Wolters Kluwer

GLOBAL TAX WEEKLY
a closer look

ISSUE 128 | APRIL 23, 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

Wolters Kluwer

GLOBAL TAX WEEKLY
a closer look

Global Tax Weekly – A Closer Look

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

Unique contributions from the Big4 and other leading firms provide unparalleled insight into the issues that matter, from today's thought leaders.

Topicality, thoroughness and relevance are our watchwords: CCH's network of expert local researchers covers 130 countries and provides input to a US/UK team of editors outputting 100 tax news stories a week. GTW highlights 20 of these stories each week under a series of useful headings, including industry sectors (e.g. manufacturing), subjects (e.g. transfer pricing) and regions (e.g. asia-pacific).

Alongside the news analyses are a wealth of feature articles each week covering key current topics in depth, written by a team of senior international tax and legal experts and supplemented by commentative topical news analyses. Supporting features include a round-up of tax treaty developments, a report on important new judgments, a calendar of upcoming tax conferences, and "The Jester's Column," a lighthearted but merciless commentary on the week's tax events.

Wolters Kluwer

GLOBAL TAX WEEKLY
a closer look

ISSUE 128 | APRIL 23, 2015

CONTENTS

FEATURED ARTICLES

NEWS ROUND-UP

For article guidelines and submissions, contact GTW_Submissions@wolterskluwer.com

T1135 — The Saga Continues

by Maureen Vance CPA, CA, Tax Software Consultant, Wolters Kluwer

This article was published in 'Tax Topics', No. 2248, April 9, 2015.

Introduction

Last year, taxpayers and tax preparers alike were scrambling to compile the necessary information to complete the Canada Revenue Agency's ("CRA's") totally revamped T1135 – Foreign Income Verification Statement. The version of the T1135 for 2013 required much more detailed reporting than had been required in the past.

The pre-2013 version of the form required only that you check a box indicating the appropriate range for the total cost of foreign property held by the taxpayer. This meant that in many cases, prior to 2013, it was not necessary to determine exact costs for all specified foreign property (or even for certain properties that were, in fact, considered specified foreign property), especially if the amount in question would not change the checkboxes selected.

As a result, even though the definition of specified property had not changed from prior years, in most cases a lot more thought and effort had to go into the preparation of the T1135 after 2012.

But now that most taxpayers and/or their advisers have identified their specified foreign Federal property and determined the appropriate cost amounts last year, and given that the vast majority of filers only hold specified foreign property within Canadian investment accounts, then completing the T1135 for the 2014 return will be a piece of cake, right?

Well – maybe not.

Changes To The T1135 For 2014

The T1135 for 2014 no longer includes the T3/T5 exception. In 2013, this option allowed a taxpayer holding investments for which a T3 or T5 was issued to tick a box on the T1135 instead of having to provide detailed reporting on the cost of the property held along with the related income and/or capital gains and losses. As a result, some taxpayers who last year simply ticked one box on the T1135 are no longer able to do so.[1]

In addition, the Transitional Method of reporting investments with a registered Canadian securities dealer, which was introduced by the CRA at the

end of February 2014, has been replaced by the Aggregate Method. Under this method, the aggregate fair market value ("FMV") of all investments held with a registered Canadian securities dealer can be reported in lieu of detailed reporting of each investment held. New Category 7 was added to the T1135 for this reporting method. However, there are some important differences between the 2013 Transitional Method and the new Aggregate Method. Under the Aggregate Method, the taxpayer has to report not only the FMV at year end of the specified foreign property held with a registered Canadian securities dealer or Canadian trust company (as they would have done with the Transitional Method), but also the highest FMV held during the year (although the CRA will accept the highest month-end value). As well, this information must now be provided on a country-by-country basis. As with the Transitional Method, the taxpayer must disclose the related income and capital gains and losses.

Electronic Filing

On the positive side, the T1135 for individuals can now be electronically filed if the preparer is using tax software (such as Taxprep and Cantax) that has been approved by the CRA for the electronic filing of the T1135. While preparers appreciate the fact that by electronically filing the T1135, they now have, for the first time, an acknowledgement from the CRA that the T1135 has been filed, this does not reduce the burden of completing the T1135. Currently, only individuals are able to file the T1135 electronically. No timeline has been established yet for electronic filing to be made available for other entities (*i.e.*, corporations, trusts, and partnerships).

Note that the T1135 is transmitted to the CRA in a separate transmission file from the T1 transmission file, although in most tax programs (like Taxprep and Cantax) it can be transmitted at the same time as the T1 return, for the convenience of the tax preparer. For taxpayers whose T1 returns are not eligible for EFILE (*e.g.*, taxpayers with income from multiple jurisdictions), the T1135 can still be electronically transmitted.[2]

Information Available From Investment Dealers

Investment dealers have made considerable efforts to put systems in place to provide the information needed to complete the T1135, which was particularly challenging considering that the requirement to segregate investments on a country-by-country basis only became known when the revised form was issued last summer. However, tax preparers may find that the availability and quality of this information will vary greatly from one dealer to another, as well as between types of accounts.

For example, very little (if any) information appears to have been provided for taxpayers using many of the popular discount brokerage accounts. Even where there is information available, you may have to double-check to ensure that the properties have been properly classified. For instance, brokerage statements often classify Canadian mutual funds

with foreign investments as "Foreign Property" for purposes of asset allocation. However, Canadian mutual funds are not specified foreign property and are not to be reported on the T1135. Similarly, the brokerage statement may classify a property such as a foreign mutual fund or an exchange-traded fund ("ETF") according to the location of the investments rather than the location of the issuer of the mutual fund or ETF.

Reporting Threshold

Remember that brokers are, in most cases, providing the information needed to use the Aggregate Method – *i.e.*, the FMV of the investments. But the taxpayer is required to file a T1135 when the cost of the specified foreign property held exceeds CAD100,000 at any time during the year. So if the taxpayer held investments that were underwater, it is possible that the cost of the property held exceeded CAD100,000 during the year while the FMV did not.

Also remember that once taxpayers have surpassed the CAD100,000 cost threshold, they must include all specified foreign property on the T1135 – no matter how small. For example, a taxpayer with a foreign vacation property may have opened a local bank account to facilitate the transfer of funds. If the taxpayer already holds more than CAD100,000 in specified foreign property (such as US stock holdings), that foreign bank account would have to be disclosed in Category 1 on the T1135. Similarly, a taxpayer buying or selling a foreign vacation property that is not specified foreign property (because it is personal-use property) may still have a T1135 reporting requirement where more than CAD100,000 was on deposit in a foreign bank account at any time during the year for the purchase of the property or as proceeds from the sale.

CRA Clarifications

Over the past 18 months, many questions have been raised by taxpayers and their representatives not only about what constitutes specified foreign property, but about how to determine the cost base for certain types of property as well as clarifications on the disclosure required by the CRA.

Some answers can be found on the CRA web page "Questions and answers about form T1135." You can also find additional questions and answers *via* the Tax Blog on the CPA Canada website.[3] These are questions raised during the CPA Canada webinar on the T1135 held last November which the CRA has been gradually addressing. While a number of these questions relate to very specific types of investments, some of the inquiries are of a more general nature.

For example, in response to a question that has arisen frequently on the reporting requirements for a taxpayer who holds multiple accounts with a registered Canadian investment dealer, the CRA has indicated: "For the 2014 and subsequent tax years, a taxpayer is permitted to use the aggregate reporting method for some accounts and the detailed reporting method for other accounts regardless of whether these accounts are with the same brokerage firm."

Conclusion

By now, most taxpayers should have received whatever T1135 information is being provided by their investment adviser. In some cases, this may be all you will need to complete the T1135. However, where the necessary information has not been provided (*e.g.*, the highest monthly FMV of the specified foreign property may not be readily available without checking 12 months' worth of statements), you will have to ensure that you have budgeted sufficient time to prepare the T1135. And remember, unlike last year, there is no filing deadline extension for the T1135: the T1135 forms are due at the same time as the tax return for that taxpayer. For individuals, that is April 30 or June 15. Tick, tock.

Endnotes

1 The T3/T5 exception was actually not as straightforward as it first seemed, as it could not be used for shares where no dividends were paid during the year and also could not be combined with the Transitional Method. Some taxpayers may have therefore incorrectly filed their 2013 T1135 using this exception.

2 Regardless of whether the T1 is EFILED or paper-filed, if a T1135 is required, it must be filed with the CRA (either on paper or electronically). A misprint in the T1 Guide, which implied that if you were electronically filing your T1 you could simply retain the T1135 to be produced upon request, was corrected by the CRA in the online version of the T1 Guide.

3 *See* https://www.cpacanada.ca/en/connecting-and-news/blogs/tax-blog/2015/March/Some-answers-to-your-T1135-questions

DLA Piper Global Stock Options Overview: Western Europe — Part Two

by Dean Fealk, DLA Piper, San Francisco

Many companies today aim to scale their businesses globally and into multiple countries simultaneously. In order to help clients meet this challenge, DLA Piper has compiled a Guide To Global Equity Stock Options. In the second article in an ongoing series, we examine the tax, compliance, and other requirements in relation to equity stock options in seven Western European countries.

Ireland

Securities: The EU Prospectus Directive has been implemented into Irish law. As a general rule, non-transferable options are not considered a security subject to the Prospectus Directive. Even if options are considered securities that require a prospectus, they may nonetheless be exempt from the prospectus requirements (*e.g.*, the 150-person exemption).

Under the provisions of the Irish Companies Law, directors may be subject to additional reporting requirements.

Foreign Exchange: Options are not subject to any specific foreign exchange restrictions.

Tax:

Employee: The spread is taxable at exercise. The proceeds from the sale of the shares are taxable, although some exemptions apply.

Employer:

- *Withholding and Reporting:* Reporting is required.
- *Deduction:* If the subsidiary reimburses the parent company for the cost of the option benefits pursuant to a written agreement, it may be able to deduct such cost from its income taxes.

Tax-favored Treatment: Tax-favored treatment may be available.

Social Insurance: Social insurances are imposed on the spread.

Data Protection: In order to comply with certain aspects of data protection requirements, employee consent for the processing and transfer of personal

data is recommended. Registration with the Data Protection Commissioner may be required.

Labor Issues: Option benefits may be considered part of the employment relationship and may be included in the calculation of severance or retirement payments. To reduce the risk of claims, employees should expressly agree in writing that: (i) participation in the option plan is discretionary; and (ii) termination of employment will result in the loss of unvested rights. In addition, anti-discrimination rules need to be considered when awarding options.

Communications: Translation is not required. Any government filings must be in English. It should be valid for an employee to execute the award agreement electronically.

Italy

Securities: The EU Prospectus Directive is effective in Italy. Generally, non-transferable options are considered a security subject to the Prospectus Directive. Accordingly, unless an offer of options is otherwise exempt (*e.g.*, the 150-person exemption), a prospectus is required. Unless the full cashless exercise method is required, an Italian financial intermediary must be engaged to advise optionees on their rights under the plan.

Foreign Exchange: Reporting may be required for shares held outside Italy.

Tax:

Employee: The spread is taxable at exercise. The gain at sale is taxed as capital gain subject to annual exemption if certain conditions are met.

Employer:

- *Withholding and Reporting:* Withholding and reporting are required.
- *Deduction:* If the parent company is reimbursed by the subsidiary for the cost of the option benefits (*e.g.*, the spread) pursuant to a written agreement, the subsidiary should be able to deduct such cost from its income taxes.

Social Insurance: Social insurance contributions generally are not imposed on the spread.

Data Protection: In order to comply with certain aspects of existing data privacy requirements, it is recommended that an employee consent to the processing and transfer of personal data. Typically, no employee's personal information can be processed or transferred until the employer registers with Italy's data protection authorities.

Labor issues: Option benefits may be considered part of the employment relationship and may be included in the calculation of severance or retirement payments. To reduce the risk of claims, employees should agree in writing that: (i) participation in the option plan is discretionary; and (ii) termination of employment will result in the loss of unvested rights. In addition, anti-discrimination rules need to be considered when awarding options.

Communications: Although not required, it is recommended that all documents regarding option plans be translated. Any government filings are required to be translated.

The Netherlands

Securities: The EU Prospectus Directive has been implemented into Dutch law. Even if options are considered securities that require a prospectus, they may nonetheless be exempt from the prospectus requirements (*e.g.*, the 150-person exemption).

Foreign Exchange: Reporting may be required to the Central Bank for transfer of funds.

Tax:

Employee: Options that first vested on or after January 1, 2005 are subject to tax on the spread upon exercise. Generally, there is no tax upon the sale of shares. However, an annual investment tax may apply.

Employer:

- *Withholding and Reporting:* Withholding and reporting requirements apply.
- *Deduction:* A local tax deduction is no longer allowed.

Social Insurance: Social insurance contributions are imposed on option benefits to the extent an employee's income does not exceed a wage ceiling.

Data Protection: In order to comply with certain aspects of existing data protection requirements, it is recommended that employee consent be obtained for the processing and transfer of personal data. The employer also is required to register any database that includes an employee's personal data with the Dutch data protection authorities.

Labor Issues: In order to reduce the risk of employee claims, the award agreement signed by an employee should provide, among other things, that vesting of an option ceases upon termination of employment and that the plan and any awards under it are discretionary. In addition, anti-discrimination rules need to be considered when awarding options.

If the Dutch employer has a works council, it may be necessary to notify the works council prior to an award. The approval of a works council may be needed to terminate a plan.

Communications: Although plan materials are not required to be translated, translation is required for any government filing and is recommended to ensure that employees understand the terms of their awards. It is generally acceptable for award agreements to be electronically executed.

Portugal

Securities: The EU Prospectus Directive has been implemented into Portuguese law. Even if options are considered securities that require a prospectus, they may nonetheless be exempt from the prospectus requirements (*e.g.*, the 150-person exemption).

Foreign Exchange: Minor reporting requirements may apply.

Tax:

Employee: The spread is taxed upon exercise. The gain from the sale of shares is taxed.

Employer:

- *Withholding and Reporting:* Tax withholding generally is not required. Reporting requirements may apply.
- *Deduction:* Reimbursement of the parent company by the subsidiary for the cost of the option benefits (*e.g.*, the spread) should enable the subsidiary to deduct such cost from its income taxes.

Social Insurance: The benefits from options are not likely to be subject to social insurance contributions.

Data Protection: In order to comply with certain aspects of existing data protection requirements, it is recommended that employee consent be obtained for the processing and transfer of personal data. Generally, the employer also is required to register any database that includes an employee's personal data with the Portuguese data protection authorities. The transfer of personal data abroad requires approval from Portugal's data protection authorities.

Labor Issues: To decrease the likelihood of claims for employee entitlements, in the option agreement evidencing the grant employees should expressly agree that: (i) participation in the option plan is discretionary; and (ii) termination of employment will result in the loss of unvested rights. In addition, anti-discrimination rules need to be considered when awarding options.

Communications: Although not legally required, it is recommended that documents regarding employee option plans be translated. Any filing with the government must be translated. In most circumstances, it is acceptable for award agreements to be electronically executed.

Spain

Securities: The EU Prospectus Directive has been implemented into Spanish law. As a general rule, non-transferable options are not considered securities subject to the Prospectus Directive. Even if options are considered securities that require a prospectus, they may nonetheless be exempt from the prospectus requirements (*e.g.*, the 150-person exemption).

Foreign Exchange: Residents are required to declare their foreign securities interests annually (solely for statistical and administrative purposes).

Tax:

Employee: The spread is taxed at exercise subject to certain exemptions. The gain from the sale of the shares is taxable.

Employer:

- *Withholding and Reporting:* Generally, withholding requirements apply.
- *Deduction:* Reimbursement of the parent company for the cost of the option benefits (*e.g.*, the spread), pursuant to a written agreement, should enable the subsidiary to deduct such cost from its income taxes.

Tax-favored Treatment: Tax exemptions are available subject to specific criteria such as shareholding periods, ownership limitations, and irregular grants.

Social Insurance: The spread at exercise is subject to social insurance contributions subject to a ceiling and exemptions.

Data Protection: Obtaining employee consent for the processing and collection of personal data is recommended. In addition, the employer must register its database with the data protection authorities.

Labor Issues: Spanish labor courts have ruled favorably for employee claims for option benefits. To reduce the risk of claims, employees should agree in writing that: (i) participation in the option plan is discretionary; and (ii) termination of employment will result in the loss of unvested rights. In addition, anti-discrimination rules need to be considered when awarding options.

Communications: Although not legally required, it is recommended that documents regarding employee option plans be translated. Any government and legal filings are required to be translated. In some circumstances, it may be acceptable for award agreements to be electronically executed.

Switzerland

Securities: There generally are no specific securities requirements so long as options are awarded only to employees and the shares issued are not listed on a Swiss exchange.

Foreign Exchange: Options are not subject to any specific foreign exchange restrictions.

Tax:

Employee: Options generally are taxed at exercise, pursuant to Swiss federal tax law. There generally is no tax on the sale of shares, but wealth tax may apply.

Employer:

- *Withholding and Reporting:* The employer must withhold and report for employees with B permits. Reporting is required on an annual salary statement for employees with C permits and residents;
- *Deduction:* Reimbursement of the parent company by the subsidiary for the cost of the option benefits (*e.g.*, the spread) pursuant to a written agreement should enable the subsidiary to deduct such cost from its income taxes.

Social Insurance: The spread is subject to social insurance.

Data Protection: Obtaining written consent from employees is recommended prior to transferring any personal information to the parent company or a third-party administrator.

Labor Issues: Although not common, option benefits may be considered part of the employment relationship and may be included in the calculation of severance or retirement payments. To reduce the risk of claims, employees should expressly agree in writing that: (i) participation in the option plan is discretionary; and (ii) termination of employment will result in the loss of unvested rights.

Communications: Although it is not legally required, it is recommended that documents regarding employee option plans be translated. Any filings with the government are required to be translated.

United Kingdom

Securities: The EU Prospectus Directive has been implemented into British law. As a general rule, non-transferable options are not considered transferrable securities subject to the Prospectus Directive. Even if options are considered securities that require a prospectus, they may nonetheless be exempt from the prospectus requirements (*e.g.*, the 150-person exemption).

Foreign Exchange: Options are not subject to any specific foreign exchange restrictions.

Tax:

Employee: The spread generally is taxed at exercise. The gain from the sale of the shares is taxable, subject to an annual exclusion.

Employer:

- *Withholding and Reporting:* Withholding is required for options if shares are deemed "readily convertible assets." Registration and annual reporting is required.
- *Deduction:* A local tax deduction generally is allowed.

Tax-favored Treatment: Tax-favored programs are available for options.

Social Insurance: National Insurance Contributions ("NICs") are due on the spread at exercise if shares are deemed "readily convertible assets."

Through an approved Joint Election or other contractual arrangement, the employer NICs obligation may be transferred from the employer to the employee.

Data Protection: In order to comply with certain aspects of the restrictions on the transfer of personal data, employee consent to the processing and transfer of personal data is recommended. Employers must register their data processing activities.

Labor Issues: Option benefits may be considered part of the employment relationship and may be included in the calculation of severance or retirement payments. To reduce the risk of claims, employees should agree in writing that: (i) participation in the option plan is discretionary; and (ii) termination of employment will result in the loss of unvested rights. In addition, anti-discrimination rules need to be considered when awarding options.

Communications: Employee communications are not subject to any specific legal requirements. In some circumstances, it may be acceptable for award agreements to be electronically executed.

it. This is a general reference document and should not be relied upon as legal advice. The application and effect of any law or regulation upon a particular situation can vary depending upon the specific facts and circumstances, and so you should consult with a lawyer regarding the impact of any of these regimes in any particular instance.

DLA Piper and any contributing law firms accept no liability for errors or omissions appearing in this publication and, in addition, DLA Piper accepts no liability at all for the content provided by any contributing lawyers. Please note that privacy and information law is dynamic, and the legal regime in the countries surveyed could change. No part of this publication may be reproduced or transmitted in any form without the prior consent of DLA Piper.

Ms. Fournie Shows Fortitude In Fight Against IRS

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

Undeclared accounts are the latest bane for Swiss banks, which are being pushed to the brink by US authorities to release details of their US accountholders who park assets there in order to avoid paying US taxes. Many Swiss banks have what are referred to derogatively as "recalcitrant accountholders." Recalcitrant accountholders are those who, despite the bank's prodding, refuse to report their foreign accounts to the IRS. Very simply, this group is what stands in the way of a "cooperating" bank opening up the kimono – *i.e.*, by sending the US government the records of its US accountholders – and the pot of gold at the end of the rainbow: immunity from prosecution and overbearing penalties. Soon, the Foreign Account Tax Compliance Act (FATCA) will change all that. If the United States' demands to expose tax-evaders are fulfilled, all data on these recalcitrant accounts will be within the possession of the IRS in a matter of days.

The French Connection

Among those resisting the FATCA is Micheline Fournie, a French citizen with a US residency permit. Her mother was named as the beneficiary of her friend Maurice Pinot's will, who had deposited FFR1m in an account at Swiss Bank Corporation before he died. The bank was a predecessor to UBS AG, and when Liechtenstein's LGT Group acquired the latter for its Swiss banking unit, they acquired Mr. Pinot's account as well.

Ms. Fournie's mother was entitled to receive the dividends and interest from the capital amount. After her mother died, Ms. Fournie continued to receive them. Ms. Fournie has no rights to the capital itself, which is destined for charity after her death.

Ms. Fournie, now 81 and a French citizen with a green card, is being urged by the bank to declare the account to the Internal Revenue Service (IRS). She has resisted their requests so far, requests that have come from great urgency: the US is investigating all Swiss banks that are "abetting" citizens in evading US taxes. For her part, Ms. Fournie insists that the bank should provide her with more details about Mr. Pinot's account, which credited her US account with USD15,924 only in January 2008. She contends that Mr. Pinot's account has been mismanaged and she deserves more details about the structure of the account.

United States vs. Swiss Banks

Swiss banks have historically helped clients from all over the world funnel their cash into accounts that eluded local taxing authorities. Foreign accountholders could take comfort in the fact that these accounts were kept hidden by Switzerland's time-honored tradition of bank secrecy. By "hidden," what I mean is that they were numbered accounts, or anonymous accounts, that could not be easily traced to their true owners.

Many of these clients were American, and the IRS was not going to take that lying down. Six years ago, the US unleashed an investigation on a level that has not been seen in decades. That probe resulted in the "take down" of some wildly popular Swiss banks with storied traditions that the US branded "aiders and abettors" of US tax evasion. These banks suffered the worse fate of all. They became ensnared in the coils of the US justice system and were prosecuted so aggressively that they were unable to live to fight another day. The tentacles of the US government had pierced a hole that was so deep that it ultimately led to their demise.

This was not lost on other Swiss banks. And how could it be? With all the media coverage, they would have had to be buried deep inside a bunker not to know what was going on. Indeed, not a day went by that the media didn't recount the salacious details of how HSBC assisted its US clients in hiding their foreign accounts from the IRS. Not wanting to become the next cooked goose lying on the IRS's table, many Swiss banks have begun waiving the white flag.

They have entered a US Justice Department self-reporting program that on its face purports to offer two enticing guarantees: immunity from prosecution and from hefty penalties (both criminal and civil). But this does not come without a price. In order to qualify, Swiss banks must disclose their US clients' accounts to the IRS. And therein lies the problem.

Given the choice, the vast majority of US clients would prefer not to have their bank disclose their account information to the US government. While the reasons for this might appear obvious, it's worth taking the time to recount them. Consenting to the disclosure of account information that has gone unreported is the equivalent of giving the IRS the ammunition that it needs to prosecute a US person for willfully failing to file a Foreign Bank Account Report (FBAR) and/or to assert onerous FBAR penalties, willful or otherwise. In the worst case scenario, it could cost the taxpayer his freedom. And in the best case scenario, it could leave the taxpayer with nothing more than the shirt on his back.

A bank that decides to participate in the self-reporting program will automatically be thrust into the role of "enforcer," in the sense that they must put the feet of their US accountholders to the fire in order to get them to declare their foreign accounts. Otherwise, they won't be able to live up to their end of the bargain with the US government. Essentially, the bank becomes the enforcement arm of the US Treasury, forced to do its "dirty work." In exchange, the bank obtains a rather illusory guarantee of immunity from prosecution along with financial incentives.

If you're wondering why Swiss banks don't just automatically turn over the names and details of their US accountholders to the US government and why they must first go through the rigmarole of obtaining the consent of their US accountholders, you've identified a critical issue. While Swiss bank secrecy has been mortally punctured with enough blows to render it virtually obsolete, it still presents a formidable barrier to Swiss banks reporting the accountholder information of un-consenting foreign clients to their respective taxing authorities. US accountholders are no exception.

While Swiss banks are far from thrilled over the role that they have been cast in, they also recognize that it is better than the alternative: *not* participating in the government's self-reporting program at all. Those banks that remain on the sidelines, choosing instead to protect their clients' identities from US authorities than to submit to the United States' strong-armed demands, do so at their own peril.

While they might be hailed as "martyrs," the fact remains that they risk being the next cooked goose on the IRS's table. They could become the target of a US investigation that is more probing than a TSA examination, not to mention criminal prosecution and penalties that could blow the roof off of the Taj Mahal (the US government calculates penalties based on the amount of undeclared US money on the bank's books).

As for US accountholders with unreported Swiss accounts, they are feeling the heat too. With the threat of prosecution hanging over their heads like the Sword of Damocles, it should come as no surprise that many US accountholders have come out of the shadows to voluntarily disclose their foreign accounts to the IRS.

And they have every incentive in the world to do so. Why? If the IRS discovers that a US taxpayer has an unreported foreign account before he voluntarily discloses it, then it is too late for the taxpayer to participate in any of the IRS's voluntary disclosure programs. And by voluntary disclosure programs, I am not only referring to the Offshore Voluntary Disclosure Program (OVDP), but also the streamlined procedures.

The analogy that I like to use here is that if the bloodhound has already caught the scent of the fox and is hot on his trail, then the fox is "squat." No amount of pleading will save the fox from the sharp and carnivorous teeth of the salivating bloodhound. Similarly, the taxpayer risks a number of parade of horribles, from audit to investigation to prosecution to cataclysmic FBAR penalties.

Once again, the mass media has played its part by reporting recent cases involving US citizens who were prosecuted for offshore tax evasion. Notwithstanding all of this, Milan Patel, a Zurich-based attorney, estimates that there are thousands, and possibly tens of thousands of recalcitrant accounts in Switzerland. He expressed surprise that in spite of all the pressure from the US government, Americans hold unreported accounts in Switzerland.

This is wreaking havoc on Swiss banks that have signed on to the self-reporting program. Saddled with a hopeless number of US accountholders who have resisted any and all attempts to disclose, these banks have resorted to such draconian measures as closing the accounts of all recalcitrant taxpayers rather than risk being unable to satisfy their end of the bargain.

While drastic times call for drastic measures, participating Swiss banks might be able to breathe a sigh of relief. Why? Tax professionals predict that the US government might be willing to cut banks some slack *vis-à-vis* their inability to prod their recalcitrant accountholders into disclosing so long as they have at least made a good faith attempt at doing so.

However, Swiss banks should not pop open the cork on the bottle of champagne so quickly. Those that get carried away by indulging in the fantasy that if they have at least urged a US accountholder to disclose but were unsuccessful, that it is no longer the bank's problem, will be in for a rude awakening. Indeed, it is very dangerous for the bank to brazenly sit back and argue, "we did all we could do but threw in the towel when we realized that it was an exercise in futility."

Returning to Ms. Fournie, it is not a matter of "if," but "when" her account will come to the attention of the IRS. Why? Thanks to FATCA, Swiss banks were obliged to send data on recalcitrant accounts – including Ms. Fournie's – to the IRS by the end of March 2015.

What does this mean for Ms. Fournie? If the US government learns about her undisclosed account before she voluntarily discloses it, not only will she become ineligible to participate in any of the IRS's voluntary disclosure programs, but she could be prosecuted criminally if the IRS is able to marshal together enough badges of fraud to establish that her failure to file an FBAR was willful.

Even if the government chooses not to prosecute Ms. Fournie, the IRS could assert onerous FBAR penalties for every year – within the statute of limitations period – that she failed to report the account. Of course, there is no statute of limitations when it comes to non-filing. Therefore, the IRS could theoretically go back to time and memorial to assert FBAR penalties. This could catapult Ms. Fournie's FBAR penalties into the penalty stratosphere.

Ironic Twist

An ironic twist to all of this is that Liechtenstein's LGT Group, the bank holding Mr. Pinot's account, does not participate in the US Justice Department's self-reporting program, despite the fact that its CEO is the son of Liechtenstein's head of state.

Notwithstanding, it has made (and continues to make) covert and ominous demands to Ms. Fournie to declare the account, telling her that her continued defiance puts her at "serious risk." US officials had earlier described LGT as "a willing partner" to tax evaders.

Conclusion

Despite its reluctance to bow under pressure and turn over the details of Ms. Fournie's accounts, insiders believe that LGT will be able to avoid the

IRS's chopping block (*i.e.*, the penalties borne by indicted Swiss banks).

Because the bank had informed Ms. Fournie about her legal obligation to disclose her account, it is not responsible for her subsequent refusal. Ms. Fournie now finds herself between a rock and a hard place. She has to weigh the cost of making a voluntarily disclosure against doing nothing.

While doing nothing might appear to be harmless, it has risks far greater than can be imagined. If the US authorities obtain Ms. Fournie's account details before she voluntarily discloses them, she is likely to be handed a hefty fine, and may even be indicted for willfully failing to file an FBAR. She should perhaps take a page out of the playbook of those Americans who have sought to "get right" with Uncle Sam by making a streamlined submission or seeking shelter in the OVDP bunker.

While the future is uncertain for Ms. Fournie – in the same way as it was for Anakin when Obi-Wan introduced him to Yoda for the first time: "Clouded, this boy's future is. Masked by his youth" – one thing is clear. The fact that LGT has frozen Ms. Fournie's account, coupled with her insistence on the bank clearing their own position on Mr. Pinot's account first, will give the US all the time that it needs to conduct its own investigation of Ms. Fournie's overseas assets.

Ms. Fournie has since moved back to France and has her son, David Fournie, at her side. David staunchly asserts that "This is going to be the last recalcitrant account to come out of Switzerland." From where I come from, "them's fightin' words!"

Topical News Briefing: Act In Haste, Repent At Leisure

by the Global Tax Weekly Editorial Team

There is widespread agreement among tax commentators and interested parties that the UK's new Diverted Profit Tax (DPT), dubbed the Google Tax, jumps the BEPS starting gun, has been rushed into law without proper consideration, and is generally a bad idea. All, that is, except the British Government itself. And now its Australian counterpart.

Given the complexity of the DPT and its likely impact on commercial transactions, the legislation had a relatively short route towards its introduction on April 1, 2015; the 25 percent tax was first announced in the 2014 Autumn Statement last December and was confirmed in the 2015 Budget in March, after a consultation on the measure that concluded in February. Following the consultation, the Government revised the draft legislation by narrowing its scope somewhat and clarifying certain provisions. The tax was introduced on April 1 but was no April Fool's prank.

The DPT is supposed to apply in two broad circumstances: when a foreign company structures its affairs to avoid the creation of a UK permanent establishment; or when a UK entity obtains a UK tax advantage as a result of transactions lacking economic substance. However, the feeling remains within the business community that the DPT could catch many everyday business transactions, and there is also uncertainty about how the DPT squares with the UK's large network of double tax avoidance treaties.

It's not as if the Government hasn't been warned about the consequences of botching the DPT. In February, the Confederation of British Industry warned that the legislation will affect many groups that do not engage in abusive tax arrangements, with the Confederation saying they will face, "at best, an additional layer of compliance, and, at worst, an erroneous tax liability." Parliament's influential Treasury Select Committee recently described the DPT legislation as "long and highly complex." And the Institute of Directors (IoD) observed that the DPT goes against the grain of the Government's tax-cutting agenda for business. Even the OECD, in more diplomatic tones, suggested that the UK should have waited for the final BEPS recommendations, due in December 2015, before deciding whether to unleash the DPT on the world.

It all points to a Government in an especial rush to push this measure through. Why? The IoD thinks the reason is a politically motivated one. There's a general election on May 7, and public antipathy towards multinational corporations has probably never been greater. The Government simply didn't have time for a long consultation process, it says.

The other danger of the UK legislating early to bring the DPT to life is that it has set a precedent other countries may follow, with their own country-specific peculiarities. Australia has been keen on the DPT idea since it was first announced last year and looks likely to follow the UK's lead, given the two countries' joint announcement, reported in this week's *Global Tax Weekly*, to consider issues arising from the DPT. The idea has prompted similar criticisms to those directed at the UK Government in Australia, with Rosheen Garnon, KPMG's National Managing Partner, Tax, telling a recent Senate inquiry on corporate tax avoidance that, at this stage, an Australian DPT could be "very dangerous." She pointed out that the UK had introduced a DPT "for a very political purpose," and cautioned that if Australia followed suit, other jurisdictions would too.

The embattled Australian Government, lacking a Senate majority, coping with a slump in tax revenue, and down on its popularity, could do with a fillip. It's probably gambling, like UK Chancellor George Osborne, that the DPT might do the Government more good in terms of political capital than harm in terms of lost foreign investment. However, the Australian Government isn't facing the prospect of contesting a general election imminently and so has time to consider its options. Given that the UK is effectively going to be a laboratory for this type of tax over the next year or two, Australia might be wise to sit on the sidelines and see how this experiment pans out.

New Russian CFC Rules Will Impact Inbound US Tax Planning

by Jeffrey Rubinger, Bilzin Sumberg

Contact: jrubinger@bilzin.com, Tel: +1 305 350 7261

According to recent estimates, the number of wealthy Russians investing in the United States ballooned in 2014 as a result of political turmoil and a disintegrating ruble causing Russians to seek a safe haven for their wealth abroad. The amount of private net capital flowing out of Russia hit USD120bn by the end of 2014, according to a recent report. That projection would nearly double the USD61bn in outflows Russia saw in 2013, according to data from the Russian Central Bank.

The primary investment sought by wealthy Russians typically has been US real estate in cities such as New York and Miami. From a US federal income tax perspective, the main obstacle facing foreign persons who invest in US real estate is the Foreign Investment in Real Property Act (FIRPTA), more specifically Section 897. Under this provision, any gain recognized by a foreign person on the disposition of a "United States real property interest" (USRPI) will be treated as if such gain were effectively connected to a US trade or business and, therefore, subject to US federal income tax at the graduated rates that apply to US persons. Additionally, when Section 897 applies, the purchaser of a USRPI typically is required to withhold and remit to the IRS 10 percent of the purchase price in accordance with Section 1445.

Typical Structure For US Real Estate Investment

A recent *New York Times* article indicates that many of the real estate investments are structured through "shell" companies, such as LLCs and partnerships. Historically, this would allow the Russian investor to hide their cash in real estate without needing to disclose their ownership to the Russian tax authorities.

For example, a typical inbound real estate structure by a Russian investor may involve establishing a US LLC to acquire the property (the LLC likely will be treated as a corporation for US tax purposes and serve as a "blocker" corporation) and a company established in a low-tax jurisdiction, such as the British Virgin Islands (BVI), that would lend money to the US LLC in an attempt to strip out a large portion of the income or gain from the sale of the property in the form of deductible interest (subject

to the Section 163(j) "interest stripping" provisions that seek to minimize the amount of deductible related party interest that is allowed where no US tax is imposed on such interest).

This structure allows the Russian investor to minimize the US federal income tax consequences of an investment in US real estate, which in many cases could be as high as 54.5 percent (when taking into account the US corporate income tax rate of 35 percent plus the 30 percent branch profits tax) while at the same time avoid having to file a US income tax return. As discussed below, however, the recent enactment of Russian controlled foreign corporation (CFC) rules certainly will have an impact on the type of structures used by Russians to invest in US real estate.

Russian CFC Rules

The Russian CFC rules, which were effective from January 1, 2015, require Russian tax residents (individuals and companies) to disclose their foreign ownership and to pay tax on profits generated by CFCs (even before such profits are distributed to Russia). The tax rate will be 20 percent for Russian corporations and 13 percent for Russian individual residents. Russia will allow, however, a foreign tax credit for withholding taxes incurred in the jurisdiction of the CFC. Beginning in 2018, penalties also will be imposed in Russia for failure to disclose the ownership of a CFC and failure to report the income attributable from the CFC.

A foreign company will be considered a CFC for Russian tax purposes if: (i) the foreign company (which includes a fund/foundation, partnership, trust or other form of collective investment or trust management that is entitled to conduct profit generating activities) is not a Russian tax resident; and (ii) the Russian tax resident owns more than 25 percent of the company (in 2015, more than 50 percent), or more than 10 percent if the aggregate ownership of all Russian tax residents in the CFC exceeds 50 percent. Russian tax residents also will be considered as controlling persons (regardless of the level of their ownership) if they have the ability to control or influence decisions regarding the distribution of profits of the CFC.

Certain profits of a CFC, however, will be exempt from Russian taxation, including (i) profits derived by a CFC established in member countries of the Eurasian Economic Union (which includes Russia, Belarus, Kazakhstan, and Armenia); (ii) profits of a CFC that is resident in a jurisdiction that has a tax treaty with Russia (it is not clear whether this is limited to income tax treaties or also includes exchange of information treaties) and the effective tax rate in the jurisdiction where the CFC is resident is at least 75 percent of the average Russian weighted tax rate; and (iii) profits of a CFC that is resident in a double tax treaty country if the passive income of the CFC does not exceed 20 percent of its total income.

Implications And Alternative Planning

With the enactment of the new CFC rules in Russia, the use of a leveraged US blocker entity along with a BVI company to strip out a large portion of the US source income in a tax-free manner no

longer will be the most tax efficient strategy. Under the CFC rules, the Russian investor will be required to report the ownership of the BVI company and will be required to pay tax currently on the income of such entity whether or not that income is distributed. Given that the effective US income tax rate at the blocker level will be somewhere close to 17 percent and these taxes will not be creditable against the Russian tax incurred under the CFC rules, other structures certainly would seem to be more tax efficient.

One such structure may be for the Russian investor to simply lend money to the US real estate venture and take back a "shared appreciation mortgage" (SAM) (*i.e.*, a loan that contains an equity kicker feature). In a typical SAM arrangement, a lender provides a developer with a loan bearing a below-market fixed rate of interest, plus a share of the profit on a subsequent disposition of the property. SAMs were popular in the 1970s and 1980s when interest rates were in the double digits, but became less attractive as interest rates declined. Fueled by rising housing prices, however, SAMs would appear to be an attractive option, especially with their tax treatment under FIRPTA and certain provisions of the US–Russia income tax treaty (the "Treaty").

As stated above, Section 897 treats any gain recognized by a foreign person on the disposition of a USRPI as if it were effectively connected to a US trade or business. A USRPI is broadly defined as: (1) a direct interest in real property located in the US, and (2) an interest (other than an interest solely as a creditor) in any domestic corporation that constitutes a US real property holding corporation (*i.e.*, a corporation whose USRPIs make up at least 50 percent of the total value of the corporation's real property interests and business assets). Regulation Section 1.897-1(d)(2)(i) elaborates on the phrase "an interest other than an interest solely as a creditor" by stating it includes "any direct or indirect right to share in the appreciation in the value, or in the gross or net proceeds or profits generated by, the real property." The Regulation goes on to state:

> "A loan to an individual or entity under the terms of which a holder of the indebtedness has any direct or indirect right to share in appreciation in value of, or in the gross or net proceeds or profits generated by, an interest in real property of the debtor is, in its entirety, an interest in real property other than solely as a creditor."

This principle is illustrated by example in Regulation Section 1.897-1(d)(2)(i). In the example, a non-US taxpayer lends money to a US resident to use in purchasing a condominium. The nonresident lender is entitled to receive 13 percent annual interest for the first ten years of the loan and 35 percent of any appreciation in the fair market value of the condominium at the end of the ten-year period. The example concludes that, because the lender has a right to share in the appreciation of the value of the condominium, he has an interest other than solely as a creditor in the condominium (*i.e.*, a USRPI).

Accordingly, a SAM that is tied to US real estate is a USRPI for purposes of Section 897. Simply owning a USRPI, however, does not necessarily trigger any adverse tax consequences under Section 897. Rather, a non-US taxpayer will be subject to tax under that provision only when the USRPI is "disposed of." Although Section 897 does not define "disposition," Regulation Section 1.897-1(g) provides that disposition "means any transfer that would constitute a disposition by the transferor for any purpose of the Internal Revenue Code and regulations thereunder."

With respect to SAMs, Regulation Section 1.897-1(h), Example 2, illustrates a significant planning opportunity for non-US taxpayers investing in US real estate. In the example, a foreign corporation lends USD1m to a domestic individual, secured by a mortgage on residential real property purchased with the loan proceeds. Under the loan agreement, the foreign corporate lender will receive fixed monthly payments from the domestic borrower, constituting repayment of principal plus interest at a fixed rate, and a percentage of the appreciation in the value of the real property at the time the loan is retired.

The example states that, because of the foreign lender's right to share in the appreciation in the value of the real property, the debt obligation gives the foreign lender an interest in the real property "other than solely as a creditor." Nevertheless, the example concludes that Section 897 will not apply to the foreign lender on the receipt of either the monthly or the final payments because these payments are considered to consist solely of principal and interest for US federal income tax purposes.

Thus, the example concludes the receipt of the final appreciation payment that is tied to the gain from the sale of the US real property does not result in a disposition of a USRPI for purposes of Section 897 because the amount is considered to be interest rather than gain under Section 1001. The example does note, however, that a sale of the debt obligation by the foreign corporate lender will result in gain that is taxable under Section 897.

By characterizing the contingent payment in a SAM as interest (and not a disposition of a USRPI) for tax purposes, the Section 897 Regulations potentially allow non-US taxpayers to avoid US federal income tax on gain arising from the sale of US real estate, if structured correctly. Non-US taxpayers generally are subject to a 30 percent withholding tax (unless reduced by treaty) on certain passive types of US source income, including interest.

An important exception to this rule exists for "portfolio interest," which is exempt from withholding tax in the US. Portfolio interest, however, does not include certain "contingent interest." For this purpose, contingent interest is defined as interest that is determined by reference to any of the following: (i) any receipts, sales, or other cash flow of the debtor or related person; (ii) any income or profits of the debtor or a related person; (iii) any change in value of any property of the debtor or a

related person; (iv) any dividend, partnership distribution, or similar payments made by the debtor or a related person; and (v) any other type of contingent interest that is identified in Regulations, where a denial of the portfolio interest exemption is necessary or appropriate to prevent avoidance of federal income tax.

Therefore, a payment on a SAM that is otherwise treated for US federal income tax purposes as interest will not qualify for the portfolio interest exemption if the payment is contingent on the appreciation of the financed real property. Accordingly, unless a treaty applies to reduce the withholding tax, the contingent interest feature of a SAM would be subject to a 30 percent withholding tax in the US.

This is where the Treaty comes into play. Under Articles 10 and 11 of the Treaty, all interest, including contingent interest, is exempt from US withholding tax, so long as the interest is not recharacterized as a dividend under US tax law. As noted above, the FIRPTA regulations clearly indicate that contingent interest on a SAM will be respected as interest and will not be characterized as a dividend simply because of the contingent nature of the payment.

As a result, so long as the other requirements of the Treaty (including the "Residence" and "Limitations on Benefits" provisions) are satisfied, a Russian investor lending money to a US real estate venture should be able to participate in the upside of the venture without being subject to the FIRPTA provisions and also avoid the Russian CFC rules. (Of course, the Russian investor will have to report the income generated from the US real estate project in Russia (but not necessarily repatriate such income to a Russian bank account), but with individual tax rates in Russia being only 13 percent at the present time, such an arrangement certainly will be more tax efficient than most other structures. In addition, US estate tax also will need to be considered if this structure is utilized by an individual Russian resident because a debt instrument with a contingent interest feature will be treated as a US-situs asset and therefore subject to US estate tax unless further planning were done.)

UK Election 2015: An Uncertain Future For Britain

by Stuart Gray, Senior Editor, Global Tax Weekly

Compared with some of its neighbors across the English Channel, the United Kingdom currently looks like a paragon of stability and growth. The outlook for economic and fiscal policy has, however, become anything but certain as the political parties prepare to contest the May 7 general election, the outcome of which is shaping up to be one of most unpredictable in modern UK electoral history.

Background

Although the UK still has a relatively large budget deficit and rising public debt – a hangover from the banking crisis of 2008 onwards – the Conservative/ Liberal Democrat coalition in power since 2010 has seemingly steadied the ship, halving the deficit, cutting taxes for low-income workers, slashing corporate tax for businesses, and presiding over a return to respectable rates of economic growth. Ordinarily, this track record would probably be sound enough to ensure that the Tories were returned to power ahead of their main opposition, the Labour Party. However, this is no ordinary election. Minority parties, notably the anti-EU UK Independence Party (UKIP) and the Scottish National Party (SNP), have emerged, experienced rapid growth in popularity, and are expected to take substantial numbers of votes away from the three main parties.

Under such a scenario, it is anyone's guess what color, or combination of colors, the next government will be. However, with the parties now having released their election manifestos, an attempt can at least be made to weigh up what might be in store for taxpayers in the UK come May 8. In the next sections, the tax pledges of the Conservatives, Labour, the Liberal Democrats (LibDems), UKIP, and the SNP are summarized, with their policies with regards the EU – with the UK's membership a topic of serious debate – also referenced. With the devolution of powers to the constituent countries of the UK well under way, a description of new tax rules in Scotland, Wales, and Northern Ireland is included in the following sections.

Conservatives

The Conservative Party manifesto confirms several pre-election promises. It includes a commitment to raise the personal (tax-exempt) allowance to GBP12,500 (USD18,439) and the threshold for the 40 percent income tax rate to GBP50,000. It also includes plans to increase the effective inheritance

tax threshold for married couples to GBP1m. National Insurance (social security) rates will also be left on hold.

Having cut corporate income tax from 28 percent at the beginning of the current parliament in 2010 to 20 percent this year, the Conservatives are not planning any further cuts to business taxation, beyond the extension and improvement of certain tax relief schemes announced in last month's Budget. However, the Conservatives would conduct a review of business rates (local business tax) by the end of 2015.

Another important factor to note is the Conservatives' pledge to hold a referendum on the UK's EU membership by the end of 2017, the result of which could have a major impact on tax policy in future years.

Labour

A UK Labour Government would not raise value-added tax (VAT), national insurance rates, or the basic or higher rates of income tax. But predictably, there is much stress on "fairness" in the tax section of the Labour manifesto, with tax cuts lined up for those on low incomes and tax rises targeted towards the wealthiest.

On personal income tax, Labour would reintroduce the 10 percent starting rate of tax and abolish the marriage tax allowance. The basic and higher rates of tax would remain at 20 percent and 40 percent respectively, but the top rate would be restored to 50 percent from its current level of 45 percent.

In the area of corporate tax, Labour would reverse the 1 percent rate reduction which took place earlier this month (at least that is what its manifesto seems to suggest), but cut business rates by some unspecified amount to help small businesses.

Other taxes will rise or be created to pay for Labour's promises to boost National Health Service funding and to subsidize higher education, among other spending commitments. These include a so-called "mansion tax" on properties worth more than GBP2m, a threshold which would rise in line with house price inflation. Those on lower incomes would be able to defer this tax until the property changes hands. Another revenue-raising measure would see "non-domiciled" personal income tax status abolished in a bid to ensure wealthy long-term residents of the UK pay tax on their worldwide income.

A Labour Government would also pursue a crackdown on tax avoidance and evasion to raise an additional GBP7.5bn a year. Included in Labour's ten-point plan would be new penalties for those who are caught by the General Anti-Abuse Rule and a requirement that "dormant companies" report more frequently. The UK's Overseas Territories and Crown Dependencies would be required to produce publicly available registries of beneficial ownership, and country-by-country information would be made publicly available.

Labour are a pro-EU party and have pledged to hold a referendum on the EU only in the event of a major transfer of new powers from London to Brussels.

Liberal Democrats

The LibDems' tax policy is centered on a principle of "rebalancing" the tax system away from taxing work and towards the taxation of "unearned wealth." However, the party's manifesto contains only three main tax commitments.

The first is a pledge to increase the personal tax allowance to at least GBP12,500, giving low- and middle-income taxpayers a modest tax cut.

The party's signature tax measure, for which it has lobbied for several years, is a mansion tax along similar lines to that proposed by Labour. This progressive "High Value Property Levy" will be paid on all properties valued at GBP2m or more. The thresholds will rise in line with house price inflation. Unlike Labour however, revenues raised from the LibDems' version of the mansion tax, which are predicted at about GBP1bn a year, will be used to pay down the budget deficit, rather than to fund new spending.

The third pillar of the LibDems' tax plan is a crackdown on tax avoidance, in particular by wealthy individuals and companies, in a bid to raise an additional GBP7bn for deficit reduction. This will entail the introduction of a general anti-avoidance rule. It is not clear, though, whether this will be in addition to, or as a replacement for, the existing General Anti-Abuse Rule. The party also advocates greater cooperation between nations to tackle tax avoidance and evasion, more corporate tax transparency including increased disclosure of inter-company transactions, and the publication of tax settlements.

The most pro-European of the main parties, the LibDems are expected to fight hard to retain Britain's EU membership should they be involved in another coalition government.

UK Independence Party

UKIP's tax policy is based on tax cuts for individuals, balanced by a tough stance on avoidance of UK tax by multinational companies.

In a similar vein to the other parties, UKIP would, by the end of the next five-year parliament, seek to raise the personal tax allowance to GBP13,000. The party would also raise the threshold for paying the 40 percent higher rate of tax to GBP55,000. Interestingly, they are the only party advocating an intermediate rate of tax, of 30 percent, which would apply on incomes ranging between GBP43,500 and GBP55,000. A long-term aspiration of the party is that the top rate of tax would be 40 percent, rather than the existing 45 percent rate, which starts on incomes over GBP150,000.

UKIP's most radical proposal is the abolition of inheritance tax.

The party also pledges changes to the VAT regime, including the zero-rating of certain goods and services which are currently charged to VAT. However, this would depend on the party achieving its central aim – Britain's exit from the EU – because

these VAT changes would be illegal under the EU VAT Directive.

With regards to tax avoidance, UKIP is proposing a tax on corporations linked to revenues derived from the UK market. This, the party says, would prevent multinationals in particular from paying little or no tax in the UK despite huge levels of sales there. Additionally, a Treasury Commission would be established to monitor the effectiveness of the new Diverted Profits Tax, and further unspecified measures would be introduced to "prevent large multinational corporations using aggressive tax avoidance schemes."

In terms of EU policy, UKIP's main *raison d'être* is to pull the UK out of the EU.

Scottish National Party

Obviously, given the party's aspirations for Scottish independence, the few tax proposals contained in its election manifesto are specific to Scotland only. These include taking control of rates of national insurance north of the border, and the ability to increase the personal tax allowance further in Scotland than the rest of the UK. The SNP also want existing plans for the devolution of Air Passenger Duty (APD) brought forward (see below).

In the area of business taxation, additional corporate tax incentives are proposed for companies in Scotland, including more tax breaks for research and development. These "targeted" tax cuts for companies replace the party's previous pledge, dumped last month, for a 3 percent cut in the rate of corporate tax in Scotland.

However, given that the SNP could have a decisive influence on certain policies affecting the UK after the election, their views on other areas of taxation are also of relevance. The problem is that nobody is really sure what these views are. As a left-wing party, senior SNP members have expressed support for Labour's 50 percent income tax, although this doesn't appear to be official policy. The party has also given the impression that it would be in favor of the mansion tax to raise additional funds for the National Health Service.

The SNP are pro-EU. However, there is some confusion over whether an independent Scotland would be permitted to join. In any event, the party would be expected to support policies leading to the UK's ongoing membership of the EU should it have a major influence on the next government.

Devolution

It is also worth mentioning here that certain tax-raising powers are already being devolved to the constituent countries of the UK, including Scotland, Wales and Northern Ireland, and it is probably safe to assume that these measures will be unaffected by the outcome of the general election.

Scotland

In January 2015, the UK Government published draft legislative clauses[1] that would give the Scottish Parliament powers over income tax, APD, and

the aggregates levy. The new powers are described by the UK Government as "extensive" and will see the Scottish Parliament control around 60 percent of spending in Scotland.

The clauses are the result of the recommendations made by the Smith Commission, a group set up by UK Prime Minister David Cameron in the wake of the "no vote" in the September 2014 Scottish independence referendum. Chaired by Lord Smith of Kelvin, the Commission was tasked with brokering a cross-party deal on devolution.

Smith's report, issued in November 2014, recommended that the Scottish Parliament be given control over income tax rates and bands. Under the draft clauses, the UK and Scottish Parliaments would share control of income tax policy. Members of Parliament representing constituencies across the whole of the UK would continue to decide the UK's Budget, including income tax. Within the new framework, the Scottish Parliament would have power to set the rates of income tax and the thresholds at which these are paid for the non-savings and non-dividend income of Scottish taxpayers. There would be no restrictions on the thresholds or rates the Scottish Parliament could set.

All other aspects of income tax would remain reserved to the UK Parliament at Westminster, including the imposition of the annual charge to income tax, the personal allowance, the taxation of savings and dividend income, the ability to introduce and amend tax reliefs, and the definition of income. HM Revenue & Customs (HMRC) would continue to collect and administer income tax. The Scottish Government would be required to reimburse the UK Government for additional costs arising as a result of the implementation and administration of these powers. The Scottish Government would receive all income tax paid by Scottish taxpayers under this scheme, and there would be a corresponding adjustment in the block grant (the portion of revenues provided by the UK Treasury each year to fund Scottish government operations).

The power to charge tax on passengers departing from Scottish airports would likewise be devolved. The Scottish Government would be free to make its own arrangements with regard to the design and collection of any tax intended to replace the APD. Once a number of legal issues in relation to the aggregates levy have been resolved, the UK Government would also devolve the power to charge tax on the commercial exploitation of aggregate in Scotland.

Also proposed is that the receipts raised in Scotland from the first 10 percentage points of the standard VAT rate be assigned to the Scottish Government's budget. These receipts would be calculated on a verified basis, to be agreed between the UK and Scottish Governments, with a corresponding adjustment to the block grant. The UK would also assign 2.5 percentage points of the revenue attributable to Scotland from the 5 percent reduced VAT rate. VAT rates would continue to be set at a UK-wide level.

The three main UK political parties have committed to take forward the clauses as part of a new Scotland Bill after the general election in May.

The powers previously agreed in the Scotland Act 2012[2] are unaffected by the new legislative clauses and will continue to be devolved to the Scottish Parliament as planned. These include:

- The replacement of stamp duty land tax (SDLT) and landfill tax in Scotland with the Land and Buildings Transaction Tax and Scottish Landfill Tax Revenue from April 2015;
- A new Scottish rate of income tax to be set by the Scottish Parliament with no upper or lower limit, from April 2016;
- The extension of Scottish borrowing powers; and
- A new GBP2.2bn capital borrowing power for the Scottish Parliament.

Wales

In December 2014, the UK Parliament approved new tax powers for Wales including the freedom to set different rates of personal income tax for each tax band. The powers will allow the territory to introduce a differential of up to 10 percent in income tax rates, compared with UK rates. Its three income tax rates would no longer need to move in tandem, under the so-called "lockstep" restriction.

Under the lockstep, the basic, higher, and additional income tax rates will only have been able to be changed by the same percentage. So if the Welsh Government wanted to increase the basic rate by 1 percent, then the other two rates will also have to be increased by 1 percent, leading to a tax structure of a basic rate of 21 percent, a higher rate of 41 percent, and an additional rate of 46 percent, compared with the 20, 40 and 45 percent rates in place in the UK.

The legislation also devolves landfill tax, stamp duty, and land tax, and there will be a *pro rata* reduction in the block grant provided by the UK (budgetary provision).

The Wales Act 2014[3] received Royal Assent on December 17, 2014.

Northern Ireland

A debate has taken place for a number of years about the merits of allowing Northern Ireland more flexibility with regards to income and other taxes, given its border with the Republic of Ireland, a sovereign nation with a quite different tax regime to that of the UK. It has been suggested that low levels of business investment in Northern Ireland relative to other parts of the UK is linked to the wide differential between the Republic's low rate of corporate tax (12.5 percent) and the UK rate, which, even after the recent cuts, remains substantially higher. Some argue that allowing Northern Ireland to lower the corporate tax rate – perhaps to the same rate as the Irish rate – would allow the province to compete more effectively for investment. The counter argument was that letting Northern Ireland reduce corporate tax to such an extent would merely encourage corporate tax avoidance within the UK without any real economic benefit for Northern Ireland.

However – devolution genie seemingly out of the bottle in Scotland and Wales – those arguing for devolution in Northern Ireland won out, and the stage was set for the province to set its own corporate tax rate when a political agreement concerning governance and fiscal arrangements, known as the Stormont House Agreement, was struck on December 23, 2014. This led to the introduction of the Corporation Tax (Northern Ireland) Bill[4] in the UK Parliament, which passed its House of Lords (upper house) stage on March 17, 2015, (which, coincidentally or not, just so happened to be St. Patrick's Day) and received Royal Assent on March 26, 2015.

In March 2015, Northern Ireland's First Minister, Peter Robinson, hinted that the Executive will pursue a reduction in the corporate tax rate to bring it into line with the 12.5 percent charged in the neighboring Republic of Ireland. The Executive will seek to introduce a new rate at the earliest possible date of April 2017. However, the new tax-setting powers come with conditions: they are dependent on the Northern Ireland Executive addressing certain structural shortcomings in the province's budget.

The Northern Ireland Executive is considering whether further devolution could result in any clear economic or social benefit for the province. The taxes under consideration include SDLT and landfill tax, and the aggregates levy.

The Outlook

Give or take a couple of percentage points, the two major parties have been neck and neck in opinion polls for a number of months, at about 35 percent each. To win an outright majority in the House of Commons and the right to form the next Government, a party needs at least 325 seats. However, there is widespread agreement that neither of the two largest parties will reach the winning post, resulting in a "hung parliament."

All sorts of unholy alliances between parties of wholly different outlooks are possible. But it seems that the outcome will essentially boil down to a left-leaning coalition between Labour and the SNP, or possibly Labour and the LibDems; or a more centrist/right-of-center government consisting of the Conservatives and the LibDems, possibly with the support of UKIP – which, despite the party's relative popularity, will probably end up with only a handful of seats at best – and then other minority parties that traditionally lend their support to the Tories, such as the Democratic Unionists in Northern Ireland. It can be assumed that the former will represent a fairly significant change of course in government policy, while the latter will likely result in fewer drastic changes, although the EU referendum is a huge source of uncertainty.

It is clear, though, that the speculation and doubt is damaging the UK's reputation with investors, and recent surveys of multinational company executives suggest that many firms are holding back investment plans until they know what the outcome of the election will be.

From a business point of view, the choice voters are about to make is between a Labour-led

administration likely to be perceived as "anti-business," and a Tory-led government which could potentially take the UK out of the EU, a seismic event with huge ramifications for the legal framework and the economy. One might call it a Hobson's choice.

Endnotes

1 https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/397079/Scotland_EnduringSettlement_acc.pdf

2 http://www.legislation.gov.uk/ukpga/2012/11/contents/enacted

3 http://www.legislation.gov.uk/ukpga/2014/29/contents/enacted/data.htm

4 http://www.legislation.gov.uk/ukpga/2015/21/contents/enacted/data.htm

Topical News Briefing: When The Gusher Runs Dry

by the Global Tax Weekly Editorial Team

The group of nations making up the Gulf Cooperation Council (GCC) together must form one of the most lightly taxed fiscal areas in the world. However, the tumble in the world oil price in the latter half of last year has reminded us all that the oil-rich Gulf states cannot rely on the bounty produced by the "black gold" *ad infinitum*.

Perhaps it is for this reason that the GCC member states are going to have another stab at creating a common value-added tax (VAT) system, with an outline legal framework to be presented at the next meeting of GCC finance ministers scheduled for May 2015.

Ostensibly the GCC VAT is intended to replace revenues lost by each member state as a result of the abolition of internal trade taxes and tariffs. But it may also have another use: to cushion the impact of oil price volatility, and, in the long term, provide a revenue buffer for when the region's oil reserves do eventually begin to run dry, even though that inevitability isn't expected to happen for a number of years.

The Gulf states have been warned repeatedly about the consequences of not diversifying their economies and revenue bases by multinational institutions like the International Monetary Fund (IMF). One of the latest warnings was sounded in February 2015, when the Fund pointed out, in a survey into the consequences of falling oil prices on the GCC economies, that in other oil-rich nations, like Mexico and Malaysia, reform efforts took about 20 years to complete once oil production began tailing off.

The IMF recommended that GCC members examine ways to encourage investment and risk-taking in the private sector, especially among small and medium-sized businesses, by easing access to finance, and providing tax incentives and free zones. But in actual fact, this is a strategy that has been successfully deployed in one of the richest corners of the GCC: the UAE's Dubai. Here, the Government has spent massive sums to create what has become the pre-eminent financial and business hub between the European and Asian time zones. The Government has also invested heavily in the free zone concept, with zones targeting specific economic sectors, from manufacturing to distribution, IT to financial services. The result is that oil currently accounts for only 2 percent of Dubai's GDP.

However, while free zones and other tax incentives may achieve economic diversification, they could leave the tax bases of the GCC states very narrow and therefore not diverse. The possibility that the UAE should begin to charge income tax has already been discussed, although that would feel like something of a seismic shift in policy given that places like Dubai sell themselves as no-tax fiscal paradises.

This is where sales and consumption taxes may come into the fiscal equation; such taxes are often seen as the antidote to a narrow tax base as, although regressive, they are typically less sensitive politically than income taxes.

While lower oil prices may have crystallized thinking about the need for a VAT in the finance ministries of the GCC, actually implementing a pan-GCC VAT is going to be another matter entirely. Getting to the point where finance ministers are going to sit round a table and discuss a concrete proposal – if indeed that does happen next month – has been a long journey. Indeed, news reports with headlines such as "A GCC VAT Within Two Years" have been appearing regularly in the regional and international tax media for something like ten years. One reason for the lack of progress has been administrative and technical shortcomings in the GCC's least affluent member states. Another reason perhaps is that, for some members, imposing VAT represents something of a leap, and maybe it is perceived as the thin end of what could turn out to be an ever-growing tax wedge. Hence, the VAT can has been repeatedly kicked down the road.

However, in the wake of the oil price fall, another difficult question may have arisen to confront the GCC: what should the VAT rate be? It seems to have been agreed that a VAT of between 3 and 5 percent will be sufficient to offset lost customs duty revenues. But will that be high enough to fully compensate all governments, especially with oil revenues expected to dwindle? VATs and equivalent taxes will be much higher in most other jurisdictions (and these days, many more jurisdictions have such taxes than don't), and governments are coming to depend on indirect taxes more and more. The GCC may at some point become equally reliant on them.

With the revenue issue having become somewhat more urgent, it will be interesting to see if GCC finance ministers are able to answer these and other questions at their upcoming summit. On the other hand, given previous form, don't be too surprised if heads are buried in the sand once more.

Financing International Operations — Recent IRS Interpretation Of The Code Sec. 267(a)(3)(B)

by L.G. Chip Harter, David H. Shapiro and Elizabeth Bouzis

L.G. "Chip" Harter and David H. Shapiro are principals and Elizabeth Bouzis is a manager in the Washington National Tax Service of PricewaterhouseCoopers LLP.

This article was published in 'International Tax Journal', Volume 41, No. 2, March-April 2015

Payment Standard Could Disrupt Taxation Of International Treasury Operations

Code Sec. 267(a)(3)(B) generally provides that a taxpayer accruing a deductible amount owed to a related foreign person is not entitled to a deduction in a year before the amount is paid. In 2013, the US Internal Revenue Service (IRS) released Chief Counsel Advice 201334037,[1] which analyzes when an amount should be considered paid for these purposes. The CCA asserts a very high standard for establishing that payment is made, in that it disregards, under a circular cash-flow analysis, actual payments if the payments are directly or indirectly funded by the related payee.

If the payment standard set forth in the CCA were a correct interpretation of the statute, the effect on modern international treasury cash management practices would be dramatic.[2] As discussed below, the goal of cash management practices – such as international cash pooling and international payment netting systems – is to minimize the need for actual cash transfers between members of an affiliated group. Applying the CCA's payment standard to such treasury structures could result in the current accrual of income by payees, while the corresponding deductions of the related payors would be deferred for US tax purposes, thus creating an artificial doubling up of earnings and profits within the affiliated group. Such an artificial inflation of the earnings and profits of group members could, in turn, have significant consequences in terms of foreign tax credit and repatriation planning and interest expense allocation.

The authors of this article believe that the payment standard set out in the CCA is not the correct standard for purposes of Code Sec. 267(a)(3)(B). As discussed below, the CCA applies the standard for payment that governs when a cash-basis payor is entitled to deduct

an expense. Code Sec. 267(a)(3)(B), however, is a matching provision, which allows a deduction to the payor of a deductible amount in the tax year when the payee is taxable on the corresponding income amount. The regulations under Code Sec. 267(a)(3)(B) therefore specifically provide that payment is considered made for purposes of that section when a cash basis *payee* would be taxable on the corresponding income. The standard for a "payment" triggering income to a cash-basis payee is a much lower standard than the one that applies to a cash-basis payor, in that a cash-basis payee can be taxed on deemed payments under the constructive receipt doctrine.

This article first traces the history and evolution of section 267(a) as applied in the international context, then reviews existing authorities governing what constitutes payment for purposes of Code Sec. 267(a)(3)(B). It next summarizes the CCA and discusses how, in the authors' view, the CCA applies the wrong standard in testing whether payments had been made. We then discuss the potential impact of the CCA's analysis on two important international treasury practices – international cash pooling and international payment netting – and explore how taxpayers might wish to modify their practices in response to the uncertainty created by the CCA.

I. Evolution Of Code Sec. 267(a) In The Cross-Border Context

A. Code Sec. 267(a)(2): 1937–1984

In 1937, Congress enacted a provision (which, in 1954, would become Code Sec. 267(a)(2)) to permanently disallow deductions for interest and other expenses accrued in a related party transaction between taxpayers with different accounting methods, unless the accrued expense was actually paid within two and a half months after the close of the tax year.[3] Thus, to be allowed a deduction for an expense payable to a related party on the cash method, a taxpayer had to pay the expense in the year accrued, or very shortly thereafter. If the accrued expense was not paid within the specified window, the deduction was permanently denied – a particularly harsh result.[4]

In 1984, Congress mitigated this harsh result by amending Code Sec. 267(a)(2) to provide for a "matching rule" rather than a permanent disallowance rule. As amended, Code Sec. 267(a)(2) provides that a payor is not allowed to deduct its accrued expense owed to a related taxpayer *until* the corresponding amount is "includible in the gross income" of the payee.[5] Notwithstanding this more lenient treatment, the rule was still designed as an anti-abuse rule, forcing related taxpayers "to use the same accounting method with respect to transactions between themselves in order to prevent the allowance of a deduction without the corresponding inclusion in income."[6] Congress explained that "the deduction by the payor will be allowed no earlier than when the corresponding income is recognized by the payee."[7]

It is worth pausing here to focus on the specific statutory mechanic of Code Sec. 267(a)(2): For a taxpayer to deduct an expense that has accrued to

a related person, the corresponding amount must be "*includible in the gross income*" of the recipient. When the related recipient is a US person, this concept is clear – Code Sec. 61 (defining "gross income") is purposefully broad, and Code Sec. 451 (describing the cash method of accounting) is not difficult to apply. However, when the related recipient is a foreign corporation, Code Sec. 882(b) provides that "gross income includes *only* (1) gross income which is derived from US sources and is not effectively connected with the conduct of a trade or business in the United States, and (2) gross income that is effectively connected with the conduct of a trade or business within the United States."[8]

In other words, foreign corporations only have "gross income" for US tax purposes when that income is subject to US tax, either as US-source fixed or determinable, annual or periodic income ("FDAPI") or effectively connected income ("ECI"). In respect of amounts constituting US-source FDAPI or ECI payable to foreign corporations, Code Sec. 267(a)(2), as enacted in 1984, was clearly designed to limit a US payor from taking a deduction for such amounts against its taxable income until such time as the foreign corporate recipient was subject to US tax on the corresponding amount.

The law was less clear where a US taxpayer owed an amount to a related foreign corporation, but the amount was *not* subject to US tax in the hands of the foreign corporate recipient as either ECI or US-source FDAPI. Such an amount would never be "includible in the gross income" of the related foreign corporation under Code Sec. 882(b). It was not clear that the US taxpayer could ever accrue an expense deduction in respect of such an amount. An example was a foreign corporation that performs services outside the United States for its related US subsidiary. Could the US subsidiary accrue a deduction for these service fees, which would constitute foreign source non-ECI in the hands of the foreign corporation? The 1984 Bluebook noted:

> The application of this provision [(*i.e.*, Code Sec. 267(a)(2))] is not entirely clear in all situations involving amounts owed to related foreign corporations which are not included in gross income under section 882(b).[9]

B. 1986 Enactment Of Code Sec. 267(a)(3)(A)

To address this uncertainty, Congress enacted in 1986 Code Sec. 267(a)(3)(A)[10] as a technical correction to Code Sec. 267(a)(2).[11] It provides that "[t]he Secretary shall by regulations apply the matching principle of section 267(a)(2) in cases in which the person to whom the payment is to be made is not a United States person."

In the legislative history, Congress again acknowledged that the application of the matching provision of Code Sec. 267(a)(2) was "unclear when the related payee was a foreign person that does not, for many Code purposes, include in gross income foreign source income that is not effectively connected with a US trade or business."[12] Congress posed the following example to illustrate the point and to explain the regulations that might be forthcoming:

> [A]ssume that a foreign corporation, not engaged in a US trade or business, performs services outside the United States for use by its wholly owned US subsidiary in the United States. That income is foreign source income that is not effectively connected with a US trade or business. It is not subject to US tax (or, generally, includible in the foreign parent's gross income). Under the bill, regulations could require the US subsidiary to use the cash method of accounting with respect to the deduction of amounts owed to its foreign parent for these services.[13]

Notwithstanding the fact that Code Sec. 267(a)(3)(A) was designed to address a specific ambiguity in the application of Code Sec. 267(a)(2), the actual text of the statutory provision grants the Treasury broad regulatory authority. The regulations can apply the matching principle to any case in which the recipient of a payment is foreign. For example, Congress noted:

> In the case of amounts accrued to a controlled foreign corporation by a related person, regulations might appropriately require the payor's accounting method to conform to the method that the controlled foreign corporation uses for US tax purposes.[14]

C. 1992 Regulations Under Code Sec. 267(a)(3)(A) (Issued Prior To The Enactment Of Code Sec. 267(a)(3)(B))

1. The General (a)(3) Matching Rule

In accordance with the statutory direction of Code Sec. 267(a)(3)(A), regulations were issued under Code Sec. 267(a)(3) in 1992. As a general rule, Reg. §1.267(a)-3(b)(1) provides:

> An amount that is owed to a related foreign person and that is otherwise deductible under Chapter 1 … may not be deducted by the taxpayer until such amount is paid to the related foreign person … An amount is treated as paid for purposes of this section if the amount is considered paid for purposes of section 1441 …

Treas. Reg. §1.1441-2(e)(1) in turn provides:

> A payment is considered made to a person if that person realizes income whether or not such income results from an actual transfer of cash or other property. … A payment is considered made when the amount would be includible in the income of the beneficial owner under the US tax principles governing the cash basis method of accounting …

This article collectively refers to these two provisions – Reg. §1.267(a)-3(b)(1) and Reg. §1.1441-2(e)(1) – as the "General (a)(3) Matching Rule." Note that defining payment by reference to when a cash-basis payee would take an amount into income is consistent with the matching architecture of Code Sec. 267(a). This definition of payment creates timing symmetry between when a payor gets to deduct an amount and when the payee would take the amount into income for US tax purposes if it were subject to US income tax.

The regulations draw a clear distinction between the basic rule of Code Sec. 267(a)(2) and the General (a)(3) Matching Rule. Thus, if an amount is otherwise "includible in gross income" of a related foreign recipient under Code Sec. 882(b), then the statutory matching rule of Code Sec. 267(a)(2) already applies, and there is no need for a clarifying regulation under Code Sec. 267(a)(3). The payor's deduction is unlocked on the day the amount is actually "includible in the gross income" of the recipient.[15] However, if the recipient/payee has no gross income from a US perspective, it also has no US accounting method with respect to such income. The General (a)(3) Matching Rule then steps in and provides one. It assigns a hypothetical accounting method to foreign persons lacking one[16] – and it does so by reference to the time at which the income would have been subject to US withholding tax if the income had been taxable by the United States. Thus, when it applies, the General (a)(3) Matching Rule looks to when the payee would otherwise have been taxed by the United States and matches the payor's deduction to this time.

2. Scope Of The General (a)(3) Matching Rule

When regulations were issued under Code Sec. 267(a)(3)(A), the drafters exercised their discretion to exclude important categories of income other than interest from the scope of the provision. For example, the General (a)(3) Matching Rule was not applied to amounts other than interest that are (1) from foreign sources and not ECI[17] or (2) from US sources but exempt by virtue of treaty.[18] For example, fees paid to a foreign related party for services performed by the related party outside the United States are not subjected to the General (a)(3) Matching Rule.

The regulations, however, applied the General (a)(3) Matching Rule much more broadly to related-party interest accruals. The rule is applied to amounts of both US and foreign-source interest to be received by a related foreign person who is not engaged in a US trade or business, whether or not the interest is exempt from tax under a tax treaty. The rule is also applied to interest payable to a foreign person who is engaged in a US trade or business, but only if the amount is exempt from tax under a tax treaty.[19]

The drafters of the regulations presumably chose to exclude from the operation of Code Sec. 267(a)(3)(A) amounts of foreign-source non-ECI other than interest, such as foreign-source related-party service fees, because such amounts typically arise in the ordinary course of business and are unlikely to involve inappropriate tax planning. As discussed below, an open issue exists as to whether these regulatory exceptions survived the enactment of Code Sec. 267(a)(3)(B) as part of the American Jobs Creation Act of 2004 ("AJCA"), described below.

3. The Pre-AJCA CFC Exception

Notwithstanding the regulation's broad approach to interest, it did provide an important exception for payments owed to controlled foreign corporations ("CFCs"). Notably, Reg. §1.267(a)-3(c)(4)(ii) (hereinafter, the "Pre-AJCA CFC Exception") provides:

> If [US or foreign-source interest] is owed to a related foreign person that is a controlled foreign corporation …, then the amount is allowable as a deduction as of the day on which the amount is includible in the income of the controlled foreign corporation. The day on which the amount is includible in income is determined with reference to the method of accounting under which the controlled foreign corporation computes its taxable income and earnings and profits for purposes of sections 951 through 964.

This rule meant that a deduction could be claimed with respect to interest owed to a related, accrual-basis CFC, *even if that interest was not subpart F income to the CFC*.[20] Thus, the fact that the amount was "includible" in the income of the CFC for E&P purposes – albeit not subject to current US tax as US source FDAPI, ECI or subpart F income – was seen as sufficient to satisfy the matching principle of Code Sec. 267(a)(2). The preamble to the regulations noted that:

> This [exception for amounts owed to related CFCs] is a substantial exception to the otherwise applicable general rule of these regulations. Relief is deemed appropriate in such cases because there is little material distortion in the matching of income and deductions with respect to amounts owed to a related foreign corporation that is required to determine its taxable income and earnings and profits for United States tax purposes pursuant to the foreign personal holding company, subpart F, or passive foreign investment company provisions.[21]

Nothing in the preamble language implies that the IRS and the Treasury were focused solely on circumstances in which a CFC payee would treat the accrued payment as subpart F income, and an example in the regulations clearly demonstrates that the IRS and the Treasury understood the implication for payments that were excludible from the payee's subpart F income.[22]

4. The Tate & Lyle/Square D Litigation

The validity of the 1992 regulations described above was the subject of considerable litigation. Two companies – Tate & Lyle and Square D – challenged the validity of the regulations in separate cases, arguing that it was improper to apply the "matching principle" to interest income that is exempt from tax under a US tax treaty.

These taxpayers acknowledged that Code Sec. 267(a)(3)(A) requires that the "matching principle" of Code Sec. 267(a)(2) be applied by regulations to amounts owed to foreign persons. However they articulated the "matching principle" in the following manner: the deduction of an accrued expense must be deferred when (1) a taxpayer accrues an expense that is otherwise deductible, (2) the taxpayer and the payee are related, and (3) the item is not included in the payee's gross income during the year *by reason of the payee's method of accounting*.[23]

These taxpayers argued that when a related payee did not include an item in its gross income by reason of an income tax treaty, which effectively exempts the item from gross income, the third prong of this principle was not met because the exclusion from gross income is unrelated to the foreign recipient's method of accounting. Thus, these taxpayers argued that the regulations were invalid to the extent that they applied the General (a)(3) Matching Rule to situations in which interest was payable to a related foreign person who was exempt from tax by virtue of tax treaty. This argument initially met with success in the Tax Court.[24] However, the IRS prevailed in the Third Circuit,[25] and subsequently in the Tax Court[26] and the Seventh Circuit.[27] These courts held that the regulation was a valid exercise of regulatory authority, even though it applied the General (a)(3) Matching Rule to taxpayers paying interest to exempt treaty recipients. These decisions indicated that the intent of Code Sec. 267(a)(3)(A) was not clear, but noted that the legislative history had anticipated that the matching principle would apply to situations where payments were made to foreign persons who did not owe US tax with respect to those amounts. Therefore, the courts held that the regulations were entitled to deference and valid.

D. 2004 Enactment Of Code Sec. 267(a)(3)(B)

As implemented by regulations, Code Sec. 267(a)(3)(A) applied predominantly to deductible amounts owed by US taxpayers to related foreign persons that were not CFCs. The Pre-AJCA CFC Exception exempted amounts owed by US taxpayers to related CFCs, provided that the CFCs were on the accrual method of accounting, which most were. Payments owed by one CFC to a related CFC were similarly exempted, provided that the payee CFC was on an accrual method of accounting.[28] Therefore, prior to 2004, Code Sec. 267(a)(3) applied mainly in the inbound context, where US subsidiaries of foreign multinationals owed deductible amounts to foreign affiliates that were not CFCs. In the outbound context, involving US-owned multinational groups, most deductible amounts owed to foreign related parties were owed to accrual-method CFCs and therefore exempt. Code Sec. 267(a)(3) therefore received relatively little attention in the outbound context.

This paradigm shifted dramatically in 2004, when Congress added Code Sec. 267(a)(3)(B) as part of the American Jobs Creation Act specifically to override the Pre-AJCA CFC Exception. Code Sec. 267(a)(3)(B) provides:

> **(i) In general.**
>
> Notwithstanding subparagraph (A), in the case of any item payable to a [CFC] …, a deduction shall be allowable to the payor with respect to such amount for any taxable year before the taxable year in which paid only to the extent that an amount attributable to such item is includible (determined without regard to properly allocable deductions and qualified deficits under section 952(c)(1)(B)) during such prior taxable year in the gross income of a United States person who owns

(within the meaning of section 958(a)) stock in such corporation.

(ii) Secretarial authority.

The Secretary may by regulation exempt transactions from the application of clause (i), including any transaction which is entered into by a payor in the ordinary course of a trade or business in which the payor is predominantly engaged and in which the payment of the accrued amounts occurs within eight and a half months after accrual or within such other period as the Secretary may prescribe.

Whereas under the prior regulations, Code Sec. 267(a)(3)(A) did not apply so long as the deductible amount was owed to an accrual-basis CFC, Congress in 2004 provided that the deduction of any amount owed to a related CFC must be deferred until payment, unless the corresponding income amount is subpart F income taxable to the US shareholder.

The relevant portions of the AJCA legislative history focused primarily on situations in which the payor of the interest (or other deductible amount) was a US net-basis taxpayer obtaining a current US tax benefit from the deduction, but the income of the related CFC was subject to US tax only on a repatriation of its earnings to its US shareholders.[29] Referring to the Pre-AJCA CFC Exception of the regulations, the House Report notes: "The Committee believes that this premise [that the subpart F regime would prevent material distortions] fails to take into account the situation where amounts owed to the related foreign corporation are included in the income of the related foreign corporation but are not currently included in the income of the related foreign corporation's US shareholder."[30]

Although the focus of Code Sec. 267(a)(3)(B) was with respect to accruals of amounts owed by US taxpayers to related CFCs, it also appears that the provision applies to payments made *between* CFCs. Thus, where a CFC is the party owing a deductible amount to another CFC, Code Sec. 267(a)(3)(B) provides, in effect, that the timing of the deduction to the CFC payor must be matched to the income recognition by the *US shareholder* of the CFC payee, *not* to the timing of recognition by the CFC payee. Code Sec. 267(a)(3)(B) thus overrides the Pre-AJCA CFC Exception in the regulations, and thus expands the application of Code Sec. 267 to many kinds of foreign-source items paid between CFCs.

Code Sec. 267(a)(3)(B) can also apply to defer the deduction with respect to a payment owed between related CFCs, even though the payee CFC must, itself, accrue income currently for all US federal income tax purposes. Whereas prior to 2004, Code Sec. 267(a)(3) was a topic of interest primarily in the inbound context, after the addition of Code Sec. 267(a)(3)(B) by the AJCA, the section potentially applies to all deductible amounts payable between all foreign subsidiaries of US-owned multinational groups.

Little thought appears to have been given by Congress to these payments made *between* CFCs,[31] and virtually no consideration was given to the interaction between Code Sec. 267(a)(3)(B) and the CFC look-thru rules that were enacted at the same time. Notwithstanding this lack of congressional consideration, when Code Sec. 267(a)(3)(B) applies, a payee CFC on the accrual method must recognize and characterize its income in a year before the payor CFC has a deduction to allocate.

This timing mismatch raises issues, such as to how to apply "look-thru" rules under the foreign tax credit basketing regime and the subpart F regime to such payments, because these "look-thru" rules base the characterization of the income accruing to the CFC payee on how the corresponding deduction to the CFC payor is allocated. These issues can be quite complex and have been addressed elsewhere.[32] But, importantly, taxpayers hoping to avoid these complex issues (rather than take advantage of them) can do so by making sure the payments are actually made between related CFCs in the years they accrue. In other words, as with all issues under Code Sec. 267(a)(2) and (3), satisfying the requirement that "payment" be made ensures that no expense will be deferred. Therefore, a key question in complying with Code Sec. 267(a)(3) is what constitutes "payment" for purposes of that section.

II. Definition Of "Payment" For Purposes Of Code Sec. 267(a)(3)

Although the AJCA expanded the types of transactions to which the Code Sec. 267(a)(3) payment requirement applies, there is no indication that Congress intended to change what constitutes a payment for purposes of Code Sec. 267(a), which had long been established by regulation.

As discussed above, Reg. §1.267(a)-3(b)(1) starts with the language:

> Except as otherwise provided … section 267(a)(3)(B) requires a taxpayer to use the cash method of accounting with respect to the deduction of amounts owed to a related person. An amount that is owed to a related person and that is otherwise deductible … thus may not be deducted by the taxpayer until such amount is paid to the related foreign person.

If the regulation ended there, the relevant authorities would be those interpreting Reg. §1.451-1(a), which governs when a cash-basis taxpayer is entitled to a deduction. Extensive case law exists interpreting what constitutes payment for this purpose.

It is crucial to note, however, that the regulation does not end there. Instead it further provides that: "An amount is *treated as paid for purposes of this section* if the amount is considered paid for purposes of section 1441 or 1442 …"[33] This specific rule providing that an amount "is treated as paid for purposes of this section," and therefore deductible, when it is considered paid for purposes of the withholding tax provisions thus shifts the frame of reference of the test in a subtle but important way:

The withholding tax provisions define payment by reference to when a *payee* must take an amount *into income* rather than when a *payor* obtains the *deduction*. Reg. §1.1441-2(e)(1) provides:

> A payment is considered made to a person if that person realizes income whether or not such income results from an actual transfer of cash or other property. For example, realization of income from the cancellation of indebtedness results in a deemed payment. A payment is considered made when the amount would *be includible in the income of the beneficial owner* under US tax principles governing the cash method of accounting.[34]

This definition of payment by reference to the treatment of the beneficial owner, or payee, is entirely consistent with the matching principle underlying Code Sec. 267(a)(3) – the timing of the deduction to the payor is intended to match the timing of the income inclusion to the payee. Therefore, defining payment by reference to what results in an income inclusion to the payee achieves that matching.

At this point, it should be noted that there is a very important difference between the standards governing when a cash-basis borrower deducts interest expense and when a cash-basis lender includes interest income. Simply put, the concept of "constructive receipt" applies to a cash-basis lender earning interest income, but it has no application to a cash-basis borrower and the timing of its deduction. This is evidenced most clearly in Reg. §1.446-2(c)(1)(i), which describes the cash method of accounting and provides that income is "to be included for the taxable year in which *actually or constructively* received … [whereas] [e]xpenditures are to be deducted for the taxable year in which *actually* made."[35]

Thus, regulations under Reg. §1.451-2, relating to the constructive receipt of income, apply to cash-basis lenders, but not to cash-basis borrowers. Under those regulations, a cash-basis lender accounts for interest income when the interest is "credited to his account, set apart for him, or otherwise made available so that he may draw upon it at any time" without substantial restrictions.[36] As an example, the constructive receipt regulations note that "interest credited on savings bank deposits … is income to the depositors … for the taxable year when credited."[37] Furthermore, "[a]mounts payable with respect to interest coupons which have matured and are payable but which have not been cashed are constructively received in the taxable year during which the coupons mature, unless it can be shown that there are no funds available for payment of the interest during such year."[38]

From the beginning, Code Sec. 267(a) has specified that the authorities regarding cash method accounting *for income recognition* are dispositive of the question of when the payor gets a deduction and that the doctrine of constructive receipt applies when determining income recognition. Indeed, the regulations that implement the pre-1984 version of Code Sec. 267(a)(2) are explicit on these points.

Recall that prior to 1984, an accrual-method taxpayer was permanently denied a deduction for interest expense owed to a related party on the cash method unless the accrued expense was "paid" within two and a half months after the close of the tax year.[39] The pre-1984 regulations provide an example that allows a deduction to an accrual-method taxpayer "if the interest [accruing in 1956] had actually been paid to [the related person on the cash method] on or before March 15, 1957, *or* if it had been made available to [him] before that time (and thus had been constructively received by him)."[40] Thus, the regulations expressly allowed a deduction if the creditor *constructively received* the interest, regardless of whether the payor *actually paid* the interest. In cases applying the matching principle of Code Sec. 267(a)(2), courts accordingly have looked to the constructive receipt doctrine of Code Sec. 451 to determine whether payees have constructively received income such that a deduction can be taken by the related payors.[41]

It should also be observed that when the current regulations specifically provide that "an amount is treated as paid for purposes of this section if the amount is considered paid for purposes of section 1441 or section 1442 …," the regulations are cross-referencing the extremely broad definition of payment used in the withholding tax context. A broad definition of payment maximizes withholding tax revenues, and a fairly mechanical definition of payment allows the withholding agents to withhold appropriately even when they need to operate based on limited facts. By deeming constructive receipts to be payments subject to withholding, the broad withholding tax definition of payment thus maximizes revenues.[42] By making all "actual" cash payments subject to withholding, the regime simultaneously institutes a mechanical rule that withholding agents can apply.

It would be inconsistent with the architecture of the withholding tax rules to conclude that an actual payment of cash was not a payment subject to withholding tax under some circular cash-flow or substance-over-form doctrine, given that such an application would reduce withholding tax revenues and require a factual inquiry that withholding agents are not capable of discharging. The authors are aware of no authority that has disregarded an actual cash payment for withholding tax purposes.

III. CCA 201334037

In CCA 201334037, however, the IRS disregarded actual payments for purposes of Code Sec. 267(a)(3)(B), notwithstanding that the definition of payment under that section is the withholding tax definition.

The CCA involved a US corporate taxpayer that had borrowed from its foreign parent. When the taxpayer owed an interest payment to its foreign parent, the IRS states that "funds sufficient to cover these 'payments' … were obtained shortly before or shortly after a claimed payment of interest, either through additional loans from the foreign parent or pursuant to draw-downs on one or more lines of credit with the foreign parent." Sometimes, interest due to the foreign parent "was 'paid' to the foreign

parent by directly netting a required interest 'payment' against a foreign parent new advance." All interest amounts were actually paid by wire transfer from a general bank account of the US subsidiary, in which it commingled its funds from operations, from third-party borrowings and from related-party borrowings.

Although the interest amounts were actually paid by wire transfer, the IRS focused on the fact that the funds used to pay the interest were directly or indirectly advanced by the lender or an affiliate of the lender. Among the permutations discussed in the CCA were cases where: (i) the parent advanced funds to the subsidiary shortly before the payment of the interest; (ii) the parent advanced funds shortly after the payment of the interest; (iii) a foreign affiliate advanced funds to the US borrower; and (iv) a foreign affiliate advanced funds to a consolidated group member of the US borrower, which in turn advanced funds to the borrower. The analysis of the CCA focused heavily on the fact that the outstanding balance of the amount owed by the US borrower to the foreign parent increased in the aggregate over the years in question.

The CCA held that, by reason of Code Sec. 267(a)(3), the taxpayer was not entitled to an interest deduction in respect of interest due to its foreign parent. Effectively, the CCA held that the interest due to the foreign parent was not "paid" for purposes of Code Sec. 267(a)(3) because the payment was directly or indirectly funded by the foreign parent. In the IRS's view, the US borrower had not "paid" the interest because it had, instead, borrowed the amount from the foreign parent and transferred it back (but not "paid" it) in a circular transaction.

The CCA based its conclusions on *Battelstein*, *Davison* and other cases[43] "dealing with the taxation of lender-borrower circular cash flows." Factually, each of the cited cases is unique, but they all involve a similar paradigm: (1) A cash-method borrower owes interest to a lender, and (2) the lender advances cash to the borrower of an equal amount, which is then paid back by the borrower to the lender in satisfaction of the interest due. The cases address the borrower's ability to deduct this payment under the cash method of accounting.

Not surprisingly, the cases focus on the "circle" of cash, observing that the funds go from the lender to the borrower and back again. Essentially, the cases probe whether the borrower: (i) has "unrestricted control" over the new funds advanced by the lender (a helpful fact in establishing that the "circle" of cash is not inevitable, and therefore, helpful to the cash method borrower sustaining its deduction); or (ii) has "specifically earmarked" the funds advanced by the lender to pay the interest due (a fact that shows that the circular flow of cash was preordained and should be disregarded as a "payment" made by a cash method borrower).

The cases cited by the CCA relate to the *deduction* of interest under the cash method of accounting – *i.e.*, they address whether the borrower has made a "payment" of interest, for which it is entitled to

take a deduction, as a cash-method taxpayer. They do not address whether a cash-method lender has received a "payment" that must be included in income. As noted above, a cash-method lender must consider the doctrine of constructive receipt when determining whether it has income.

As discussed above, when Code Sec. 267(a)(3) applies, it assigns a cash method of accounting to the *recipient* of the income and matches the payor's deduction to the timing of this income inclusion. In other words, Code Sec. 267(a)(3) does not put the payor on the cash method of accounting; rather, it puts the payee on the cash method of accounting and matches the payor's deduction to the payee's inclusion.

The CCA does not reflect that Reg. §1.267(a)-3(b)(1), by providing in its last sentence that "[a]n amount is *treated as paid for purposes of this section* if the amount is considered paid for purposes of sections 1441 or 1442 …,"[44] shifts the test from that of a cash-basis payor to a cash-basis payee. The CCA similarly does not reflect that the withholding tax definition of payment incorporated into the Code Sec. 267 regulations is a broad definition that incorporates all actual payments as well as deemed payments under the constructive receipt doctrine. The CCA thus applied the wrong legal standard in analyzing the transactions before it, and the cases it relies upon dealing with cash-basis payors are not relevant. If the interest payments discussed in the CCA had been subject to withholding and the issue was whether payment had been made for purposes of Code Secs. 1441 and 1442, it is difficult to imagine that the IRS would have determined that no withholding tax was due.

IV. Application Of Code Sec. 267(a)(3)(B) To International Treasury Operations

The potential application of Code Sec. 267(a)(3)(B) to international treasury operations is extremely broad, given that the section can apply to payments made by both domestic corporations and CFCs to foreign related persons. With respect to US-based multinational groups, both outbound and foreign-to-foreign deductible payments are potentially covered. With respect to foreign-based multinational groups, payments from US group members to foreign affiliates are the main concern, unless the US group members themselves own CFCs. Rather than attempt to catalogue all potential applications of Code Sec. 267(a)(3)(B) to international treasury operations, the analysis that follows will focus on two types of international treasury structures frequently used by multinational corporations: International Cash Pools and International Netting Centers.

A. International Cash Pools And International Netting Centers

To better manage their liquidity and to fund operations internally, most large multinational groups have established international cash pooling structures. The group typically designates an entity (a "Treasury Center") that effectively acts as an internal bank to the group, taking deposits from affiliates with excess cash and extending loans to affiliates that require funding. The Treasury Center will typically earn a modest spread

between what it earns on the loans and what it pays on the deposits.

Such a cash pooling arrangement has several operational advantages. If each member of the group simply deposited with or borrowed from an external bank, that practice would tend to "balloon" the group's balance sheet and cost the group the difference between the rate charged on loans and the rate earned on deposits. Cash pooling allows free cash to be efficiently employed within the group. It also can simplify banking relationships by avoiding the need for each group member to have external banking transactions. Another important benefit of cash pooling is that it helps centralize the management of foreign currency risk because each depositor can place deposits with the Treasury Center in the depositor's functional currency, while each borrower can borrow in its functional currency. The Treasury Center then can hedge its net foreign currency position with respect to its portfolio of deposits and loans.

International Netting Centers are structured to simplify the settlement of amounts owed by different affiliates of a multinational group to each other. The members of the group frequently do business with each other, resulting in payment obligations for the sale of goods, provision of services, payment of royalties and the like. In a group with dozens of affiliates doing business with each other, each affiliate can have numerous obligations to dozens of other affiliates, resulting in a complex matrix of intercompany payment obligations. If each affiliate were itself to make payment on all of its related-party obligations, it would need to make numerous payments in multiple currencies.

Netting Centers simplify this process through a broad multilateral netting process. One group entity, the Netting Center, effectively acquires from each affiliate all of the affiliates' intercompany receivables and assumes the obligations under all of the affiliates' intercompany payables. To the extent the amount of receivables acquired by the Netting Center from a given affiliate in a netting cycle exceeds the amount of the affiliate's payables that it assumes, the Netting Center credits the affiliate for the difference in an intercompany account between the Netting Center and the affiliate. To the extent that the Netting Center assumes more payables than the receivables it acquires, that excess is charged against the affiliate in its account with the Netting Center.

Once the Netting Center has acquired all of the intercompany receivables and payables from each affiliate in the group, the affiliates no longer have amounts payable to and receivable from multiple affiliates; instead, all of the obligations run to and from the Netting Center. The Netting Center then has a single net balance with each affiliate in that affiliate's functional currency, which then can be settled or carried forward. Through this mechanism, multinational groups can avoid the need to make thousands of intercompany payments and mitigate the foreign currency exposures of affiliates as they deal with each other in multiple currencies.

International Cash Pools and International Netting Centers are both structures used to minimize the need for cash payments among global affiliates and the need for external bank accounts and banking activity. Given that these structures are used to make payments of deductible expenses among related parties, a question arises whether such payments satisfy the requirements of Code Sec. 267(a)(3)(B) and what the consequences might be if those requirements are not met. This article next separately considers International Cash Pools and International Netting Centers and discusses how the payment requirement of Code Sec. 267(a)(3)(B) could be satisfied in each case.

B. Application Of Code Sec. 267(a)(3)(B) To International Cash Pools

1. What Is At Stake If The Payment Requirement Is Not Satisfied?

If the payment requirement is not satisfied with respect to a deductible amount accrued by a US person with respect to a related foreign payee, Code Sec. 267(a)(3)(B) simply defers the deduction for the accrued amount until the payment requirement is satisfied. Where the related foreign person is a CFC, however, payment is not required if the corresponding income accrual to the CFC is currently taxable to its US shareholder under subpart F. Where the related foreign person is not a CFC, the payment requirement must always be satisfied for the payor to obtain a deduction. To the extent that the IRS seeks to apply a standard of "payment" that is inappropriately narrow, it therefore will be deferring deductions for US payors where such amounts are properly deducted currently.

If the payment requirement is not satisfied with respect to a deductible amount accrued by a CFC in favor of a related CFC, the effects can be more complex. Because a deduction is allowed to an accrual basis payor regardless of whether payment is made if the corresponding income item is currently taxed to a US shareholder under subpart F, these issues arise only if the income accrued by the related CFC payee is not currently taxed to the US shareholder. Given the broad availability of subpart F exceptions for related-party interest, rents and royalties under Code Sec. 954(c)(6), and the same-country exceptions under Code Sec. 954(c)(3), however, the income of the CFC payee often will not be subject to current subpart F taxation. In those cases, if the payment requirement is not satisfied, the net effect of Code Sec. 267(a)(3)(B) is a doubling-up of offshore earnings and profits until payment is made. The CFC payee, as an accrual-basis taxpayer, will accrue the unpaid amount into income currently, while the related CFC payor will not have a deduction for purposes of computing either income or earnings and profits[45] until the year payment is made.

To illustrate the effects in the context of an international cash pooling structure, assume that a Treasury Center takes a deposit from CFC1 and lends a corresponding amount to CFC2. For the sake of simplicity, assume that the Treasury Center earns no spread on the transactions and earns USD100 of interest on the loan to CFC2 and pays USD100 of interest on the deposit from CFC1. Further assume that no actual payments of interest are made during

the tax year. If the Treasury Center and CFC1 are not considered in constructive receipt of the accrued interest and the payment requirement is not otherwise satisfied, the results would be as follows.

CFC2's USD100 interest deduction with respect to its borrowing from the Treasury Center would be deferred for US tax purposes until the year the interest is paid. The interest expense likely would be currently deductible for foreign tax purposes, with the result that CFC2 would be reporting more current net income for US tax purposes than for foreign tax purposes. This mismatch would lower the foreign effective tax rate on CFC2's earnings pool during years before the interest is paid. Therefore, distributions made out of CFC2's earnings pools during this period would carry fewer foreign taxes to credit against the US tax liability on the distributions.

The Treasury Center would currently accrue into income the USD100 of interest on the loan to CFC2, notwithstanding that no payment had been made and that CFC2 is not able to deduct a corresponding amount currently. Code Sec. 267(a)(3)(B) would simultaneously defer the Treasury Center's deduction for its USD100 of interest expense accrued with respect to its deposit from CFC1. Therefore, the Treasury Center would currently report USD100 of net income for US tax purposes, notwithstanding the fact that it has no economic income. The Treasury Center would likely accrue currently both its USD100 of interest income and its USD100 of interest expense for foreign tax purposes and have no net income for foreign tax purposes. Therefore, the USD100 of earnings and profits that the Treasury Center would have until it pays its interest expense would have zero foreign tax credits associated with it.

CFC1, meanwhile, would currently accrue into income its USD100 of interest on its deposit with the Treasury Center and would likely do so for foreign tax purposes as well, creating a USD100 earnings pool taxed at the foreign statutory rate. The combined effect on the three group members involved in the deposit and the loan is that they experience an increase in their combined earnings and profits of USD200 from intercompany transactions that produce no net income to the group. The foreign effective tax rate on the earnings of CFC2, the borrower, is reduced by the fact that it is likely entitled to a current deduction for foreign tax purposes, despite the deduction being deferred for US tax purposes. The USD100 earnings pool created in the Treasury Center likely has a zero-percent foreign effective tax rate, and the USD100 earnings pool created at CFC1, the depositor, likely has a rate equal to the foreign effective tax rate. The mismatched effects to CFC2 and the Treasury Center can reverse out if interest payments are made in a subsequent year before either CFC2 or the Treasury Center makes a dividend distribution and before their earnings and profits are otherwise taken into account, for example, under Code Sec. 1248 or Code Sec. 956. Even if interest payments are made in a subsequent year prior to any distributions or deemed distributions, however, the temporary doubling up of earnings and profits within the CFC group would have

adverse interest expense allocation effects under Reg. §1.861-12(c)(2).

The example discussed above is the simplest possible illustration of Code Sec. 267(a)(3)(B) applying to an International Cash Pool among CFCs. As a practical matter, because dozens of CFCs can participate in a cash pool, the complexity soon becomes overwhelming if the payment requirement is not satisfied prior to every year-end with respect to all interest accruals.

If the payment requirement has not been satisfied, but the group has not taken into account the application of Code Sec. 267(a)(3)(B), the earnings and profits pools of the group members will be incorrectly calculated, as will the effective foreign tax rates on those pools. Such errors would likely lead to errors in repatriation planning and in analyzing the impact of corporate restructurings, both of which are heavily dependent on the correct calculation of such tax attributes. In addition, more of the taxpayer's consolidated interest expense would be allocated against foreign-source income, thereby eroding the group's foreign tax credit limitation because the inflated earnings and profits of the CFCs would increase the group's foreign asset basis for interest expense allocation purposes.

2. Observations On Satisfying The Payment Requirement
It should be possible for taxpayers to draft the legal agreements implementing a cash pooling agreement in such a way to provide a strong basis for concluding that each creditor is in constructive receipt of its accrued interest income immediately prior to the end of each tax year. The deposit agreements can provide that accrued interest income must be paid periodically to the depositors unless the depositors affirmatively notify the Treasury Center to roll the principal and accrued interest into a new deposit shortly before the maturity date of the existing deposit.

Provided that the decision to re-invest the accrued interest is the exercise of a unilateral right of the depositor, the depositor should be considered in constructive receipt of the accrued interest income, and the payment requirement of Code Sec. 267(a)(3)(B) should be satisfied under the authorities discussed above. Having such deposits mature on a 30-day cycle, for example, with a maturity date falling very shortly before year-end, should provide that essentially all of the interest accrued on the deposits over the year would be treated as paid during the year for purposes of Code Sec. 267(a)(3)(B); that result would entitle the Treasury Center to deduct its accrued interest expense.

The documentation of the loans made by the Treasury Center can similarly be drafted to support a conclusion that the Treasury Center is in constructive receipt of the interest accruing on the loans. The loan or overdraft agreements, like the deposit agreements, can be structured as a series of short-term (*e.g.*, 30-day) advances, with the Treasury Center entitled to receive a full repayment of principal and interest at the maturity of each advance. Provided that any relending of the principal and accrued

interest at the maturity of a loan is based on a new mutual agreement of the parties, the Treasury Center should be viewed as in constructive receipt of the interest income accrued on the first loan even if it is refinanced in the second loan rather than paid. It is important to note, however, that if the borrower has the unilateral right to roll its accrued interest expense into a new borrowing, the constructive receipt doctrine might not be available. It therefore can be problematic to combine committed credit facility terms with an international cash pooling structure.

As discussed above, the IRS's analysis in the CCA appears to be inconsistent with a reliance on the constructive receipt doctrine to satisfy the payment requirement of Code Sec. 267(a)(3)(B). Although the authors of this article believe that the IRS's analysis in the CCA is incorrect and that constructive receipt should constitute payment for purposes of Code Sec. 267(a)(3)(B), taxpayers may wish to consider what additional steps they could implement with respect to their cash pooling structures to avoid potential conflicts with the IRS. Unfortunately, implementing payment procedures that would clearly satisfy the IRS's analysis in the CCA would often end up undermining the commercial utility of cash pooling structures.

To clearly satisfy the CCA's payment standard, each debtor in a cash pooling structure would need to make a cash transfer in payment of its accrued interest expense for the year and show that the creditor has not directly or indirectly financed the payment of the accrued interest. Seeking to satisfy this standard would present a number of commercial difficulties.

With respect to the interest owed by the Treasury Center to the depositing affiliates, the commercial reality is that the depositing affiliates typically do not want to receive a current payment of their accrued interest income. The depositors are depositing cash that they hold in excess of the needs of their businesses. The interest earned on the deposits represents additional excess cash that must be invested somewhere. The central purpose of the cash pooling structure is to give such affiliates an efficient place to invest such excess cash within the group so that they are not required to maintain deposit balances with external banks. In theory it would be possible to satisfy the CCA's payment standard by requiring each depositor to take cash payment from the Treasury Center of its accrued interest income and to deposit that amount with an unrelated party for a considerable period of time before lending it back to the Treasury Center. Requiring such operational protocols, however, would considerably undermine the commercial utility of a cash pooling structure.

Similar commercial inefficiencies would arise if one were to satisfy the CCA's definition of payment with respect to the accrued interest on the loans from the Treasury Center to the borrowing affiliates. Some borrowing affiliates may need increasing levels of funding over time. If the Treasury Center (or other affiliates) provides increasing levels of funding to an affiliate, the analysis in the CCA would conclude that the Treasury Center has directly or indirectly

financed interest paid or accrued by the borrower. The only lending by a Treasury Center that would satisfy the CCA's standard would be a loan in respect of which all of the interest is currently paid in full and the balance of which never increases.

In light of the uncertainty created by the CCA and the commercial inefficiencies that arise if one were to attempt to implement payment protocols that fully satisfy the analysis of the CCA, taxpayers might consider taking an intermediate position. At least with respect to participants in the cash pool that have external bank accounts, it could be worthwhile to make actual wire transfer payments prior to year-end of interest accrued during the year. Even if this interest amount is then immediately re-lent to the Treasury Center or to the borrowing affiliate, producing a circular cash flow, the authors of this article believe that it is unlikely that the IRS could successfully disregard a demonstrable payment through the external banking system for purposes of Code Sec. 267(a)(3)(B). Although the IRS disregarded circular cash flows in the CCA, we believe that its analysis is incorrect because the definition of payment for purposes of Code Sec. 267(a)(3)(B) is the definition of payment provided under the authorities interpreting the withholding tax provisions of Code Sec. 1441. We are not aware that a circular cash flow analysis has ever been applied to disregard an actual payment for purposes of Code Sec. 1441.

If a group drafts the agreements implementing a cash pooling structure to place the creditors in constructive receipt of their accrued interest income and actually makes annual payments of such income by wire transfers, we believe it its highly unlikely that the IRS could successfully assert the circular cash flow analysis of the CCA to defer the deduction of interest under Code Sec. 267(a)(3)(B).

C. Application Of Code Sec. 267(a)(3)(B) To International Netting Centers

1. What Is At stake If The payment Requirement Is Not Satisfied?

Netting Centers present many of the same issues as International Cash Pools, but with at least two additional sources of complexity.

First, Netting Centers typically net payment obligations arising from a wide range of transactions in addition to interest accruals, including, for example, payment obligations arising with respect to fees for services, the purchase price of goods and the accrual of royalties. The statutory language of Code Sec. 267(a)(3)(B), as enacted in 2004, literally appears to apply to any payments made to related foreign persons that could give rise to a deduction. It is not clear whether Congress intended to override the existing regulatory exceptions for accruals of amounts representing foreign-source income to the payee that are neither interest nor treaty-benefitted ECI. For example, a CFC's obligation to pay a service fee to a related CFC for performance of services outside the United States might literally be pulled within Code Sec. 267(a)(3)(B). Given that a wide variety of potentially deductible payment obligations typically are netted within a Netting

Center, additional issues as to the scope of Code Sec. 267(a)(3)(B) are raised if the payment requirement is not satisfied.

Second, the operational complexity of Netting Centers is also often much greater than for Cash Pools. Dozens of separate CFCs may be settling thousands of obligations with each other, each *via* a single net credit or debit through its account with the Netting Center. The purpose of the system is to minimize or eliminate the need for cash payments. The Netting Center therefore must rely for purposes of the payment requirement under Code Sec. 267(a)(3)(B) entirely on the principle that offset of obligations by netting constitutes payment. If, however, a given CFC's growing negative balance over year-end in its account with the Netting Center were viewed as evidence that the CFC has not made full payment to the other participants in the system, it would be difficult to unscramble the egg and determine how Code Sec. 267(a)(3)(B) would apply.

2. Observations On Satisfying The Payment Requirement
The principle that netting offsetting obligations constitutes payment of those obligations for purposes of the Code Sec. 1441 definition of payment is well established.[46] The IRS's analysis in the CCA does not appear to be inconsistent with this principle. The scenario in which the IRS might seek to apply the analysis in the CCA might be where the Netting Center effectively finances a participant's shortfall by allowing the participant to maintain a negative balance in its account with the Netting Center over year-end. A cautious taxpayer therefore might wish to avoid having a Netting Center effectively finance its participants by requiring that such negative balances be paid to the Netting Center before year-end. This can be accomplished where a cash pooling system is maintained separately from the netting system so that a participant with a negative balance with the Netting Center can draw from the Cash Pool to pay the netting system. This technique obviously shifts the Code Sec. 267(a)(3)(B) analysis back to the Cash Pool, but those issues typically can be better limited and managed in the Cash Pool context, as discussed above.

Endnotes

1 CCA 201334037, dated April 3, 2013, publicly released August 23, 2013.

2 A number of articles have catalogued a variety of complex subpart F issues facing international treasury operations and the transactions that they execute to manage foreign currency and interest rate exposures. This article does not address these issues, but focuses solely on interest deductions under Code Sec. 267(a)(3). For a discussion of these other issues, *see, e.g.*, L.G. "Chip" Harter, *The Subpart F Treatment of Financial Transactions and Hedges Entered into by Controlled Foreign Corporations*, 38 Tax Management Memorandum Corporate Tax and Business Planning Review No. 6, S-70 (1997); Michael J. Feder, *Making CFC Hedging Work – Avoiding Whipsaws in an Ambiguous Environment*, J. Taxation of Financial Products, Winter 2003; L.G. "Chip" Harter, Rebecca E. Lee and David H. Shapiro, *Inherently Hedgeable: Hedging Foreign Currency Exposure Arising from the Branch Operations of a CFC*, International Tax J., September–October 2011,

at 11; John D. McDonald, Ira G. Kawaller, L.G. "Chip" Harter and Jeffrey P. Maydew, *The Devil is in the Details: Problems, Solutions and Policy Recommendations with Respect to Currency Translation, Transactions and Hedging*, Taxes, March 2011, at 199; New York State Bar Association Tax Section, *Report on Subpart F Issues Involving Currency Gain and Loss*, June 3, 2013 Tax Analysts Doc. # 2013-13534.

3 *See* Act Sec. 301(c) of the Revenue Act of 1937 (P.L. No. 75-377).

4 This rule is still reflected in the regulations applicable to years prior to 1984 – *see* Reg. §1.267(a)-1(b). The 1937 legislative history indicates that Congress was particularly concerned with abusive transactions in which taxpayers accrued expense deductions for payments that were never subsequently made. *See* H.R. Rep. No. 75-1546 (1937), *reprinted in* 1939-1 CB (Pt. 2) 704, 724–25.

5 *See* 1984 Bluebook, p. 541.

6 H. Rep. No. 98-432, 98th Cong., 2nd Sess*., reprinted in* 1984 USC.C.A.N. 697, 1206. Like the 1937 legislative history, the 1984 legislative history also expresses a view that the provision is an "anti-abuse rule." The Ways and Means Committee stated that "[t]he failure to use the same accounting method with respect to one transaction involves unwarranted tax benefits, especially where payments are delayed for a long period of time, and in fact may never be paid."

7 *Id*.

8 Emphasis added.

9 1984 Bluebook, p. 542, endnote 18.

10 As enacted in 1986, the provision was enumerated simply as Code Sec. 267(a)(3). However, in 2004, the provision (otherwise unchanged) was re-numbered to be Code Sec. 267(a)(3)(A). For ease of reference, we simply refer to it as Code Sec. 267(a)(3)(A) (its current number).

11 Because the provision was enacted to clarify the application of the matching principle of Code Sec. 267(a)(2), it was included in the Tax Reform Act of 1986 as a technical correction of Code Sec. 267(a)(2). Because it was added as a technical correction, Code Sec. 267(a)(3)(A) carries the same effective date as Code Sec. 267(a)(2). *See* Act Sec. 1881 of the Tax Reform Act of 1986, P.L. No. 99-514, 100 Stat. 2085, 2914.

12 S. Rep. No. 99-313, 99th Cong., 2d Sess., at 959 (1986), *reprinted in* 1986-3 CB (Vol. 3) 1, 959. *See also* H.R. Rep. No. 426, 99th Cong., 2d Sess. 939 (1986).

13 *Id*.

14 *Id*.

15 Thus, if the foreign recipient/payee receives an amount that constitutes ECI, the regulations explicitly provide that the provisions of Code Sec. 267(a)(2) apply, and not the General (a)(3) Matching Rule. *See* Reg. §1.267(a)-3(c)(1). The regulation further states, however, that if the income is exempt under a treaty (*e.g.*, because the foreign recipient has no PE), the General (a)(3) Matching Rule does apply – *i.e.*, the rule is needed to "step in" and provide a cash method of accounting for a recipient/payee for whom such concept would otherwise be irrelevant. The Tax Court noted this dynamic in *Square D*: "The authority granted by section 267(a)(3) does not apply in the case of effectively connected income because … the foreign recipient in this instance would have a US method of accounting for such income, triggering a straightforward application of section 267(a)(2) (*i.e.*, 'present law already imposes matching'). Regulations under section 267(a)(3) would be necessary, however, where treaty benefits are available."

[16] As the Tax Court noted in *Square D*: "[T]he fundamental principle underlying the intended regulatory authority, in our view [is] namely, the scope of the regulations under section 267(a)(3) is generally determined by the presence or absence of a US method of accounting for the income item in the hands of the foreign recipient, where the US payor seeks to accrue a deduction with respect to that item. … [T]he regulations … reflect this principle. The provisions in general impose the cash method on the US payor under section 267(a)(3) only where the related foreign payee lacks a US method of accounting for the item otherwise accruable by the payor and apply section 267(a)(2) where such payee has a US method of accounting for the item."

[17] *See* Reg. §1.267(a)-3(b)(2) (third sentence). Thus, the example described in the 1986 legislative history (relating to foreign services provided by a foreign corporation to its domestic subsidiary) is not covered by the General (a)(3) Matching Rule, and the payor gets to take a deduction as it accrues.

[18] *See* Reg. §1.267(a)-3(c)(2).

[19] If a foreign person is engaged in a US trade or business and is not exempt from tax under a treaty, the General (a)(3) Matching Rule does not apply; instead Code Sec. 267(a)(2) applies. *See* note 15, *supra*.

[20] *See* Reg. §1.267(a)-3(c)(iv), Example 2 (deduction permitted where corresponding income is excludible from subpart F income under the *de minimis* rule of Code Sec. 954(b)(3)(A)).

[21] 56 FR 11531-01, 1991-1 CB 944.

[22] *See* Reg. § 1.267(a)-3(c)(4)(iv), Example 2 (US affiliate owes interest to a CFC where the subpart F *de minimis* exception applies).

[23] Among other things, these taxpayers pointed to the following passage of Notice 89-84 to support their position:

[24] *See Tate & Lyle, Inc.*, 103 TC 656, Dec. 50,241 (1994).

[25] *See Tate & Lyle, Inc.*, CA-3, 96-2ustc ¶50,340, 87 F3d 99, reversing Tax Court.

[26] *See Square D*, 118 TC 299, Dec. 54,687 (2002) (essentially reversing the Tax Court's prior position in *Tate & Lyle*, and agreeing with the Third Circuit's opinion in that case – "To the extent our opinion in *Tate & Lyle* is inconsistent, we will no longer follow it").

[27] *See Square D*, CA-7, 2006-1ustc ¶50,162, 438 F3d 739, affirming Tax Court.

[28] *See* Reg. §1-267(a)-3(c)(4)(iv), Example 3 (CFC owes accrued interest to a related cash method CFC).

[29] These circumstances are similar to those involved in Enron's Project Apache, where the interest deductible to the US affiliate was income to a related CFC, but the interest accrual did not result in a subpart F inclusion. (Following Enron's failure, the Joint Committee on Taxation reviewed the company's old tax returns and tax opinion letters, and published a comprehensive report describing the company's tax planning. Several legislative changes were made in response to this report.) *See* Joint Committee on Taxation, 108th Cong., *Report of Investigation of Enron Corporation and Related Entities Regarding Federal Tax and Compensation Issues, and Policy Recommendations*, Vol. 1-3 (the "JCT Enron Report"). Project Apache is described in Volume 1, p. 242. In the words of the JCT Enron Report:

"Project Apache was a financing arrangement in which the Enron group borrowed funds from third-party foreign lenders. By channeling this third party borrowing through an Enron controlled for-

eign corporation and blending this borrowing with debt that the Enron group owed itself, the Enron group sought to claim US tax deductions not only for interest paid on the third party debt, but also for the interest paid to itself, without triggering any offsetting income inclusion on the Enron controlled foreign corporation's receipt of such interest."

The JCT Enron Report primarily focused on the impact of specific subpart F provisions on the Project Apache structure (including the allocation of subpart F income under Code Sec. 951, which the IRS and the Treasury have since addressed by regulation – see Reg. §1.951-1(e)). While the current accrual of a deduction for interest by a US taxpayer with no current subpart F inclusion to the US shareholder of the CFC payee created some of the US tax benefits from the Project Apache structure, the predominant benefits of the structure related to the allocation of earnings and profits of the CFC under Code Sec. 951. This conclusion is further supported by the fact that, while the JCT Enron Report mentions the Code Sec. 267(a)(3) issue, the legislative history to the AJCA amendments to section 267(a)(3) does not specifically mention Project Apache (while other AJCA amendments do).

30 H.R. Rep. No. 108-393, 108th Cong., 1st Sess., at 267 (2003).

31 There is one reference in the legislative history to a mismatch that could arise where a CFC accrues a deduction with respect to an amount owed to a related CFC, and the deduction offsets subpart F income earned by the payor CFC but does not result in a subpart F inclusion to the US shareholder of the payee CFC. *See* H.R. Rep. No. 108-548(I), 108th Cong., 2d Sess., at 291 (2004) (repeal of the FASIT rules specifically addresses the use of a FASIT in Project Apache). However, this statement in the legislative history ignores the fact that a payment or accrual by a CFC that reduces the payor CFC's subpart F income would not qualify for a subpart F exemption in the hands of the payee CFC under either the same country exception of Code Sec. 954(c)(3) or the new CFC look-thru rule of Code Sec. 954(c)(6). (The potential mismatch which concerned Congress would appear to arise only in very limited circumstances – where the corresponding income to the payee CFC qualified under either the *de minimis* exception of section 954(b)(3) or the high-tax exception of Code Sec. 954(b)(4).)

32 *See* L.G. "Chip" Harter and Rebecca E. Lee, *The Application of Code Section 267(a)(3)(B) to Expenses Accrued by Controlled Foreign Corporations*, International Tax J., May–June 2008, at 15.

33 Emphasis added.

34 Emphasis added.

35 Emphasis added.

36 Reg. §1.451-2(a).

37 Reg. §1.451-2(b).

38 *Id*.

39 *See* Part 1, A, *supra*.

40 Reg. §1.267(a)-1(b)(4), Example (emphasis added).

41 *See, e.g.*, *Kaw Dehydrating Co.*, 74 TC 370, Dec. 36,963 (1980); *Young Door Co., Eastern Division*, 40 TC 890, Dec. 26,283 (1963).

42 *Casa de la Jolla Park, Inc.*, 94 TC 384, Dec. 46,450 (1990). In FSA 200006003, FSA 199922034, FSA 199926018, for example, the IRS argued that a capitalization of accrued interest owed to a shareholder resulted in a deemed payment to the shareholder subject to withholding tax, whether or not shares were issued in the capitalization.

[43] *B.L. Battlestein*, CA-5, 80-2ustc¶9840, 631 F2d 1182 (*en banc*), *cert denied*, SCt, 451 US 938; *C.H. Davison*, 107 TC 35, Dec. 51,524 (1996), *aff'd*, CA-2, 98-1ustc¶50,296, 141 F3d 403; *D.L. Wilkerson*, CA-9, 81-2ustc¶9657, 655 F2d 980, *rev'g and rem'g*, 70 TC 240, Dec. 35,156 (1978); *N.W. Menz*, 80 TC 1174, Dec. 40,248 (1983); *N.A. Burgess*, 8 TC 47, Dec. 15,550 (1947).

[44] Emphasis added.

[45] Given that Code Sec. 267(a)(3)(B) merely defers a deduction, rather than denying it permanently, it is generally believed that a corporation's earnings and profits under Code Sec. 312 are reduced by the deferred amount only when it is recognized for purposes of calculating income. There is some confusion on this point, given that Reg. §1.312-7(b)(1) states that losses disallowed under Code Sec. 267 reduce earnings and profits currently. Given that the regulation was last amended in 1972, it appears to be referring to cases where section 267 permanently denies a deduction. Since the regulation was issued, Code Sec. 267(a)(2), Code Sec. 267(a)(3) and Code Sec. 267(f) have been amended or added to provide for temporary deferral, rather than permanent denial of deductions.

[46] *See, e.g.*, Reg. § 1.1441-2(e)(1): "A payment is considered made to a beneficial owner if it is paid in partial or complete satisfaction of the beneficial owner's debt to a creditor."

GCC States Seek VAT Framework Outline By May

Gulf Cooperation Council (GCC) states reportedly consider that it is still feasible to introduce a shared value-added tax (VAT), despite deadlines for the agenda being repeatedly pushed forward for several years.

The *Kuwait News Agency* quoted the Undersecretary of Kuwait's Finance Ministry, Khalifa Hamada, as saying that the 46th meeting of GCC finance and economy officials had concluded with an agreement that a legal framework for VAT be tabled at their next meeting in May.

A pan-GCC VAT has been proposed to offset the loss of customs revenues from the removal of internal customs duties between the states, a proposal that has been under discussion for several years.

It is anticipated that, if adopted, the GCC states – Kuwait, Bahrain, Saudi Arabia, Qatar, the United Arab Emirates, and Oman – would levy a rate of between 3 and 5 percent. It was said that GCC states could agree to a VAT by the end of this year, but – based on the pace of progress to-date – this is an optimistic deadline, unless states can quickly overcome a number of hurdles that have so far stymied progress.

Brazilian Gov't Continues To Seek ICMS Harmonization

Brazilian states failed to agree upon reform of the nation's provincial value-added tax, ICMS, during recent meetings, despite a more concrete offer of compensation from the Brazilian central Government.

Proposals to harmonize ICMS rules, in particular to eliminate tax competition between states and enforce restrictions on the introduction of tax breaks, have been under discussion for almost two decades. In general, the discussions have focused on introducing a single rate of 4 percent, but concessions allowing for higher rates for certain states have been discussed.

ICMS is a tax on the interstate sale of goods and services, at rates ranging between 7 percent and 12 percent. The regime is critically flawed as states may compete to win investment by undercutting each other with targeted ICMS tax breaks. To have a tax break authorized, states must theoretically receive unanimous approval from the National Council of Fiscal Policy (CONFAZ) which houses a representative from each province; however, the case has usually been that they sidestep the process and introduce the tax break anyway.

Less affluent provinces, which have doggedly refused a unified rate over the years, have experienced

stronger rates of growth averaging 3 percent; while richer, resource-heavy provinces Rio de Janeiro, São Paulo, and Minas Gerais have seen growth rates averaging 2.2 percent.

In a bid to achieve consensus, the Government has now put forward proposals to pay compensation to the states worth USD3bn in 2016. This figure would increase to up to USD13bn in eight years, when the reform would be completed. At the recent meeting, three states that had previously been opposed to the plans voted in favor of a unified rate. Four states continued to oppose the deal.

Deloitte Releases Annual Indirect Tax Survey

Deloitte, the business advisory firm, has released the findings of its 2015 indirect tax survey, charting the key considerations for indirect tax professionals in recent times.

Indirect tax continues to be a topic of discussion at board and senior management level, the survey says. Two-thirds of respondents (67 percent) said that value-added tax (VAT) and/or goods and services tax (GST) had been discussed by the board or senior management in the last year.

Kendra Hann, Indirect Tax Leader at Deloitte, said: "There are definite themes in the topics discussed at boardroom and senior management level. HMRC's policy on the VAT treatment of holding companies, the implications of the Skandia case about VAT grouping, managing compliance risk, and managing partial exemption were all topics cited by a number of respondents."

Over half of indirect tax professionals have been asked to justify their indirect tax strategy over the last year, receiving questions from a broad range of stakeholders within their organizations. There continues to be interest from employees inside (36 percent) and outside (38 percent) the tax function, commercial teams (34 percent), non-executive directors (7 percent), and board members (30 percent).

Around two-thirds of respondents say that their organization has started to look at the impact of the OECD base erosion and profit shifting (BEPS) project, and in the majority of these cases (57 percent) they involve the indirect tax team. In a fifth of cases (22 percent), the indirect tax team was closely involved and over a third (35 percent) said they were involved in a limited way.

Over 70 percent of UK respondents said they have met with the UK tax authority, HM Revenue & Customs (HMRC), to discuss VAT in the past year and describe their relationship as good (59 percent) or excellent (21 percent).

Hann added: "Many respondents referred to regular meetings with HMRC, risk reviews, and other customer relationship manager meetings. Aside from these regular meetings, the most-often cited reason for a meeting with HMRC was to discuss partial exemption. Discussions also took place regarding a number of other issues, including VAT

return queries and changes to business structures and systems."

Almost 60 percent of respondents said they were responsible for indirect tax outside the UK, mostly in the EU, but significant numbers said they were responsible for indirect tax matters in other regions. This is consistent with the findings from previous surveys.

Hann concluded: "Indirect tax professionals are faced with ongoing global developments in indirect tax law and policy, with countries continuing to adopt VAT and GST systems and adapt their existing systems in line with international norms. Significant recent developments include the introduction of GST in Malaysia, the proposed GST in India, ongoing changes in China, and changes to the VAT and GST treatment of electronically supplied services in a number of jurisdictions."

UK, Australia To Push Diverted Profits Taxes

UK Chancellor George Osborne and Australian Treasurer Joe Hockey have committed to establishing a working group to urgently consider and develop initiatives centered on the UK's Diverted Profits Tax (DPT).

The announcement was made at the G20 Finance Ministers and Central Bank Governors Meeting, which was held in the US on April 16–17, 2015.

One of the issues highlighted at the G20 meeting was that, through contrived arrangements, some multinational corporations are diverting profits to avoid tax in their relevant/host jurisdictions.

The two ministers agreed that, subject to the UK Government's reelection, they will establish a working group comprising senior officials to develop measures to address the issue.

The working group, which will be open to all G20 members, will build on the UK's experience in operating its DPT, which came into effect at the beginning of April 2015. Previously, Australia has expressed interest in introducing a similar arrangement.

The ministers said that any working group initiatives will be consistent with the OECD's ongoing work on base erosion and profit shifting, and other international initiatives.

Earlier in March 2015, the UK announced that it is sharing information with five foreign tax administrations, including Australia, to identify and tackle the international tax issues caused by the digital economy. The information is being shared under the "E6" initiative, which was launched in August 2013 by a group of six nations to collaborate and exchange information on complex tax avoidance schemes and structures.

NZ Calls For Conclusion Of GCC FTA

New Zealand's Prime Minister, John Key, said that he will use an upcoming visit to the Middle East to push for the conclusion of a free trade agreement (FTA) with the Gulf Cooperation Council (GCC), a political and economic union comprised of Bahrain, Kuwait, Oman, Qatar, Saudi Arabia, and the United Arab Emirates (UAE).

Key will lead an 18-member New Zealand business delegation to the UAE, Saudi Arabia, and Kuwait from April 26 to May 1, according to a statement from the New Zealand Government.

"A key priority for me will be talking to key figures in the region about the importance of progressing New Zealand's [FTA] with the GCC," the Prime Minister said.

Negotiations on the New Zealand–GCC FTA were successfully concluded on October 31, 2009, following six rounds of talks, but the agreement has not yet

been signed by ministers from the relevant countries. Details about the agreement, including information on tariffs, will be made public upon signature.

New Zealand has previously said that a key reason for pursuing an FTA with the GCC is to bring about the removal of the GCC's 5 percent common external tariff for New Zealand goods as well as the tariffs imposed by individual GCC states.

"Although the GCC's tariffs are generally low by international standards, New Zealand's competitive edge, most obviously in agricultural products but also in New Zealand's rising manufactured exports, could be eroded by agreements the GCC is reaching with a number of economies," the Government said. "Many of these countries are New Zealand's major competitors in the Gulf region."

The GCC is New Zealand's fifth largest export destination with goods exports worth NZD1.9bn (USD1.46bn) in the year to December 2014. Exports of goods have grown by an average 10 percent per year over the last decade, the Government said.

During a recent visit to the Gulf, Australian Trade and Investment Minister Andrew Robb called for the signing of the Australia–GCC FTA.

Tax Compliance Burden Falling, Say New Zealand SMEs

Tax compliance costs for small and medium-sized enterprises (SMEs) in New Zealand have continued to fall, according to the findings of a recent survey.

Inland Revenue and Research New Zealand surveyed 1,206 SMEs about tax compliance costs in 2013/14 and compared the findings with results from two earlier surveys in 2004 and 2009. The report shows tax compliance costs have fallen by 11.7 percent since 2004.

Commenting on the findings, Small Business Minister Craig Foss said: "This is excellent news for New Zealand's small businesses but there is still more work to be done."

"The Government is committed to further reducing the cost of doing business with measures such as the Rules Reduction Taskforce and the recently launched public consultations on modernizing and simplifying the tax system," he added.

The Government said discussions were held with 25 business owners following the 2013/14 survey to determine how Inland Revenue could further help ease compliance costs.

Foss said: "I encourage small business owners to keep engaging with the Government and sharing their ideas for improving the business environment. Helping our small businesses grow will help the New Zealand economy grow."

Hong Kong Gazettes Budget Tax Relief Bills

The Inland Revenue (Amendment) (No. 2) Bill 2015, which will implement the concessionary salaries and profits tax revenue measures proposed in Hong Kong's 2015/16 Budget, was gazetted on April 17.

The Budget's tax relief policies include an increase to the basic and additional child allowances under the salaries tax and tax under personal assessment from HKD70,000 (USD9,000) to HKD100,000; and a reduction to salaries tax, tax under personal assessment, and profits tax for the year of assessment 2014/15 by 75 percent, subject to a ceiling of HKD20,000 per taxpayer.

"The Bill will be introduced into the Legislative Council on April 29," a Government spokesperson said. "Subject to the passage of the Bill, the proposal of increasing the basic and additional child allowances will take effect from the year of assessment 2015/16 onwards. The proposal will benefit about 370,000 taxpayers and involve HKD2bn a year as revenue foregone."

On the other hand, the reduction of salaries tax, tax under personal assessment, and profits tax for the year of assessment 2014/15 will be reflected in the taxpayers' final tax liability for 2014/15.

"The proposal will benefit about 1.82m persons paying salaries tax and tax under personal assessment, as well as about 130,000 corporations and unincorporated businesses paying profits tax. The estimated one-off revenue foregone is HKD17.7bn," the spokesperson added.

Return Of UK's 50 Percent Rate 'Would Encourage Avoidance'

The London School of Economics' Centre for Economic Performance (CEP) has said that proposals to reintroduce a 50 percent top rate of income tax would likely result in a negligible fall in the working hours of higher earners but will lead to an increased tax avoidance risk. It says tougher enforcement will be required to ensure payment of tax at the higher rate.

The findings are included in a new report from the CEP, released ahead of the May 2015 UK general election.

In 2010, Labour raised the top rate of income tax (the "additional rate") from 40 percent to 50 percent for those with taxable income over GBP150,000. The personal allowance was phased out for those with income above GBP100,000, leading to a marginal tax rate of 60 percent for affected earners.

The coalition Government reduced the additional rate to 45 percent in 2013 but retained the

phase-out of the personal allowance. The Labour manifesto proposes to restore the 50 percent rate for those with taxable income over GBP150,000, while the Green Party proposes raising it to 60 percent. The UKIP manifesto mentions the ambition to lower the rate to 40 percent. The Liberal Democrat and Conservative manifestos do not mention the top rate of tax, though it was widely reported that the Conservatives wanted a rate of 40 percent when the rate was reduced in 2013.

According to the CEP paper, in 2012/13, only 0.9 percent of taxpayers (273,000 people) had taxable income above GBP150,000. They received 11 percent of total taxable income and paid 25 percent of income tax. It warns that as rates increase, reported taxable income tends to decline. It says that revenue could fall under plans for a higher rate on account of a drop in compliance.

Professor Alan Manning, the report's author, said that if the next government hopes to raise the top tax rate, it must be complemented by a redoubled effort to tackle tax avoidance. He said: "If politicians want to raise the top rate of tax, they need a more aggressive approach to dealing with tax avoidance and tax evasion."

Austria To Cut Income Tax Rates

In an announcement on April 13, 2015, the Austrian Government has confirmed that its proposed tax reforms will include significant cuts to the individual income tax burden.

The Government has now provided more detail, in German, of its plans for individual tax cuts, which were first announced in March. Among the proposed changes are a cut in the lowest rate of tax from 36.5 percent to 25 percent, and a rise in the threshold for the highest rate of 50 percent, from EUR60,000 (USD64,800) to EUR90,000. There will also be increased social security reliefs for the lowest earners and pensioners, and an increase in child and family allowances.

The cuts will be financed by increases in the capital gains tax rate to 27.5 percent and property tax from 25 percent to 30 percent, and initiatives to improve compliance rates.

Earlier it was announced that the 10 percent reduced rate of value-added tax, which is applied broadly, would be raised to 13 percent for certain supplies.

Belgium Announces Tax Breaks For Digital Start-Ups

Belgian Minister for Digital Agenda Alexander de Croo has promised significant tax breaks as part of government plans to support the digital economy sector.

As part of this plan, de Croo has promised a "tax shelter" for such enterprises, focusing on labor taxes. Tax incentives are also planned for crowdfunding initiatives.

The tax measures are aimed at creating 1,000 new start-ups and 50,000 new jobs by 2020.

Iceland May Tax Payments To Bank Sector Creditors

Iceland's Prime Minister, Sigmundur Davíð Gunnlaugsson, anticipates that Iceland will be in a position to settle claims against Icelandic banks that went bust in 2008 by the middle of this year, alongside the imposition of a "stability tax."

During his speech to the Progressive Party conference on April 10, Gunnlaugsson indicated that plans for such a stability tax – an exit tax – would be introduced before the Icelandic Parliament's summer recess. It would be imposed on foreign creditors, including hedge funds, on funds recovered and repatriated when the assets of the banks are divvied out.

The Prime Minister confirmed that the Government has been preparing the measure for some time, while waiting for administrators to present concrete plans to wind up the banks. The tax would be introduced before this process is complete.

The tax could limit the flight of capital out of Iceland, which the Government says will prevent a rapid fall in the Icelandic currency. According to Gunnlaugsson, it would also generate "hundreds of billions of krona."

Previously, a tax rate of up to 40 percent was mooted, with a lower rate considered for situations in which creditors agree to take receipt of funds over a longer period.

Singapore Extends FATCA Reporting Deadline

For the 2014 reporting year only, the Inland Revenue Authority of Singapore (IRAS) is extending the filing deadline for reporting Singaporean financial institutions (SGFIs) to submit their US Foreign Account Tax Compliance Act (FATCA) data to July 31, 2015, from May 31.

FATCA requires all financial institutions outside the US to submit regular information on financial accounts held by US persons to the Internal Revenue Service (IRS), or otherwise face a 30 percent withholding tax on certain payments of US-sourced income.

To ease FATCA compliance for SGFIs, Singapore concluded a Model 1 Intergovernmental Agreement (IGA) with the US, which was signed on December 9, 2014, and which entered into force on March 18 this year. Model 1 IGAs provide for financial institutions to report account information relating to US persons to their relevant domestic tax authority – in Singapore's case, the IRAS – which, in turn, shares this information with the IRS.

A reporting SGFI must, in respect of the 2014 reporting year (FATCA's first) and in every following calendar year, prepare and provide to the IRAS a return setting out the required information in relation

to every US reportable account that is maintained by the SGFI at any time during the calendar year in question.

A reporting SGFI that does not maintain any US reportable accounts for reporting year 2014 must provide a nil return by either preparing a FATCA reporting packet and transmitting it through the IRS's International Data Exchange Service, or by completing a paper FATCA Nil Return (which will be made available at a later date) and mailing it to IRAS by July 31, 2015.

US House Passes Hiring Ban On Tax-Delinquent Contractors

On April 15, alongside a series of bills concerning oversight of the Internal Revenue Service (IRS), the US House of Representatives approved a bi-partisan bill to prohibit the award of contracts or grants to companies or individuals with seriously delinquent tax debt.

The Contracting and Tax Accountability Act, introduced by House Oversight and Government Reform Committee Chairman Jason Chaffetz (R – Utah), would apply to contracts and grants awarded 270 days after enactment of the legislation. Any government executive agency that issues an invitation for bids greater than an acquisition threshold much obtain evidence that each proposed contractor does not have a seriously delinquent tax debt.

The Government Accountability Office found that thousands of federal contractors had substantial amounts of unpaid federal taxes in 2007 – for example, about 27,000 Department of Defense, 33,000 civilian agency, and 3,800 General Services Administration contractors owed USD3bn, USD3.3bn, and USD1.3bn, respectively.

In addition, in 2013, the Treasury Inspector General for Tax Administration reported there were 1,168 IRS contractors that owed a combined USD589m in delinquent taxes.

"If you have unaddressed tax delinquency issues, you should not be awarded government contracts or grants," said Chaffetz. "It is antithetical to use taxpayer resources to fund contractors who aren't fulfilling their own tax responsibilities. This bill is a common sense way to ensure that we prioritize law-biding taxpayers above those who are skirting their legal duty to pay taxes."

Committee Ranking Member Elijah Cummings (D – Maryland) agreed that "contractors seeking to do business with the federal Government should have paid their taxes before they can receive a federal contract and ensure that responsible contractors no longer have to compete with tax delinquents."

However, another bill that would have also made individuals with tax debts ineligible for federal employment did not receive the necessary two-thirds majority in the House, and did not pass.

Although IRS figures showed that, in 2014, over 113,800 civilian federal employees owed a total of USD1.14bn in taxes, the Federal Employee Tax Accountability Act (also sponsored by Chaffetz) was not supported by Cummings, who pointed out that the IRS has confirmed that it does not have a problem collecting delinquent taxes from federal employees.

It was confirmed that the IRS has the Federal Payment Levy Program in place to recoup funds from federal employees who fail to pay their taxes. Under

this program, the agency imposes a continuous levy on federal salaries and pensions of up to 15 percent until the debt is paid. It has collected over USD5bn in this way since 2000.

Other bills concerning the IRS, all sponsored by Republican representatives on the Ways and Means Committee and passed by the House with bipartisan support on April 15, included the incorporation of a Taxpayer Bill of Rights into the agency's core responsibilities; and an improvement to the process for making determinations with respect to whether organizations are exempt from taxation. For example, the IRS would be prevented from targeting organizations because of their political or religious beliefs, and groups would be allowed to declare their tax-exempt status rather than wait to gain approval from the agency.

All of the approved bills now move to the Senate, where it is expected that they will again receive bipartisan support.

US Congress Receives AGOA, GSP Extension Bills

The four leaders of the US Senate Finance and House of Representatives Ways and Means Committees have announced legislation to renew both the African Growth and Opportunity Act (AGOA) and the US Generalized System of Preferences (GSP).

The two trade preference programs would be extended by the bipartisan, bicameral AGOA Extension and Enhancement Act of 2015, which was introduced by Finance Committee Chairman Orrin Hatch (R – Utah) and its Ranking Member Ron Wyden (R – Oregon), along with Ways and Means Committee Chairman Paul Ryan (R – Wisconsin) and its Ranking Member Sander Levin (D – Michigan), on April 16.

Both programs have increased trade with beneficiary countries by lowering US tariffs on their exports. Under the US GSP, which last expired on July 31, 2013, up to 5,000 types of products from 126 beneficiary developing countries were eligible for duty-free treatment when exported to the US. In 2012, the total value of imports that entered the US duty free under GSP was USD19.9bn.

The AGOA's trade preferences, along with those under the US GSP and its third-country fabric provision, allow for almost all goods produced in AGOA-eligible countries – approximately 6,800 products – to enter the US market duty free. It is currently in effect until September 30, 2015, and has contributed, since 2000, to a near doubling of trade with those eligible African countries, which are now seeking a longer-term extension.

The proposed legislation would extend the AGOA for a further ten years, together with its third-country fabric provisions. It also contains measures to: promote greater regional integration by expanding rules of origin to allow AGOA countries greater flexibility to combine inputs, to strengthen congressional oversight through additional notification and reporting requirements, and to improve

transparency and participation in the AGOA review process.

The US GSP would be extended until December 31, 2017, and would provide retroactive relief to eligible products that were imported while it had lapsed. In addition, US World Trade Organization commitments would be implemented by making duty-free certain cotton articles eligible from least-developed beneficiary developing countries.

"By strengthening trade relations through the renewal of trade preference programs, we can better promote trade liberalization and economic reform around the world," said Hatch. "These programs have helped to make trade with the developing world mutually beneficial, worked to reduce global poverty, and created growth and opportunity for American job creators by reducing tariffs and lowering costs."

"This long-term extension and update of the AGOA … provides certainty for sub-Saharan African countries, investors, and workers while strengthening our economic and political ties with Africa," Wyden added. "By retroactively extending our GSP, our legislation will save American businesses an estimated USD2m a day."

"This legislation will promote American trade and strengthen our economic ties with important countries," Ryan concluded. "It demonstrates that more trade can create opportunity at home and promote our economic values abroad."

EU Council Endorses Beneficial Ownership Proposals

The Council of the European Union on April 20, 2015, endorsed proposals to require member states to maintain a central register of information on the beneficial ownership of corporate and other legal entities. It would be at the discretion of member states whether such information would be publicized.

Under the proposals, beneficial ownership information would be accessible to competent authorities and financial intelligence units and, in the framework of the conduct of customer due diligence, to obliged entities.

The plan was endorsed as part of a package of measures aimed at preventing money laundering and terrorist financing. The following information on beneficial owners would be retained:

- Name;
- Month and year of birth;
- Nationality;
- Country of residence; and
- The nature and approximate extent of the beneficial interest held.

As for trusts, the central registration of beneficial ownership information will be used where the ownership of a trust has tax consequences.

France Seeks To Curb Tax Bureaucracy

The French Government has indicated its willingness to tackle the lack of trust between enterprises and the tax authorities.

In a new report entitled "Improving The Relationship Between The Tax Administration And Businesses," the Government says that to "invest, innovate and employ, economic players need stability, security and transparency." It goes on to set out a series of measures designed to create a better relationship between the state and businesses, which it hopes will both facilitate enterprise and decrease tax fraud.

The report sets out three steps. First, the Government noted the recent publication of tax structures deemed to be abusive. Second, the document sets out a ten-point charter on how authorities will behave when dealing with taxpayers. It states that businesses should refer to this charter and will have the right to cite it in any dispute with the tax authorities.

Last, the Government seeks to address the current lack of a clear process for tax disputes, particularly in respect of larger cases. To remedy this, a "Committee of Experts" is to be established, comprising tax professionals. This committee will be able to give expert advice to the administration, including on payment demands, fines, and penalties.

Irish SMEs Fear Impact Of Lower NI Corporate Tax

Two in five small Irish firms are concerned that the introduction of a lower corporate tax rate in neighboring Northern Ireland could have a negative impact on the Republic's economy, according to a new survey.

The findings come from the latest Close Brothers Business Barometer, a quarterly survey that canvasses the opinion of small business owners and managers across the UK and Ireland. Of those surveyed in the Republic, 41 percent said that they are concerned Ireland may face increased competition for foreign investment as a result of the devolution of corporate tax powers to the Northern Ireland Executive.

Legislation passed by the UK Parliament last month will enable the Executive to set a lower rate of corporation tax from April 2017. First Minister Peter Robinson has signaled his support for a 12.5 percent rate, in line with that charged in the Republic. The current rate, applicable across the UK, is 20 percent.

Adrian Madden, from Close Brothers Commercial Finance, said: "It's understandable for there to be a sense of unease about the proposed changes but we also need to consider the positives over and above any negative implications. Competition is the lifeblood of strong and effective markets and encourages businesses to be innovative, not complacent, with pricing structures, technology, and quality of service, for example. With this in mind, now is the time for firms to raise the bar to continue to compete within their own industries and ensure Ireland remains at the forefront of foreign investment."

CCAB-I Discusses Ireland's 'Patent Box' Plans

The Consultative Committee of Accountancy Bodies – Ireland (CCAB-I) has responded to a public consultation, issued by Ireland's Department of Finance, on the introduction of the Knowledge Development Box (KDB).

Earlier in January 2015, the Government announced that it will offer a tax rate below 12.5 percent on intellectual property income under its KDB. It invited stakeholders' views on how the KDB should be designed to ensure it meets the key objective of being the most competitive of its type, while remaining within the recently agreed international parameters for fair tax competition in this area, as part of the OECD's ongoing base erosion and profit shifting (BEPS) work on harmful tax practices.

Commenting on the plans, the CCAB-I said: "As with any system that provides tax incentives, anti-avoidance should be a key consideration in the development of any KDB provisions. Any anti-avoidance rules pertaining to an Irish KDB clearly should be formulated to ensure we do not fall foul of EU or BEPS harmful tax measures concerns."

The CCAB-I said that "careful consideration needs to be given to the current research and development (R&D) regime in operation in Ireland. We would suggest that the regime be further enhanced to cement Ireland's reputation as a center of excellence for R&D activity. We believe that the KDB can and should work hand in hand with the R&D tax incentive scheme to ensure that a strong intellectual property environment remains at the heart of Ireland's foreign direct investment (FDI) offering."

The CCAB-I further noted: "[I]n the UK the full benefit of the Patent Box regime [has been phased in] from April 1, 2013, with the full benefit not realizable until the financial year commencing on April 1, 2017. Italy has recently introduced a Patent Box regime in 2015 and has also taken a phased approach to its implementation. We suggest that consideration be given to the merits of this approach regarding the KDB and whether the Irish KDB regime should be permanent and irrevocable (as in the UK) or reviewable after a period of time (as in Italy)."

The CCAB-I continued: "The method of providing relief for qualifying KDB profits should also considered. The UK provides a reduced rate of corporation tax of 10 percent (50 percent of the current UK main rate of 20 percent) whereas Italy provides a 50 percent exemption for qualifying royalties derived from the licensing of qualifying intangibles. The latter methodology (as opposed to a 6.25 percent rate of corporation tax) may be helpful in communicating the benefit of this incentive to prospective FDI investors."

The CCAB-I concluded: "We are mindful of the OECD's Forum on Harmful Tax Practices work in relation to BEPS Action 5 … Work within the Forum on Harmful Tax Practices has led to the development of proposals for new rules, known as the Modified Nexus approach. However, these are far from final. Perhaps Ireland should consider an exemption from capital gains realized upon the sale of intellectual property assets, under the condition that at a substantial percent (say at least 90 percent) of the proceeds received are reinvested into [R&D] activities in Ireland, possibly within a two-year time frame."

IMF Says Now Is Opportune Time For Energy Tax Reform

The International Monetary Fund (IMF) has called on governments around the world to take advantage of low oil prices and reform energy taxes to support sustainable economic growth.

"Getting energy prices right would be beneficial to the economy, environment, and public health," says a new IMF report. "It would assist governments with their fiscal consolidation efforts or to make further investment in critical areas such as education and health. In advanced economies, taxes on labor could be cut and paid for with higher energy taxes."

It noted that more than 20 countries have recently taken steps to cut energy subsidies, including Angola, Côte d'Ivoire, Egypt, India, Indonesia, and Malaysia.

Previously the IMF in particular urged countries to bring tax rates on energy products into line with their environmental impact and to remove support for diesel and petrol compared with more environmentally friendly alternatives.

Greenpeace Seeks Tax Breaks From Brazil For Solar Panels

Environmental organization Greenpeace is lobbying the Brazilian Government to eliminate the state value-added tax, ICMS, on supplies of solar panels.

"Brazil is one of the countries with the best potential for solar energy in the world, but still has a lot of work to do to encourage use of the energy source," says Barbara Rubim, who is leading the Climate and Energy Campaign for Greenpeace Brazil. "One of the tasks to be fulfilled is to solve the ICMS."

Greenpeace has pointed out that Brazil does not yet produce enough energy to meet demand. If solar panels were exempt from ICMS, the cost of panels could be reduced by 20 percent and uptake would increase by 55 percent, Greenpeace estimates.

It said that if the federal Government wants to give a signal that it is seeking investment in renewable energy, this step needs to be taken.

To raise awareness of its efforts, on April 7, 2015, Greenpeace members campaigned outside the offices of the Ministry of Finance, calling on the Minister, Joaquim Levy, to introduce the concession, and on April 10, 2015, similar efforts took place at the offices of the National Council for Financial Policy (CONFAZ), which would be responsible for making the required legislative changes.

CYPRUS - SOUTH AFRICA

Signature

Cyprus and South Africa signed a Protocol to their DTA on April 1, 2015.

GUERNSEY - MONACO

Into Force

The DTA signed between Guernsey and Monaco will enter into force on May 9, 2015.

IRAQ - KUWAIT

Negotiations

Iraq's Cabinet has approved the launch of negotiations towards a DTA with Kuwait, according to a statement released on April 2, 2015.

ITALY - HOLY SEE (VATICAN CITY)

Signature

Italy and the Vatican signed a TIEA on April 1, 2015.

MEXICO - GUATEMALA

Signature

Mexico and Guatemala signed a DTA on March 13, 2015.

MEXICO - UNITED STATES

Into Force

According to preliminary media reports, the Protocol amending Mexico's DTA with the United States entered into force on April 16, 2015.

NETHERLANDS - MALAWI

Signature

The Netherlands and Malawi have signed a DTA, the Dutch Ministry of Finance announced on April 20, 2015.

NEW ZEALAND - CANADA

Ratified

New Zealand on April 13, 2015 enacted legislation to ratify the pending DTA and two accompanying Protocols with Canada.

NEW ZEALAND - JAPAN

Terminated

New Zealand on April 13, 2015 enacted legislation to terminate the 1963 DTA with Japan, effective from April 28, 2015.

NEW ZEALAND - MARSHALL ISLANDS

Into Force

New Zealand's TIEA with the Marshall Islands entered into force on April 9, 2015.

POLAND - BERMUDA

Into Force

The TIEA between Poland and Bermuda entered into force on March 15, 2015.

PORTUGAL - SAUDI ARABIA

Signature

Portugal and Saudi Arabia signed a DTA on April 8, 2015.

QATAR - ECUADOR

Ratified

Qatar on April 14, 2015 ratified the pending DTA signed with Ecuador.

SEYCHELLES - GUERNSEY

Ratified

The Seychelles has adopted legislation ratifying the DTA signed with Guernsey.

SINGAPORE - ETHIOPIA

Negotiations

According to preliminary media reports, Singapore has expressed interest in launching DTA negotiations with Ethiopia.

UNITED ARAB EMIRATES - ETHIOPIA

Signature

The United Arab Emirates and Ethiopia signed a DTA on April 12, 2015.

VIETNAM - MYANMAR

Negotiations

According to preliminary media reports on March 17, Vietnam and Myanmar are to engage in negotiations towards a DTA.

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

THE AMERICAS

TAX PLANNING FOR DOMESTIC & FOREIGN PARTNERSHIPS 2015 - CHICAGO

PLI

Venue: Skadden, Arps, Slate, Meagher & Flom LLP, 155 N. Wacker Drive, Suite 3500, Chicago, IL 60606-1420, USA

Co Chairs: Stephen D. Rose (Munger, Tolles & Olson LLP), Eric B. Sloan (Deloitte Tax LLP), Clifford M. Warren (Internal Revenue Service)

4/28/2015 - 4/30/2015

http://www.pli.edu/Content/Seminar/Tax_Planning_for_Domestic_Foreign_Partnerships/_/N-4kZ1z129zc?ID=223947

US INTERNATIONAL TAX COMPLIANCE WORKSHOP

BNA

Venue: Bloomberg BNA, 1801 South Bell Street, Arlington, VA 22202, USA

Key Speakers: Jon Brian Davis (Ivins Phillips & Barker Chtd), Adam Halpern (Fenwick & West LLP), Matthew Harrison (PwC LLP), Meg Hogan (KPMG LLP), Josh Kaplan (KPMG LLP), among numerous others

5/4/2015 - 5/5/2015

http://www.bna.com/uploadedFiles/BNA_V2/Professional_Education/Tax/Live_Conferences/IntlTaxWorkshopDynamicsEPMay2015.pdf

US TAX ASPECTS OF INTERNATIONAL SHIPPING

BNA

Venue: Mayer Brown LLP, 1999 K Street NW, Washington, DC 20006, USA

Chair: Kenneth Klein (Mayer Brown LLP)

5/4/2015 - 5/5/2015

http://www.bna.com/uploadedFiles/BNA_V2/Professional_Education/Tax/Live_Conferences/ShippingMay2015.pdf

TAX PLANNING FOR DOMESTIC & FOREIGN PARTNERSHIPS 2015 - NEW YORK

The Americas

PLI

Venue: The Roosevelt Hotel, 45 East 45th Street, New York, NY 10017, USA

Co Chairs: Stephen D. Rose (Munger, Tolles & Olson LLP), Eric B. Sloan (Deloitte Tax LLP), Clifford M. Warren (Internal Revenue Service)

5/12/2015 - 5/14/2015

http://www.pli.edu/Content/Seminar/Tax_Planning_for_Domestic_Foreign_Partnerships/_/N-4kZ1z129zc?ID=223947

4TH CROSS BORDER PERSONAL TAX PLANNING

Federated Press

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

Chairs: Jonathan Garbutt (Dominion Tax Law), Martin J. Rochwerg (Miller Thomson LLP)

5/26/2015 - 5/27/2015

http://www.federatedpress.com/pdf/HGLegal/CBP1505-E.pdf

TAX PLANNING FOR DOMESTIC & FOREIGN PARTNERSHIPS 2015 - SAN FRANCISCO

PLI

Venue: PLI California Center, 685 Market Street, San Francisco, California 94105, USA

Co Chairs: Stephen D. Rose (Munger, Tolles & Olson LLP), Eric B. Sloan (Deloitte Tax LLP), Clifford M. Warren (Internal Revenue Service)

6/9/2015 - 6/11/2015

http://www.pli.edu/Content/Seminar/Tax_Planning_for_Domestic_Foreign_Partnerships/_/N-4kZ1z129zc?ID=223947

14TH ANNUAL INTERNATIONAL MERGERS AND ACQUISITIONS CONFERENCE

International Bar Association

Venue: Waldorf Astoria New York, New York, NY 10022, USA

Key Speakers: TBC

6/10/2015 - 6/11/2015

http://www.ibanet.org/Article/Detail.aspx?ArticleUid=7ca03d57-41c9-44ba-b1a4-7434572160e9

GLOBAL TRANSFER PRICING CONFERENCE

BNA

Venue: Fairfax Embassy Row, 2100 Massachusetts Avenue Northwest, Washington, DC 20008, USA

Key Speakers: TBC

6/11/2015 - 6/12/2015

http://go.bna.com/transfer-pricing-conference-primer/

INTRODUCTION TO US INTERNATIONAL TAX - BOSTON

Bloomberg BNA

Venue: Morgan Lewis, 225 Franklin Street, Boston, MA 02110, USA

Chair: TBC

6/15/2015 - 6/16/2015

http://www.bna.com/intro2015_boston/

US INTERNATIONAL TAX COMPLIANCE WORKSHOP - SAN DIEGO

BNA

Venue: Manchester Grand Hyatt, One Market Place, San Diego, CA 92101, USA

Key Speakers: TBC

6/15/2015 - 6/16/2015

http://www.bna.com/compliance_sd/

THE 6TH ANNUAL PRIVATE INVESTMENT FUNDS TAX MASTER CLASS

Financial Research Associates

Venue: Princeton Club of New York, 15 W 43rd St, New York, NY 10036, United States

Chairs: Elaine B. Murphy (Ropes & Gray), Jay G. Milkes (Ropes & Gray), Anthony Tuths (Withum Smith+Brown)

6/15/2015 - 6/16/2015

https://www.frallc.com/pdf/B957.pdf

INTERMEDIATE US INTERNATIONAL TAX UPDATE - BOSTON

Bloomberg BNA

Venue: Morgan Lewis, 225 Franklin Street, Boston, MA 02110, USA

Key Speakers: TBC

6/17/2015 - 6/19/2015

http://www.bna.com/inter2015_boston/

BASICS OF INTERNATIONAL TAXATION 2015

PLI

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

Chairs: Linda E. Carlisle (Miller & Chevalier Chartered), John L. Harrington (Dentons US LLP)

7/21/2015 - 7/22/2015

http://www.pli.edu/Content/Seminar/Basics_of_International_Taxation_2015/_/N-4kZ1z129zs?ID=223955

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

BASICS OF INTERNATIONAL TAXATION 2015

PLI

Venue: PLI California Center, 685 Market Street, San Francisco, California 94105, USA

Chairs: Linda E. Carlisle (Miller & Chevalier Chartered), John L. Harrington (Dentons US LLP)

9/28/2015 - 9/29/2015

http://www.pli.edu/Content/Seminar/Basics_of_International_Taxation_2015/_/N-4kZ1z129zs?ID=223955

ASIA PACIFIC

12TH ANNUAL ASIA-PACIFIC TAX FORUM

ICRIER

Venue: The Taj Mahal Hotel, No.1, Mansingh Road, New Delhi, India

Key Speakers: Dr. Jeffrey Owens (OECD), Dave Hartnett (Revenue and Customs), Dr. Sijbren Cnossen (University of Maastricht), Wayne Barford (Australian Taxation Office), among numerous others

5/5/2015 - 5/7/2015

http://www.iticnet.org/images/APTF12Flyer.pdf

THE 6TH OFFSHORE INVESTMENT CONFERENCE HONG KONG 2015

Offshore Investment

Venue: Conrad Hong Kong Hotel, One Pacific Place, Pacific Place, 88 Queensway, Hong Kong

Chair: Michael Olesnicky (KPMG China)

6/17/2015 - 6/18/2015

http://www.offshoreinvestment.com/pages/index.asp?title=The_Offshore_Investment_Conference_Hong_Kong&catID=12190

3RD GLOBAL CONFERENCE ON FINANCE & ACCOUNTING

Asia Pacific International Academy

Venue: Concorde Hotel, 100 Orchard Rd, 238840 Singapore

Chairs: Dr Raymond KH Wong (The Chinese University of Hong Kong), Prof. Dan Levin (Wharton Business School, University of Pennsylvania)

7/29/2015 - 7/30/2015

http://academy.edu.sg/gcfa2015/

MIDDLE EAST AND AFRICA

TRENDS IN INTERNATIONAL TAXATION: AN AFRICAN PERSPECTIVE

IBFD

Venue: Zambezi Sun, Mosi-oa-Tunya Road, Livingstone 20100, Zambia

Key Speakers: Prof. Annet Wanyana Oguttu (University of South Africa), Antonio Russo (Baker & McKenzie), Belema Obuoforibo (IBFD), Eleni Klaver (Carrara Legal), Fredrick Omondi (Deloitte), among numerous others

6/18/2015 - 6/19/2015

http://www.ibfd.org/IBFD-Tax-Portal/Events/Trends-International-Taxation-African-Perspective

WESTERN EUROPE

STEP TAX, TRUSTS & ESTATES CONFERENCE 2015 - BIRMINGHAM

STEP

Venue: Crowne Plaza Birmingham City Centre, Central Square, Birmingham, B1 1HH, UK

Key Speakers: Helen Clarke, George Hodgson (STEP), Helen Jones (BDO LLP), Lesley King

(LK Law Ltd), Lucy Obrey (Higgs and Sons), Peter Rayney (Peter Rayney Tax Consulting Ltd), Chris Whitehouse (5 Stone Buildings).

4/24/2015 - 4/24/2015

http://www.step.org/tax-trusts-estates-step-conference-2015

STEP TAX, TRUSTS & ESTATES CONFERENCE 2015 – LEEDS

STEP

Venue: Hilton Leeds City, Neville Street, Leeds, LS1 4BX, UK

Key Speakers: Helen Clarke, George Hodgson (STEP), Helen Jones (BDO LLP), Lesley King (LK Law Ltd), Lucy Obrey (Higgs and Sons), Peter Rayney (Peter Rayney Tax Consulting Ltd), Chris Whitehouse (5 Stone Buildings).

4/29/2015 - 4/29/2015

http://www.step.org/tax-trusts-estates-step-conference-2015

STEP TAX, TRUSTS & ESTATES CONFERENCE 2015 - LONDON

STEP

Venue: The Queen Elizabeth II Conference Centre, Broad Sanctuary, London, SW1P 3EE, UK

Key Speakers: Helen Clarke, George Hodgson (STEP), Helen Jones (BDO LLP), Lesley King (LK Law Ltd), Lucy Obrey (Higgs and Sons), Peter Rayney (Peter Rayney Tax Consulting Ltd), Chris Whitehouse (5 Stone Buildings).

5/8/2015 - 5/8/2015

http://www.step.org/tax-trusts-estates-step-conference-2015

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

INTERNATIONAL CROSS BORDER ESTATE PLANNING

IBC

Venue: Grange Tower Bridge Hotel, 45 Prescott Street, London, Greater London, E1 8GP, UK

Key Speakers: Steven Kempster (Withers), Michael Wells-Greco (Speechly Bircham), Dominic Lawrence (Speechly Bircham), Edward Stone (Collas Crill), Jon Edmondson (Mourant Ozannes), Richard Dew (Ten Old Square), among numerous others.

5/15/2015 - 5/15/2015

http://www.iiribcfinance.com/event/International-Cross-Border-Estate-Planning

ESTATE & TAX PLANNING FOR THE US CITIZEN IN THE UK

IBC

Venue: Crowne Plaza London - The City, 19 New Bridge St, London, EC4V 6BD, UK

Key Speakers: Kehrela Hodkinson (Hodkinson Law Group), Christopher Horton (Deloitte), Suzanne Reisman (Law Offices of Suzanne Reisman), Peter Cotorceanu (Anaford), among numerous others

5/19/2015 - 5/21/2015

http://www.iiribcfinance.com/event/US-UK-Estate-Planning

INTERNATIONAL BUSINESS TAXATION: INCREASING TRANSPARENCY

ERA

Venue: ERA Conference Centre, Metzer Allee 4, Trier, Germany

Key Speakers: Raquel Guevera (MNKS), Howard M. Liebman (Jones Day), Prof. Jacques Malherbe (Liedekerke Wolters Waelbroeck Kirkpatrick), Alain Steichen (Bonn Steichen & Partners)

4/23/2015 - 4/24/2015

https://www.era.int/upload/dokumente/16950.pdf

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

THE INTERNATIONAL TAX PLANNING ASSOCIATION 40TH ANNIVERSARY CONFERENCE

ITPA

Venue: Sofitel Legend The Grand Amsterdam, Oudezijds Voorburgwal 197, 1012 EX Amsterdam, Netherlands

Chair: Milton Grundy

6/7/2015 - 6/9/2015

https://www.itpa.org/?page_id=9907

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

TAX FOR OFFSHORE SHIPPING

Informa

Venue: Bonhill House, 1-3 Bonhill Street, London, EC2A 4BX, UK

Key Speakers: Harrie van Duin (KPMG Meijburg), Dorte Cock (EY), Jurjen Bevers (Baker & McKenzie), Gavin Stoddart (Moore Stephens CIS), among numerous others

6/16/2015 - 6/17/2015

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

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

TAX PLANNING WORKSHOP

IBFD

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

Key Speakers: Shee Boon Law (IBFD), Tamas Kulcsar (IBFD), Boyke Baldewsing (IBFD), Carlos Gutiérrez (IBFD)

7/2/2015 - 7/3/2015

http://www.ibfd.org/Training/Tax-Planning-Workshop

PRIVATE WEALTH AFRICA 2015

IIR & IBC

Venue: TBC, London

Key speakers: Richard Howarth (African Private Office LLP), Chris Moorcroft (Harbottle & Lewis LLP), Camilla Dell (Black Brick Property Solutions), Jonathan Burt (Harcus Sinclair), Liam Bailey (Knight Frank)

7/8/2015 - 7/8/2015

http://www.iiribcfinance.com/event/Private-Wealth-Africa-Conference

UPDATE FOR THE ACCOUNTANT IN INDUSTRY AND COMMERCE - LONDON

CCH

Venue: Sofitel St James Hotel, 6 Waterloo Place, London SW1Y 4AN, UK

Key Speakers: Toni Trevett, Dr. Stephen Hill, Kevin Bounds, among others.

7/8/2015 - 7/9/2015

https://www.cch.co.uk/AIC

OFFSHORE TAXATION - A BRAVE NEW WORLD

IIR & IBC

Venue: TBC, London

Key Speakers: Emma Chamberlain (Pump Court Tax Chambers), Patrick Soares (Gray's Inn Tax Chambers), Simon McKie (McKie & Co LLP), Giles Clarke (Author - Offshore Tax Planning)

7/14/2015 - 7/14/2015

http://www.iiribcfinance.com/event/offshore-taxation-budget-special

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

DUETS ON INTERNATIONAL TAXATION: GLOBAL TAX TREATY ANALYSIS

IBFD

Venue: IBFD Head Office Auditorium, Rietlandpark 301,1019 DW Amsterdam, The Netherlands

Key Speakers: Richard Vann, Pasquale Pistone, Marjaana Helminen, Peter Harris, Adolfo Martin Jimenez, Scott Wilkie

9/7/2015 - 9/7/2015

http://www.ibfd.org/IBFD-Tax-Portal/Events/Duets-International-Taxation-Global-Tax-Treaty-Analysis-1#tab_program

UPDATE FOR THE ACCOUNTANT IN INDUSTRY AND COMMERCE - BRISTOL

CCH

Venue: Aztec Hotel and Spa, Aztec West, Almondsbury, Bristol, South Gloucestershire BS32 4TS, UK

Key Speakers: Toni Trevett, Dr. Stephen Hill, Kevin Bounds, among others.

9/9/2015 - 9/10/2015

https://www.cch.co.uk/AIC

UPDATE FOR THE ACCOUNTANT IN INDUSTRY AND COMMERCE - MILTON KEYNES

CCH

Venue: Mercure Abbey Hill Hotel, The Approach, Milton Keynes MK8 8LY, UK

Key Speakers: Toni Trevett, Dr. Stephen Hill, Kevin Bounds, among others.

9/15/2015 - 9/16/2015

https://www.cch.co.uk/AIC

INTERNATIONAL TAXATION OF BANKS AND FINANCIAL INSTITUTIONS

IBFD

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

Key Speakers: Ronald Aw-Yong (Beaulieu Capital), Peter Drijkoningen (French BNP Paribas bank), Francesco Mantegazza (Pirola Pennuto Zei & Associati), Omar Moerer (Baker & McKenzie), Pedro Paraguay (NautaDutilh), Nico Blom (NautaDutilh)

9/16/2015 - 9/18/2015

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

UPDATE FOR THE ACCOUNTANT IN INDUSTRY AND COMMERCE - MANCHESTER

CCH

Venue: Radisson Blu Hotel Manchester, Chicago Avenue, Manchester, M90 3RA, UK

Key Speakers: Toni Trevett, Dr. Stephen Hill, Kevin Bounds, among numerous others

9/22/2015 - 9/23/2015

https://www.cch.co.uk/AIC

UPDATE FOR THE ACCOUNTANT IN INDUSTRY AND COMMERCE - OXFORD

CCH

Venue: Oxford Thames Four Pillars Hotel, Henley Road, Sandford-on-Thames, Sandford on Thames, Oxfordshire OX4 4GX, UK

Key Speakers: Toni Trevett, Dr. Stephen Hill, Kevin Bounds, among numerous others

10/6/2015 - 10/7/2015

https://www.cch.co.uk/AIC

THE ITPA MONTE-CARLO MEETING

ITPA

Venue: Hôtel Hermitage Monte-Carlo, Square Beaumarchais, 98000 Monaco

Chair: Milton Grundy

10/11/2015 - 10/13/2015

https://www.itpa.org/?page_id=9909

INTERNATIONAL TAX STRUCTURING FOR MULTINATIONAL ENTERPRISES

IBFD

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

Key Speakers: Boyke Baldewsing (IBFD), Tamas Kulcsar (IBFD)

10/21/2015 - 10/23/2015

http://www.ibfd.org/Training/International-Tax-Structuring-Multinational-Enterprises#tab_program

THE AMERICAS

United States

The US Fifth Circuit Court of Appeals has ruled against a decision by the Commissioner of Internal Revenue to partially disallow BMC Software, Inc.'s (BMC's) repatriated dividends tax deduction under 26 USC Section 965(b)(3).

Section 965 of the USC permits a one-time tax deduction of 85 percent of certain dividends paid by an overseas subsidiary to its US-based parent. Section 965(b)(3) provides that the amount of repatriated dividends otherwise eligible for a dividends-received deduction must be reduced by the amount of any increase in related-party "indebtedness" within a specified testing period.

The Commissioner had based its decision on the ground that subsequently created accounts receivable constituted "indebtedness" and reduced BMC's eligibility for the deduction.

In the 2006 tax year, BMC decided to take a Section 965 deduction by repatriating USD721m from its wholly owned foreign subsidiary, BMC Software European Holding (BSEH), *via* a cash dividend. Of this sum, roughly USD709m qualified for the Section 965 dividends-received deduction, which permitted BMC to deduct 85 percent of that amount, USD603m, from its taxable income on its 2006 tax return.

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

The Court said BMC accurately reported no related-party indebtedness on its 2006 tax return. Therefore, neither party disputed that, at the time BSEH paid its USD721m cash dividend to BMC, the Section 965(b)(3) related-party indebtedness exception had no relevance or effect.

Then, in a matter completely unrelated to the repatriation under Section 965, BMC and the Commissioner signed a transfer pricing closing agreement in 2007 to correct BMC's net overpayment for royalties from its foreign subsidiary, BSEH. In this agreement, BMC agreed to a primary adjustment for each tax year from 2003 to 2006, increasing its

taxable income by approximately USD102m in total. Because the USD102m BMC had "overpaid" BSEH remained in the cash accounts of BSEH, BMC was also required to make secondary adjustments to conform its books and records to reflect that fact.

Under one of two available options under IRS Revenue Procedure 99-32, BMC treated the USD102m "overpayment" to BSEH as a series of interest-bearing accounts receivable, one for each tax year, rather than a capital contribution. BMC's stated goal was to put the company in the same place that it would have occupied had the primary adjustments been reflected on its original tax returns. BMC and the Commissioner then executed another closing agreement to execute the secondary adjustment, effective as of September 25, 2007 (the 99-32 Closing Agreement).

The 99-32 Closing Agreement created two accounts receivable, established on November 27, 2007, and payable from BSEH to BMC, with deemed establishment dates of March 31, 2005 and March 31, 2006. The parties also agreed that when BSEH paid off the newly created accounts receivable, such payment would be "free of the federal income tax consequences of the secondary adjustments that would otherwise result from the primary adjustment."

In 2011, four years after the execution of the 99-32 Closing Agreement, the Commissioner issued to BMC a notice of tax deficiency in the amount of approximately USD13m for the 2006 tax year. The Commissioner asserted that the accounts receivable which BMC established pursuant to the 99-32 Closing Agreement constituted related-party indebtedness between BMC and BSEH during the relevant Section 965(b)(3) testing period, thereby reducing BMC's eligibility for the Section 965 deduction.

However, the Court ruled that the text of the legislation does not warrant treating the accounts receivable as "indebtedness," given that Section 965(b)(3) specifically requires that the determination of the final amount of "indebtedness" be made as of the close of the taxable year for which the election under Section 965 is in effect. "Here, the relevant taxable year is 2006, and the close of that taxable year occurred on March 31, 2006. So the relevant testing period ended on March 31, 2006," the Court said.

The Court noted the Commissioner had made much of the fact that, in the 99-32 Closing Agreement, BMC agreed to backdate the accounts receivable. The Court said this is an incorrect interpretation of the testing period requirements of Section 965:

> "The fact that the accounts receivable are backdated does nothing to alter the reality that they did not exist during the testing period. Even assuming *arguendo* that a correction of a prior year's accounts could create indebtedness for purposes of Section 965(b)(3), that is not what happened in this case. This is not a situation in which a subsequent adjustment

was made in order to accurately reflect what actually happened in the taxable year ending on March 31, 2006. Rather, with the secondary adjustments, BMC agreed to create previously non-existent accounts receivable with fictional establishment dates for the purpose of calculating accrued interest and correcting the imbalance in its cash accounts that resulted from the primary adjustment."

In respect of this point, it concluded:

"The text of Section 965(b)(3) requires that, to reduce the allowable deduction, there must have been indebtedness 'as of the close of' the applicable taxable year. Because the accounts receivable were not created until 2007, BMC's Section 965 deduction cannot be reduced under Section 965(b)(3)."

The judgment was delivered on March 13, 2015.

http://www.ca5.uscourts.gov/opinions%5Cpub%5C13/13-60684-CV0.pdf

Fifth Circuit Court Of Appeals: *BMC Software v. Commissioner (No. 13-60684)*

ASIA PACIFIC

India

The case concerned four sets of appeals, all relating to the same taxpayer, Detergents India Limited (DIL), regarding the interpretation of Section 4(1)(a)(iii) and Section 4(4)(c) of the Central Excise and Salt Act as it stood prior to an amendment in 2000. The case looked at the definition of "related person" under these provisions and the application of the arm's length principle in respect of supplies to related persons in the course of wholesale trade.

The Commissioner (the appellant in the case) had concluded that goods were cleared from the factory premises to the depot of a holding company, Shaw Wallace, at a much lower price as compared with the price at which these goods were sold by the assessee in the market to wholesale purchaser Hindustan Lever and another.

However, the Customs, Excise, and Gold Appellate Tribunal (CEGAT) said that Shaw Wallace cannot be said to be "related" to DIL within the meaning of this expression, as used in Section 4(1)(a), as no "mutuality of interest" between the two companies has been established in this case. It concluded that, as DIL and Shaw Wallace have already been found not to be "related persons," it cannot be said that the former suppressed (in their price lists filed with the department) any "relationship" before the department with an intent to evade payment of duty.

Considering the two parties' arguments, the Supreme Court of India recalled that the Government had argued that "there can be no doubt, in view of a number of factors, that Shaw Wallace and DIL are related persons within the meaning of Section 4(4)(c) of the Act."

The Government had stated that some of these factors were that: advertisement expenses of DIL brands had been borne by the holding company Shaw Wallace; processing charges paid by Shaw Wallace to DIL were less than processing charges paid to Hindustan Lever; employees of Shaw Wallace and its subsidiaries were freely transferred from one company to another; depots of Shaw Wallace and DIL were in the same premises; DIL sent monthly newsletters to Shaw Wallace showing production, despatches, purpose, technical problems, quality problems, details of power consumption, *etc.* – and Shaw Wallace fixed the price of DIL products; and substantial unsecured loans were given by Shaw Wallace to its subsidiary DIL. The Government argued that all these facts showed that Shaw Wallace and DIL were related entities and that the price paid by Shaw Wallace to DIL was an artificially depressed price.

The taxpayer however argued that even though Shaw Wallace and DIL may be holding and subsidiary companies, based on a true construction of Section 4(4)(c), they are not related persons within the meaning of the definition clause. It was argued that on a true construction of proviso (iii) to Section 4(1)(a), it is necessary that the assessee must first enter into an arrangement with the related person, and that arrangement should lead to a price being charged that is lower than the normal price.

Further, the proviso only properly applies when such arrangement is predominantly a sale to or through a related person, it said. The company therefore argued that there was no arrangement between Shaw Wallace and DIL which led to any depression in the normal price at which such goods are sold. Last, it noted that since only 10 percent of the production of DIL was sold to Shaw Wallace, the goods were not "generally" sold to Shaw Wallace.

Discussing the provisions and arguments, the Supreme Court observed: "The first thing that one notices on a reading of Section 4(1)(a), as it then stood, is that a duty of excise is chargeable with reference to 'normal price,' that is to say the price at which such goods are ordinarily sold by the assessee to a buyer in the course of wholesale trade. The price should be the sole consideration for the sale. If the buyer is a related person, there is a presumption that a sale to a related person would be at a price which is not the sole consideration for the sale."

Proviso (iii) then deals with the price that is to be taken into consideration in the case of sales made to related persons (to establish an arm's length price), it added.

The Supreme Court said that three basic ingredients are necessary before proviso (iii) applies: first, the assessee must "arrange" that goods are sold by him in a particular manner; second, such arrangement must be such that the goods are "generally" sold by the assessee in the course of wholesale trade to or through a related person; and third, such sale need not be to the related person – it can even be through the related person.

The Supreme Court concluded that Shaw Wallace and DIL had been classified as "related persons" due to their holding/subsidiary relationship.

"However, from this, it does not follow that there is any arrangement of tax avoidance or tax evasion on the facts of this case. This being the case, proviso (iii) to Section 4(1)(a) would not be applicable. Further, it would also not be applicable for the reason that there is no predominance of sales by Detergents India Limited to Shaw Wallace," given that just 10 percent of sales were made to the subsidiary. The Supreme Court therefore dismissed the Commissioner's appeal.

The judgment was released on April 8, 2015.

http://judis.nic.in/supremecourt/imgs1.aspx?filename=42564

Supreme Court of India: *Commissioner of Central Excise, Hyperbad v. M/S. Detergents India Ltd (9049-9051/2003)*

WESTERN EUROPE

United Kingdom

The UK's Upper Tribunal (Tax And Chancery Chamber) has dismissed an appeal brought by HM Revenue & Customs (HMRC) against the earlier decision of the First Tier Tribunal (FTT) to deny HMRC's right to recoup a VAT repayment, made *via* a contractual agreement, that it later decided had been made in error.

The case concerned a payment in 2010 of nearly GBP1.4m (USD2.08m) to Southern Cross Employment Agency Limited, which specializes in the supply of dental nurses to dentists. Southern Cross had written to HMRC to say it considered such supplies to be exempt from VAT. HMRC responded, agreeing that the supplies were exempt for VAT purposes. In light of that response, Southern Cross sought repayment of VAT it had accounted to HMRC between 1998 and 2001. HMRC met the claims. Subsequently, Southern Cross submitted a claim for the period 1973 to 1997.

HMRC objected to the full repayment of this amount, and later, after negotiations between HMRC and Southern Cross, the company agreed to accept repayment of 76 percent of the claim.

However, on July 23, 2010, HMRC notified Southern Cross that they had made assessments under sections 80(4A) and 78A of the Value Added Tax Act (VATA) to recover the payment. In its correspondence with the company, HMRC said: "Since authorizing this claim, I have been advised by colleagues in VAT policy that the claim should not have been paid. As part of a wider review, the Commissioners have received legal advice to confirm that supplies of staff are not care or medical care, and that the published guidance at that time amounted to an informal concession …"

"That the exemption of the supplies in question was a concession means that when your client charged VAT on their supplies between 1973 and 1995 they were right to do so …"

In fact, the year before, HMRC had already refused to make a repayment to a Ms. Sally Moher, who had run a business that supplied temporary dental staff to dentists.

In a subsequent decision released on May 3, 2011, the FTT dismissed an appeal from HMRC's decision as regards Ms. Moher. The FTT held that the relevant supplies were of staff to dentists rather than supplies to dental patients, and so were not exempt (*Moher v. R&C Comrs* [2011] UKFTT 286 (TC), [2011] SFTD 917).

The case between HMRC and Southern Cross therefore centered on whether the company had the right to retain the repaid VAT.

Earlier, in reaching its decision, the FTT identified the following three main issues:

(a) Did Southern Cross and HMRC enter into a binding compromise agreement?
(b) If the parties did enter into a compromise agreement, was that agreement *ultra vires* because HMRC had no power to enter into such an agreement with Southern Cross?
(c) If there was a valid compromise agreement, was HMRC entitled under sections 80(4A) and 78A(1) VATA to make the assessments under appeal to recover the sums paid?

The FTT found in favor with regard to the first question, and found against the second and third questions.

In the latest appeal before the Upper Tribunal, HMRC argued that section 80 VATA operates to prevent them entering into any binding compromise agreement for the repayment of money paid by way of VAT unless section 85 VATA is applicable. Section 80, HMRC argued, establishes a comprehensive regime for the repayment of VAT and the recoupment of such payments. HMRC cannot make a repayment otherwise than pursuant to section 80(1)–(2A), and section 80(4A) empowers them to reclaim any payment so made if and to the extent that it turns out not to have been due, it said.

"The recipient of a repayment is protected by the limitation period for which section 80(4AA) provides. That apart, Parliament has chosen to adopt a regime under which HMRC [is] entitled to revisit any repayment they have made unless doing so would conflict with (a) a judicial determination, (b) an agreement settling an appeal pursuant to section 85 or (c) a legitimate expectation of the recipient of the repayment (as found in *Al Fayed v. Advocate General for Scotland* [2004] STC 1703)," it was argued.

HMRC's case centered in particular on section 80(7) VATA. This provision states that, except as provided by section 80, HMRC "shall not be liable to credit or repay any amount accounted for or paid to them by way of VAT that was not VAT due to them."

For its part, Southern Cross argued that section 80(7) VATA is designed to prevent taxpayers from seeking to recover overpayments by common law claims for restitution or through their tax returns. It was not, Southern Cross said, meant to prevent HMRC from

settling claims made under section 80. The case law shows, it was submitted, that HMRC cannot use section 80(4A) to recover a payment made in pursuance of a judicial determination or a settlement under section 85. There is similarly no objection to HMRC entering into a contract to settle a claim where no appeal is on foot, it said. On this first point, the Upper Tribunal agreed with Southern Cross.

The Upper Tribunal said that, contrary to HMRC's arguments, section 80 VATA does not bar HMRC from entering into a binding agreement with a company such as Southern Cross. Further, on issue (b) above, it said: "There is, I think, no reason at all to believe that HMRC acted for an improper purpose in their dealings with Southern Cross. Miss Simor [arguing on behalf of HMRC] did not suggest that Mr. Knight [who negotiated the HMRC settlement] had any wish for Southern Cross to receive money to which it was not entitled, and there is in any case no evidence to that effect. The correspondence … indicates that Mr. Knight was seeking to limit the amount paid to Southern Cross, not to pay it too much."

"Nor, in my view, can it be maintained that HMRC acted irrationally. They had in the past accepted that Southern Cross's supplies were exempt from VAT, and it has not to my mind been established that it was irrational for Mr. Knight (or whoever else was responsible for HMRC's decision-making) to continue to proceed on that basis in 2009–2010."

Last, the Upper Tribunal agreed that, based on the correspondence between the taxpayer and agency, the agreement reached between the two parties had been a binding compromise agreement. It noted that in agreeing the settlement offered by HMRC (for repayment of 76 percent of the amount), Southern Cross was giving up 24 percent of its claim forever. "Apart from anything else, any attempt to recover the 24 percent would have been time-barred. I accept [Southern Cross's] submission that HMRC obtained complete protection against further claims for all relevant periods," it was observed.

"I agree with [Southern Cross] that the pattern of correspondence …, and specific wording used in it, tend to point towards a process of negotiation and, in the end, an intention to conclude a contractual agreement."

"For example, Mr. Knight [of HMRC] suggested on March 26, 2010, that the parties reach a 'compromise position' on a 'without prejudice' basis; Horwath Clark Whitehill [for Southern Cross] referred in [his] reply to the 'offer' Mr. Knight had made and then, on April 14, to being 'willing to negotiate'; and Mr. Knight said on April 29 that HMRC would 'accept' that 74 percent of the claim would be paid."

"Viewed objectively, such matters seem to me indicate contractual negotiation rather than HMRC doing no more than ascertain the extent of their liability under section 80 of the VATA," the Court concluded.

The Upper Tribunal therefore dismissed HMRC's appeal on each of the three issues specifically targeted in the FTT's earlier ruling in favor of Southern Cross.

The judgment was released on April 1, 2015.

http://www.tribunals.gov.uk/financeandtax/Documents/decisions/HMRC-v-Southern-Cross.pdf

Upper Tribunal (Tax and Chancery Chamber): *HMRC v. Southern Cross [2015] UKUT 0122 (TCC)*

Dateline April 23, 2015

When measured against its competitors, the Australian tax system isn't actually that bad. PwC ranks Australia 39th out of 189 countries in terms of how easy it is for a medium-sized company to discharge its tax obligations, which isn't a brilliant score, but it's by no means the worst. Yet the Government is determined to make improvements. It can't help that the Tax White Paper, the pithily-titled "Re:think," has come so soon after the last government's failed attempt at comprehensive tax reform. Indeed, the Labor administration's "Future Tax" review was just one of a long line of tax system assessments that must be putting taxpayers in Australia, especially corporate investors with long planning horizons, on a near-constant state of alert about the risks of legislative change.

The Government must also be mindful of promising, or appearing to promise, things it can't deliver. Governments all over the world are guilty of pledging radical, growth-boosting changes to tax legislation and administration, envisioning such fantasies as tax returns that can be completed in minutes as opposed to hours, but falling drastically short of initial objectives when it comes to the crunch. And Australia, straitjacketed as it is by a huge fiscal hole, is hardly in a position to begin slashing taxes. The Government's inability to deliver even the most modest of corporate tax cuts – a planned 1.5 percent reduction was canceled last week – is evidence of that. The Government's heart is in the right place, but I wouldn't be getting my hopes up if I were an Australian taxpayer.

It's a rare occasion that I agree with something the OECD says. So when it does happen, mostly begrudgingly, it's probably worth a mention. In this instance, there are some qualifications, and while I concur with the broad thrust of the OECD's report on Japan, I don't necessarily agree with all its proposed remedies. It's an inescapable reality that Japan is going to need to collect a lot more tax revenue if it is going to face the future with confidence about its ability to pay its way. And it will be a delicate balancing act between growth and austerity-type policies.

But perhaps it's time to end the world's fixation on Japan's consumption tax. We've seen in the past how the Japanese economy responds to tax hikes – not very well as it turns out – and we were given more evidence of this just last year, when consumption tax increased from 5 percent to 8 percent and economic growth took a worrying dive into the red in the subsequent quarter. Given that the consumption tax is a political toxin in Japan, Prime Minister Shinzo Abe seems to have got away lightly as a result of last year's hike. But there is no doubt he is handling the issue with kid gloves, as demonstrated by the decision to postpone the next hike to 10 percent, which had been due in October 2015.

Given that previous consumption tax hikes, or just the mere suggestion of an increase in this tax, has

ended the career of more than one prime minister early, it is perhaps unrealistic for the OECD to suggest that there is scope to raise consumption tax to the average OECD consumption tax rate of nearly 20 percent. That just isn't going to happen. Even in an age when the tax burden is shifting from direct to indirect taxation, as numerous tax studies tells us, it could be very counterproductive in Japan, with the country's notoriously price-sensitive consumers likely to clasp shut their wallets and purses after a sales tax increase of such magnitude. A more holistic approach to Japan's fiscal problem, and one that will encourage growth rather than throttle the economy, is surely needed. Looking in from the outside at least, it seems that measures far more radical than the modest corporate tax cuts currently in the pipeline (which are actually going to be canceled out by changes to loss carry backs) are required. That's easier said than done though.

Mexico has extended a hand of economic cooperation towards Cuba with its proposal for a bilateral FTA, another sign that the long-isolated Caribbean nation is being welcomed back into the fold of trading nations. Mexico's gesture follows the removal of Cuba from America's list of nations that sponsor terrorism and the lifting of travel restrictions to the country by US citizens. Given the length of time that has elapsed since Fidel Castro was replaced by his more liberal and reform-minded younger brother Raul, President Obama's move was arguably long overdue, although it remains controversial in some quarters of America; while allowing capitalism in small but increasing doses, Cuba is still an unapologetically socialist country. There is a long way for Cuba to travel before its inhabitants can hope to enjoy the sort of economic and political freedoms that people take for granted just 70 miles away in Florida – including many of Cuban heritage who fled in search of a better life (and still they flee: over 14,000 Cubans risked life to cross into the US in 2013).

The country never really recovered from an economic crisis in the 1990s, which was largely the result of the collapse of the Soviet Union and the termination of around USD5bn in annual economic support from Moscow. Yes, as many people who visited Cuba in the Fidel Castro era will no doubt agree, Cuba will lose much of its charm when fast food joints start springing up all over Havana, the billboards of Cuba's political heroes are replaced with adverts for soft drinks, and the 1950s Cadillacs which have come to epitomize Cuba for so long are outnumbered by Fords, Volkswagens, and Toyotas. But the Cuban people would probably accept that as a price worth paying for progress.

So, silly season – aka, the general election campaign – has officially commenced in the United Kingdom. All the significant parties have now released their manifestos, but to be truthful there's nothing really radical or scary in any of them. The Labour Party, whose leader has been dubbed "Red" Ed Miliband by the right-wing press, won't exactly soak the rich with its tax plans, which are fairly predictable: the restoration of the 50 percent top rate, a so-called "mansion tax," a levy on tobacco firms,

a vague promise to restrict "non-dom" tax status, and a crackdown on offshore tax havens, including an unworkable proposal for public beneficial ownership registries.

On the fringe, the UK Independence Party wants, of course, to cancel the UK's EU membership, and it also promises to abolish inheritance tax, but as popular as the party seems, it probably won't get enough seats to influence anything. What's more worrying is that the election is likely to result in a hung parliament, and so the fringe parties are probably going to have a major say on who the next Prime Minister will be. Unless, that is, one of the main parties attempts to have a stab at minority government, which raises the prospect of watching either Cameron or Miliband stagger from one crisis to the next. Hardly a recipe for stability. And there is evidence to suggest that companies are holding back their investment plans accordingly. If he does lose the election, Cameron could be forgiven for wondering what he did wrong, having reduced the budget deficit, cut taxes, and overseen a growing economy. Indeed, IMF chief Christine Lagarde was recently heard praising UK economic policies.

Not everyone is so enamored with the Coalition's track record though. In a somewhat amusing, yet quite alarming, piece of analysis quoted in the press, Albert Edwards, who heads Société Générale's global strategy team, observed in a note to the bank that, following five years of the Con/Lib's policies, the UK economy looks like a "ticking time bomb" waiting to explode after the election, with the country "up to its eyeballs in macro manure." According to Edwards, this is largely because Cameron's Government has failed to deal with two key deficits, the fiscal one and the trade one – the latter is at its widest for 60 years. Eventually, Edwards predicts, "the stench will fill the nostrils of currency markets with the inevitable result – another sterling crisis." So, with voters' choice essentially boiling down to a Conservative-led Government which talks a lot tougher than it acts on the deficit, and a Labour Party with a reputation for fiscal irresponsibility, possibly in coalition with the free-spending SNP, perhaps the really scary thing is not what the parties intend to do, but what they're going to avoid doing: shoveling the muck.

The Jester