant. Withholding agents must report these withholdings to the IRS on Forms 1042 and 1042-S.[10] FFIs must also report on any NPFI, Specified US Person and recalcitrant on IRS Form 8966[11] or its IGA equivalent.

A payee may rebut these presumptions by providing reliable documentation to the withholding agent or, if applicable, to the IRS. Without such documentation, the presumptions trump the withholding agent's knowledge or reason to know that the payee's FATCA classification or status is incorrect, if the presumption rules result in withholding a greater amount than would apply if the withholding agent relied on its knowledge or reason to know the payee has a different FATCA classification or status.

## Withholding Agent's Liability

A withholding agent will be liable to the IRS for tax, interest and penalties if it fails to report and withhold in

accordance with the presumptions. A withholding agent will not be liable to the payee if it withholds on the basis of presumptions even it is later established that the payee's presumed FATCA classification or status was incorrect.

## Compliance Program/International Tax Compliance Arrangements

At the 3rd Annual FATCA and Global Tax Compliance Forum, presenters from Goldman Sachs, Barclays Capital, BNY Mellon, UBS, Deutsche Bank, Brown Brothers Harriman and other major financial institutions emphasized the importance for USWAs and FFIs to have a written FATCA compliance program to document policies and procedures regarding FATCA due diligence, withholding and reporting obligations. In the Cayman Islands, this may be labeled "International Tax Compliance Arrangements" to reflect the broader scope of domestic regulations. Whatever label is used, it is clear that documented policies and procedures will be critical in the event of a regulatory audit. Withholding agents and FFIs must have "standardized processes and procedures for validating tax documentation" and for recording this information electronically. Client/customer records must be searched for any US *indicia* so that this can be cured where possible. Personnel responsible for client relations and onboarding should be trained to avoid giving tax advice to clients on FATCA classifications.

## On The Bucket List

USWAs and FFIs must create a "bucket list" for payees and account holders.[12] Someone, or more likely a team, at every USWA and FFI must sort every payee and account holder and, in the case of entities, Substantial US Owners, Controlling Persons and Beneficial Owners, into the correct bucket on that list in preparation for reporting. Bucket selection entails answering a series of questions, such as whether the payee/holder is US or foreign. If the payee/holder is US, is it specified, exempt or non-consenting? If the payee/holder is a foreign individual, are there any US *indicia*? If it is exempt, which one of 14 types is it?

If the payee/holder is a foreign entity, is it an FFI, NFFE or Exempt Beneficial Owner ("EBO"), such as a government entity or foreign investment entity owned by an EBO? If it is an FFI, does it have a GIIN? If it has a GIIN, is it the beneficial owner of the account? If it is not, does it have FATCA withholding responsibilities in respect of the beneficial owners?

If the holder fails to provide valid documentation supporting those classifications, the USWA or FFI must presume the holder is an NPFI or treated as recalcitrant. In either case, it is subject to withholding and reporting. FFIs (but not USWAs) must also report on Specified US Persons.

## The Bottom Line

Certain FFIs must establish additional buckets labeled "UK-IGA" and, by 2016, "CRS" in addition to their "FATCA" buckets. FFIs based in the United Kingdom's Crown Dependencies and Overseas Territories (*e.g.*, Channel Islands, Cayman Islands, British Virgin Islands, and Bermuda) were required to comply with the UK's IGA from July 1, 2014. By 2016, FFIs in those and dozens of other jurisdictions will also be subject to the OECD's Common Reporting

Standard. FATCA has indeed sown the seeds for an entirely new crop of international tax compliance.

## Endnotes

[1] IRS Notice 2013-43. Revised Timeline and Other Guidance Regarding the Implementation of FATCA. http://www.irs.gov/pub/irs-drop/n-13-43.pdf.

[2] Marcus Evans. 3rd Annual FATCA and Global Tax Compliance Forum. Navigating Tax Compliance and Standards through Sustainable Reporting and Withholding Strategies. http://www.marcusevans-conferences-northamerican.com/marcusevans-conferences-event-details.asp?EventID=21508.

[3] Rev. Proc. 2014-38. FFI Agreement for Participating FFI and Reporting Model 2 FFI, §4.03 Liability for Failure to Withhold. http://www.irs.gov/pub/irs-drop/rp-14-38.pdf.

[4] IRS guidance on "Withholding Agent." http://www.irs.gov/Individuals/International-Taxpayers/Withholding-Agent.

[5] US Treasury FATCA Regulations, §1.1471-2 as amended. Requirement to deduct and withhold tax on withholdable payments to certain FFIs.

[6] Rev. Proc. 2014-38. FFI Agreement for Participating FFI and Reporting Model 2 FFI, §4.01 Withholding Requirements. http://www.irs.gov/pub/irs-drop/rp-14-38.pdf.

[7] Model 1B IGA Non-Reciprocal, Preexisting TIEA or DTC, Article 4. June 6, 2014. http://www.treasury.gov/resource-center/tax-policy/treaties/Documents/FATCA-Nonreciprocal-Model-1B-Agreement-Preexisting-TIEA-or-DTC-6-6-14.pdf.

[8] IRC, §1473(1)(A).

[9] US Treasury FATCA Regulations, §1.1471-3(e)(4).

[10] Withholding Tax Returns.

[11] Form 8966 FATCA Report. http://www.irs.gov/pub/irs-pdf/f8966.pdf.

[12] The "bucket list" can be constructed from the Chapter 3 and Chapter 4 individual and entity classifications on the IRS Forms W-8 and W-9 and their accompanying instructions:

1042 – Annual Withholding Tax Return for US Source Income of Foreign Persons – *http://www.irs.gov/pub/irs-pdf/f1042.pdf*;

1042-S – Foreign Person's US Source Income Subject to Withholding – *http://www.irs.gov/pub/irs-df/f1042s.pdf*;

W-9 – Request for Taxpayer Identification Number and Certification – *http://www.irs.gov/pub/irs-pdf/fw9.pdf*;

W-8BEN – Certificate of Foreign Status of Beneficial Owner for United States Tax Withholding and Reporting (Individuals) – *http://www.irs.gov/pub/irs-pdf/fw8ben.pdf*;

W-8BENE – Certificate of Status of Beneficial Owner for United States Tax Withholding and Reporting (Entities) – *http://www.irs.gov/pub/irs-pdf/fw8bene.pdf*;

W-8IMY – Certificate of Foreign Intermediary, Foreign Flow-Through Entity, or Certain US Branches for United States Tax Withholding and Reporting – *http://www.irs.gov/pub/irs-pdf/fw8imy.pdf*;

W-8EXP – Certificate of Foreign Person's Claim That Income Is Effectively Connected With the Conduct of a Trade or Business in the United States – http://www.irs.gov/pub/irs-pdf/fw8eci.pdf;

W-8ECI – Certificate of Foreign Government or Other Foreign Organization for United States Tax Withholding and Reporting – http://www.irs.gov/pub/irs-pdf/fw8exp.pdf

## Topical News Briefing: Squaring The Fiscal Circle

by the Global Tax Weekly Editorial Team

The decision by the Japanese Government to further reduce corporate tax from April 2015 will leave the US decisively at the head of the OECD corporate tax league table, unless, of course the US Congress agrees on a rate-cutting tax reform plan in the near future – something which seems highly unlikely. However, it is debatable whether Japan's latest corporate tax cut will lead to the burst of entrepreneurial activity and economic growth that the Government is hoping for.

The scale of the tax reform plan finalized by the Liberal Democrat/Komeito coalition Government last month can hardly be described as ambitious. The 2.5 percent corporate tax cut will leave Japan with a rate of just over 32 percent in the 2015 fiscal year, and will be followed up with an additional reduction to 31.33 percent in 2016. By international comparison, this is still high; the average OECD corporate tax rate in 2013 was 25.5 percent. Other studies also hint at Japan's lack of competitiveness: the 2015 Paying Taxes report from PwC and the World Bank places Japan 122nd out of 189 countries in terms of how easy (or not) it is for a mid-sized company to discharge its tax obligations. In this respect Japan is being significantly outperformed by the US even given the latter country's increasingly complex tax code and growing calls for tax simplification. The study also concludes that an average company in Japan will pay 51.3 percent of its profits in income, labor, consumption and other taxes. The total tax rate for a comparable firm in the US is just under 44 percent – itself relatively high but substantially less than the rate in Japan.

The Government has pledged to eventually reduce corporate tax below 30 percent so as to make Japan more internationally competitive. However, given the fairly aggressive corporate tax cuts in many countries over the last few years, it is difficult to envisage the latest reforms making much of a difference. Indeed, the tax cut is packaged together with a restriction on the amount of losses companies can offset, which could see many firms facing a tax rise rather than a tax cut. Given Japan's dire fiscal position – public debt almost two-and-a-half times the size of the economy and rising – it is no surprise that a supposed tax cut could actually turn out to be a tax hike.

On the other hand, perhaps the Abe Government deserves some credit for beginning to address some of the root causes of Japan's lack of competitiveness. Worryingly though, two other statistics indicate just how tough it will be to balance the books: the overall tax burden is around 28 percent, but the Government is spending 42 percent of GDP. In the absence of spending cuts, the equation will only add up through additional taxation, and lots of it.

## Lackluster Tools For International Collection: An Explanation For Why Things Go 'Bump' In The Night?

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

The United States has entered into income tax treaties with several countries that provide for the exchange of information.[1] But only "five treaties provide for assistance in collecting tax judgments against US citizens living abroad."[2] Those are with the following countries: Canada, France, Holland, Denmark, and Sweden.[3]

Let me explain to you what I mean by "collection of tax judgments." Specifically, I'm referring to the ability of the *United States* to collect tax claims against its *own* citizens who happen to be living in one of these five countries.[4] Because these treaties are bilateral, the reverse is also true: partner countries may collect tax claims against their own citizens who happen to be living in the United States.[5]

To avoid any unnecessary confusion, an important distinction must be made. As expansive as these treaties may be, they do not provide a mechanism for the *foreign government* to collect foreign taxes owed by US citizens.[6] For example, France cannot rely on the US–French Treaty to collect French taxes from a dual French-American citizen, even if that person happens to live in Bordeaux and enjoys feasting on some of the world's most expensive and prestigious wines.

Very simply, the present treaty policy of the United States is to "disallow the collection of foreign debts or foreign tax judgments against US citizens."[7]

How does the collection of tax judgments with countries that the US has collection treaties with work? By the terms of the treaties, such claims:

> "may be accepted for enforcement by the other State and collected in that State in accordance with the laws applicable to the enforcement and collection of its own taxes. The State to which application is made shall not be required to enforce executory measures for which there is no provision in the law of the State making the application."[8]

Consider the following example. Pierre is a dual citizen of the US and Canada who presently resides in Montreal. He has fastidiously filed US and Canadian tax returns for the last ten years. Following an audit of his 2012 US tax return, the IRS determined that there was a USD20,000 deficiency and mailed him a notice of deficiency. Pierre timely filed a

protest but Appeals found in favor of the IRS. Having failed to file a petition with the tax court, that deficiency soon became a USD20,000 assessment.

The IRS now seeks to collect on its claim by imposing a tax lien on real estate owned by Pierre in Canada. Essentially, what the US Government is attempting to do is cajole collection officials from the Canadian Revenue Agency (L'Agence du revenue du Canada) to do its dirty work for it: namely, to collect Pierre's unpaid US taxes by enforcing an IRS tax lien on property located within Canada.

As incredible as this might sound, reliance upon a foreign taxing authority for assistance in collecting a tax judgment against a citizen of the requesting country is entirely permissible under the terms of the US–Canadian Treaty. Of course, such a request must be accompanied by documents firmly establishing that the taxes have been finally determined.[9]

Therefore, the Canadian Revenue Agency would have no choice but to enforce the lien and to collect the unpaid taxes. But what if Pierre filed a motion in a Canadian court to have the tax lien imposed by the Canadian Revenue Agency, at the behest of the IRS, set aside? Not surprisingly, the court would refuse Pierre's request on the grounds that the imposition of the tax lien was proper under the terms of the treaty.

Believe it or not, a similar case actually exists, but with an ironic twist: the facts are the mirror opposite to those presented in this hypothetical. There are three key differences. First, the taxpayer lived in the United States, and not in Canada. Second, it was the Canadian Government, and not the US Government, that sought to impose a tax lien on the taxpayer's property. And third, the property was located in the United States.

At the behest of the Canadian Revenue Agency, the IRS imposed a tax lien on property belonging to the taxpayer in New York. The taxpayer filed a motion in the federal court for the Southern District of New York to have the tax lien set aside.[10] The court refused to interfere with the tax lien, finding that it was appropriate under the terms of the US–Canada treaty.[11]

With such a modest number of partner countries that the US can rely upon for bilateral assistance and support in collecting tax, does that mean that delinquent taxpayers can avoid collection altogether simply by moving themselves and their money to one of the other 190 countries in which the US has no collection treaties?

In other words, are there any tools available to international revenue officers to collect taxes from US persons who have conveniently "parked themselves and their assets" beyond "the reach" of the IRS?[12] While such tools do exist, they are few and far between.

If you think that it is as simple as the IRS filing a notice of federal tax lien with the foreign taxing authority, as is typical in a domestic collections

case, or using foreign courts to collect US taxes, you would be sadly mistaken. These collection devices are useless when it comes to the cross-border collection of taxes.

So if the regular, run-of-the-mill domestic collection techniques are off limits, what techniques can it use? One technique that has been getting a lot of attention lately – not to mention gathering up steam – is the "Customs Hold," in which I have firsthand experience. This consists of detaining delinquent taxpayers at the border, not unlike an ICE detainer.[13]

Let me share with you a story. On a weeknight not too long ago, I was just getting back from a late-night walk with Bella, my two-month old Labrador who has not slept a full night since arriving at her new home back in October (that's a story for another day). After putting Bella in her cage, I crawled back into bed.

Just then, my cell phone started ringing (not unusual even for the late hour considering the fact that many of my clients live abroad). I picked it up. Almost immediately, I could hear heavy breathing on the other end. The caller was speaking very fast and stumbling all over his words.

I might have hung up the phone and blamed it on a "prank caller" if I didn't recognize the voice on the other end. It was "Joe," my client. But he was not calling for reasons you might expect. No, Joe had not just been arrested for a DWI and in dire need of legal advice (although I've had many such calls). Instead, Joe was at a major metropolitan airport being detained by a Customs and Border Patrol Agent in a tiny room off in the corner. Upon investigating, I learned who was behind this: none other than the IRS. Under what authority? A two-year-old program designed to prevent any US person who has an unresolved collection issue with the IRS from either entering or leaving the United States.

Very simply, Joe owed Uncle Sam money, and Uncle Sam wanted to collect it.

Before discussing how the program works, some background information is necessary. The program relies upon the sharing of information between two governmental agencies: the Department of Homeland Security (DHS) and the IRS.

IRS revenue officers have access to the Treasury Enforcement and Communications System, or TECS for short. TECS is a computer system that is maintained by the DHS and which provides access to a number of proprietary databases, including: (1) Federal, national, state, and local law enforcement agencies; (2) the FBI's National Crime Information Center (NCIC), Financial Intelligence Branch (FIB); and (3) the National Law Enforcement Telecommunication Systems (NLETS).

TECS is used extensively by the law enforcement community. Indeed, it gives a new meaning to the phrase, "Uncle Sam is watching you!"

How would a delinquent taxpayer like Joe get ensnared in something as thorny as this? Remarkably, the procedure for detaining such taxpayers is so simple that it could happen to virtually anyone. First, the revenue officer prepares Form 6668, TECS Entry Request, to have a Customs Hold placed on a delinquent taxpayer.[14] The completed form is sent to the group manager for approval, which consists of nothing more than a signature.[15]

After signing it, the group manager emails it to the TECS Coordinator.[16] The TECS Coordinator adds the taxpayer's name into TECS. Finally, DHS notifies the IRS whenever the taxpayer attempts to re-enter the United States.[17]

Is there any procedure for notifying delinquent taxpayers of the Customs Hold? As a matter of fact, there is. Taxpayers are informed with a Letter 4106, *Letter Advising Taxpayer of Department of Homeland Security Notification*, that an international revenue officer has notified the DHS "that the taxpayer has outstanding tax liabilities."[18]

What happens when a taxpayer whose name is in the TECS database attempts to re-enter the United States? Joe's story provides the hint. It allows for brief detainment of the person by a Customs and Border Protection Officer for the purpose of gathering his or her "contact information" (*i.e.*, "where he will be staying while in the United States").[19] Nothing more. Nothing less.

In other words, while it is supposed to be a tool for collecting taxes from delinquent taxpayers, it offers no ironclad guarantee that the person being detained will actually pay the tax. And therein lies the problem. Holding individuals as they seek to return to the United States only works as a collection device if the experience itself was so emotionally traumatic as to convince them to pay. At a primitive level, it only works if it instills the fear of God in the taxpayer.

While it might potentially cause the person some alarm, it's hard to imagine that it will have the desired effect of inspiring taxpayers to take out their checkbooks and write out a check to Uncle Sam. And before we can even get to that point, do not forget that the person has to attempt to re-enter the United States. Suffice to say, it would be a cold day in hell before someone who receives Letter 4106 steps foot back in the United States again.

For those wondering what impact being detained at the airport by a border patrol agent had on poor 'ole Joe, you may be surprised to learn that Joe did not waste any time in paying his tax bill. In fact, he mailed the check the very next day. Thus, detainment had the same effect on Joe that the IRS hopes it will have on all delinquent taxpayers.

No discussion of this program would be complete without some statistics. According to recent statistics, there are approximately 1,700 taxpayers on the TECS with approximately USD1.6bn in delinquent tax assessments.[20] This includes assessments

of approximately USD1.1bn exclusively owed by international taxpayers.[21] Unfortunately, there are no statistics citing how many taxpayers who are actually detained later wind up paying their tax bill.

An additional remedy allowing for detention of a taxpayer in a civil case is called the "*Writ Ne Exeat Republica*." Don't let the Latin root scare you. It is nothing more than a "labor-intensive option" that allows the IRS "to stop a taxpayer from leaving the country with their money."[22] According to the Internal Revenue Manual, such a writ is appropriate when the taxpayer: "[1] is about to leave the US, [2] is unlikely to return to the US, and [3] has conveyed or concealed the property so that [it] may be taken out of the US."

As demonstrated above, the only collection tools that are at the IRS's disposal – reliance on delinquent taxpayers "living in one of five countries" or "trying to catch individuals one by one as they attempt to re-enter the country"[23] – are woefully inadequate. Indeed, these tools pale in comparison with the rights enjoyed by those living in the twenty-first century to freely move both themselves and their assets anywhere in the world.

If the Treasury truly means what it says about repatriating money offshore back to the United States, then I agree with the position taken by Mr. Fogg in his article, "International Collection Efforts by the IRS – Expanding the Number of Treaties in which We Have Collection Language": it must pursue collection efforts with the same vigor that it uses to track down money stashed in offshore tax havens.[24] It can begin by expanding the list of countries with which the United States has collection treaties beyond just five. Very simply, collection language – similar to that which already appears in the United States' other collection treaties – must be added to pre-existing treaties and any subsequent treaties that the United States enters into. Otherwise, the IRS will continue to fight a losing battle "to those who have parked themselves and their assets beyond their reach."[25]

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[13] ICE Detainers, Frequently Asked Questions (ICE detainers are used to identify and ultimately remove aliens who are currently in federal, state or local custody. ICE relies on the cooperation of state and local law enforcement partners in this effort), available at http://www.ice.gov/factsheets/detainer-faq.

[14] *See* Note 12, *supra*, at p. 2.

[15] *Id*., *supra*.

[16] *Id*., *supra*.

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[18] *Id*., *supra*.

[19] *Id*., *supra*.

[20] *Id*., *supra*.

[21] *Id*., *supra*.

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# High Time For Special Penalty Regime For Malaysia Transfer Pricing

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## Introduction

Ever since the corporate tax self-assessment system was implemented in Malaysia early last decade, tax audits have been a permanent feature of compliance-checking by the tax authorities. A self-assessment system means that the onus is on taxpayers to be compliant with tax regulations, report the correct amount of tax, and pay the said amount when it is due. As the responsibility to comply with tax regulations is placed in the hands of taxpayers, a critical feature of the system is the imposition of penalties when an audit adjustment is made.

A transfer pricing audit is no different to a tax audit in this context. Prevailing tax laws and regulations in Malaysia do not distinguish between transfer pricing audits and other tax audits conducted by the Inland Revenue Board (IRB). Hence, in a transfer pricing audit, when there are tax adjustments, penalties are imposed.

## The Penalty

According to the Transfer Pricing Guidelines 2012 issued by the IRB, tax adjustments as a result of a transfer pricing audit are subject to penalty under Section 113(2) of the Income Tax Act. A check

of the Income Tax Act reveals that Section 113(2) states that if there is tax undercharged as a result of understatement of income or incorrect information furnished in tax returns, then the Director General may require that a penalty equal to the amount of tax that has been undercharged is added to the tax adjustment. Thus, in a transfer pricing audit, a taxpayer can be hit with penalties up to the same amount as the tax adjustment itself.

The interesting part of the Section mentioned is the link made between the tax undercharged and the understatement of income through furnishing incorrect information in tax returns. Bearing in mind that this is the applicable penalty section for a transfer pricing audit, it is intriguing that this section directly links transfer pricing with understatement of income and incorrect information furnished in tax returns. From a tax practitioner's perspective, transfer pricing can be many things and can be applied in many ways in the workings of multinationals, but it can hardly be construed that transfer pricing is directly related to understatement of income in the same sense as it is applied in a broader tax context.

So is it appropriate to impose penalties under Section 113(2) in transfer pricing audit cases?

## The Argument

In Malaysia's first transfer pricing case, *MM Sdn. Bhd*. before the Special Commissioners of Income Tax, one of the rulings made by the Special Commissioners (referenced from the OECD Guidelines) was: transfer pricing is not an exact science. In this context, transfer pricing cannot then be taken to be a subject matter which is defined by certainties and absolutes. Thus, how does one connect a subject matter that is not surrounded in absolutes and certainties to something as direct as understatement of income or furnishing of an incorrect return?

It is on this point that this article seeks to drive home the notion that the transfer pricing audit needs to be considered in a different light to other tax audits; it needs to be classified as a special provision on its own. If there needs to be new provisions passed for this to take effect, then new provisions should be put in place to ensure that MNCs are able to conduct their transactions and expand their businesses globally, making their best efforts to determine an arm's length price, without being unduly penalized if the tax authority takes a different view in an audit.

Perhaps in order to see that transfer pricing is in principle a neutral concept, it can be likened to accounting. In many ways, these subjects are similar. In many ways too, these subjects can be used as a tool to achieve certain objectives. It is true that transfer pricing can be used as a tool to structure transactions in a way to reduce taxes in certain jurisdictions. This is no way different from how accounting can be misused to overstate income and assets, for instance. There are many infamous examples of this – the demise of the global accounting firm Arthur Andersen in the Enron fiasco comes to mind. Few would, though, at the outset consider accounting as a means of achieving ulterior motives. Just like accounting, a company can, in planning and implementing transfer pricing systems, adopt certain "standards" – much similar to accounting standards. These standards, in transfer pricing terms, are known as methodologies. These methodologies are the tools used to determine the arm's length price or profits in a particular transaction. As long as companies conduct proper analysis and adopt proper parameters to arrive at the determined arm's length price or profits, it does not seem right to argue that the company has not done its best to adopt a certain standard and apply it. This has much been affirmed by the Special Commissioners in *MM Sdn. Bhd.*, when they ruled that the taxpayer's comparable reports and expert evidence offered by the taxpayer were reliable in establishing that the taxpayer's pricing methodology was acceptable.

This is where the importance of preparing contemporaneous documentation comes into the picture. In the context of tax audits, the IRB's view is very much guided by the board's own Malaysian Transfer Pricing Guidelines 2012. In the guidelines, the section on penalties indicates the following:

- No contemporaneous transfer pricing documentation; 35 percent
- Transfer pricing documentation prepared not according to the Guidelines; 25 percent

The above means that if a taxpayer takes the proactive step to prepare contemporaneous transfer pricing documentation and takes further steps to ensure that the documentation is prepared according to the Guidelines, there is very high chance that the taxpayer can escape any imposition of penalties in the event of tax adjustments during the transfer pricing audit. Thus, the value of preparing transfer pricing documentation is clearly evident – and not just preparing it, but also preparing it according to the Guidelines. If the taxpayer takes the proactive step to prepare the documentation contemporaneously and prepare it according to the Guidelines, at the very least, the taxpayer can rely on this penalty provision in the Guidelines that a direct 35 percent penalty will be avoided in the event of tax adjustments.

The decision of the Special Commissioners of Income Tax in *MM Sdn. Bhd.* can also be reflected as evidence on the importance of documentation as a strong defense mechanism of the taxpayer's transfer pricing positions, wherein the Special Commissioners ruled that MM Sdn. Bhd.'s comparable reports and expert evidence were reliable in establishing that the taxpayer's transfer pricing position was acceptable.

## The Conclusion

Transfer pricing is not an elaborate scheme to understate income or taxes – though some companies may use transfer pricing structures as a means to achieve such objective. Transfer pricing is a neutral subject matter which should be considered in a neutral light on the outset by tax authorities. This is especially so for a transfer pricing audit: simply because some companies use transfer pricing to achieve an ulterior motive, this does not and should not make all companies applying transfer pricing guilty of evading or understating taxes.

Hence the Malaysian tax authorities should reconsider the application of penalties under Section 113(2) for transfer pricing cases. The authorities should consider whether application of penalties at all is just, and if it is, it may very well be high time that a special penalty provision for transfer pricing is introduced.

# At The Intersection Of International Tax And Technology

by Channing Flynn, Stephen Bates and Jess Martin, Ernst &Young LLP, US

## Wishing In A New Year Of Consensus

2014 was an active and challenging year in the global technology sector. The velocity of change and innovation in the digital economy has put increasing strain on existing international tax norms. Individual nations have been hard-pressed to keep up with globalizing business models in borderless clouds – even while seeking new (potentially digital) sources of tax revenue.

All that said, there may be cause for optimism – albeit cautious, patient optimism – in 2015. For despite all the political grandstanding and media headlines running in the foreground, 2014 was also about something entirely different. Running in the background, throughout the year, was an increasingly collaborative effort at deep analysis and assiduous consensus-building among policymakers and multinational companies worldwide – all intent on ensuring a workable global tax framework for the 21st century.

Some of the pessimism of early 2014 has, in fact, already receded. Policymakers and corporate tax professionals from around the world have found common ground on at least some of the difficult digital tax questions that have arisen. They have often worked collaboratively, reached compromises and made decisions in what is, after all, an inherently contentious field of endeavor – one in which skeptics had initially predicted nothing more than unending deliberation, if not chaos.

There are, of course, cautionary notes. Differences remain to be resolved in many areas. And, as exemplified by the December 3 UK Autumn Statement on 2015 tax policy, instances of unilateral action to increase taxation on technology companies still threaten to dampen optimism.

With 2014 having come to a close, though, 2015 is opening on a higher note. In an environment of growing consensus, one can see a glimmer of tax certainty at the end of the tunnel of digital tax policy deliberation – but at a cost that is as yet uncertain.

## Recapping The Highlights And Lowlights

Over the course of the past year, we have taken the pulse of domestic, regional and international taxation in the technology sector, in our regular *Global Tax Weekly* column. This edition recaps some of

2014's highlights and lowlights, on matters ranging from the location of profits in global cloud computing environments, to the taxation of cross-border mobile apps, to R&D incentives, to early discussions on such forward-looking matters as the treatment of virtual currencies.

## Consensus Sets The Stage For The Year To Come

Perhaps the single most important consensus in 2014 addressed the broad question of how to tax the new digital economy. This topic was, in fact, taken up as Action 1 by the Organisation for Economic Co-operation and Development (OECD) in updating the current global tax framework through its far-reaching Base Erosion and Profit Shifting (BEPS) initiative. The key question posed by the OECD in March 2014 was "whether it is possible to ring-fence the digital economy from the rest of the economy, and if not, whether specific types of digital transactions could be identified and addressed through specific rules."

The answer came six months later, following private sector input, public consultation and further deliberation among governments. The global digital economy *is* the economy; it cannot be treated differently for tax purposes, concluded the final report on BEPS Action 1: Address the Tax Challenges of the Digital Economy.

The OECD's consensus-building process succeeded in moving some countries off earlier positions favoring internet-specific tax legislation, according to Pascal Saint-Amans, Director of the OECD's Centre for Tax Policy and Administration. Speaking at EY's 33rd Annual International Tax Conference in October 2014,[1] Saint-Amans declared the overall BEPS Action Plan halfway completed, with seven of 15 deliverables published. Others are in draft form. He promised completion in 2015.

Still, some of the thorniest international digital tax issues remain unresolved. Permanent establishment, transfer pricing of intangibles and value-added tax (VAT) on digital business-to-consumer transactions are among those matters now delegated to various BEPS working groups for resolution in the coming year.

## Timing Is Of The Essence In Many Countries

At the local country level – at least in the near term – complexity may only be increasing for some international tax practitioners, as a growing number of national tax authorities get out ahead of the OECD with their own new policies.

Coherence is a tall order for the global tax landscape, considering its nearly 200 sovereign nations and 3,000 existing bilateral tax agreements. Yet the OECD points to a public policy commitment by 90 percent of the world's economy (G20 plus OECD nations) to the BEPS project it began in 2012. Strong endorsement of the work at the G20 Summit in November 2014 underscores that commitment. (Work is underway with developing countries to achieve something closer to 100 percent as well.)

Over the past year or so, some individual governments (Australia, Canada, Mexico and Spain among them) have invoked the BEPS "brand" in passing new national tax policies and instituting enforcement practices that may need to be further rationalized once the global framework is finalized. To that end, some of these countries have included what we call "BEPS provisos" in their legislation.

As 2014 came to a close, the UK Chancellor released details of a "diverted profits tax," which is intended to apply to those large multinational enterprises that conduct business activities in the UK and that enter into "contrived" arrangements to divert profits from the UK. The proposal represents a new approach to a problem the OECD has been grappling with in its BEPS initiative. If adopted, it would set a penalty rate of 25 percent of diverted profits relating to UK activity.

Other countries (notably, the US) have suffered political gridlock on tax legislation. And yet others (such as the Netherlands) say they will await the OECD's final framework. For its part, the OECD expresses cautious optimism about a convergence – not further fragmentation – of national tax policies over time.

## BEPS Is Only One (Big) Piece Of The Tax Puzzle

Beyond BEPS, today's growing spirit of consensus has helped produce compromises over controversies specific to individual countries as well. Ireland recently closed a tax residency loophole that some of its peers claimed to be enabling profit-shifting.[2] The UK agreed in November to modify its patent box incentives for R&D in a compromise with Germany[3] and in December published further patent box policy changes to be finalized in 2016.

Sometimes, consensus has then served as a stepping stone to the next issue. For example, 2014 saw companies located in the EU bringing their arrangements for electronic services VAT in line with a new EU rule based on the country of consumption rather than supply (effective January 2015). Recently, the digital VAT debate in Europe has been moving on to virtual currencies, with the EU being asked to provide guidance on related transactions.

Often in 2014, change came in fits and starts. In our July column, for example, we reported Japan's plans for a cross-border digital sales tax that has since been delayed amid national economic and political change.[4] Meanwhile neighboring South Korea has proposed a tax on sales of mobile apps made by vendors located overseas.[5]

Many technology companies are fielding good news/bad news tax policy developments. For instance, the UK Government promised more generous tax credits for R&D even as it announced it would reduce patent box incentives. Spain unveiled reductions in the overall corporate tax rate even as it focused more intently on ensuring taxation of digital goods and services.

## Considerations

Writing regularly for *Global Tax Weekly*, we will continue to discuss the business and technology impact

of changes like these and so many more through 2015. In that vein, look for further information about the news we touched on above, regarding the UK's December tax proposals, in our next column for *Global Tax Weekly*; meanwhile, our initial summary is available as an EY Global Tax Alert.[6]

What will the next tax year bring? Only the most intrepid would dare predict, with no letup expected in the pace of global digital business innovation.

What is clear is that the volume of work still to be done on the OECD BEPS Action Plan is significant. And while BEPS is a focal point, it did not monopolize the international technology tax stage in 2014 – and nor will it in 2015. Important digital tax questions will continue to trigger policy debates and trial balloons in many fora. Also in 2015, recent changes and policy evolutions such as those in Australia, Ireland and the UK will require significant attention from multinational technology companies.

All of this serves to underscore change as a constant in the digital economy. Tax uncertainty will always be a matter of degree. But signs point to a more positive start to 2015, if today's spirit of consensus holds. Light is glimmering at the end of the BEPS tunnel, as consensus promises greater clarity and coherence – less uncertainty and controversy – for the long run.

Throughout our work, we often see tax departments struggling to deploy the people, processes and technologies needed to adapt and thrive in these uncertain times. Others look to wait out the debate. And who could blame them, given what could be a three-year lag before widespread adoption of national laws embodying the final BEPS framework?[7]

Yet, waiting for every "t" to be crossed, every "i" to be dotted, in every jurisdiction, is simply not a good strategy. Global tax policy consensus has a clear value for tax practitioners: it gives a sense of direction and of the rules to come. 2015 is not only, therefore, a year to be vigilant, but also a year to anticipate and prepare for a new tax environment for the digital economy.

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## Endnotes

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## Topical News Briefing: A Game With No Winners

by the Global Tax Weekly Editorial Team

When is a tax break illegal? When the EU says so, might be one answer.

The European Commission is fairly vigorous when it comes to upholding the principles underpinning Europe's economic union, especially in the area of taxation, and in the last few years it has systematically targeted tax measures it thinks distort economic activity in the Single Market. The EU is also active in defense of the cause of free trade, and regularly takes non-EU countries to task *via* the World Trade Organization's (WTO's) dispute mechanism for breaking international trade rules; the EU has been the complainant in 94 trade disputes since the inception of the WTO in 1994, second only to the US.

It could be argued, however, that the EU's trade policy isn't motivated entirely by a sense of idealism; economic self-interest and politics are two reasons why the EU tends to pick and choose its trade fights. And in that it is by no means alone.

The latest round of the decade-long trade row between the EU and the US regarding state support for aircraft manufacturers Airbus and Boeing could be considered one such example. These two companies now supply the vast bulk of the world's civilian aviation fleet, and competition between them is intense. Given the direct and indirect impact these two companies have on their local economies in terms of jobs and consumer spending, it is not surprising that the authorities in Europe and America are anxious that they remain successful. But developing new aircraft is a very expensive and risky business in this cut-throat environment, and no local politician wants to see such high value manufacturing vanish on his or her watch. Hence state support is seen as vital to encourage these companies to invest.

So the EU could be accused of being somewhat hypocritical by challenging the tax incentives renewed by Washington State last year, offered in the hope that Boeing will develop the latest iteration of the 777 airliner in the state, when Airbus has benefited from subsidies to the tune of billions of euro over the past two decades (subsidies it claims to have paid back with interest). It is also noticeable, looking through the list of trade disputes initiated by the EU since 1994, that it hasn't challenged tax incentives granted by other US states to encourage large employers to move there or stay put, as the case may be.

Does the EU even have a case? According to Article 1 of the Agreement on Subsidies and Countervailing Measures, which states that a subsidy is deemed to exist if government revenue that is otherwise due is foregone or not collected, it sounds like it does. But then surely every tax incentive in the world could be challenged under this criterion, and it would probably be equally possible to argue, in

what is a very complex field of litigation, the other way. Indeed, there hardly ever seems to be a clear-cut winner in international trade disputes, and the ten-year history of the Boeing-Airbus wrangle suggests there won't be a winner here either, at least not for a long time.

## United States Taxation Of Income From International Shipping – Compliance By Taxpayers

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*This is the seventh article 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 corporations that receive such income.*

The first six articles in this series have described the tax that applies to foreign entities[1] that earn US source gross transportation income (USSGTI), the distinction between taxable income and income that can be excluded from tax, and the exemptions that are available to avoid paying tax.

This article begins a discussion of the compliance obligations of corporations that earn USSGTI. There is one simple rule to start with: if a corporation earns USSGTI in any tax year, it must file a US tax return for that tax year, using Form 1120-F. There are no exceptions even if the corporation is exempt from tax. Thus, there are going to be corporations that must pay tax, those that qualify for exemption by reason of a tax treaty, and those that qualify for exclusion under Section 883. We will discuss the compliance obligations of each group in turn. Only those paying tax will be covered in this article.

Article 3 in the series described what the Internal Revenue Service has determined is to be included in "transportation income" subject to the 4 percent tax under Section 887. For those paying the tax, Revenue Procedure 91-12 [1991-1 CB 473, February 11, 1991] applies.

As a general rule, taxpayers report hire in the tax year in which it is earned. Bareboat and time charter hire is earned for each day of a voyage. Accordingly, calculation of the hire subject to tax is relatively straightforward and can be done upon completion of each voyage.

Freight hire, on the other hand, is not fully earned until the cargo is discharged. Thus, it is only reported upon the conclusion of the voyage. It should be remembered that Rev. Proc 91-12 includes demurrage, deadfreight and dispatch in the definition of transportation income. As a result, tax is due on those amounts, if there are any, associated with the voyage. As a practical matter, the net amount of these additional items is not usually agreed and paid by charterers until sometime after a voyage is

completed. Thus, payment of the tax on these additional items of income should only be made in the tax period in which the amount has been paid by charterers.

Examples will illustrate the differences. Company A owns a vessel that called at a US port once during 2014 while on time charter. The vessel commenced loading at a foreign port at 12:00 GMT on July 1, 2014 and completed discharge at a US port at 18:00 GMT on July 31, 2014. The gross daily hire per the charter party was USD10,000. Upon completion of discharge, Company A can calculate the tax due for the voyage to the penny. The vessel was engaged on a laden voyage to the US for 30.25 days, during which it earned USD10,000 per day, for a total of USD302,500, only 50 percent of which is USSGTI, in which case Company A pays tax on USD151,250. Four percent of that amount is USD6,050. If Company A was the disponent owner of the vessel which it had taken from Company B for a bareboat hire of USD2,000 per day, Company B would use the same day calculation and pay tax on a gross daily rate of USD2,000, resulting in a tax due of USD1,210 (30.25 days × USD2,000 = USD60,500 ÷ 2 = USD30,250 × 0.04 = USD1,210).[2]

Company C owns a vessel that called at a US port on a voyage basis for which it earned gross freight of USD950,000. The voyage commenced on November 21, 2013 but did not complete by the end of that calendar year. The vessel discharged its cargo on January 22, 2014. On September 6, 2014, the charterers and owners agree on a demurrage charge of USD175,000 which was paid to owners ten days later. Assuming Company C's vessel did not call at the US at any other time during 2013 or 2014 except for this one voyage, it has no tax filing obligation for 2013, but will be liable for tax on 50 percent of USD950,000 plus USD175,000 in 2014, a total of USD562,500 or a tax of USD22,500.

If Company C was the disponent owner of the vessel which it had taken from Company D on a bareboat basis at USD2,000 per day, Company D would pay tax based on the bareboat hire it earned during the voyage irrespective of the fact that Company C was earning freight and would not pay tax on the basis of the days of the voyage. Thus, Company D would calculate its tax based on the days engaged on the voyage from commencement of loading on November 21, 2013 to the completion of discharge on January 22, 2014, using the same calculation as Company B in the previous example.

Foreign corporations that must pay the tax are required to make estimated tax payments during the tax year. The US uses a pay as you go tax system. That is, just like ordinary taxpayers who have their income tax deducted at source from their paychecks, corporations must pay tax during the tax year. Obviously, most corporations will not be able to calculate their final tax bill until after the close of the tax year, but the Internal Revenue Code (IRC) requires them to make "estimated tax payments" during each tax year.[3]

For the three companies described above, "estimated" is a misnomer. As illustrated above, they can readily calculate their tax liability. The IRC requires that estimated tax payments be made by the 15th day following the end of the 3rd, 5th, 8th, and 11th months of a corporation's tax year. For calendar year taxpayers, that translates into payments in April, June, September and December. Tax on USSGTI earned in the last month of the year can be paid with the tax return.

In the case of Company A, which earned all of its USSGTI for 2014 during a voyage that lasted from July 1 to July 31, 2014, it should have paid the tax due on or before September 15, 2014. The same is true for Company B. For Company C, its first quarterly tax payment for 2014 was due on or before April 15 (for the freight earned on the voyage that completed on January 22, 2014). The tax due on the demurrage that was paid in September should have been paid on or before December 15, 2014. Company D should have made its first estimated tax payment on December 15, 2013 for the hire earned between November 21 and November 30, 2013 and then should have paid the balance of the tax due on the hire earned from December 1 to December 31, 2013 with its Form 1120-F for the tax year 2013. It should have paid the tax due on the hire earned from January 1 until January 22, 2014 on April 15, 2014.

Taxes can only be paid by same day wire[4] or, more conveniently, through the Electronic Federal Tax Payment System (EFTPS). As the name suggests, EFTPS permits the electronic payment of estimated taxes. EFTPS records payments when made and offers prompt confirmation of payment. It is the surest and safest way to ensure that payments are made on time, are correctly credited to the taxpayer's tax account, and are applied to the correct tax period.

The final compliance step involves the filing of Form 1120-F. For those corporations filing on a calendar year basis, the return is due on or before June 15 in the year following the end of the calendar year. Any tax that may be due for USSGTI earned in the final month of the year can be paid when the return is filed. The Form 1120-F essentially reconciles the tax payments made during the year with the total USSGTI earned in the year. The balance of tax due, if any, is shown on the return and is usually paid *via* EFTPS. A taxpayer must include a Schedule V with its Form 1120-F. Schedule V requires the taxpayer to report the name and IMO number of the vessel that earned USSGTI and the name of every charterer that paid USSGTI to the taxpayer along with the amount of USSGTI paid.

A taxpayer can obtain a six-month extension to file the Form 1120-F as long as it pays any tax due and files an extension request on Form 7004 on or before the June 15 deadline. An extension request, even if filed on time, is not valid unless the full amount of tax due is paid by the filing deadline.

## Endnotes

1 USSGTI flows up to the first regarded entity (usually a corporation) in the ownership structure (see the

sixth article in this series, in *Global Tax Weekly*, No. 110, December 18, 2014). Thus, it is more likely than not that the tax return filer will be a corporation and will use the Form 1120-F, US Income Tax Return of a Foreign Corporation. We will refer to the tax return filers as corporations from here on in.

2 The tax under Section 887 is a gross tax. As a result, Company A cannot deduct the bareboat hire paid to Company B from its USSGTI. It must pay tax on the gross amount of the hire received.

3 The rules governing estimated quarterly tax payments are very complex because almost all taxpayers are subject to tax on their "net" income. Taxpayers subject to Section 887 pay tax on a gross basis, which essentially eliminates the complexity.

4 *See* http://www.irs.gov/uac/Electronic-Payment-Options-Home-Page for information on such payments

## Italy Introduces Patent Box

As a means of encouraging the development of intellectual property (IP) in Italy, rather than elsewhere, a "patent box" preferential tax regime has been introduced with effect from January 1, 2015, at the same time as a restructuring of the country's research and development (R&D) tax credit system.

Following the recent parliamentary approval and gazetting of Italy's 2015 Stability (Budget) Law, and on similar lines to the incentives granted in other EU countries, the new patent box regime, covering income derived from the use or licensing of qualifying intangible assets (such as patents, trademarks, processes, and other IP), is linked to R&D activities carried out in the country.

Under the scheme, businesses are able, at their option, to exclude 50 percent of their income derived from such assets from income taxes (either corporate or individual) and the regional tax on production. Foreign residents can also exercise the option in Italy, as long as they are resident in a country which has a double taxation agreement with Italy, and with which there is an "effective" exchange of tax information.

Once taken, the option is irrevocable and has a duration of five years. For the first two years of its operation, the income exclusion will amount to 30 percent (in 2015) and 40 percent (in 2016), reaching 50 percent only in 2017, when (on the present corporate tax rate) the effective tax rate on such intangibles will be 13.75 percent.

The income on which the tax exemption is applied is to be calculated proportionally to the R&D activities actually performed by a taxpayer, while it has also been foreseen that, where the assets are used within a business or in a related business, there will also need to be a system of rulings by the Italian Revenue Agency to ascertain the relevant applicable income.

The legislation establishes that the profit derived by a business from the sale of the intangibles will be free of tax, on condition that at least 90 percent of the proceeds received are ploughed back into similar investments before the end of the second fiscal year following the relevant sale.

In addition, the Stability Law has introduced a new R&D tax credit. It is applied with effect from a resident business's fiscal year following that in course on December 31, 2014, and is planned to be in effect until the fiscal year in course on December 31, 2019.

The new 25 percent tax credit, up to a maximum of EUR5m (USD6m) to each taxpayer, will be given on annual amounts of qualifying R&D expenditure (minimum EUR30,000) that exceed the average spent in a business's three previous fiscal years. Furthermore, it increases to 50 percent when applied to the cost of highly qualified personnel and R&D activities outsourced to universities and other educational establishments.

## EU Challenges US Tax Breaks For Boeing

The EU has notified the World Trade Organization (WTO) of a request for consultations with the US over tax incentives offered to commercial aircraft manufacturers, arguing that these incentives violate WTO rules.

The EU said that, in November 2013, Washington State vastly expanded and amended its existing aerospace tax incentives program as part of its efforts to induce Boeing to manufacture its new 777X model of large civil aircraft in Washington State. According to the EU, the expanded program effectively provides "billions of dollars" in additional subsidies (as defined by Articles 1 and 2 of the WTO's Agreement on Subsidies and Countervailing Measures (the "Agreement")) to Boeing.

The expansions and amendments also made the continuing availability of such tax incentives, in whole or in part, contingent upon siting production of the wings and final assembly for a new commercial aircraft model or variant in Washington State, and maintaining all wing assembly and final assembly of such commercial aircraft exclusively in Washington State, the EU said. The bloc argued that the program is inconsistent with Articles 3.1(b) and 3.2 of the Agreement, as it "conditions billions of dollars in subsidies upon the use of aircraft components manufactured in Washington State."

The request for consultations formally initiates a dispute in the WTO. Consultations give the parties an opportunity to discuss the matter and to find a satisfactory solution without proceeding further with litigation. After 60 days, if consultations have failed to resolve the dispute, the EU may request adjudication by a panel.

## Portugal's Green Tax Reform Enters Into Force

Portugal's green tax reform entered into force on January 1, 2015, expanding the scope of the carbon tax to sectors not covered by the EU's emissions trading scheme.

The expansion of the carbon tax is expected to generate revenues worth more than EUR95m (USD113m) in 2015. In addition, vehicle tax (ISV) rates are newly to be calculated according to a vehicle's carbon dioxide emissions, generating a further EUR28m.

The reform also includes value-added tax breaks for electric and hybrid vehicles and a charge on plastic bags of EUR0.08 per bag. The revenue raised from the charge on plastic bags will partly be used to finance nature conservation projects. Last, municipal property tax breaks of 50 percent will be provided to facilities that generate renewable energy and, on certain conditions, to farm buildings that provide ecosystem services.

The reform is fiscally neutral, meaning that any tax hikes it introduces will fund tax reductions or environmental projects. The nation's Ministry for the Environment, Spatial Planning and Energy noted

that the reform has been praised by the United Nations and the World Bank as an international example of best practice.

## Ireland Enhances Film Production Tax Breaks

Changes to Ireland's film tax incentive have entered into force, which, according to the Government, will help attract major international film production activities, boosting the domestic industry.

The amendments to the initiative, known as Section 481, were announced in Budget 2014, and entered into force on January 1, 2015. The rate of tax relief is now 32 percent of eligible Irish expenditure, up from the previous 28 percent. The tax credit is now based on the cost of all cast and crew working in Ireland, regardless of nationality. In addition, the scheme has been extended to 2020.

Arts Minister Heather Humphreys said that the improved tax breaks will be essential to achieving her goal of making Ireland "a first choice destination for international film makers." The revised definition of "eligible individual" will enable the inclusion of "major Hollywood actors and actresses" and will bring Ireland into line with the UK and other European countries, she said.

Humphreys added that she has secured a commitment from Finance Minister Michael Noonan "to keep these changes under close review, with a view to introducing additional improvements which would help further boost the indigenous film sector and attract big budget productions to Ireland."

## UK Targeting A Leaner, More Efficient Tax Agency

By 2021, HM Revenue & Customs (HMRC) "will be a smaller, more highly-skilled, increasingly digital organization based in fewer locations," the agency has said in its mid-year report.

The report covers the period from April to September 2014. It shows that HMRC increased the number of calls it handled through its customer helplines by 1.8 percent, to 74.5 percent. The agency has also introduced voice recognition services, along with cheaper telephone numbers. On the other hand, HMRC has underachieved in the processing of queries received by post, compared with its targets. It expects to miss its target of clearing 80 percent of post within 15 working days.

The Government asked HMRC to reduce its budget by 25 percent between 2010 and 2015, and by an additional 5 percent in 2015/16.

Cost efficiency savings of GBP75m (USD114.9m) were made between April and September, 2014, and more than GBP850m has been saved since 2010. The number of individuals employed by HMRC has fallen from 105,000 in 2005 to 64,706 (57,454 full-time equivalent) at the end of September 2014. By the end of the 2014/15 tax year, it anticipates that it will employ 57,000 full-time equivalent staff, based in 180 offices, in 99 towns and cities.

The report also reveals that HMRC brought in total tax revenues of GBP243.6bn in the first half of 2014, up approximately GBP7bn on the same period in 2013. Compliance activity secured GBP8.8bn in additional revenue, and HMRC says that it is confident of achieving its updated year-end compliance target of GBP26bn. It expects to secure more than GBP110bn in compliance revenues between 2011/12 and 2015/16.

## Spanish Income Tax Reform Measures Take Effect

Spain cut its corporate income tax rate from 30 percent to 28 percent from January 1, 2015, and substantially restructured its personal income tax regime, as part of comprehensive tax reform measures approved at the end of last year.

The income tax measures were included in Law No. 27 of 2014 – one of three tax reform Bills – which was published in the Official Gazette on November 28, 2014. The corporate tax rate cut is the first of a two-step reduction that will install a 25 percent rate from 2016.

The personal income tax reforms, also effective since the start of the year, reduce the number of tax rates from seven to five. The minimum personal income tax rate was reduced to 24.75 and will fall to 19 percent next year. The top marginal tax rate, newly 47 percent, will also fall in 2016 to 45 percent. However, the threshold for the top rate has been cut substantially, from EUR300,000 to EUR60,000. The tax-exempt threshold rose to EUR12,000 on January 1.

Tax rates on savings income fell from January 1. A tax rate of 20 percent will now apply to savings income up to EUR6,000; a rate of 22 percent will apply to income of up to EUR50,000; and a 24 percent rate will apply to savings income thereafter. Each of these rates is due to fall by 1 percent in 2016.

Also included in Law No. 27 of 2014 were substantial changes to Spain's transfer pricing and controlled foreign corporation (CFC) rules, also effective from January 1. The Bill included a revision to the definition of "related party" to include a 25 percent participation threshold, up from 5 percent presently, in Article 18 of the Bill.

In line with OECD recommendations, provisions were introduced to allow taxpayers to use the "most appropriate" transfer pricing method, replacing wording in regulations that recommended the use of profit-based methods in certain circumstances. As a backstop, the law also allows the use of the "sixth method," not prescribed in the OECD Guidelines, in cases where the method would produce satisfactory arm's length prices.

Other changes – in line with the OECD's work on base erosion and profit shifting – aim to tackle non-taxation in the case of hybrid instruments. For interest payments to be deductible, the taxpayer must demonstrate that as a result of tax re-characterization, income will be generated that will be subject to tax at a rate of 10 percent or more. Hybrid instruments issued by related parties must be

re-characterized as equity instruments, and interest payments made on such instruments will not be tax deductible.

The law also tightens the nation's CFC rules to tackle contrived arrangements; makes substantial changes to tax group rules; and enhances the Advance Pricing Agreement regime, including provisions enabling authorities to permit rulings to apply on a retrospective basis.

Last, the Bill approved simplified transfer pricing documentation requirements for companies with an annual turnover of less than EUR45m (USD55.3m).

## Japan's Coalition Parties Agree Corporate Tax Rate Cut

On December 30, Japan's ruling Liberal Democratic Party and its coalition partner Komeito finalized their tax reform plans, including a corporate tax rate cut, to be effective in the next fiscal year, which begins on April 1, 2015.

As part of Prime Minister Shinzo Abe's promised growth strategies, the Government took a decision earlier this year to reduce the country's corporate income tax rate from its current rate of more than 35 percent to below 30 percent over the next few years, so as to reach a more internationally competitive level.

As the first steps in that plan, it has been decided by the parties that the headline corporate tax rate will be cut by 2.51 percent to 32.11 percent in the 2015 fiscal year, and then to 31.33 percent in 2016. Further rate cuts can then be expected in succeeding fiscal years.

The Government had previously indicated that corporate rate cuts would only be possible with other measures to offset most of the consequent revenue losses, given Japan's fiscal deficit position. However, while much of the lost revenue from the rate reduction will be offset by broadening the corporate tax base, it is estimated that the 2015 rate reduction will still cost around JPY300bn (USD2.5bn) in lost revenue.

With only around 30 percent of Japan's companies presently paying corporate tax because of previous losses, the base-broadening reform proposals include a reduction in the amount of declared business income that can be written off to cover previous losses. The current limit of 80 percent will decrease to 50 percent in April 2017.

Other measures have been added to the package in an attempt to encourage the transfer of the wealth that is concentrated in Japan's older generations towards younger people. A gift tax exemption will be given to parents or grandparents that fund marriages and childcare, and the current JPY10m exemption limit for gifts to pay for their offspring's housing will be extended to 2019. The exemption limit will also be increased to JPY15m in 2015 (and JPY30m in 2016) for purchases of energy-saving homes.

## China To Accelerate FTA Talks With GCC

China aims to speed talks on its free trade agreement (FTA) with the Gulf Cooperation Council (GCC) states and will launch new talks with Israel this year, Chinese media reported.

Zhang Shaogang, Director-General of the Department of International Trade and Economic Affairs at the Ministry of Commerce, told state-owned newspaper China Daily: "GCC countries consider China as a major market for their petrochemical products, and this FTA will assist those nations in their industrial development."

Talks on a China–GCC FTA initially opened in 2004, with substantial progress said to have been made on the scope of the agreement after five rounds of negotiations. However, talks are thought to have stalled, with China last year calling on Bahrain to push the GCC for a conclusion. The GCC's other members are the United Arab Emirates, Saudi Arabia, Oman, Kuwait, and Qatar.

The main products traded between China and the GCC are oil, steel, electronic products, mechanical equipment, and textiles.

China also aims to conclude an FTA with Israel in the next few years, and the Finance Ministry has concluded a study on the feasibility of such a treaty, Zhang said.

## South Korea–Canada FTA Enters Into Force

Ed Fast, Canada's International Trade Minister, has welcomed the entry into force of a landmark free trade agreement (FTA) with South Korea, saying that it will create thousands of new jobs and provide a gateway for Canadian exporters to Asia.

The FTA – Canada's first with an Asia Pacific region economy – entered into force on January 1, 2015. From this date, South Korea automatically removed duties on 81.9 percent of tariff lines. When the agreement is fully implemented, South Korea will have eliminated duties on 100 percent of Canadian non-agricultural exports and 97 percent of agricultural exports. Canada will remove duties on approximately 99.9 percent of South Korea's exports to the country. Canadian exporters stand to benefit most from the tariff concessions; average South Korean tariffs are three times higher than Canada's, at 13.3 percent, compared with 4.3 percent.

Fast will lead a trade mission to South Korea in February to provide what the Canadian Government describes as "on-the-ground support" to Canadian businesses as they take advantage of the opportunities the deal will create. The Government is also providing a series of workshops to ensure that firms can make the most of the FTA's benefits.

The implementation of the FTA fulfills the commitment made by Canadian Prime Minister Stephen Harper and South Korean President Park Geun-hye to bring the treaty into force as soon as possible. The implementation timetable is the fastest ever achieved for a Canadian FTA. It moved from signature to entry into force in just over three months.

Talks had been put on hold in 2008 after South Korea maintained an import ban on Canadian beef. The ban was lifted in January 2013. The terms of the FTA were eventually agreed in March 2014.

South Korea is Canada's third-largest trading partner in Asia. Bilateral merchandise trade between Canada and South Korea reached almost CAD11bn (USD9.5bn) in 2013. The FTA is projected to increase Canadian merchandise exports to South Korea by 32 percent and boost Canada's economy by CAD1.7bn.

## UK Digital Firms Granted Reprieve From EU VAT Changes

The UK is to permit micro businesses to rely on information from payment processing firms to determine the location of their customers for six months, to ease the burden of complying with new value-added tax (VAT) rules on digital services effective since January 1.

In revised guidance on December 29, 2014, HM Revenue & Customs (HMRC) has said that micro businesses that are below the current UK registration threshold of GBP81,000 and who register for the VAT Mini One Stop Shop (MOSS) service may, until June 30, 2015, base their "customer location" VAT taxation and accounting decisions on information provided to them by their payment service provider.

The announcement concerns new rules on businesses that supply broadcasting, telecommunications, and electronic services to EU consumers. Since January 1, 2015, they have been required to collect and account for VAT on their supplies based on the location of the recipient, at that member state's VAT rate, rather than in the location that they – as the supplier – are based.

According to HMRC, the concession will mean that businesses need not require further information to be supplied by the customer until after this six-month transitional period. As payment service providers already collect and hold a minimum of two pieces of information about the member state where their customer usually resides, the transitional period will give micro businesses additional time to adapt their websites to meet the new data collection requirements, after warnings from small businesses that the identification requirement was the most onerous.

Under the EU's new regime for digital business-to-consumer supplies, businesses are being required to identify the location of their customer by either using place of supply "presumptions" for certain supplies, or by collecting two sets of non-contradictory information.

Types of supplies covered by the presumption rule include where the digital service is supplied:

- Through a telephone box, a telephone kiosk, a wifi hot spot, an internet café, a restaurant, or a hotel lobby, in which case VAT will be due in the member state where those places are actually located.
- On board transport traveling between different countries in the EU, in which case VAT will be due in the member state of departure;
- Through a consumer's telephone landline, in which case VAT is due in the member state where the consumer's landline is located;
- Through a mobile phone, in which case the consumer location will be based on the member state country code of the SIM card; or
- For satellite television systems, in the member state of the postal address where the decoder is located or the viewing card is sent.

Where the digital services are supplied other than in the circumstances listed above, the business making the supply must obtain and keep two pieces of non-contradictory information to support and evidence the member state where the customer is normally located. Examples of the type of supporting evidence that tax authorities will accept include:

- The billing address of the customer;
- The Internet Protocol (IP) address of the device used by the customer;
- The customer's bank details;
- The country code of the SIM card used by the customer;
- The location of the customer's fixed land line through which the service is supplied; or
- Other commercially relevant information (*e.g.*, product coding information which electronically links the sale to a particular jurisdiction).

## Bahamas Introduces Value-Added Tax

The Bahamas' new value-added tax (VAT) regime, featuring a 7.5 percent headline rate, was introduced in the territory from January 1, 2015.

Noting the long-awaited implementation of the regime, the Government said it had immediately begun checks to ensure compliance by VAT-registered businesses and to tackle abuse.

All businesses with taxable sales of BSD100,000 (USD100,000) or more were required to register by November 30, 2014.

Ahead of the introduction of VAT, the Government updated much of the guidance that it has released to date, including its specific industry guides, its guide on the completion of VAT returns, its main VAT guide, and its guidance on transitional arrangements.

VAT was proposed to be introduced in the Bahamas to broaden the territory's tax base in anticipation of its accession to membership of the World Trade Organization, which will require that the territory substantially reduce its trade tariffs. Alongside, the introduction of VAT, the territory has introduced a broad range of reductions to custom and import tariff rates, also effective from January 1, and has newly released guidance on these changes.

Duty has been removed on a number of items – mainly construction materials – that had previously been subject to a 7 percent rate; duty on a number of items that had been subject to a 10 percent rate has been halved; and other rates ranging from 25 percent to 45 percent have been cut to as low as 5 percent.

## Luxembourg Hikes VAT Rates

Luxembourg's value-added tax (VAT) rates rose on January 1, 2015, to counteract the revenue hit for the nation from changes to EU place of supply rules for broadcasting, telecommunications and electronic (BTE) services from the same date.

With the exception of its super reduced rate, Luxembourg has hiked each of its VAT rates by 2 percent, establishing a headline rate of 17 percent and reduced

rates of 8 and 14 percent. The rate of the super reduced rate is unchanged at 3 percent, but its scope has been altered. The supply of alcohol and alcoholic beverages sold by pubs and restaurants is now subject to the new 17 percent headline VAT rate. In addition, the super reduced rate now applies only to work done on a person's own primary residence and not to housing for third parties. A transitional rule was allowed for projects notified before January 1, 2015, providing they are completed by December 31, 2016.

The rate changes were announced in response to the EU place of supply rule changes, which mean that BTE services are, from January 1, 2015, newly taxable in the location of the consumer at that member state's rate, rather than in the location of the supplier. The previous rules had favored Luxembourg, which has the EU's lowest VAT rates, as businesses had located their operations in the nation to make tax-efficient digital supplies to EU consumers.

In a last-minute concession, Luxembourg secured compensation from EU member states worth about USD1.375bn over four years.

## Czech Republic Introduces New Reduced VAT Rate

At the start of this year, the Czech Republic introduced a third value-added tax (VAT) rate of 10 percent, after several months of negotiations between lawmakers last year.

The new 10 percent rate, seen as one of the Czech Government's flagship measures of last year, has been introduced on food, which had been subject to a 15 percent rate, and books, baby food, and medicines, which had been subject to the headline VAT rate of 21 percent.

Previously, Czech lawmakers had proposed the introduction of a single rate of VAT from 2016 of about 17.5 percent, and the debate concerned whether to proceed with a simplified regime – as favored by the International Monetary Fund – or push ahead with the concessions for basic items.

## IRS Will Open US Tax Filing Season On Time

Following the congressional renewal of the "tax extenders" package of measures earlier this month, the US Internal Revenue Service (IRS) has announced that it still anticipates opening the 2015 tax filing season as scheduled in January.

The IRS will begin accepting tax returns electronically and processing paper returns from January 20.

Referring to the passage of legislation to extend the tax extenders for one year, IRS Commissioner John Koskinen said: "We have reviewed the late tax law changes and determined there was nothing preventing us from continuing our updating and testing of our systems. Our employees will continue an aggressive schedule of testing and preparation of our systems during the next month to complete the final stages needed for the 2015 tax season."

The IRS has also sought to highlight that filing electronically is the most accurate way to file a tax return and the fastest way to get a refund. The agency pointed out that there is no advantage, in terms of processing times, for those people filing tax returns on paper in early January rather than waiting for e-filing to begin.

The IRS confirmed that more information about the 2015 filing season will be available in January.

## Walgreen Completes 'Non-Inversion' With Alliance Boots

On December 31, Walgreen Co. completed its combination with Alliance Boots GmbH to form Walgreens Boots Alliance, Inc, with its headquarters remaining in the US, rather than being transferred abroad by way of a "corporate inversion."

At a special meeting of shareholders held on December 29, Walgreens shareholders approved the share purchase to combine fully the two companies into what is being called "the first global pharmacy-led health and wellbeing enterprise." It will include Walgreen Co. (the largest drugstore chain in the US), Boots (the UK and Ireland's leading pharmacy-led health and beauty retailer), and Pharmaceutical Wholesale and International Retail (including Alliance Healthcare, Europe's largest pharmaceutical wholesaler).

It was confirmed that the companies have received all regulatory approvals required to complete the transaction and that the new holding company will be domiciled in the US and headquartered in Deerfield, Illinois. Walgreen Boots Alliance common stock will be listed on the NASDAQ Stock Market.

Although Walgreens itself had an effective tax rate close to the headline US corporate tax rate of 35 percent, it was decided in August 2014 not to gain the reported USD4bn in tax savings over five years that could have been available to it by moving the

company's base to Switzerland, where Alliance Boots was headquartered.

Corporate inversions have been used by US companies when bidding for foreign companies as a means of moving away from America's high corporate tax rate. Under the present tax code, a company that merges with an offshore counterpart can, under certain conditions, move its headquarters abroad and take advantage of the lower corporate tax rates in foreign jurisdictions.

When taking the decision in August not to transfer its tax domicile abroad, Walgreens had then confirmed that it "undertook an extensive analysis to explore the feasibility of a restructured inversion transaction that would provide the company with the customary level of confidence needed to withstand Internal Revenue Service (IRS) review and scrutiny."

Aside from concerns that it could have been involved in a protracted argument with the IRS, and that it could risk losing a major portion of its revenues derived from Government-funded reimbursement programs, Walgreens was also thought to have been influenced by the growing anti-inversion political discussions in the US, draft legislative proposals in Congress, and White House efforts, which became a reality in September, to introduce administrative actions and reduce the tax benefits from inversions.

## US Dynamic Tax Scoring Called 'Republican Ruse'

With the Republican party looking to require the Joint Committee on Taxation (JCT) and the Congressional Budget Office (CBO) to apply "dynamic scoring" to major pieces of tax legislation in the next Congress, Edward Kleinbard has called it "a ruse to make tax cuts look good."

Currently a professor of law at the University of Southern California, but previously a JCT chief of staff, Kleinbard has concluded, in an op-ed in *The New York Times*, that a change to dynamic scoring "could have significant, negative consequences for enacting sustainable, long-term fiscal policies."

It has been noted that the CBO and the JCT currently use "static" revenue estimating techniques, which make the assumption that tax policy changes – regardless of their magnitude – have no impact on the economy's performance. This methodology has been widely criticized on the grounds that it could provide policymakers with inaccurate numbers and create a bias against lower tax rates.

On the other hand, dynamic scoring, which is championed by the Republican party, is said to recognize that taxes do affect economic growth. For example, dynamic scoring assumes that higher tax rates would discourage work, saving and investment, and reduce economic growth, thereby not raising the amount of revenue suggested by static estimates.

However, in his article, Kleinbard pointed out that the reality of dynamic scoring is more complex: "in order to look at the effects across the entire economy, dynamic modeling relies on many simplifying

assumptions. … The resulting estimates are likely to incorporate greater uncertainty about the magnitude of any revenue-estimating errors."

"The Republicans' interest in dynamic scoring is not the result of a million-economist march on Washington," he added. "They will use dynamic scoring to justify a tax cut that, under conventional scorekeeping, loses revenue."

In addition, in line with most Democrat lawmakers, House of Representatives Ways and Means Committee Ranking Member Sander Levin (D – Michigan) also stated that, "in the guise of dynamic scoring, Republicans are trying to rig the system in ways that can be very destructive. The proposed change would undermine fiscal responsibility."

Orrin Hatch (R – Utah), Finance Committee Chairman in the new Republican-led Senate, has recognized that dynamic scoring is "not a panacea[, as] macroeconomic analysis providing projections of future effects of policy changes are, of course, subject to uncertainties."

Nevertheless, he has concurred with the new approach to evaluating major tax reforms, believing that "the expanded and sensible use of dynamic analysis can, if done correctly, be an important tool to help us achieve our goals."

## Zambia Proceeds With Mining Royalty Hikes

Despite threats of reduced production and employment in the mining sector, the Zambian Government has gone ahead with sharp increases in mining royalties, which were first announced in its 2015 Budget in October last year.

In his budget speech, Finance Minister Alexander Chikwanda had proposed that, instead of the current 6 percent royalty for all mines, split levels of 8 percent and 20 percent mineral royalties would be introduced as a final tax on underground mining and on open cast mining operations, respectively.

Chikwanda had explained that the measure is intended to increase Government income from the mining sector and achieve a more equitable distribution of mineral returns between the Government and the mining companies.

However, the Chamber of Mines of Zambia had immediately emphasized that, although mining companies will no longer be subject to corporate income tax, the increased royalties would cause a shutdown of some mines, which would then be unprofitable.

In fact, last month, Canada-based Barrick Gold announced that it has suspended operations at the Lumwana copper mine in Zambia on account of the plan. Its Co-President, Kelvin Dushnisky, said: "Despite the progress we have made to reduce costs and improve efficiency at the mine, the economics of an operation such as Lumwana cannot support a 20 percent gross royalty, particularly in the current copper price environment."

Nevertheless, despite a recommendation from the International Monetary Fund last month that Zambia should reconsider its plan, its acting President, Guy Scott, assented to the relevant legislation as an amendment to the Mines and Minerals Development Act 2008, and the increased royalties went into effect on January 1.

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## Oman Abandons Expat Tax Plan

The Economic Committee of Oman's State Council has rejected a plan to levy a tax on the remittances sent by foreign workers to their home countries, local media reported recently.

In November 2014, the Middle Eastern country's Shura Council suggested that the Government tax remittances at the rate of 2 percent as a way of easing growing pressure on the state budget.

However, Salim bin Said Al Ghatami, the head of the Economic Committee, told the *Times of Oman* that "it is not the right time to impose a tax just on working expatriates." He said that the proposed tax needs to be examined by expert committees before it can be adopted.

The official explained that the proposed tax would violate the terms of certain international agreements that Oman is party to and would affect investment prospects in the country.

Oman has about 1.5m expatriate workers, most of whom come from south and southeast Asia. Based on the OMR3.1bn (USD8bn) which expatriates sent abroad as remittances in 2012, the proposed tax would generate about OMR62m in annual tax revenue.

## Canadian Think Tank Challenges Share Option Tax Break

The Canadian Centre for Policy Alternatives, a think tank, has called for the closure of an income tax "loophole" that it says benefits company executives.

Under Canadian law, when a qualifying employer grants an option to an employee, the employee's tax situation is not affected until they exercise or dispose of the option. If an employee decides to exercise an option and acquire securities at less than their fair market value, they will receive a taxable benefit. The Income Tax Act provides a 50 percent deduction in computing taxable income if certain conditions are met when an employee exercises, transfers, or disposes of rights under an employee stock option agreement.

According to the Centre, company executives are able "to pay half the income tax rate on the proceeds from cashing in stock options by claiming that revenue as capital gains." The Centre adds that "from an after-tax perspective, a dollar received from the exercise of a stock option is worth two dollars of salary income."

"At a subsidy rate of half the top marginal rate of 52 percent, or 26 percent, the estimated tax subsidy for the options granted to the top 100 CEOs in 2013 is CAD82m (USD69.6m), and the anticipated tax subsidy related to their stockpile of unexercised 'in the money' options is CAD413m," the Centre calculates, in its new report on CEO pay.

## Taiwan Reduces Imputation Tax Credit

To boost revenue, the National Taxation Bureau of Taipei (NTBT) began implementing from January 1, 2015, the approved measure that halves the benefit of the full dividend imputation system previously allowed in Taiwan.

The full dividend imputation system had allowed for tax on corporate profits to be offset against individual tax liability arising from the receipt by individual resident shareholders of a dividend from that company. This system has now been replaced by a 50 percent tax credit instead.

The NTBT has further interpreted the new measure to mean that the halved imputation tax credit should also be allowed for distributed dividends or earnings paid to shareholders who are not resident in Taiwan.

## AUSTRIA - TAIWAN

### Effective

The DTA between Austria and Taiwan came into effect on January 1, 2015.

## BARBADOS - RWANDA

### Signature

According to preliminary media reports, Barbados signed a DTA with Rwanda on December 22, 2014.

## BRITISH VIRGIN ISLANDS - GUERNSEY

### Into Force

The TIEA between the British Virgin Islands and Guernsey entered into force on November 11, 2014.

## BRITISH VIRGIN ISLANDS - POLAND

### Effective

According to preliminary media reports, the TIEA signed between the British Virgin Islands and Poland on November 29, 2013, became effective on January 1, 2015.

## CYPRUS - ICELAND

### Signature

Cyprus and Iceland signed a DTA on November 13, 2014.

## DENMARK - GHANA

### Ratified

Denmark on December 19, 2014, completed its domestic ratification procedures in respect of the DTA signed with Ghana on March 20, 2014.

## DENMARK - LUXEMBOURG

### Into Force

The Protocol to the DTA between Denmark and Luxembourg entered into force on December 28, 2014, according to a notice published in Luxembourg's Official Gazette on December 30, 2014.

## ITALY - MEXICO

### Forwarded

Italy's lower House of Parliament on December 18, 2014, approved a law that would ratify a pending DTA Protocol with Mexico.

## JAPAN - HONG KONG

### Forwarded

Japan and Hong Kong exchanged diplomatic notes on December 10, 2014, to amend the scope of the tax information exchange provisions in their existing DTA. The amendment is subject to the two territories' normal domestic ratification procedures.

## KAZAKHSTAN - QATAR

### Forwarded

Kazakhstan's lower House of Parliament approved the DTA signed with Qatar on December 24, 2014.

## KAZAKHSTAN - THAILAND

### Negotiations

According to preliminary media reports, Kazakhstan and Thailland agreed to begin DTA negotiations on December 24, 2014.

## MALI - MOROCCO

### Forwarded

Mali's Cabinet on December 24, 2014, approved the DTA signed with Morocco.

## MEXICO - PHILIPPINES

### Negotiations

Mexico and the Philippines held DTA negotiations over five days, concluding on December 19, 2014.

## NETHERLANDS - VARIOUS

### Negotiations

On December 10, 2014, the Dutch Government said it is to begin negotiating DTAs with Iraq, Mozambique and Senegal, and will continue DTA negotiations with France and Thailand, as well as negotiations towards DTA Protocols with Belgium and Germany.

## SAUDI ARABIA - BELGIUM

### Initialed

According to an update from the Saudi tax authority on December 29, 2014, Saudi Arabia and Belgium recently initialed a DTA following the second round of negotiations towards a DTA.

## SAUDI ARABIA - MACEDONIA

### Signature

In an update published on December 16, 2014, the Saudi tax authority confirmed that it had signed a DTA with Macedonia.

## SPAIN - SENEGAL

### Into Force

The DTA between Spain and Senegal entered into force on October 22, 2012.

## SPAIN - UZBEKISTAN

### Forwarded

The Spanish Government on December 26, 2014, approved a law that would ratify the DTA signed with Uzbekistan.

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

## THE AMERICAS

### 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

## INTERNATIONAL ESTATE & TAX PLANNING 2015

Practicing Law Institute

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

Chairs: Dean C. Berry (Cadwalader, Wickersham & Taft LLP), Robert L. Dumont (Deloitte Tax LLP)

## 2/13/2015 - 2/13/2015

http://www.pli.edu/Content/Seminar/International_Estate_Tax_Planning_2015/_/N-4kZ1z1297k?ID=222616

## ADVANCED INTERNATIONAL TAX PLANNING

Bloomberg BNA

Venue: Treasure Island Hotel, 3300 S. Las Vegas Blvd, Las Vegas, NV, 89109, USA

Chair: TBC

## 2/23/2015 - 2/24/2015

http://go.bna.com/advanced_lasvegas.aspx

## AMERICAS TRANSFER PRICING SUMMIT 2015

TP Minds

Venue: Biltmore Hotel, Miami, Florida, 1200 Anastasia Ave Coral Gables, FL 33134, USA

Key Speakers: Samuel Maruca (IRS), Michael Lennard (United Nations), Mayra Lucas (OECD), David Ernick (PwC), Sergio Luis Pérez (SAT Mexico), among numerous others

## 2/24/2015 - 2/25/2015

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

### INTRODUCTION TO US INTERNATIONAL TAX

Bloomberg BNA

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

Chair: TBC

**3/16/2015 - 3/17/2015**

http://www.bna.com/intro_SF2015/

### INTERMEDIATE US INTERNATIONAL TAX UPDATE

Bloomberg BNA

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

Chair: TBC

**3/18/2015 - 3/20/2015**

http://www.bna.com/inter_SF2015/

### INTERNATIONAL TAX ISSUES 2015 - CHICAGO

Practicing Law Institute

Venue: University of Chicago Gleacher Center, 450 N. Cityfront Plaza Drive, Chicago, Il 60611, USA

Chair: Lowell D. Yoder (McDermott Will & Emery LLP)

**9/9/2015 - 9/9/2015**

http://www.pli.edu/Content/Seminar/International_Tax_Issues_2015/_/N-4kZ1z12a24?ID=223915

## 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

### 2015 FINANCIAL SERVICES TAXATION CONFERENCE

The Tax Institute

Venue: Surfers Paradise Marriott Resort & Spa, 158 Ferny Avenue, Surfers Paradise QLD 4217, Australia

Key Speakers: Rob Colquhoun, ATI (Australian Financial Markets Association), Dr Stephen Kirchner

(Australian Financial Markets Association), Rob McLeod (EY), Greg Fitzgerald (Macquarie Group), Robert Gallo (PwC), Warren Dunn (EY), Patrick Grob, CTA (Suncorp), among numerous others

### 2/18/2015 - 2/20/2015

http://eportal.taxinstitute.com.au/StaticContent/Download/1150202M1WD.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

### EMPLOYMENT TAX PLANNING CONFERENCE

IIR & IBC Finance 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

### 1/20/2015 - 1/20/2015

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

### 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

Chair: Jack Bernstein (Aird & Berlis)

**2/9/2015 - 2/10/2015**

http://www.int-bar.org/conferences/conf618/binary/London%20Tax%20Issues%202015%20programme.pdf

## 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

## THE 37TH ANNUAL OFFSHORE TAXATION CONFERENCE

IIR & IBC financial Events

Venue: TBC, London, UK

Key Speakers: Emma Chamberlain (Pump Court Tax Chambers), Patrick Soares (Field Court Tax Chambers), Giles Clarke (Offshore Tax Planning)

### 3/24/2015 - 3/24/2015

http://www.iiribcfinance.com/event/offshore-tax-planning-conference

## THE 9TH ANNUAL FORUM ON COLLECTIVE INVESTMENT SCHEME (CIS) TAXATION

Infoline

Venue: TBC, London, UK

Key Speakers: Malcolm Powell (Investec Asset Management), Kevin Charlton (KPMG), Teresa Owusu-Adjei (PWC), Lorraine White (Bank of New York Mellon), Jorge Morley-Smith (Investment Management Association), Christopher Mitchell (BNY Mellon)

### 3/25/2015 - 3/25/2015

http://www.infoline.org.uk/event/Collective-Investment-Scheme-Taxation

## 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

## INTERNATIONAL TAXATION OF E-COMMERCE

IBFD

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

Key Speakers: Bart Kosters (IBFD), Tamas Kulcsar (IBFD)

### 5/11/2015 - 5/13/2015

http://www.ibfd.org/Training/International-Taxation-e-Commerce#tab_program

## 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: Bart Kosters (IBFD)

### 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

## THE AMERICAS

### Canada

The Tax Court of Canada heard the case of a company which provided management services to mutual fund trusts, and charged Goods and Services Tax (GST) on the cost of the services. In order to attract the business of larger investors the company occasionally reduced the management fees included in the costs of its services, resulting in a special distribution from the funds to the investors equal to the reduced amount called "Management Fee Distributions".

Since these special distributions were not included by the company in GST calculations, the tax authority objected to them and assessed the company for the GST amounts based on the assumption that the distributions were part of the consideration paid by the funds to the company for its managerial services.

The company argued that the special distributions represented transactions between the funds and the larger investors who received them, which meant they were separate from the consideration for the services, but the tax authority maintained that rather than reducing the management fees, a portion of them was paid not to the company but to the investors and that therefore the special distributions remained part of the consideration for the services. The argument was also made that "there is both a legal and an economic link or connection between

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

the unreduced gross management fee and the supply of management services to the Funds."

The Tax Court first stated that according to national legislation tax shall be charged on the amount of consideration paid for the supply of taxable services, which in the present case were the managerial services, and that "there must be a link or connection between the consideration and the supply itself." The company, while referring to legislation under which consideration must be either expressed as monetary value or fair market value, contended that the tax authority had not offered evidence for the fair market value of the legal obligation to pay the special distributions to the investors which was also part of the consideration for the managerial

services as per the authority's argument. The authority countered with the opinion that the market value of the obligation was equal to the value of the special distributions.

With regard to the tax authority's contention that the funds continued to pay the gross amount of managerial fees following the introduction of the special distributions and therefore they made up the consideration already being paid for the company's services, the Tax Court disagreed, observing that the reduced managerial fees were paid weekly and monthly while the special distributions were made monthly and quarterly.

As a result of its interpretations of the Management Agreement and the accompanying correspondence as evidence, the Tax Court ruled that the Management Fee Distributions were not part of the consideration paid for the supply of managerial services but were separate payments made by the funds to the large investors. The reduced amount of managerial fees remained subject to GST and the monetary value was the only consideration involved, it concluded; the tax authority had failed to argue that the distributions had value which should have been included as part of the consideration for the services. The company's appeal against the re-assessment for GST purposes was therefore allowed, with costs payable by the appellant.

The judgment was delivered on December 23, 2014.

Tax Court: *Invesco Canada Ltd v. The Queen (TCC 375)*

http://decision.tcc-cci.gc.ca/tcc-cci/decisions/en/item/100158/index.do

## WESTERN EUROPE

### Italy

The European Court of Justice (ECJ) was asked for a preliminary ruling concerning an Italian company that failed to follow domestic value-added tax (VAT) invoicing requirements for intra-community acquisitions from two other companies, which were established in France and the Netherlands.

The tax authority imposed a VAT assessment and a penalty on the company for failing to register the VAT invoices concerned – being a monthly requirement under Italian law.

On appeal, the District Tax Court dismissed the assessment, but the Regional Tax Court ruled in favor of the authority, stating that "the failure to register was a breach which was not formal but substantive in nature and that it constituted an infringement such as to warrant a notice of reassessment and/or recovery." The company further appealed to the Court of Cassation, arguing that its failure to register the VAT invoices was not a substantive breach and argued that the tax authority had erred in assessing the company's VAT liability. The ECJ was approached for an interpretation of provisions regarding a company's right to deduct VAT in circumstances where that company had failed to register VAT invoices following intra-Community acquisitions.

The ECJ said, according to case law, that the right to deduct VAT "is an integral part of the VAT scheme and in principle may not be limited." It said the reverse charge mechanism applies because the transactions were between two member states and the

recipient should therefore be entitled to deduct the input tax it incurs for receiving the supply.

The ECJ further stated that EU law allows member states to create requirements for the application of the right to deduct VAT, but they must be not go beyond what is necessary to ensure that the reverse charge procedure has been correctly applied. In addition, it said member states may impose obligations together with the obligations under EU law for the sake of collecting taxes and preventing fraud, as long as they do not interfere with the principle of neutrality.

Drawing on previous rulings, the ECJ said, with regards the reverse charge procedure, that fulfillment of the substantive requirements may be enough to allow the right to deduct VAT, even if the more formal requirements were not satisfied by the company. A tax authority which identified evidence that the company complied with the substantive requirements cannot therefore prevent the company from applying the right "for practical purposes."

The ECJ concluded that the company in the present case fulfilled all the necessary substantive requirements and should be eligible for an input tax credit on VAT incurred under a reverse charge on goods acquired for use in making taxable supplies. The ECJ concluded that EU law precludes a tax authority from denying the company the right to deduct VAT if that company has fulfilled the most necessary requirements, despite its failure to register its VAT invoices.

The judgment was delivered on December 11, 2014.

European Court of Justice: *Idexx Laboratories Italia Srl v. Italy (C-590/13)*

http://curia.europa.eu/juris/document/document.jsf?text=&docid=160567&pageIndex=0&doclang=EN&mode=lst&dir=&occ=first&part=1&cid=7842

## Spain

The European Court of Justice (ECJ) was asked for a preliminary ruling concerning Spain's national law stating that a Spanish tax representative is required when pension funds and insurance services based in other EU member states provide services (*e.g.*, occupational pension schemes) in Spain. The European Commission was of the opinion that the law was incompatible with European legal provisions with regard to freedom to provide services, and brought an action against Spain when it failed to implement measures to change the law; Spain then approached the ECJ for a ruling.

The Commission argued that requiring a tax representative only in the case suppliers of pension funds and insurance based in other member states was an infringement of the freedom to provide services available under EU law, because it imposed an additional burden on such companies providing services in Spain and therefore discouraged them from doing so. Spain admitted that the law was affecting the freedom to provide services of non-resident companies, but argued that the measure was "justified by the need for effective fiscal supervision and the prevention of tax evasion."

Spain believed that appointing a tax representative in the case of non-resident suppliers reduced the possibility of tax evasion occurring since the representative could be more easily contacted by the Spanish tax authority in case they required more information. In addition, the requirement under Spanish law for the representative to withhold tax on non-resident pension fund and insurance services meant that foreign companies could fulfill the same obligation under EU law to withhold tax as resident companies.

France argued (in support of Spain) that the tax representative law was "justified by the need to ensure the effective collection of tax, which the Court has recognized as an overriding reason in the public interest." A representative meant that the receivers of the services did not have to withhold tax themselves, which would have made foreign companies less attractive since business with resident companies did not carry the same burden, France claimed. The Commission rejected the arguments of both Spain and France on the basis that appointing a tax representative was not necessary to ensure the efficient collection of tax from the provision of non-resident services.

The ECJ pointed out that EU law prevents the application of any national law that makes foreign provision of services more difficult than the domestic provision of services, or impedes "the activities of a provider of services established in another Member State where he lawfully provides similar services."

Spain argued that the ECJ had stated in the past that the prevention of tax evasion was a legitimate reason for restricting the freedom to provide services according to past cases. The ECJ agreed for the most part that a tax representative was an appropriate measure to ensure effective tax collection; however, exchange of information between tax authorities of different member states for the sake of accurately collecting income tax is permitted under EU law, and although Spain attempted to argue that a tax representative was necessary because the relevant EU legal provisions were ineffective, it failed due to a lack of supporting evidence.

The fact that the tax representative was intended to withhold tax on behalf of the foreign service providers, which the ECJ had held also to be a legitimate reason, was not deemed relevant because the main issue according to the Commission was the obligation to appoint a tax representative rather than the tax withholding method itself.

The ECJ ruled that Spain had failed to adhere to EU law by enacting legislation which restricted foreign companies' freedom to provide services in Spain by requiring them to appoint a tax representative.

The judgment was delivered on December 11, 2014.

European Court of Justice: *Commission v. Spain (C-678/11)*

http://curia.europa.eu/juris/document/document.jsf?text=&docid=160569&pageIndex=0&doclang=EN&mode=lst&dir=&occ=first&part=1&cid=121573

## DATELINE JANUARY 8, 2015

Vietnam seems to be coming to terms with Uber in a way which will allow tax to be collected on its operations while legacy taxi firms receive some benefit from the revenues they are losing. I'm not quite sure whether this deserves approbation or censure. As with other mold-breaking Internet-based developments, entrenched monopolies, whether they be established taxi firms or central banks, are threatened by such new phenomena, which work outside conventional legal and tax structures, to the benefit of consumers and individuals. Reacting by banning or taxing them is not pro-consumer, and to that extent, Vietnam's efforts to muzzle Uber's operations even before it gets off the ground in the country are reprehensible. So they get a reprimand.

Uber's tax structures are indeed complex, and its critics, such as Margaret Hodge, UK Labour Chair of Parliament's Public Accounts Committee, use its fiscal vulnerability as a stick with which to beat the company, although their underlying agenda may have more to do with the defense of existing employment-heavy monopolies. Uber's drivers are self-employed, but unlike most mini-cab drivers are paid out of Uber's credit-card receipts, making it difficult if not impossible for them to cheat the tax-man. The balance of Uber's receipts appear to be divided between national or regional licensed operators and international holding structures, and that's perhaps where there is a chance for BEPS-style tax avoidance, although no-one is suggesting that there is anything illegal as such about Uber's structure. The biggest danger to Uber from a tax perspective may be that its drivers could be classified as employees, and tax authorities the world over are probably exploring their chances of following that route. At first blush, it would seem unpromising: a driver, paying all her maintenance and running expenses, and free to work for any licensed operator (that may be Uber's weakness) seems to be a classic case of self-employment. At all events, one supposes that Uber's lawyers have crawled all over their driver contracts with that in mind.

For Uber's enemies, and there are plenty, the licensing aspect seems more promising ground, and many countries have seen partial or total bans on Uber operations, sometimes as a result of court action taken by taxi operators' associations, and sometimes through direct action by governments. The grounds for such bans are extremely murky, and in many cases there would seem to be a large element of hysteria, whipped up by existing operators. This court activity will run and run, presumably reaching constitutional courts in many cases. Countries taking direct administrative action against Uber (bad marks for all of them) include Australia, France, India, South Korea, Spain, and Thailand. Government should get out of the way, stop interfering with individuals' freedoms to operate and use motor cars for hire, and concentrate on ensuring a fair and conclusive legal process. There can hardly be a person on the planet who thinks that traditional licensed taxi-drivers are anything other than a conspiracy against the public. Except the taxi-drivers themselves, of course.

It would be carping not to acknowledge Japan's reduction of its corporate tax rate, although it is no great shakes, and still leaves Japan towards the top end of the rates table, currently and ignominiously headed by the USA. It's difficult to believe though that it will be enough to inject real life into the moribund Japanese economy. So one has to ask: what will? And the question can be asked just as well of those European countries which are bidding fair to join Japan in its deflationary stasis. The answer is not to be found in macro-economic nostrums: economic growth happens because individuals make decisions to hire workers, take an entrepreneurial risk, or get a job, if one is available, and not because government pulls a lever. Governments like to think they can influence economies by taking macro-economic decisions, but they are wrong. What Japanese businessperson is going to alter their behavior even one jot because corporation tax has been reduced by a measly 2 percent? Ten percent, perhaps, but 2 percent? And any benefit gained from the reduction is more than wiped out by the reduction in loss offsets from 80 percent to 50 percent. Actually that is a swingeing tax increase of 10 percent for any profitable company with past losses. How can that possibly influence business investment? It is a tax rise, pure and simple. In Europe, of course, there is no question of lowering taxes; they need every penny they can find just to avoid looming default.

So we need to look at the reality of animal spirits at the individual level. Our Japanese hero, Shinzo Abe (no relation) is at breakfast with his wife Yuna. He operates a small sandwich bar, and has nearly finished paying off the loan he took from a local cooperative bank to buy the sandwich stand after losing his salarimen job. He is busy out of sight with corporate lunch orders. "It's getting you down," says Yuna, "You never laugh any more. And I never see you nowadays. Why don't you take on a helper?"

"You know why," says Shinzo. "I would have to install a toilet, and rest facilities. There is a minimum wage, there is payroll tax, there are social security payments. And there is consumption tax; we already have to charge a high price because of the cost of beef. What if the market gets weaker? If it all goes wrong and the worker is no good, it will cost a fortune to get rid of them, and I might not survive. Then our home would be in danger. It's just too risky."

"But can't you take on a freeter? What about that young lad from the next street, the one who cleans our windows? He wouldn't ask much."

"He's not trained," said Shinzo. "I did ask him, actually, but he lives with his parents and he wants a real job with a corporation. He's not too interested in hard work making sandwiches! If I took him and if he was willing, he would have to be a real employee, with insurance and all the other issues. There are apprenticeship programs, it's true, but he is already quite old. I'm sure he wouldn't want five years as a catering apprentice, and I am not qualified to be his master, anyway."

Very little has been done in Japan to encourage job formation in such situations: no subsidized loans; no entrepreneurial incentives; no tax breaks; no employment subsidies for individual entrepreneurs; no bankruptcy forgiveness or halfway-house insolvency legislation. Of course Shinzo will battle on, on his own, and of course he won't take on an employee. Yuna offers assistance from her aunt, who has recently been widowed, has a substantial pension, and is quite keen to have something to do to take her mind off her problems. She's a dab hand at sandwich-making after a lifetime of putting together her hubbie's lunch-boxes. Yuna will give her aunt small sums of money from her own quite handsome salary as a teacher, and they will get by. It will all be strictly unofficial, and completely outside the recorded economy, and of course no tax will be paid. But a small business with the capacity to become a larger business will be stultified, to no-one's benefit at all.

With minor differences, we could have been talking about almost any eurozone economy. Until governments get down and dirty with the reality of life as it is lived in the tenements of Naples, the banlieus of Marseilles and even the back streets of Dusseldorf, there won't be any answer to the problem. There has to be a bonfire of regulations, and widespread abandonment of taxation for start-ups; then, and only then will animal spirits ignite into a blaze of creativity and new jobs. Unfortunately, they are not capable of thinking that way in the Treasuries of Europe, and if they were, the unions and the lawyers would soon stop them.

The Jester