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GLOBAL TAX WEEKLY
a closer look

ISSUE 109 | DECEMBER 11, 2014

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

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a closer look

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Starbucks: State Aid Or Just Tax Planning?

by Wiecher Munting, tax advisor with Otterspeer Haasnoot & Partners (www.ohp.nl)

** Brussels, 11.06.2014 C(2014) 3626 final: letter from European Commission announcing that procedure Article 108(2) (formal investigation procedure) of the Treaty regarding the functioning of the European Union will be started.*

Recently, several well-known multinational enterprises ("MNEs"), like Apple, Starbucks and FIAT, have been the subject of a wide variety of publications regarding so-called tax avoidance, base erosion and profit shifting, and measures that should be taken to deal with such issues. These three MNEs and others have also recently been the subject of the European Commission's investigation procedures on state aid, within Ireland, Luxembourg and the Netherlands, respectively.

In this article, the Starbucks State Aid case will be discussed in an effort to reach a conclusion on whether or not the Starbucks legal structure and tax ruling actually must be regarded as state aid or should rather be qualified as a way of developing an efficient company group structure with certain tax consequences. This conclusion will be based only on the facts and circumstances presented in publicly available sources.[1]

I will start with an introduction on state aid. Then I will make some remarks on state aid and transfer pricing. And finally, I will comment on the Starbucks case and draw my conclusions.

I. An Introduction On State Aid

State aid is a concept applicable to member states of the European Union (EU). By joining the EU, these member states explicitly accepted the rules laid down in several EU treaties and directives, superseding their own domestic laws. These EU rules can be enforced by the EU government – being the European Parliament, the European Commission (daily executives), and Counsel of Europe (formed by the Ministers of the Member States) – whereby the European Commission, though officially not the European legislator, is often the driving force behind European laws, with the European Court of Justice (ECJ) judging matters of EU law.

The EU Treaty's primary aim is to create and maintain a free and open market within the EU (and to some extent even beyond the EU, as far as the freedom of capital is concerned), allowing as few – justifiable and proportionate – restrictions as possible (the common market). This is why the EU "freedoms" are crucial. The most important freedoms to be enforced are: the freedom of establishment; the freedom of capital; the freedom of goods and services; and the freedom of persons (including employees). It is essential, for the functioning of the common market, that nationals (citizens as well as legal persons) of the member states can rely on these freedoms being applied and respected in all member states, and that, if necessary, they can have them enforced through the European Commission (infringement proceedings) and/or the ECJ – whereby member state judges may ask for a binding legal opinion on questions of EU law from the ECJ.

Another tool, created to ensure the proper functioning of the common market, is the state aid regulations.[2] If any measure taken by a member state is considered state aid, the company or individual who received the state aid must repay all explicit or implicit subsidies, in order to restore the common market. The member state is responsible to see to it that the company or individual indeed repays any aid received.

The following conditions must be fulfilled before a measure can be regarded as unlawful state aid:

i. the measure can be attributed to the member state and is paid from the member state's own funds;
ii. the measure must give an advantage/subsidy to the recipient of the payment;
iii. the measure needs to be "selective"; and
iv. the measure must disturb the common market or threaten to disturb the common market and may disturb the economies of several member states.

According to the EU Commission officials responsible for the Starbucks investigation, condition iii, selectivity, is the most decisive one.

I agree that indeed the selectiveness of the measure is crucial, because it is only when a measure is selective, *i.e.*, favoring only certain specific taxpayers, that conditions ii and iv are fulfilled. If a taxpayer is implicitly and selectively granted a lower tax liability than another taxpayer, it can probably also be argued that this is a matter of national tax law and that the tax revenue can be booked on the member state's own account;[3] therefore, condition i will also probably be fulfilled in most cases. Like the European Commission officials in the Starbucks case, hereinafter I will concentrate on the selectivity criterion.

II. State Aid (Selectiveness) And Transfer Pricing

Under the internationally accepted and adopted arm's length principle, associated parties are obliged to deal with one another under terms and conditions which they would also apply to third parties in comparable transactions and circumstances. In the absence of arm's length terms and conditions (including, but not limited to, pricing), tax administrations often have authority to impose adjustments to "controlled transactions" (also known as intercompany transactions, *i.e.*, transactions between associated parties) so as to reflect the at arm's length character of the transaction. In order to arrive at arm's length prices for intercompany transfers and/or transactions, tax administrations and tax practitioners use transfer pricing tools.

Why is it necessary that prices used for intercompany transactions are at arm's length? Otherwise, it would be possible to create tax gaps which do not reflect the real economic functions performed by a specific company, and/or in a specific state (also referred to as principle of residence and principle of territory). In order to avoid these artificial tax gaps, the OECD has developed the arm's length principle which has been adopted by all its members and by the vast majority of non-member states in the world. The arm's length principle has therefore become the standard for valuating intercompany prices (transfer pricing). This standard has been laid down in Article 9 (related party transactions) and Article 7 (attribution of profit to permanent establishments) of the OECD Model Tax Treaty for avoiding double taxation and double non-taxation, regarding direct taxation, and has been adopted by many countries when concluding bilateral tax treaties. The arm's length principle has been explained in detail in the OECD Transfer Pricing Guidelines for Multinational Enterprises and Tax Administrations ("the OECD TP Guidelines") which serve as an explanatory guide and even as a black letter rule (once implemented in domestic legislation) in many countries around the world.

To some extent, the arm's length principle serves the same principle as the EU State Aid principle: to avoid states losing their tax base due to artificial contracting as a result of selective market disturbance (false competition towards market parties who do not have a foreign parent or subsidiary).

In this Article, I will not elaborate on transfer pricing too much. However, in order to understand what happened in the Starbucks State Aid case (which really only deals with transfer pricing) I will point out some difficulties which transfer pricing practitioners face during their quest for a set of comparable (arm's length) prices to support the at arm's length character of a controlled transaction.

(1) *Functional and financial analysis*
Before determining the specific transaction price, *i.e.*, benchmarking the controlled transaction against comparable third party transactions, we first have to describe the content of the transaction, which is called *functional analysis.* To do this, many steps described in the OECD TP Guidelines must be applied. However, in practice it is at least as important to also meet with the relevant officials within the company who bear end responsibility concerning the activity to be benchmarked, by means of performing an interview. After this, the outcome of the interview must be laid down in a description of functions performed, and this description must be compared with the financials, the descriptions in the books of the company, and the company's own understanding of the importance of the functions. After this,

the assets used and risks incurred in relation to these functions must be allocated, and again, must be verified with the allocation of assets in the books (financial accounts) of the company. If this has resulted in a weighted description of functions performed, which can be agreed upon by the management of the company and is in line with the facts (interview!), the benchmark can be performed.

(2) *Benchmark (comparability analysis)*
Performing a benchmark is really searching for uncontrolled market transactions, which are comparable to the controlled transaction described in the functional analysis, in a database. Sometimes, the company performs the exact same transaction also in relation to third parties, in which case we can use this transaction as a comparison. This is called an "internal" comparable uncontrolled price (CUP); in most cases, due to too many factual differences between the intercompany transaction and the CUP transaction, we cannot use the third party transaction as a benchmark. In such cases, we use an alternative solution by comparing with comparable transactions between independent companies in the market who perform comparable functions to the companies described in the functional analysis (database-search). We call this an "external" comparable uncontrolled price.

When performing a database benchmark analysis, transfer pricing practitioners typically try to search for so-called *routine activities*. Routine activities are activities which could just as well be outsourced to third parties in the market, and which are not directly related to the valuable or even unique expertise and capabilities of the company, such as marketing and/or R&D activities. Often these routine activities can be distinguished as manufacturing, logistic, maintenance, and sales. The reason is very clear: activities comparable to the company's valuable or unique activities (also referred to as "key entrepreneurial functions") cannot be found, as transactions performed between unrelated parties in the market are found, and can therefore not be benchmarked. Typical key entrepreneurial functions are: R&D; marketing; and (although questionable whether is should be considered an actual and separate function) corporate excellence. Together, the key entrepreneurial functions form the core business and value drivers of the company.

(3) *Determining the pricing method*
After the functions to be benchmarked have been given a price, one can reflect the arm's length price in the financial accounts of the relevant related group companies, by means of intercompany agreements. Such agreements may grant the company performing the routine functions a net remuneration or gross remuneration. A net remuneration is typically granted if the routine functions-performing company bears limited risks. If the routine functions-performing company bears *e.g.*

efficiency risks, a gross remuneration can be more appropriate since the risks are managed by the company and the success in managing the risks is reflected in the company's remuneration. The principal or parent company performing the key entrepreneurial functions therefore typically receives a variable remuneration (royalty) which can be compared to a franchise fee or similar setups. The variable remuneration fixes the remuneration of the routine functions-performing company to the – benchmarked – arm's length remuneration for its limited risk functions. The routine profit flows to the key entrepreneurial functions. The principal or parent company performing the key entrepreneurial functions therefore typically bears the high risks (and high profit or loss) associated with a high risk-controlling profile.

Finally, when the appropriated transfer pricing method has been determined and applied, it can be laid down in a transfer pricing report, which typically can be actively or passively audited by tax authorities.

Taking into account the above typical transfer pricing methodology, it can be concluded that both transfer pricing and state aid regulations more or less aimed at the same goal: taxation should disturb the objective economic market behavior as little as possible, in order to ensure an EU-wide (through state aid) and even global (through transfer pricing) level playing field.

However, there is one very important distinction: before getting state aid, it should be concluded that the state willingly (*selectively*) grants an advantage to a certain (group of) taxpayer(s).

III. The Starbucks Case: Considered State Aid?

How do the above paragraphs apply to the Starbucks case?

Let's look at the case in more detail:

Starbucks, a US-based MNE, in its activity of globally marketing/developing/manufacturing/selling a coffee brand, is active in the Netherlands through its subsidiary Starbucks Manufacturing EMEA BV ("SBME BV"), which operates as a *consignment*[4] manufacturer of coffee in the Netherlands. The coffee is manufactured following the precise formula from the principal on roasting the coffee beans. The green coffee beans are purchased from a related Swiss company. SBME BV also performs certain logistic activities concerning the unpackaging and packaging of *e.g.* cups and napkins.

Starbucks has approached the Dutch Tax Inspector (APA/ATR team in Rotterdam) to obtain certainty in advance of the arm's length remuneration for the manufacturing function.

In order to determine the arm's length price, Starbucks performed a benchmark analysis of the routine manufacturing function performed in the Netherlands, arguing that for this function, typically, a remuneration based on limited initial cost plus 7.8 percent mark-up for risks incurred should apply. Considering that SBME BV, according to Starbucks, did not bear inventory risk, an adjustment was made by reducing the cost base, and adjusting the mark-up to 9–12 percent.

Also, from the performed transfer pricing analysis it followed that SBME BV should not be entitled to higher risk bearing functions such as branding/marketing and R&D which were performed outside the Netherlands (apparently, in this case they were for risk and account of a non-resident Irish Limited Partnership ("Irish LP")).

While determining the cost base, which should be used as a "profit level indicator" ("PLI", the basis by reference to which the appropriate profit level is determined) for the cost plus remuneration, Starbucks argued that *e.g.* the logistic purchase costs caused by the logistic activities should not be included in the PLI because the logistic activity is only an auxiliary activity to which normally no profit (or very limited profit) is attributable.

Based on Starbucks' request, the Dutch Tax Inspector signed an advance pricing agreement ("APA") with Starbucks, determining that SBME BV was allowed to report a cost plus remuneration calculated over a limited PLI. Also, apparently Starbucks was allowed to – at the end of the fiscal book year – take into account a "quasi franchise fee," payable to Irish LP for the key entrepreneurial functions performed by Irish LP.

The European Commission argued that the APA signed by the Dutch Tax Authorities, based upon the facts described by Starbucks, must at this moment be considered state aid and has asked for further information and responses from the Dutch Tax Authorities.

The reasoning of the Commission can be summarized as follows:

- The Dutch Tax Authorities remain responsible for the judgment whether the franchise payment (referred to as a *royalty* in the Starbucks case) is based upon arm's length principles;
- Also, the Dutch Tax Authorities are responsible for the drop in taxable base of SBME BV as a result of the franchise payment;
- The Commission doubts whether the remuneration as described in the APA is in line with the facts found by the Commission – especially the fact that SBME BV is qualified as a consignment manufacturer with low risk, while there is evidence from the books that SBME BV bears inventory risk, in which case it should be remunerated for such risk;
- The Commission questions whether Starbucks has sufficiently explained the adjustment of the tax base (PLI) and the cost plus.

APAs which are a straightforward explanation of the applicable tax rules, without adjustment from administrative practice, cannot be considered as a selective advantage. However, rulings which refrain from this practice may result in a lower tax burden in comparison with comparable enterprises in comparable legal and factual circumstances. In Article 8b of the Dutch Corporate Income Tax Act, the Netherlands has incorporated the arm's length principle. As far as the Dutch Tax Authorities depart from this principle in an APA, the APA can be qualified as selective.

Does this reasoning make sense if we compare it with the transfer pricing principles?

As far as it concerns the reasoning that Starbucks apparently reported inventory and inventory risk in its Dutch financial accounts, it seems that the APA is not in line with the facts. Therefore, the remuneration should be adjusted. However, the Dutch Ministry of Finance and/or Starbucks might argue that although SBME BV reports inventory in its balance sheet, it in fact did not bear any inventory risks because these risks were actually incurred and managed/controlled in or by the Swiss related company. If this is the case, in theory Switzerland (if actually performing the inventory and procurement function) should make an upward adjustment in its balance sheet, and SBME BV should make a downward adjustment. The result would be that the fiscal balance sheet is in line with the APA again. Whether this is the case depends on the facts and is a matter of burden of proof (as regards the commercial and fiscal financial statements, the burden of proof is on Starbucks and the Dutch Tax Authorities, not on the Commission).

As far as the Commission's reasoning is concerned, the Dutch Tax Authorities remain responsible for the judgment whether the franchise payment is based on the arm's length principle, supposedly leading to the conclusion that the APA is in fact state aid – this reasoning cannot be followed.

If we compare the Starbucks case to the sound economic transfer pricing approach, it follows that in general Starbucks applied the residual profit methodology. That is why the manufacturing function performed was benchmarked (appropriately or not, see above) and the residual profit flows to the principal by means of floating franchise fee. It is not the Netherlands Tax Inspector who can be held responsible for picking up this franchise fee, because the branding, marketing and/or R&D activities are not performed in the Netherlands. Whether or not the franchise fee remuneration is picked up for tax reasons is the responsibility of the state on whose territory those key entrepreneurial functions are performed. As long as this is not the Netherlands, the franchise fee/floating remuneration APA cannot be considered state aid by the Netherlands.

Finally, if the Netherlands made a mistake in not taxing the profit (if any) that Starbucks made with holding the inventory on its balance sheet, must this be considered selective?

In my opinion, this can only be the case if not taxing this profit was deliberate. If not, selectivity cannot easily be concluded upon. Considering that Starbucks performed a substantial and well documented transfer pricing analysis, it is hard to understand why the Dutch Tax Authorities would deliberately give a tax advantage to enable Starbucks to perform its activities on Dutch territory at a lower tax burden than similar manufacturers.

Therefore, only if the Dutch Tax Authorities deliberately did not take into account the inventory risk when determining the cost plus percentage and PLI, may it be determined that state aid was granted by the Netherlands.

IV. Starbucks: An Efficient Tax Structure?

If we come to the conclusion that the Starbucks case cannot be considered state aid, is something else "wrong"?

It is clear that Starbucks is a US-based MNE with many retail and manufacturing activities all over the world.

It is up to all the individual states on whose territories Starbucks is active to pick up their rightful corporate tax base. If, and only if, the key entrepreneurial function as described in this article is performed on US territory, it is up to the US to pick up the profit allocable to these functions.

Therefore, it is up to the individual states if and when the profit is picked up for tax purposes.

Currently, several States, through the OECD, work on this issue in the project called Base Erosion and Profit Shifting ("BEPS"), emphasizing individual member states' and non-member states' responsibilities to actually pick up these profits or losses for tax reasons.

Endnotes

1 Case published at http://ec.europa.eu/competition/elojade/isef/case_details.cfm?proc_code=3_SA_38374

2 The Treaty of Lisbon on December 1, 2009: *Article 107*(ex Article 87 TEC):

3 According to Article 5.2. of the (*Maastricht*) EU Treaty, member states are responsible for their own direct taxes (the member states have not derogated responsibilities to the EU).

4 A consignment manufacturer does not own the goods it produces; neither does it maintain any risk regarding those goods. Usually, a consignment manufacturer performs limited (also known as routine) functions.

Road Forward To A Multilateral Tax Treaty Regime?

by Michael Xu and Linda E.S. Pfatteicher, DLA Piper, Silicon Valley San Francisco

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The Organisation for Economic Co-operation and Development ("OECD") has issued its paper, *Developing a Multilateral Instrument to Modify Bilateral Tax Treaties*, discussing the framework for Action Point 15 of the Base Erosion and Profit Shifting ("BEPS") Action Plan. The OECD has a set goal to draft a proposed treaty based on recommendations of the Action Plan by December 2015.

The report, released in mid-September, analyzes the benefits, feasibility and other legal issues relating to the formation of a multilateral treaty, which could also lead to renegotiation of all the bilateral treaties currently in effect. Ultimately, the report recommends that this multilateral treaty instrument should be implemented to curtail BEPS abuses, but adds that existing bilateral treaties should remain in effect, subject to modifications, in order to synchronize all the changes.

Benefits Of A Multilateral Tax Treaty Regime

An effective multilateral tax treaty may potentially reduce abuses in cases of dual residence, transparent entities (hybrids), and so-called triangular cases of payments to permanent establishments from third countries. Such a treaty would also allow for multi-jurisdictional dispute resolution, which would facilitate the ability of tax authorities to have better insight into transfer pricing structures. The multilateral treaty could also impact the likely increase in use of the transactional profit split method for cases involving intangibles.

In addition, the report states that a multilateral instrument would improve confidentiality issues in relation to the sharing mechanism for country-by-country reports and for allocation of interest deductions.

Implementation And Acceptance

The implementation of broad multilateral tax treaties has been rare. Typically, such multilateral tax treaties are concluded between regional countries that have similar legislative structures. Some examples of multilateral tax treaties are the 2007 Ibero-American Social Security Convention; the 2005 SAARC (South Asian Association for Regional Cooperation) Income Tax Agreement; the 1994 CARICOM (Caribbean) Income Tax Agreement; and the 1988 OECD/Council of Europe Convention on Mutual Administrative Assistance in Tax Matters.

Based on this history, obtaining a draft proposal treaty on all the tax issues described in Action Plan 15 by the timeline goal described above seems very ambitious, and getting more than a few member governments to sign on to such a treaty may prove even more difficult.

US Impediments To Adopting A Multilateral Tax Treaty

One of the greatest impediments to US adoption of a multilateral tax treaty is Article 1(2) of the 2006 US Model Treaty, which states that a tax treaty shall not restrict in any manner any benefit accorded by the laws of either contracting state. In light of this, the US could be hesitant to accept any provisions of the proposed BEPS Action Plan that restrict benefits granted under the Internal Revenue Code ("IRC") and Treasury Regulations. In particular, the BEPS Action Plan's treatment of hybrid instruments could be questioned by the US. The US has already incorporated such a concept into many of its tax treaties by adding special rules for determining the residence of a hybrid entity and will most likely decline to deviate from the US Model Treaty on this issue.

Another area problematic for US acceptance is the multilateral treaty's anti-treaty-abuse provision. Virtually all US bilateral treaties with generous reductions in withholding tax have a comprehensive "limitations on benefits" article. It is highly likely that the OECD approach on this issue will resemble the "main purpose test" that limits reduced withholding tax, which is currently included in many OECD countries' bilateral treaties. The US Senate has previously rejected this approach as being overly subjective and unduly vague.

Other important issues addressed by the Action Plan are changes to the definition of permanent establishment and changes to transfer pricing rules. The US will likely not broaden its definition of "US trade or business" or expand attributable income to be broader than effectively connected income. Changes to the transfer pricing rules may be more acceptable to the US, considering that broadening Article 9's application is unlikely to conflict with the broad scope of IRC §482.

Likely Outcome

Due to the significant changes to domestic laws and existing regimes that would be required, countries that are highly protective of their sovereignty and laws, such as the US, China, Russia and the UK, are unlikely to conform to the proposed BEPS multilateral tax treaty. Although narrow selections of the multilateral tax treaty proposal may be palatable to most significant countries, a final agreement based on this limited scope would also decrease the significance of Action Point 15. Thus, it is likely that such a multilateral tax treaty will remain regional in nature and have a merely limited impact on the worldwide tax regime.

Topical News Briefing: Beware Chancellors Bearing Gifts

by the Global Tax Weekly Editorial Team

Chancellor of the Exchequer George Osborne delivered a few surprise presents in the run-up to Christmas in the UK Government's autumn fiscal statement, which has taken on the role of a second annual budget. In keeping with recent UK tax policy, however, not all of the gifts pulled out of the Chancellor's bag were welcome ones.

Probably the most eye-catching measure announced by Osborne was a reform of stamp duty land tax (SDLT). The changes have introduced a band-based system akin to personal income tax, so that only the portion of the value of a property above a certain threshold pays the higher rate of SDLT, replacing the former "slab" system. The changes mean that the first GBP125,000 of the property price is exempt from SDLT altogether, with rates above this threshold ranging from 2 percent to 12 percent. Under the previous system, a property purchased for GBP260,000 would have been taxed on the full amount at the then 3 percent rate (*i.e.*, GBP7,800), whereas under the new system, only the amount exceeding GBP125,000 and then GBP250,000 is taxed (in this case, GBP125,000 at a rate of 2 percent, then GBP10,000 at a rate of 5 percent, *i.e.*, GBP3,000). The move is expected to benefit 98 percent of home buyers, saving them a total of GBP800m (USD1.25bn) in tax.

In line with the Con-Lib coalition Government's aim to create an "aspiration nation," there were also plenty of sweeteners for small business, to encourage investment in new ventures and research and development.

So all good so far. But what about the bad and the ugly? Unfortunately, these two characters figure large in the Autumn Statement also. As has become customary in UK budgetary announcements, there are anti-avoidance measures aplenty. This is understandable of course, given the UK's stubbornly high budget deficit, which at 5 percent of GDP is substantially higher than most of the eurozone countries, including Greece, and Osborne would have been accused of being fiscally irresponsible if he hadn't peppered the Statement with revenue raisers. Notably, the Disclosure of Tax Avoidance Schemes regime, the forerunner of the UK's new General Anti-Abuse law which now runs in parallel with the GAAR, is being strengthened in a bid to stamp out aggressive tax planning. This will doubtless give the UK's already clogged up tax tribunals and court system plenty more to chew on, risking further uncertainty in the tax system. And patching up the tax system piecemeal with anti-avoidance legislation hardly helps the Government's simplification cause, which now seems to have fallen well by the wayside.

The most controversial aspect of the Autumn Statement was another anti-avoidance measure: the so-called "tax on diverted profits." The details of this levy remained sketchy at the time of writing, but the rationale behind the move is to discourage multinationals from artificially diverting profits from the UK to avoid UK tax. Whether or not this legislation succeeds in its objective will hinge on the definition of "artificially" diverted profits, and perhaps the risk is that more of HM Revenue & Customs' resources will be diverted into a game of cat and mouse with multinational companies at a time when the department is already overstretched, despite a huge investment in its anti-avoidance campaigns by the Treasury. And given that the UK has one of the most improved corporate tax systems among the industrialized countries, it could be seen as an unnecessary move. However, according to some observers, the measure means that multinationals now have a clear choice: play by the rules and benefit from one of the most favorable corporate tax regimes in the G20, or be prepared to be punished by the stick of the diverted profits tax.

The diverted profits tax will raise the relatively minor sum of GBP85m in its first year, rising to GBP350m after 2016/17, which is still small change given the UK's GBP90bn budget deficit. But the objective of this tax isn't really to raise revenue. It is more like a signal to the world (and especially voters in the UK going into the 2015 elections) that the Government is tough on corporate tax avoidance and at the vanguard of the OECD's BEPS project. However, a successful BEPS project will depend on countries acting multilaterally on the OECD's recommendations – and these won't be ready for another year – not unilaterally before the OECD has even completed its work. Ironically then, by being seen to be tough on BEPS, the UK has probably further undermined the cause.

Onward And Upward Towards Corporate Tax Reform

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

Introduction

I will be honest. I had to ask myself more than once if I really wanted to do this. Did I really want to take a stand in the corporate tax reform debate? I mean, this is one of the most politicized issues in the media today – one that brings out strong emotions in people and that can be very divisive. Indeed, there is no more vibrant of a political debate going on in America today than the one involving corporate tax reform.

Expressing such a strong opinion on a controversial topic is like dangling a piece of red meat in front of a lion. It is sure to earn me my share of critics, and yes, even enemies. But in the words of the great Winston Churchill, "You have enemies? Good. That means you've stood up for something, sometime in your life."

First, let me tell you what I mean by the corporate tax reform debate. Corporate tax reform proposals have always been "out there." But few reforms have garnered as much support as the one introduced by the Obama administration. Unlike past attempts at corporate tax reform, this one involves tax-writing committees and the White House. The last time the United States witnessed

tax reform on a magnitude of this scale was between 1984 and 1986.

What factors have contributed to the current reform debate? There are three: first, the global financial crisis of 2008[1]; second, federal budget deficits[2]; and third, a broken corporate tax system[3]. Let me expound on all three.

Let's get into our time machine and travel back to 2008. That was the year that the global financial crisis hit its peak. Who could forget? It threatened the total collapse of large financial institutions and was considered by many economists to be the worst financial crisis since the Great Depression. It was marked by the failure of once vibrant businesses and prolonged unemployment. The housing market wasn't spared either. It too suffered, resulting in evictions and foreclosures.

Not surprisingly, the 2008 global financial crisis was the impetus behind corporate tax reform talks.[4] It breathed new life into reform proposals and put it on the straight and narrow path.[5]

But even before the financial crisis reared its ugly head, federal budget deficits was the flavor of the day.[6] While Republicans and Democrats were at each other's throats – Democrats blaming tax cuts from the Bush administration; Republicans blaming Democrats for outlandish spending – once the smoke cleared, all parties, regardless of their political affiliation, realized that something had to be done to fix the deficit.[7]

And fix it is what the Obama administration set out to do. But the economic downturn complicated matters. For example, Obama's pre-election proposal to "close loopholes" and raise taxes on high-income earners drew harsh criticism in light of the sputtering economy and an anemic job market.[8]

Getting back to the debate itself, where are the battle-lines drawn? On one side of the fence are those who argue that "US companies face a high tax burden as compared to their foreign-based competitors," and are quick to point out that "they face the second-highest effective tax rate in the world."[9]

On the other side of the aisle are those who argue that "United States corporations don't pay enough taxes," and are quick to cite the following statistic: "United States corporations pay only *slightly* more on average than their counterparts in other industrial countries."[10]

Right about now, the prudent and rational side of your brain might be asking the question, "Wait a second. How can these statistics be reconciled? US corporations either pay more, the same, or less tax in comparison to foreign corporations. So who is right? Do US corporations face the second-highest tax burden or the second-lowest?"

There is a simple explanation for this inconsistency. And it can be summed up in one phrase that was popularized in a well-known TV ad: "90 percent of all statistics can be made to say anything … 50 percent of the time."[11] Because corporate taxation is a political football, the results of corporate tax burden comparisons between different countries often times depend on the "agenda" that the researcher intends to advance.[12]

But even if a researcher has the purest of intentions and isn't beholden to an agenda, there are myriad ways to calculate corporate tax liability, and to think that the choice of which method to use is free of making biased assumptions is nothing more than wishful thinking.[13] As we know all too well, assumptions are often based on a person's political and ideological beliefs.

Regardless of political and ideological beliefs, one thing is certain. After all is said and done, the corporate tax reform debate has a unique quality about it: it is a "*comparative* legal discourse."[14] What I mean by that is that those who have taken a stand in the debate – from politicians to nonprofit organizations to lobbyists to the media to tax practitioners and anyone else with a pulse – frame their arguments in a *comparative* way.[15]

The role that comparative law plays in the corporate tax reform debate is nothing short of staggering. The following is an example of an argument that relies heavily on legal comparisons to advance a specific proposal for legislative tax reform: "The most critical element of the current corporate tax reform debate is competitiveness."[16] And arguments about international competitiveness are, not surprisingly, comparative.[17] Consider the Bowles-Simpson report. It states that US statutory corporate tax rates are "significantly higher than the average for industrialized countries."[18] It goes on to list that "statistic" as one of the primary reasons why US corporations are put "at a competitive disadvantage against their foreign competitors."[19]

Thus, the report begins by comparing statutory rates, cites how disproportionate US corporate tax rates are to other industrialized nations, and then summarily concludes that because the United States has higher tax rates than the rest of the world, it has created an environment that puts American corporations at a competitive disadvantage in the global marketplace.

So enough procrastinating, what side of the debate do I fall on? I won't mince words. The corporate tax system in the United States is broken and needs to be fixed. Very simply, it falls woefully short of achieving its purpose: revenue collection. I base this view on three arguments.

First, the corporate tax system in the United States is like a lost sheep that is trying to find its way back to pasture. To say that the United States lags behind the corporate tax systems of other industrialized countries is like saying that "Moaning Myrtle," the ghost that haunts the girls' dormitory at Hogwarts in "Harry Potter," is a "little emotional."

To add insult to injury, the United States' broken corporate tax system could not have come at a worse time in history – at a time when other countries have overhauled their corporate tax systems to make them "lean and mean" and more competitive in the global marketplace. In doing so, these countries have made a bold statement to the US: "Eat my dust."

And if you thought that these countries have made only modest reductions in their statutory rates, you would be mistaken. On the contrary, they have slashed statutory rates not with a scalpel, but with a hatchet. Second, the corporate tax system is riddled with loopholes as large as Swiss cheese and preferences as large as lunar craters, resulting in very little revenue actually being collected. Very simply, the corporate tax system is too complex, making compliance and administration by corporate taxpayers who want to "get right" with Uncle Sam all but impossible.

My position can be summarized as follows:

> The US corporate tax system must be overhauled so that it can become more competitive, simple, and fair, while at the same time addressing the nation's deficit. While my primary focus is on competitiveness, this is not

to suggest that simplicity and fairness should go the way of the baby with the bathwater. On the contrary, they are also relevant, as demonstrated by the fact that many countries that were suffering similar deficits gave them full consideration,[20] just not to the same extent as competitiveness. Indeed, it is hard to dispute that the 800-pound gorilla is competiveness.

Lest you think that I am merely going to sit back and criticize the existing structure without making any recommendations of my own, you are mistaken. With these three purposes in mind – competitiveness, simplicity, and fairness – I make three recommendations. As a preliminary matter, there is nothing sweeping about these recommendations. They've been made before and I'm merely adding my two-cents.

First, the statutory corporate tax rate must be reduced. "Holy smokes, Batman! That will result in the loss of a lot of revenue." I don't disagree. That's why I recommend that if the corporate tax rate is to be reduced, then the tax base must be broadened in order to compensate for the resulting loss in revenue. This "lower the rates, broaden the base" theme is a recurring theme in the debate. Second, the current system of taxing US multinational corporations on their worldwide income must end. Very simply, this antiquated system must give way to a territorial one.

Below is a more detailed analysis of all three arguments, along with my recommendations.

Point Of Emphasis Number 1: The US Statutory Corporate Tax Rate Must Be Reduced

The United States imposes a statutory corporate tax rate that is among the highest in the world. A recent statistic proves it. According to Organisation for Economic Co-operation and Development (OECD) data, the combined federal and average state corporate tax rate for 2010 for a US corporation was about 39.2 percent, significantly higher than the unweighted average of 25.6 percent for other OECD countries (excluding the United States).[21]

While US statutory rates have remained consistent overall since 1986, other countries have continued to cut their statutory rates.[22] For example, Germany dramatically lowered its rates by ten percentage points as part of a 2008 reform[23]; the UK lowered its statutory rate from 28 percent to 27 percent in 2011, with gradual reductions taking the rate to an eventual 20 percent in 2015[24]; Canada lowered its statutory rate from 22 percent in 2007 to 18 percent in 2011, with planned gradual reductions to 15 percent starting in 2012[25]; and China lowered its corporate tax rate from 33.3 percent to 25 percent in 2008.[26]

Why delve into these statistics? To make the following point: with such astonishing evidence of differences in rates, lawmakers in Washington would have to be living under a rock not to recognize how disproportionate the US corporate tax rate is to most industrialized nations. Turns out that these sobering statistics were the wakeup call that certain lawmakers needed – specifically, those who were "cynical" – in order to convince them that the US corporate tax rate was broken and needed fixing. As quoted in one law journal, "[t]here is increasing recognition in Washington that the US corporate tax rate is out of step with the lower tax rates of most industrialized and emerging nations."[27] The proof is in the pudding, or should I say, in the multiple bills and other legislative proposals for corporate tax rate reduction that this call-to-action inspired.

But a wide disparity in tax rates is not the only reason why lawmakers in Washington have taken action. The 800-pound gorilla sitting in the room is the negative impact that this disparity in tax rates has on the competitiveness of US businesses, and indirectly, the "average Joe" who works for these companies. And who is the average Joe? None other than h*onest, hard-working* Americans who, as citizens of the United States, enjoy a right that embodies the spirit of American democracy: the right to vote. Indeed, not only do we have the power to elect representatives to office but we also have the power to *remove* representatives from office. Suffice it to say, this is not lost on our elected men and women who serve in Congress.

This raises an interesting question: "Who *ultimately* bears the burden of corporate taxation in the United States?" It is the subject of a lively, sometimes contentious, debate among economists.[28] Is it the shareholders of a corporation, the workers (through a decrease in wages), or the customers through increased output prices? Or could it be some combination of two or more of these groups? Personally, I'd argue that one group does not bear the burden entirely, but instead that it is spread over two or more of these groups.

While this view sounds rational, it is not universally accepted by economists. On the contrary, some economists argue that shareholders shoulder the burden through lower after-tax returns. However, recent studies show otherwise: "in a world where capital is much more mobile than labor, much of the burden is shifted to workers in the form of lower wages."[29]

In fact, one recent study suggests that in the United States, between 45 percent and 75 percent of the corporate tax burden is shouldered by labor, with the rest shouldered by capital.[30] What does this mean? With tax rates *higher* in the United States compared to the rest of the world and with labor shouldering the lion-share of the tax burden, "US workers are worse off compared to workers in other countries."[31]

Point Of Emphasis Number 2: Effective Rates And Revenue Collection

Why is only a small amount of revenue actually collected from US corporations? One need look no further than recent media reports. Such reports have brought attention to a subtle, yet ironic contrast between high US statutory corporate tax rates and the low *actual* taxes paid by US multinational corporations.

In a story published by the *New York Times* on May 2, 2011 entitled "US Business Has High Tax Rates but Pays Less," author David Kocieniewski states: "by taking advantage of myriad breaks and loopholes that other countries generally do not offer, US corporations pay only slightly more on average than their counterparts in other industrial countries."

In another story entitled "G.E.'s Strategies Let It Avoid Taxes Altogether," Kocieniewski explains how General Electric, the nation's largest corporation, paid little or no taxes despite reporting billions of dollars in profits. The story created so much outrage that it led to a public relations nightmare for the company with the harmonic slogan, "we bring good things to life." Indeed, it forced the company into a defensive position with public relations consultants on call twenty-four seven.[32]

It is important to recognize that the term "effective rates" refers to several different measurements of the tax burden faced by corporate entities. The easiest method used to measure a US multinational corporation's tax burden is the effective tax rate (ETR).[33] It is defined as the total amount of actual taxes paid divided by the pretax income.[34]

A PricewaterhouseCoopers (PwC) study "found that the ETR faced by US multinationals from 2006 to 2009 was 27.7 percent, which is only moderately higher than the un-weighted average in the OECD countries (excluding the United States) of 22.6 percent."[35]

Other studies examined the effective marginal tax rate (EMTR). A study from the American Enterprise Institute (AEI) "found that the EMTR faced by US multinational corporations was 23.6 percent, which is substantially higher than the OECD average (excluding the United States) of 17.3 percent."[36]

Another reason for the small amount of revenue collected from corporations in the United States is that only C corporations are subject to corporate-level taxes.[37] The shareholders of a C corporation are subject to a second level of tax when the corporation distributes earnings to them.[38] This results in "double taxation: once at the corporate level and again at the shareholder level."[39]

On the other hand, other business entities, such as limited liability companies (LLCs) and S corporations, are treated as "pass-throughs" for tax purposes.[40] This means that the entity is *not* subject to taxation. Instead, "the tax liability passes through to the owners, who are subject to a single level of tax."[41]

Not surprisingly, most small business owners prefer to operate their businesses as a pass-through than as a C corporation. The tax planning opportunities associated with pass-throughs has been highly scrutinized in recent years, with some lawmakers calling for "corporate tax reform to address this issue."[42] For example, Senator Max Baucus, the Senate Finance Committee Chairman, said that Congress should consider taxing pass-throughs as corporations.[43]

I strenuously disagree. Because much of the US workforce is employed by pass-through entities[44], taxing pass-throughs would pose a substantial risk to jobs. But there is yet another cause for concern. After peeling back the layers, a petulant issue lies at the heart of the debate on whether pass-throughs should be taxed, one that is no less polarizing than the general question of whether the US corporate tax rate makes it difficult for US multinational corporations to compete in the global marketplace: "What types of business entities should be subject to entity-level tax in the first place."[45] This question will inform the debate and help lawmakers to think long and hard before expanding entity-level taxation beyond the C corporation.

Point Of Emphasis Number 3: The United States Must Transition From The Current System Of Taxing US Multinational Corporations On Their Worldwide Income To A Territorial One

While the United States might be a "Canaan of capitalism,"[46] it is also one of the only countries left on earth that still taxes its corporate entities on a global basis. Global taxation means that the United States imposes taxes on the worldwide earnings of US corporations without regard to its source. Worldwide taxation by the US does not "disarm the taxing power of other countries."[47] On the contrary, US multinational corporations pursuing income outside of the US are likely "to encounter tax collectors asserting their own national claims."[48]

To eliminate the effects of possible double taxation of a US company's earnings by both the United States and the country from which the earnings were obtained, US multinational corporations are entitled to a credit.[49] That credit, called the foreign tax credit, is a "concession" that the US Treasury makes "to the taxing power of the country of source."[50] It "rests on a simple idea: income taxes paid to the US Treasury are reduced (*i.e.*, credited) by the amount of income taxes paid by US persons to foreign governments."[51]

A credit is nothing more than "a dollar-for-dollar reduction of US income tax by the amount of foreign income tax."[52] The following example serves two purposes: first to demonstrate how the credit works, and second to illustrate a fundamental concept: when foreign tax rates are identical to US tax rates, it does not matter "whether the US Treasury simply ignores foreign income [altogether] or allows [a credit] of its own tax by"[53] an amount proportionate to that paid by the US taxpayer to the foreign government.

John is a US citizen who lives and works in country A. Assume that the US and country A's income tax rates are both 35 percent. For each dollar that John earns in country A, John would have to pay 35 cents in foreign tax to country A. The US tax on John's country A income, pre-credit, would also be 35 cents (remember that the US taxes its citizens, residents, and multinational corporations on their worldwide income).

However, the US tax of 35 cents would be completely offset by a 35-cent credit for the foreign taxes that John paid to country A. At the end of the day, the tax that John pays to the US Treasury would be zero, making John's overall effective tax rate 35 percent, the same rate paid by a US taxpayer living in the United States.

What if country A's tax rate was *lower* than the US rate of 35 percent? For example, assume it was 25 percent. In that case, the foreign tax that John paid to country A would be credited in full and the US would collect a balance that is the excess of the US rate over the foreign rate. The end result is that John would pay 25 cents of tax to country A and 10 cents of tax to the US.

Another way of looking at this is that the US asserts *secondary* jurisdiction over the foreign income of US multinational corporations. From a simple idea, the foreign tax credit has evolved into a sophisticated scheme that is more confusing than the elaborate labyrinth that Harry Potter had to navigate in the "Triwizard Competition." Much of the blame for that lies with Congress.

In 1921, Congress enacted the foreign tax credit limitation. The limitation puts a cap on the credit that a US person (human or entity) is entitled to. How so? By limiting the credit to the amount of US tax attributable to foreign source income.[54] In one fell swoop, what Congress giveth in the foreign tax credit it taketh in the foreign tax credit limitation.

Armed with this knowledge, my argument can be easily made and understood as follows: "US worldwide taxation makes US corporations *less* competitive in foreign markets."

No discussion of the global taxation system of multinational corporations by the United States would be complete without recognizing that there is a timing issue. If your mind immediately turned to "deferral," you are on the right track. What is tax deferral? It refers to instances where a taxpayer can delay paying taxes to some future period.

To understand the benefits of tax deferral in the context of US multinational corporations doing business abroad, some background information is needed. Recall that corporations have their own unique, separate identities.[55] The separateness of a corporation is the very reason why its earnings are subject to two levels of taxation: (1) one imposed on the corporation's income, and (2) one on dividend distributions received by shareholders.[56]

Foreign-sourced profits of a US multinational corporation are not always *immediately* taxed.[57] For example, consider profits earned by a controlled foreign corporation ("CFC") that is a subsidiary of a US multinational corporation. Generally speaking, because a CFC is a separate foreign person, it is not subject to US taxation on its income derived from outside the United States.[58] The one caveat, of course, is if the CFC repatriates its earnings back to its parent (*i.e.*, the US multinational corporation), and the parent distributes those earnings to its shareholders in the form of dividends.[59]

This feature of the US tax system is known as "deferral," because US taxation is deferred until foreign earnings are paid to US shareholders as dividends. In light of the fact that the distribution of dividends is largely optional, deferral can theoretically go on indefinitely.[60]

The advantages of this kind of tax deferral can be attributed to two interdependent effects: "the tax rate effect and the interest effect."[61] The *tax rate effect* is based on the fact that as long as the profit of a subsidiary is not distributed to the domestic (*i.e.*, corporate) shareholder, the profit is not taxed in the shareholder's country.[62] If the foreign tax rate is lower than the domestic one, profits can be retained in order to shelter them from domestic taxation.[63]

The *interest effect* is due to the fact that if the foreign tax rate is low, the tax rate effect on the net yield is growing with time as the amount of additional interest increases exponentially (interest advantage).[64] The net yield is higher in a low-tax country than in a high-tax country and hence the capital grows at a faster rate.[65]

These features of the US tax system create an incentive for US multinational corporations to accumulate foreign earnings offshore.[66] This phenomenon is known as the "lock-in effect."

The global taxation system of the United States is radically different than the corporate tax systems of other nations. Most countries tax their corporations on a territorial basis. Under a territorial system, only the earnings of a corporation from sources within that country's borders are subject to taxation. Countries that impose taxes on a territorial basis "accommodate other tax systems in the simplest way possible: by not extending their own."[67]

For example, a French corporation that invests in the United States will not be subject to taxation in France on the profits earned from sources in the United States. The fact that the United States stands in virtual isolation when it comes to taxing its corporations on a worldwide basis puts US multinational corporations at a competitive disadvantage when compared to multinational corporations in countries that employ a territorial tax system.[68]

My competitive comparative argument can be summarized as follows:

> "Because most countries employ a territorial tax system, the active foreign earnings of corporations in these countries are exempt from taxation in their home country."[69] US multinational corporations, on the other hand, are *not* exempt from paying taxes on their worldwide income in the United States. As a result, a US multinational corporation has a snowball's chance in hell of being able to compete for another country's investment, by perhaps submitting a lower bid on a project than a foreign corporation.[70]

Consider the following example, based on the hypothetical presented by Omri Y. Marian in his article, "Meaningless Comparisons: Corporate Tax Reform Discourse in the United States."[71] Suppose that a German corporation invests in a subsidiary in country Y. Because Germany employs a territorial system, the German corporation only has to shoulder the burden of taxes imposed by country Y on its country Y subsidiary.

Assume that country Y imposes a low tax rate – one that is lower than the tax rate in the United States. Because the earnings of the country Y subsidiary were earned "outside" Germany, Germany will not impose any taxes on the repatriated earnings of the German corporation from its country Y subsidiary.

Now compare that to a US corporation investing in a country Y subsidiary. Like the German corporation, the US corporation must pay the same taxes to country Y. But that is not all. Unlike the German corporation which has no tax obligation to the German government on the repatriated earnings of its country Y subsidiary, the US corporation does. Very simply, the US corporation is subject to an additional level of US tax upon repatriation of such earnings to the United States. This problem is referred to as "outbound competitiveness."[72]

This leads me to my final point: US worldwide taxation makes US corporations *less* competitive in foreign markets.

The higher tax burden on US multinational corporations does not just create a problem of outbound competitiveness, but it also creates a problem of "inbound competitiveness."[73]

How so? The lock-in effect:

> "prevents US corporations from bringing the money earned abroad back to the United States for reinvestment in the US economy, thereby hampering the creation of US jobs. Rather, the lock-in effect encourages US multinational corporations to seek investment opportunities overseas to avoid the repatriation tax."[74]

Some commentators have rejected each of these arguments as justification for territoriality. At a hearing before the Ways and Means Committee, one critic testified that there was no evidence to suggest that the tax burden faced by US multinationals in foreign jurisdictions was higher than that of their foreign counterparts.[75] I find this argument unavailing.

Conclusion

At a hearing before the Ways and Means Committee back on May 24, 2011, Representative Sander M. Levin said the following:

> "To say simply that we want to adopt certain territorial features and low statutory rates offered by other countries' tax systems is somewhat like going out to shop for a car and

saying, I would like to have a Corvette engine without worrying about anything else."[76]

Analogizing corporate tax reform to the engine of a car made me think about roads. Almost immediately, I thought about a line from my favorite movie – "Back to the Future." That line is the inspiration behind my response to Senator Levin's cynical comments.

Marty McFly: Hey, Doc, we better back up. We don't have enough road to get up to 88.

Dr. Emmett Brown: Roads? Where we're going, we don't need roads.

In that same vein, "worrying about anything else" is analogous to a road. But where we're going Senator – onward and upward to a territorial system and low statutory rates – we don't need roads.

Endnotes

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A Review Of 2014 – Corporate Acquisitions And BEPS

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Corporate acquisitions have returned with a vengeance in 2014 – the greatest number of deals since 2007. This is partly because the US and UK economies have recovered, partly because larger companies have amassed significant amounts of cash in the downturn and are now turning their attention to acquisitions, and although banks are still hesitant to lend again, interest rates are low and therefore money, when available, is cheap.

Perhaps the most significant phenomenon in 2014 has been the US corporate inversion, where the acquisition of a non-US company enables the US company to become a subsidiary of the non-US company where tax rates are lower, such as the UK and Ireland. But it is not only the higher tax rates in the US which are relevant, it is primarily the territorial approach of countries such as the UK and Ireland, as opposed to the worldwide approach in the US, which has triggered these inversions. The key sectors to see movement have been in pharmaceuticals and health care, energy and power, and industrial chemicals.

Therefore, one of the driving forces in US corporate inversions is that overseas earnings, which have attracted low rates of tax, cannot be brought back to the US without significant additional US tax under their worldwide system of taxation. US tax reform is unlikely in the short term, so the US is adopting a sticking-plaster policy of trying to make inversions more difficult, partly through moral persuasion and particularly where the foreign parent company has limited substance. Indeed, this may be where foreign jurisdictions themselves may help the US in demanding substantial management activities to ensure local tax residence. In the meantime, perhaps the US could adopt a semi-amnesty policy of reducing the US corporate tax rate on foreign earnings to, say, 10 percent, without a full-scale tax reform program being required.

Outside the US, acquisitions have been prevalent within the EU countries, either through traditional take-overs or through cross-border mergers. The former is fairly quick but requires minority shareholders to relinquish their shares, a protection more often afforded within Continental EU countries than in the UK. Mergers in the UK are less common and may require court approval, hence taking more time but with greater certainty as regards minority shareholders.

All corporate acquisitions, whatever their nature, have to factor in the significant costs involved, including transfer taxes and professional fees. It is clearly beneficial if the eventual holding company has a territorial approach in its tax system, while companies being acquired should preserve any tax losses and avoid potential tax claw-backs. The shareholders have to ensure that any paper-for-paper exchanges do not trigger a capital gains tax liability, but a deferral until the new shares are eventually sold. From a regulatory point of view, corporate acquisitions need to ensure that Competition and Markets Authority clearance is obtained if there is any potential that consumers will be harmed by take-overs or merger arrangements.

Private equity deals involved in corporate acquisitions are necessarily more short term in nature than longer term cross-border mergers. They also feature a high degree of leverage, and may involve structures which may be perceived as embodying aggressive tax planning. Thus thin capitalization issues may create challenges for interest deductibility, and the creation of holding companies whose substance may be questioned is more likely to come under attack by tax administrations. For example, Luxembourg holding companies have been used extensively in such deals involving hybrid instruments such as PECs (Participating Equity Certificates), treated as interest in Luxembourg but equity in, for example, the US.

The OECD in its BEPS initiative would wish to attack such structures in three ways: first, by negating the tax benefits to be derived from hybrid instruments under Action 2 of BEPS; secondly, by denying treaty access to a Luxembourg entity without the required degree of substance recognized by other countries under Action 6 of BEPS; and thirdly, by attacking Luxembourg itself for granting what the OECD considers State Aid to finance companies through their practice of beneficial tax rulings. Indeed, the OECD has attacked Malta and Ireland for similar State Aid practices involving financing and intellectual property licensing structures.

It appears that a whistle blower in Luxembourg has leaked that 548 tax rulings are currently being investigated by the European Commission involving Luxembourg companies created by entities in the US, Japan, China, Russia, Brazil, and many other countries, particularly in the EU. It remains to be seen whether the accusations of State Aid will be upheld by the Courts, and yet further if any claims may be made against the companies involved to repay the tax benefits obtained. And what happens in the event that a company benefiting from such tax rulings has since been acquired by another, and where tax indemnities have been entered into by the vendor shareholders?

If monies have been placed into escrow accounts to cover such tax indemnities, claims may be easy to satisfy. But the consequences of State Aid being upheld could create huge ripple effects in terms of claims, perhaps against the advisers themselves who have been instrumental in obtaining these beneficial tax rulings.

What is clear is that the BEPS initiative is changing the way international business structures are being implemented. The first and foremost requirement is that any entity within a corporate structure has to have the relevant degree of substance to ensure it is tax resident in the particular country, and that it merits access to double tax treaty arrangements. Aggressive tax planning in the form of hybrid instruments, for example, are to be avoided, and intercompany arrangements have to clearly demonstrate the arm's length principle of transfer pricing. Indeed, country-by-country reporting, as recommended in Action 13 of BEPS, will provide transparency to tax administrations so that they can easily identify exceptional profits in jurisdictions which may suggest tax benefits and lack of required substance.

Ultimately, companies will consider the reputational risk of transgressing the recommendations inherent in the new era of BEPS, rather than the benefits to be obtained from tax mitigation. There will therefore be a continual conflict at Board level between corporate governance involving reputational risk, and the financial requirements of maximizing shareholder value. This does not mean, however, that the minimization of tax costs isn't a fundamental consideration when developing the growth of a company, or becoming involved in corporate acquisitions, and certainly the avoidance of double taxation is a fundamental requirement. Nowhere is this more obvious than in emerging markets, where the risks at all levels are considerably higher than in developed markets.

In countries such as China, South Korea, Africa, and India, tax risks are at best uncertain, as has been demonstrated in the *Vodafone* case in India and the *Lone Star* case in South Korea. These countries prefer to levy taxes according to what they consider the source of income or gains, as opposed to the perceived tax residence of the recipient entity. Where other countries impose tax on the residence basis of taxation, there may be instances where tax liabilities in these emerging markets cannot be credited against tax liabilities elsewhere.

Bilateral investment treaties may be useful in protecting investors in these regions from governmental actions such as expropriation of assets, although their practical effect may be somewhat theoretical, but they do little to address the issue of potential double taxation. What is of greater effect is to maintain assets outside the relevant country where possible. These assets may be cash assets, but are also likely to be intellectual property required for the development of any local projects. Although BEPS addresses the issue of transfer pricing of such intangible rights, their foreign ownership not only allows protection of such rights, but may enable an element of double taxation to be avoided.

Thus although 2014 may have witnessed a resurgence of the mega deals and generally witnessed more corporate acquisitions than in the previous six years, it may be remembered more as the year in which the emphasis companies and their professional advisers place on tax mitigation has changed in the light of the BEPS initiative. Reputational risk is seen as a much higher priority than tax savings, and international business structuring consultants must reflect carefully before advising on corporate arrangements. This is true whatever their professional discipline, be they lawyers, accountants, tax practitioners, private equity managers, or corporate finance specialists. With the threat of more State Aid investigations, 2015 will be an interesting year for all of us.

Topical News Briefing: A Good Tax

by the Global Tax Weekly Editorial Team

It is uncommon for a tax to be viewed as "growth friendly" from an economic standpoint, and many of us, while accepting that taxes are necessary, pay them begrudgingly. But there do seem to be some exceptions around the world. India's long overdue goods and services tax, which will replace a plethora of inefficient indirect taxes, is expected to boost the country's economic output. China, with its ever-expanding value-added tax (VAT) regime, is another example.

VAT was implemented in China in 1984, so is not strictly speaking a new tax. But VAT is replacing the business tax, a levy unique to China, which the Government feels is holding back the economy; as a type of turnover tax, the business tax is not creditable and therefore cascades throughout a supply chain, and is also applicable to both the export and import of services. And if the Government's figures are to be believed, the gradual replacement of business tax with VAT, which, like many tax reforms in China started on a limited pilot basis, in 2012, has already had a positive impact on the economy.

During a news briefing held by the State Administration of Taxation (SAT) on July 24, 2014, to report half-year tax statistics, the tax agency said that the implementation VAT had secured savings worth a total of CNY267.9bn (USD43.6bn) for businesses, although some industries have benefited more than others. Of those services recently added to the VAT base, the railway transportation sector and the postal sector, both included from January 1, 2014, benefited from reductions in their tax burden of CNY21.8bn and CNY200m, respectively, and the telecoms sector, added from June 1, 2014, saw an early reduction worth CNY3bn. Across all sectors subject to VAT, total savings were estimated at CNY85.1bn for the full six months to the end of June. As reported in this issue, the Government will pilot the introduction of VAT on financial services next year, before completing the reforms by replacing business tax with VAT on the "living services sector."

Since the beginning of 2012 and up until June 2014, 3.42m taxpayers have registered for VAT purposes, up from the 2.47m reported to be registered at the end of October 2013. So the changes appear to have been a "win-win" for the Government and businesses alike: the SAT said that tax revenues were up significantly after the reform, potentially due to the incentives for businesses to account for VAT on supplies to recover input tax; such was unavailable under the business tax regime that VAT is replacing. The Chinese authorities have estimated that the tax benefit of the introduction of VAT could be as much as CNY120bn annually.

The SAT's statistics suggest that the VAT rollout is a step in the right direction and the Government has been praised by the likes of the IMF for its ongoing program of tax reforms. However, there is certainly a lot of work that remains to be done by the Chinese authorities to make the country's tax system more appealing. The recently released Paying Taxes report by PwC and the World Bank ranks China 120th out of 189 countries in terms of how easy it is for a mid-sized company to comply with its tax obligations, and as economic growth continues to slow this is in sore need of improvement.

Corporate Tax In Ireland: Pulling In Two Directions?

by Stuart Gray, Senior Editor, Global Tax Weekly

Ireland's tax system, and indeed the country's economy as a whole, has arrived at a critical juncture. After exiting its bailout program a year ago, and registering modest economic growth, the Government is promoting changes to corporate taxation that are designed to boost Ireland's appeal to foreign investors. Yet, there is a growing tension in Irish tax policy. Increasing awareness of corporate tax planning techniques has focused much negative publicity on Ireland, and the OECD and the EU seem to be holding the country up as one of the main villains responsible for base erosion and profit shifting. The Irish Government is therefore keen to portray the country as a responsible international citizen with regard to taxation, and is considering new measures to fall into line with OECD BEPS recommendations. These issues are explored in this article.

Introduction

The Celtic Tiger was severely wounded by the financial crisis. Irish Central Bank Governor Patrick Honohan has described its effect on Ireland as "one of the most expensive banking crises in world history," and the country was only saved from bankruptcy by an injection of cash by the "troika" of lenders from the EU and the International Monetary Fund (IMF). Predictably, as a result taxes were increased, and new levies introduced to tackle the budget deficit. But investors didn't desert Ireland. Quite the reverse. Foreign direct investment (FDI) figures remained solid throughout the crisis, and investment from the US in particular is on the rise.

The reason for this is that the fundamentals which attracted investors to Ireland in the Celtic Tiger years essentially remain in place. Crucially, Ireland has fought hard to ensure continuity of its corporate tax rules, the keystone of which is the low 12.5 percent corporate tax rate, in the face of increasingly vocal condemnation of the regime from the OECD, the EU, the US Government and (usually Democratic) members of the US Congress.

It is a strategy that appears to be paying dividends. According to KPMG's Annual Survey of Tax Competitiveness 2014, Ireland has leapfrogged the UK to top the rankings, leaving Luxembourg, the Netherlands, and Switzerland, in third, fourth, and fifth places, respectively. Chris Morgan, Head of Tax Policy, KPMG UK, said: "While Ireland has come in for criticism from some quarters on its tax policies, it appears that companies accept its very clear cross-party commitment to retaining the low rate."

Much of the criticism leveled at Ireland with regard to tax is based on the issue of "substance." Many outside observers consider that Ireland is merely a key stop-off on the circuitous journey that the multinational profits take to limit exposure to tax, and the existence of structures like the soon-to-be-abolished "Double Irish" are cited as justification for these views.

While Ireland undoubtedly is a key plank in many international tax planning strategies, it is not the sort of investment that the Government is keen to encourage, as Finance Minister Michael Noonan explained in a December 2 speech to the Institute of International and European Affairs. According to Noonan, the "Double Irish" was never part of the tax code, nor was it "a sustainable way to build a thriving [FDI] sector for the long-term." In an earlier speech to his Department's Tax Policy Conference, Noonan insisted that "the issue of substance and taxation is, and always will be, a core column of the Irish taxation system."

In fact, contrary to outside perceptions, Ireland isn't just a haven for brass plate companies, having attracted substantial amounts of "physical" investment from abroad: over 115,000 people are employed by 700 US companies in Ireland and, collectively, US companies have USD204bn in FDI invested in the country, representing just less than 10 percent of all US investment in the EU. And in the first six months of 2014, over 100 investments were secured by inward investment agency IDA Ireland, expected to lead to the creation of an additional 8,000 jobs. The second half of the year "looks equally encouraging," the agency said.

Budget 2015

In October, Noonan announced plans to cut the marginal rate of tax for individuals and set out plans for reform of the corporate tax regime, in a tax-heavy 2015 Budget aimed at shoring up Ireland's economic recovery.

Signaling an end to austerity budgets, Noonan told Parliament on October 14: "The progress made over the past three years in improving public finances, increasing economic growth, and creating jobs, means the Government can focus on reforming the income tax system in a manner that positively contributes to and strengthens that recovery. These reforms will give confidence about the future and create the opportunity for businesses to grow again."

Noonan said that income tax changes will make it more attractive to work in Ireland. The marginal tax rate of 52 percent will be lowered "in a manner that maintains the highly progressive nature of the Irish tax system." Changes will be introduced over a number of budgets, with the 2015 Budget lowering the marginal rate from 52 percent to 51 percent through changes to income tax rates and thresholds. In particular, the top rate of income tax is to fall from 41 percent to 40 percent, and the Universal Social Charge (USC) will be restructured. For lower income persons, USC rates will fall and the exempt threshold will rise to EUR12,012 from EUR10,036. Those on higher incomes will see rates restructured and the rate of USC on self-assessed income over EUR100,000 will rise by 1 percent to 11 percent.

Further measures to lower the income tax burden will feature in next year's Budget, and also in subsequent budgets if the Government is re-elected, Noonan said.

A key announcement was the continuation of the Special Assignee Relief Programme, which supports Irish employers to compete with other countries to attract talented individuals.

While retaining the 12.5 percent corporate income tax rate and a number of other key tax incentives for businesses, a report called "Competing in a Changing World: A Road Map for Ireland's Tax Competitiveness"[1] was published alongside the Budget, setting out plans to alter Ireland's tax regime in particular for multinationals.

Included were plans to prevent the use of "Double Irish" arrangements by no later than 2020. The Double Irish arrangement has been used to enable a US parent to exploit intellectual property (IP) rights owned by a subsidiary offshore without that income becoming taxable in the US (unless the profits are remitted). The structure includes two Irish companies, one incorporated in a lower tax territory, which is deemed not to be tax resident in Ireland, while another Irish company, responsible for central management and control, is based and taxed in Ireland. Under US and Irish rules, profits accruing from the IP received by the subsidiary offshore are neither taxable in Ireland nor taxable in the US.

Companies already with operations in Ireland will be given until 2020 to unwind their Double Irish arrangements. For new companies, from 2015, Ireland intends to amend its residency rules to expand the nation's taxing rights to prevent such arrangements.

Noonan also announced a new "Knowledge Development Box" income-based tax regime for intangible assets. This is to be introduced in 2015 to encourage companies to locate their research and development (R&D) activities in Ireland.

In addition, Ireland's existing section 291A capital allowances regime for expenditure on intangible assets will be enhanced. The current 80 percent cap on the aggregate amount of allowances and related interest expense that may be claimed will be removed, and the definition of specified intangible assets will be amended to explicitly include customer lists. In addition, Ireland is to phase out the base year restriction under the R&D tax credit regime.

Noonan said: "These measures will enhance Ireland's corporate tax regime and align it with best practice internationally. It will ensure that Ireland continues to be the home of the best and most successful companies in the world. It will attract and retain companies with real substance offering real jobs."

The 2015 Budget received a stamp of approval from US businesses, and AmCham Ireland President Louse Phelan said the roadmap will "allow American companies currently considering setting up operations in Ireland, and those already here, to plan accordingly."

She said: "Ensuring Ireland remains a highly attractive location for investment must be a top priority. In this context the American Chamber welcomes the vision within this roadmap, which sends out a very positive and powerful signal that – as the Minister has previously stated – in the global competition for FDI jobs, Ireland will play fair but will play to win. This plan contains a range [of] major improvements across the key pillars which are central to Ireland's tax offering: Intellectual Property; the Research and Development Tax Credit Regime; financial services; and Income Tax. The American Chamber had, in the lead up to the budget, highlighted the opportunities presented by such enhancements."

"In the current international tax environment, it is imperative that Ireland makes it attractive for multinational companies to hold, develop, and exploit their [IP] from Ireland. The planned introduction of a new Knowledge Development Box will be a major asset to Ireland in securing these valuable investments. Changes to the R&D Tax Credit, which the Chamber had called for, are also to be welcomed as it is well established that the location of R&D activity has significant impact on economic growth."

Welcoming the reduction in the marginal rate of individual income tax in the Budget, Phelan said: "The personal taxation burden had reached an unsustainable level and the changes announced in the Budget will support greater levels of job creation in both multinational and indigenous companies. The improvements to the Special Assignee Relief Programme will also help Ireland attract key leadership talent into the country."

She concluded: "The measures announced and the certainty they provide are extremely valuable and will make Ireland an even more attractive location for [FDI] in future."

Financial Services Strategy

The Government also has a plan to reinvigorate Ireland's financial services industry, and on November 21 it launched a public consultation to inform the development of a new strategy for the international financial services sector.

Simon Harris, Minister of State responsible for International Financial Services, said that the strategy must clearly identify what actions the Government needs to take, and set out how the new plan will be implemented. A draft strategy will be published early next year.

The current "Strategy for the International Financial Services Industry 2011–16"[2] was prepared in early 2011. The Government said that, since the publication of that strategy, Ireland's economic circumstances have significantly improved and the focus should now be on devising a longer-term strategy.

Harris explained: "Ireland has a vibrant and competitive international financial services sector. It has grown and evolved significantly over the past three decades to become a major component of our economy in terms of employment, exports, and tax revenues. As stability returns to our economy we must now focus on enhancing this sector's continuing contribution to sustainable growth and job creation."

The development of the new strategy will be coordinated through a Public Sector Group, chaired by Harris. The consultation takes the form of a questionnaire, which asks respondents to indicate the factors they believe constitute a competitive advantage or disadvantage.

It will review the perceived competitiveness of Ireland's corporation, personal, and R&D taxation regimes; the business environment, including business costs; and Ireland's reputation as a center for international financial services.

Respondents are also requested to identify opportunities for the future development of the sector, along with the likely risks. In addition, they are asked to detail the key areas that should be addressed by the Government and its agencies over the short- and medium-term.

BEPS

As Noonan said in parliament in September, the Government is well aware that Ireland has "suffered some reputational damage" as a result of the bad press given to its corporate tax system, and the introduction of measures designed to increase Ireland's share of foreign investment are probably only going to antagonize the country's most fervent critics – especially the Knowledge Development Box, which is likely to fall foul of the OECD's campaign against "harmful" tax regimes, and reignite the debate about substance.

Yet, at the same time, the Irish Government is still managing to put a positive spin on the BEPS initiative, and Noonan expressed the view that the project "offers more opportunities for Ireland than risks."

Answering parliamentary questions on September 23, Noonan noted that the OECD "singl[ed] out Ireland again for special mention" in its recent base erosion and profit shifting (BEPS) reports, and that there is "no doubt" that the Government is under increasing international focus.

Noonan was nevertheless positive about the BEPS project, which he described as being based on "a simple concept with two key pillars, namely, to align more strictly substance and taxing rights, in other words, companies should be taxed where they have their substantive operations; and to address harmful tax regimes." This is in line with Ireland's strategy for attracting FDI, he said.

He argued that the BEPS project "offers more opportunities for Ireland than risks," and he welcomed the OECD's acknowledgement that the digital economy cannot be ring-fenced from the economy as a whole.

Noonan said Ireland also stands to benefit from the closure of international tax loopholes. Its 12.5 percent corporate tax rate is the lowest in the OECD, and Noonan believes that it will become even more attractive as BEPS recommendations are implemented.

Irish business group Ibec agrees with the Finance Minister on this point, with Head of Policy and Chief Economist Fergal O'Brien noting that: "Implementation of the BEPS reports would constitute a significant change in international corporate tax rules. Many of the recommendations are needed to reflect the modern reality of how global business operates."

"From an Irish perspective, there are significant opportunities to attract increased investment and employment as the BEPS proposals are implemented by governments. A key focus of the recommendations will be to align business substance with profit allocation. Ireland is well placed to be a location of choice for manufacturing, business decision making, [R&D], and [IP]."

Ibec stressed, however, that the recommendations must be implemented in coordination with other countries. Referring to new country-by-country reporting requirements on multinationals, Ibec said that Irish businesses must not face unnecessary administrative and reporting burdens.

Nevertheless, the Government is preparing itself for possible changes to tax legislation to bring it into line with the OECD's BEPS recommendations, and a report released alongside the 2015 budget maps out the potential impact of the BEPS project on Ireland.

On the area of transfer pricing, the report states: "The Actions which focus on value creation (Actions 8, 9, and 10) are likely to result in changes internationally. It is clear that certain structures, with little substance, are in their winter, and as such there are opportunities for Ireland to become a location of choice for groups who wish to bring their intangible assets onshore together with the relevant substance."

The report moves on to suggest consideration of the adoption of controlled foreign corporation (CFC) rules, stating: "While Ireland does not operate a CFC regime, we do have rules which seek to tax profits once remitted to Ireland. Similarly Ireland has significant legislation relating to interest deductions and as such any further recommended changes would need to be brought about in line with other potential reforms."

The report notes Ireland's concerns about potential restrictions on interest deductions as part of BEPS Action 4, which seeks to prevent base erosion through the use of related-party and third-party debt to achieve excessive interest deductions or to finance the production of exempt, deferred income, or other financial payments that are economically equivalent to interest payments. "At present it is not possible to determine the level of impact of any recommendations which may be proposed under Action 4. However … it will be important that these rules do not unduly impact on some industry groups," it says.

The report also rules out any changes to the Irish 12.5 percent corporation tax rate: "The BEPS project as a whole, or via any of its individual actions, is not focused on Ireland's, or indeed any other jurisdiction's tax rate. The BEPS project is built upon two pillars which are to align profits with substance and to address double non-taxation. Each country's tax rate is not open to discussion." It says that Ireland does not expect any impact on its rules from the OECD's work on tackling harmful tax practices under BEPS Action 5 either, but concludes: "While the BEPS project offers a lot of positives, there will also be challenges for Ireland."

The EU

There is also the EU for Ireland worry about. Economically, Ireland has benefited greatly from its EU membership, but at the same time Brussels could be said to be the country's greatest nemesis as it seeks to sweep aside the kinds of tax rules that have been partly responsible for Ireland's success. Plans to harmonize the EU corporate tax base would likely wipe out Ireland's competitive advantage over other member states in tax terms, and while the European Commission insists that corporate tax rate harmonization isn't on the agenda, key figures in the EU have made no secret of their support for the idea.

The latest EU challenge to Ireland's tax system comes in the form of state aid investigations into tax rulings provided to Apple by the Irish tax authority – a new tactic in the Commission's bid to eradicate tax base erosion by certain member states.

In a letter published online on September 30, 2014, the Commission has said that two advance tax rulings provided by the Irish Revenue may have conferred a selective advantage to technology giant Apple in breach of state aid rules.

Following an in-depth investigation into the rulings, the Commission has explained its "Opening Decision" in a 21-page letter to the Irish Foreign Affairs Minister Eamon Gilmore. The Commission is now proceeding with the next stage in its investigation process and has asked Ireland for additional information on Apple's operations in Ireland.

The investigation concerns tax rulings made in 1991 and 2007 on the attribution and calculation of taxable profits to the Irish branches of Apple Operations Europe (AOE) and Apple Sales International (ASI). In March 2014, the Commission informed Ireland that it was investigating whether the tax rulings constituted "new aid." The Commission is also investigating tax rulings agreed in other member states with two other multinationals.

Article 107(1) of the Treaty on the Functioning of the European Union[3] (TFEU) stipulates that any aid granted by an EU member state or through state resources that distorts or threatens to distort competition by favoring certain undertakings or the provision of certain goods will be deemed incompatible with the common market.

For a measure to constitute state aid under the provisions of Article 107(1), it must meet all of the following conditions: it must be imputable to the state and financed through State resources; it must confer an advantage on its recipient; that advantage must be selective; and the measure must distort or threaten to distort competition and have the potential to affect trade between member states.

According to the Commission's letter, there is "no indication that the contested measure can be considered compatible with the internal market," as it "appears to constitute a reduction of charges that should normally be borne by the entities concerned in the course of their business, and should therefore be considered as operating aid."

The Commission letter says that it has "doubts about the appropriateness of the transfer pricing method chosen for the 2007 ruling" and said it had found "several inconsistencies in the application of the transfer pricing method chosen when determining profit allocation to AOE and ASI that do not appear to comply with the arm's length principle."

"To the extent the Irish authorities have deviated from the arm's length principle as regards Apple, the contested rulings should also be considered selective," the letter adds.

The Commission also raises questions about the "open-ended duration" of the 1991 ruling's validity and "the discrepancy between the sales growth and the Irish operating capacity" of ASI.

The Commission has decided to initiate the procedure laid down in Article 108(2) of the TFEU.[4] It provides that if the aid is found to be incompatible, the member state in question must abolish or alter such aid within a period to be determined by the Commission. Ireland was given one month to provide the Commission with specific additional information.

However, on this issue also, Noonan is confident that Ireland has nothing to fear, and that the Commission does not have "a very strong case." Speaking to reporters after a meeting of European Finance Ministers last month, Noonan said: "My legal advice is that the Irish authorities will win the case quite easily and that there isn't a very strong case by the Commission."

The Irish Finance Department maintained: "Ireland is confident that there is no breach of state aid rules in this case and has already issued a formal response to the Commission, addressing in detail the concerns and some misunderstandings contained in the Opening Decision. Ireland welcomed that opportunity to clarify important issues about the applicable tax law in this case and to explain that the company concerned did not receive selective treatment and was taxed fully in accordance with the law."

Nevertheless, in spite of the Irish Government's confidence, the fact that the Commission has decided to bring the case, and that it could drag on for up to five years, has probably already dented Ireland's business environment to a certain degree. And the wording of the Opening Decision, in which the Commission already seems convinced of Ireland's guilt, is also a worry, suggesting that it will take some persuasion for Ireland to be exonerated.

Conclusion

Despite the Government's confidence in matters to do with tax and the economy, it cannot be denied that the country still faces some challenges, especially on the budget front with fiscal space at a premium. Individual income tax is high, and although the Government lowered the top rate of tax by 1 percent in the 2015 Budget, and plans further cuts next year and in 2017, the Irish Fiscal Advisory Council warned last month that there is no room for such measures given current budget projections. And earlier in the year, the IMF urged the Government to offset any future tax cuts, to ensure that the overall fiscal adjustment "envelope" is maintained.

Moreover, while the Finance Department's medium-term "Strategy for Growth" paper, released in December 2013, attempts to steer Ireland away from "the failed policies of boom and bust," the severity of the financial crisis in Ireland highlighted how vulnerable the economy is to international economic shocks. And as a member of the eurozone, where economic danger signs have once again begun to flash, there is a sense that trouble may be lurking just around the corner.

Of course, the Government cannot be condemned for putting a positive slant on Ireland's prospects. Ireland depends on foreign investment and it is trying to project a sense of confidence and certainty about the future at a time when the international tax landscape, and Ireland's place within it, has probably never been so uncertain as a result of BEPS. It seems to be largely succeeding, based on the business community's reaction to the Government's recent statements and proposals on tax, and healthy inward investment figures. But Ireland's tax regime remains firmly in the sights of the OECD and the EU, and while it continues to play hard to win vital FDI inflows, the wolves are going to continue circling. Unfortunately, nobody is really sure what the outcome for Ireland will be.

Endnotes

1 http://budget.gov.ie/Budgets/2015/Documents/Competing_Changing_World_Tax_Road_Map_final.pdf

2 http://www.fsi.ie/Sectors/FSI/FSI.nsf/vPages/Advocacy_and_Policy_Development~ifsc-strategy-2011-2016/$file/IFS+Strategy+2011.pdf

3 http://eur-lex.europa.eu/legal-content/EN/TXT/HTML/?uri=CELEX:12008E107&from=EN

4 http://eur-lex.europa.eu/legal-content/EN/TXT/HTML/?uri=CELEX:12008E108&from=EN

The Emergence Of The African Tiger

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Nigeria has emerged as a force to be reckoned with in Africa and the world in general. Beset by a myriad of negative issues ranging from insecurity and terrorism to unemployment, the country continues to come out stronger, often debunking the negative assumptions of critics. Nigeria's history is unique in itself, having taken independence from the British in 1960 in anticipation of a brighter and more prosperous future for the newly emerged republic. At that time, the visions of the founding fathers and national leaders helped to sustain the concept of a rosy future for our beloved country. Unfortunately, this vision was somewhat undermined by the overturning of the then democratically elected government by the Nigerian military, with military rule perpetuated through successive coup and counter-coup over the next 28 years.

All these periods were characterized by mass looting, embezzlement, mismanagement, annihilations and self-aggrandizement by the various military rulers. Research has shown that the country lost a staggering USD300bn to looting and mismanagement during this period of military rule. Nigeria experienced its deepest downturn during this era: from a multi product-based economy, strong currency, and envied educational system, to a situation of mass unemployment, mono-product economy (crude oil), devalued currency, and gross mismanagement of public funds.

Yet the country recently took the world by surprise with the announcement that it has the biggest economy in Africa, with a GDP nominal value of USD522bn in 2013 – ahead of South Africa's USD350bn. This new evaluation is premised on the restatement of the Nigerian GDP using a new base year (2010, rather than 1990). Controversies arose both within and outside Nigeria, contesting the robustness of these new figures as published by the nation's National Bureau of Statistics; but the success story of this sleeping African giant is based on measurable milestones that clearly demonstrate its rise to this status.

The return to a democratic government in 1999 has been the main factor in kick-starting the economic recovery of the Nigerian state. The change of governance opened up more political and trade relationships with other countries, boosting the confidence of expatriate Nigerians to return and establish more businesses and industries, as well as encouraging increasing numbers of foreign-owned enterprises in Nigeria. Economic indicators show that the Nigerian GDP has more than doubled over the last 15 years of democratic government, whilst inflation and interest rates have steadily decreased.

While the change to a democratic setting in itself did not transform the country, the developmental and economic processes put in place by the government did much to shift Nigeria to its current position as the largest economy in Africa. Four main factors have been responsible for this unprecedented development: the creation of a favorable legislative operating environment for business; infrastructural development; sound and realistic economic policies; and sustainable trade and investment strategies.

In this democratic setting, the country has witnessed an unprecedented growth of new legislation passed by the national assembly. The new laws cut across all sectors that are fundamental to development – offering new security in the fields of investment, banking, insurance, aviation, maritime and labor, while protecting against financial crime and corruption. Most of the new legislation forms the framework for business in each of these sectors. For instance, the Investment and Securities Act 2007 guides all business dealings and activities in the Nigerian capital market. The Tertiary Education Tax Act 2011, Companies Income Tax Act (Amendments) 2007, Personal Income Tax (Amendment) Act 2011, and Value Added Tax Act (Amendment) 2007 have modified the taxation of business and individuals in Nigeria within the last 14 years.

Another factor that has featured prominently in advancing the growth and development of Nigeria is the sound economic policies put in place by the democratic government. The first step taken by the government in 1999 was to acknowledge that only the private sector can drive the economy towards real growth and development. As a result, the government sold all of its interest in various business entities through the Bureau of Public Enterprises (BPE) and concentrated on its role as regulator of the economy and business environment. The BPE, which serves as the brain behind the government's economic policy, was established by the Public Enterprise Act 1999 and has packaged the sale of more than 30 government businesses and entities in diverse areas such as banking, insurance, aviation, cement manufacturing, automobile manufacturing and assembly, hotels and hospitality, mining, oil palm production, port management, sugar manufacturing, and steel-making.

The government then rolled out various economic policies to address the macroeconomic issues of unemployment, underproduction (as Nigeria was largely import-dependent at that time), price and fiscal stability, interest rates and exchange rate stability. One of these policies was the National Economic Empowerment and Development Strategy (NEEDS), whose core objectives are to empower the Nigerian people, promote private enterprise, and change the way government conducted its works. President Yar'adua also introduced the Seven Point Agenda with the aim of reducing poverty through wealth creation and the generation of employment, sustainable real sector growth, peace, security and stability. Other new initiatives included various fiscal and monetary policy measures put in place to further the government's objectives.

Aggressive infrastructural development was also a key step: having identified the importance of a stable and adequate infrastructure in supporting business and sustaining the economy, the government has invested heavily in infrastructural repairs and construction of roads, ports, airports, major bridges, power and agricultural facilities, as well as social facilities. A holistic approach was taken to power and electricity, recognized as crucial to business success and real sector growth. Until recently, the power sector was under the sole direction of the government through the Power Holding Company of Nigeria (PHCN). The company has been unbundled into 11 generating companies, one transmission company and 18 distribution companies; these were sold to individual investors, as provided by the Power Sector Reform Roadmap and the Nigerian Electricity Reform Act 2005. This decisive move has significantly improved the provision of electricity to commercial and private users across the country, although supply has yet to fully meet demand.

The fourth factor responsible for Nigeria's economic growth is the sound trade and investment strategies pursued by the government, which has recognized the importance of small and medium-scale enterprises (SMEs). New initiatives have enabled these entities to flourish, including the Small and Medium Enterprise Development Agencies (SMEDAN) and readily accessible finance *via* the Bank of Industry (BOI) and the Central Bank of Nigeria (CBN). Tax holidays, for a cumulative period of five years, are now available to businesses on the pioneer list – a list of 71 different businesses and products that is continuously expanding. Other investment strategies include the removal of restrictions relating to a foreigner's ability to do business in Nigeria. The current law and regulations allow non-Nigerians to own businesses; bring in capital; and repatriate capital, interest and dividends if the need arises. The one-stop registration point for these investors in Nigeria also facilitates business. The introduction of the Nigerian Local Content Act 2010 also gives indigenous businesses more participation in contracts emanating from the oil and gas industry. The trade-free zones created all over Nigeria offer an additional impetus to trade and business expansion in the country.

Doing business in Nigeria has never offered greater potential, with its established market of over 170 million people and various incentive options available to investors. This, however, does not mean a completely problem-free business environment. Importantly, power supply is still suboptimal: a business owner in Nigeria must provide for an alternative source of power through generators. Access to capital is also somewhat limited, as most SMEs cannot meet the conditions for accessing the SME funding available through the BOI and CBN. The issue of multiple taxes and levies also remains to be resolved. Nigeria operates a multiple government system at federal, state and local levels, with varying powers to demand taxes and levies for business owners.

In conclusion, Nigeria has rightfully claimed its lead position in the African continent: research demonstrates that the revenue of the Nigerian subsidiary of a multinational telecom company outstrips that of its subsidiaries and parent company. In celebrating the country's new status, and striving towards an even brighter future, we invite others – including the more skeptical – to join us in the success story by coming to start business in Nigeria.

US Anti-Inversion Bill 'Could Save More Revenue'

The Joint Committee on Taxation (JCT) has increased, from USD19.5bn to more than USD33.5bn, its estimate of tax revenue that could be saved over a ten-year period from legislation to restrict corporate inversions introduced by Democrat lawmakers in the US House of Representatives in May this year.

A recent letter from the JCT explained that the rise in revenue savings from the Bill is mainly due to an underestimation of the number of companies that wanted to pursue inversions deals. The JCT said its May 2014 forecast "did not properly reflect the appetite of some US corporations for inversions," or "the increased inversion activity that has occurred over the last year, or has been announced."

Under current law, a company that merges with an offshore counterpart can move its headquarters and tax residence abroad (even though management and operations remain in the US), and take advantage of lower taxes, as long as at least 20 percent of its shares are held by the foreign company's shareholders after the merger.

The Stop Corporate Inversions Act of 2014, introduced by House Ways and Means Committee Ranking Member Sander M. Levin (D – Michigan), would include a proposal made by President Barack Obama in his 2015 Budget proposals to restrict corporate inversions by putting the minimum foreign shareholding cap at 50 percent.

The restriction would apply to inversions after May 8, 2014, and would effectively require US companies to merge with foreign companies that are roughly equal or larger in size in order to move their location for tax purposes outside the US.

In September this year, the US Treasury Department introduced administrative measures to deter inversions, and, in particular, to prevent the methods by which inverted companies access a foreign subsidiary's unrepatriated earnings while continuing to defer US tax. However, Levin has still expressed his belief that "inversions remain a serious problem that must be immediately addressed through legislation."

While leading Democrat and Republican lawmakers now appear to consider tax reform – to cut the corporate tax rate and change the way the US taxes foreign earnings – to be the only real long-term solution for halting inversions, Levin professed that "action cannot wait for tax reform."

"The Treasury Department's proposed rules are an important step toward stemming the tide of inversions," he added, "but the new [JCT] estimates make clear that immediate legislative action is necessary."

House Passes One-Year US Tax Extenders Renewal

In a move that the Senate is likely to have to follow, the US House of Representatives has passed, by a bipartisan vote of 378–46, a Bill that approves a one-year renewal for the "tax extenders."

Following the failure of other more selective and longer-term proposals, the Tax Increase Prevention Act of 2014 takes in all of the 50-plus tax provisions for individuals and businesses that expired at the end of 2013 and extends them until the end of this year. They will therefore need to be revisited by the next Republican-led Congress sometime in 2015.

Renewal of the measures will, however, mean greater certainty for those individual and business taxpayers who are affected by the expired provisions, and also reduce operational and compliance risks that could have delayed the tax filing season and the processing of taxpayer refunds.

The provisions that expired at the end of 2013, which have previously also been rolled forward annually, include, for individuals, mortgage tax relief, the deduction for state and local sales taxes, and education tax deductions.

For businesses, the package of measures includes increased expensing under Section 179; 50 percent bonus depreciation; the work opportunity tax credit; the credit for research and development expenses; and tax breaks promoting renewable energy, such as the production tax credit that is relied upon by the wind industry.

President Barack Obama does not appear to be against the new short-term proposal, following his threat to veto a previous, much more costly proposal that would have permanently extended some of the provisions. In addition, Senate Democrats will probably have to put aside the two-year renewal that they have been seeking and vote through the House bill.

Osborne Delivers UK Autumn Statement

UK Chancellor George Osborne's Autumn Statement introduced an overhaul of the stamp duty system and a raft of new anti-avoidance measures and small business tax incentives.

Osborne delivered his annual mini-Budget on December 3, 2014. The main thrust of his Statement was "low taxes, but taxes that will be paid."

Osborne announced a major shakeup of the slab-rate stamp duty land tax regime, effective from midnight on December 3. According to Osborne, under the old system, stamp duty was a "badly designed tax on aspiration," and one of the UK's "worst-designed and most damaging" regimes. His new system is band-based, with each rate applicable only on the part of the property value that falls within the given band.

The first GBP125,000 (USD195,793) of the property price is now exempt from stamp duty. A rate of 2 percent is payable on the portion up to GBP250,000, 5 percent up to GBP925,000, 10 percent up to GBP1.5m, and 12 percent on the value above GBP1.5m. Anyone who had exchanged contracts but not completed by midnight on December 3 can choose whether to pay under the old system or the new. The changes will apply in Scotland until the Scottish Government's new Land and Buildings Transactions Tax comes into effect in April 2015.

Osborne said that these reforms represent a tax cut of GBP800m a year and will benefit 98 percent of homebuyers who pay the duty.

Osborne also dedicated much of his Autumn Statement speech to a package of anti-avoidance measures. He announced plans for a 25 percent Diverted Profits Tax, to be implemented in April 2015. It is expected to raise more than GBP1bn over the next five years. The Government is also to limit to 50 percent the amount of profit in established banks that can be offset by carried-forward losses, meaning that banks will contribute almost GBP4bn more in tax over the next five years.

In addition, the Disclosure of Tax Avoidance Schemes (DOTAS) regime will be strengthened and a DOTAS taskforce will be set up, to ensure that the rules cannot be circumvented. HM Revenue & Customs (HMRC) will be allowed to publish summary information about notified tax avoidance schemes and their promoters. It will consult in early 2015 on the introduction of further deterrents for "serial tax avoiders" and on penalties for tax avoidance cases where the General Anti-Abuse Rule applies.

The Government will introduce legislation on country-by-country reporting, consult on the introduction of new hybrid mismatch rules, and review how best to enhance the collection and use of information on offshore tax evasion. It will stop tax relief from being claimed on reimbursed business expenses when they are paid in conjunction with a salary sacrifice scheme, crack down on the avoidance of stamp duty on takeovers, and take steps to prevent the disguising of fee income by investment managers.

Individuals and partnerships will be prevented from gaining an "unfair" tax advantage by transferring their business to a company they control and then claiming corporation tax deductions for assets linked to the business's reputation and customer relationships. Individuals will be unable to claim Capital Gains Tax Entrepreneurs' Relief on the transfer of these assets to the company.

The other major tranche of tax-related reforms announced in the Statement is targeted at small and medium-sized enterprises (SMEs). The Government will increase the research and development (R&D) tax credit for SMEs from 225 percent to 230 percent. The credit for large firms will rise from 10 percent to 11 percent. Qualifying expenditure for R&D tax credits will be restricted from April 1, 2015, so that the costs of materials incorporated in products that are sold are not eligible. The application process for smaller companies investing in R&D will be streamlined.

The Government will allow gains that are eligible for Entrepreneurs' Relief (ER) and deferred into investment under the Enterprise Investment Scheme (EIS) or Social Investment Tax Relief (SITR) to benefit from ER when the gain is realized. The annual investment limit for SITR will rise to GBP5m a year, up to a total of GBP15m per organization, from April 2015.

The inflation-linked increase in business rates (property tax) will remain capped at 2 percent, and the structure of business rates will be reviewed in time for Budget 2016. The Government will extend the doubling of the 100 percent Small Business Rate Relief to April 2016, and the rate discount for shops, pubs, cafes, and restaurants with a rateable value of GBP50,000 or less will be increased from GBP1,000 to GBP1,500.

Osborne also announced that:

- The threshold for the 40 percent personal income tax rate will rise in line with inflation for the first time in five years, from GBP41,865 to GBP42,385 from next April;
- The planned increase in the personal tax allowance will go up from GBP500 to GBP600, taking the allowance to GBP10,600 from April 2015;
- From April 2016, the Government will abolish employer National Insurance contributions on earnings up to the upper earnings limit for apprentices aged under 25;
- The non-dom levy for individuals who have been resident in the UK for 12 of the last 14 years will rise to GBP60,000, and a new GBP90,000 charge will apply to those who have been resident for 17 of the past 20 years;
- Corporation tax setting powers will be devolved to Northern Ireland, subject to an inter-party agreement;
- The rates of the Annual Tax on Enveloped Dwellings (ATED) will be increased by 50 percent above inflation;
- The Supplementary Charge on North Sea activity will be reduced from 32 percent to 30 percent

from January 1, 2015, and the ring fence expenditure supplement will go up from six to ten accounting periods for all ring fence oil and gas losses and qualifying pre-commencement expenditure incurred on or after December 5, 2013;

- The Government will aim to make the taxation of employee benefits and expenses more straightforward and effective. It will consider accepting 51 recommendations made by the Office for Tax Simplification;
- Companies substantially benefiting from Government support for the generation of renewable energy will be excluded from benefiting from other tax-advantaged venture capital schemes;
- Air Passenger Duty for children under 12 will be scrapped from May 1, 2015, and for children under 16 from 2016;
- A new children's television tax relief will be introduced in April 2015, with eligible companies able to claim 25 percent of qualifying production expenditure back through the relief;
- The 55 percent so-called "death tax" that applies when an unused pension pot is passed on to a relative will be abolished;
- Search and rescue and air ambulance charities will be eligible for value-added tax (VAT) refunds, and the Government will refund unrecoverable VAT incurred by the hospice sector; and
- The inheritance tax exemption will be extended to cover aid workers and emergency services personnel who die responding to emergency circumstances.

Henry Stuart, Partner at international law firm Withers, commented: "There's no doubt that the proportional approach to stamp duty announced today will reduce the volume of high-value purchases. The concern is cost, and buyers will reassess their current approach accordingly from midnight tonight. Certainly non-UK buyers will now consider buying high value properties through corporate structures again, as the 15 percent duty won't appear so daunting under the new bands, and these structures will offer them an [inheritance tax] shelter. Of course, as stamp duty land tax is a tax on transactions, it isn't accurate to compare this with the annual charge proposed under 'mansion tax' models, which is a tax on wealth."

On the anti-avoidance measures announced, Paul Rutherford, Tax Partner at DLA Piper, stated: "The Chancellor has announced that the UK will introduce a 25 percent 'diverted profits tax' – already being referred to as a 'Google tax' – on multinationals that artificially move profits out of the UK to lower-taxed jurisdictions. While the Chancellor didn't name names, it is likely that he had large multinational tech companies – many of which have been criticized recently for the amount of UK corporation tax they pay – in mind when making his announcement. It is entirely unclear how this new tax will work as the Government is yet to provide further detail."

Stephen Jones, Legal Director at DLA Piper, added: "The Government's launch of a consultation into measures to adopt the OECD's recommendations in relation to hybrid instruments is welcome. Rumors of immediate changes to the rules on the taxation of hybrids were proved to be false. The Government's willingness to engage with the international community on tax avoidance must be a good thing: the UK continues to combine low corporate tax rates with an internationally respected emphasis on fairness, which makes us a good place to base an international business."

UK Legislation Due On Diverted Profits Tax Plans

The UK Government is due to release legislation to introduce its new Diverted Profits Tax, announced in Chancellor George Osborne's Autumn Statement.

From April 2015, the tax will be levied on profits "artificially" shifted from the UK at a rate of 25 percent. The legislation, due on November 10, will clarify how the plans are intended to work in practice, with questions already raised about the tax's scope and its enforcement.

The rate is higher than the rate of corporate income tax, which is due to fall to 20 percent from April 2015. Osborne said the measure is intended to dissuade companies from shifting profits out of the UK, alongside the introduction in the UK of the joint lowest corporate income tax rate among the G20 nations. The UK Government estimates that the new levy could generate GBP25m within its first year, with revenues projected to grow to GBP270m in the fiscal year 2016/17. The levy is projected to generate about GBP350m in each subsequent fiscal year.

Introducing the measure, Osborne said: "We will make sure big multinational businesses pay their fair share. Some of the largest companies in the world, including those in the tech sector, use elaborate structures to avoid paying taxes. Today I am introducing a 25 percent tax on profits generated by multinationals from economic activity here in the UK, which they then artificially shift out of the country. That's not fair to other British firms, it's not fair to the British people either, today we're putting a stop to it. My message is consistent and clear – low taxes that will be paid. Britain has led the world on this agenda and we do so again today."

Osborne has hailed the measure as part of the UK's efforts to lead the way on responding to base erosion and profit shifting (BEPS), yet the OECD and stakeholders to its BEPS project have consistently underlined the need for countries to refrain from unilateral measures, to allow time for consensus to be reached on an international response. The measure, therefore, will be highly controversial, as it may lead to instances where the UK seeks to levy tax on income taxable under other countries' tax regimes, heightening the risk of double taxation.

Tax expert Heather Self, of law firm Pinsent Masons, said: "The Diverted Profits Tax will be very complex and could encourage retaliation against UK businesses trading overseas. The expected yield of around GBP1bn could be far outweighed by the harm done to UK businesses seeking to expand internationally."

Martin Lambert, Head of International Large Corporate Tax at Grant Thornton UK LLP, added: "This tax rate, which at 25 percent is 5 percent higher the general corporation tax rate that will apply at the time the rules come in to place, feels like an additional penalty for groups that are not complying with the Government's principle of fairness. We await further details as to how this tax will be administered and what additional evidence groups will be required to support their compliance with these rules. We understand that further details will be published later this month."

Chris Morgan, Head of Tax Policy at KPMG in the UK, said: "This is a completely radical approach we've never seen before. The Chancellor has brought in a new rate for 'artificially diverted' profits. As this rate is higher than the prevailing rate of corporation tax, this move totally removes any tax avoidance advantage achieved by diverting profits. As such it's a very clever move."

"The Chancellor has repeatedly offered businesses operating in the UK a pledge to provide the most competitive tax system in the G20 provided they play by the rules. This 'carrot' is now balanced with an enormous stick."

"Details are sketchy at this stage but it appears that any amount perceived to have been diverted artificially will be deemed to be a profit which is taxable in the UK at the new 25 percent rate. Taxing a deemed profit rather than adjusting the profits of an existing UK taxpayer may enable HMRC to defend the tax charge from the argument that the profits are only taxable elsewhere under a double tax treaty."

"The reality is that this tax is unlikely to be paid since we expect that companies affected will restructure to ensure profits are not artificially diverted. They will then be taxed at the standard rate of corporation tax in the normal way. The on-the-ground effect is therefore likely to be that the kind of aggressive tax planning through artificial structuring that this measure targets will come to sudden and abrupt halt."

"However, some companies may be concerned that legitimate commercial structures could be affected or other countries may jump on the bandwagon in an opportunistic way leading to a tax grab. It's vital, therefore, that there is proper consultation on any draft legislation. To employ a well-used analogy – like an elephant, you know artificial diversion when you see it. The difficulty is that the law has to be able to define it in order to tax it and, as with defining the elephant, this can be tough to do."

Experts React To UK Banking Tax Changes

The revenue effect of a new restriction on the use of carried-forward losses for UK banks is similar to a 36 percent increase in the bank levy, according to accountancy firm EY.

Chancellor George Osborne's 2014 Autumn Statement included plans to limit to 50 percent the amount of profit in established banks that can be offset by carried-forward losses. During his Statement speech on December 3, Osborne described the current system, whereby banks can offset all their losses from the financial crisis against tax on profits in years to come, as "totally unacceptable."

According to Osborne, "the banks got public support during the crisis and they should now support the public in the recovery."

Anna Anthony, Head of Financial Services Tax at EY, commented: "In the short term it is likely to represent a significant cash tax cost, and the ongoing recognition of deferred tax assets will need to be considered. To put the point in context, last year major banks paid GBP2.2bn (USD3.4bn) in bank levy in the UK. The Chancellor hopes to raise an average of GBP800m a year from the measures on bank losses. Therefore, the revenue effect of the measure is similar to a 36 percent increase in bank levy in cash terms."

Wayne Weaver, banking tax partner at Deloitte, explained that the changes will ensure that banks pay some corporation tax when they make profits. He added that "some banks will now need to reassess the value of their deferred tax assets for accounting and regulatory capital purposes, although recent regulatory changes mean that the capital impact should be less severe than in previous years."

The British Bankers' Association (BBA) confirmed that it will work with the Treasury to implement the new rules. BBA Chief Executive Anthony Browne said: "It is absolutely right that this important industry pays its fair share in tax, but it is important to note that where banks have offset losses they have done so legally, just as all other businesses can."

China Confirms Schedule For VAT On Financial Services

China's Ministry of Finance has announced that it will launch plans early next year to pilot the introduction of value-added tax (VAT) on financial services.

China hopes to have VAT in place on the sector fully by January 2016. The nation is expected to announce that a rate of either 6 or 11 percent will be levied on insurance premiums, but the rate could reportedly be as high as 16 percent.

Although an announcement is still expected on introducing VAT on the "living services sector," this newly announced date will likely mark the end of several years of reform for China, replacing its business tax regime with a VAT, to remove the distortions caused by businesses' inability to recover input tax under the business tax regime.

China has yet to roll out VAT on the construction and real estate sectors, but is expected to do so from January 1 of next year, with an 11 percent rate, which would be substantially higher than the 3 and 5 percent business tax rates the two sectors respectively face currently.

China is yet to confirm the introduction of VAT on the "living services" sector, which includes those involved in the provision of basic essentials, such as food, catering, and accommodation, as well as services such as hairdressing, but the Government said earlier this year that it hoped to be able to flesh out these plans by the end of this year also.

The announcement follows the expansion of the nation's VAT regime to telecoms providers from June 1, 2014, and rail transportation and postal services from January 1, 2014. Earlier, in August 2013, VAT was extended nationwide for the first time, covering the transportation industry and six modern services sectors (research and development, information technology, cultural and creative industries, logistics, and authentication and consulting services).

Small businesses are currently exempt from VAT and business tax, under Circular No. 71 (*Cai Shui* [2014] No. 71). This circular provided a temporary exemption for small businesses from business tax and VAT from October 1, 2014, to December 31, 2015. For these purposes, a small business is one that has monthly sales of between CNY20,000 (USD3,250) and CNY30,000 (USD4,880). Businesses with monthly sales of no more than CNY20,000 were already temporarily exempt.

Greece Concedes Hotel VAT Hike To Appease Troika

Greece has offered to hike the value-added tax (VAT) rate on hotel stays as part of a package of measures put forward in a bid to have its Budget and a bailout review signed off by the troika of lenders this month.

The VAT rate on hotel stays, which was cut to 6.5 percent in 2012, would be raised to 13 percent under the package, which also includes a two-year pension freeze and a proposal to introduce a VAT lottery to boost voluntary compliance rates.

The package is thought to offer a half-way compromise on a list of remedies called for by the troika in a recent 47-page letter received by the Greek authorities, in which the troika – comprising the European Central Bank, the European Commission, and the International Monetary Fund – had rejected the initial fiscal plans put forward by Greece. The nation's counterproposal has since been rejected by the troika, but the Greek Government is stubbornly digging in.

Greek Prime Minister Antonis Samaras, who has aspirations to cut Greek tax rates across the board, said: "I cannot accept unreasonable demands. We are at the end of 2014 and nobody has the right to treat us like they did two-and-a-half or four years ago, when everything was collapsing. We are ready for the final agreement."

The troika has long been calling for a simpler VAT regime in Greece to support fiscal consolidation efforts and to fund a reduction in the headline rate of VAT, in a move that it believes will improve compliance rates. Greece's headline rate of 23 percent would fall to about 19 percent, under proposals put forward by the International Monetary Fund, providing Greece also limits its extensive list of goods and services subject to reduced rates or exemptions.

The Greek Government, however, is unlikely to give way to pressure for further changes to its VAT regime, having struggled for months to secure approval to expand the scope of its higher 13 percent reduced rate to restaurants, eateries, cafes, and tavernas from August 1, 2013.

Greece had hoped that its latest Budget, hailed by Samaras as the country's first balanced budget in decades, would free the nation from the troika's grip. However, the troika reportedly challenged the Government's estimates, according to *The Wall Street Journal*, which saw the letter received by Greece and its response.

With the deadline for the final review of Greece's bailout scheduled in the coming days, along with a final tranche of bailout funds, the dispute between the country and the troika is expected to lengthen the period that Greece's fiscal position is under scrutiny, with member states that are invested in Greece's recovery reportedly keen to maintain oversight for an additional six months.

Greece levies three VAT rates, and very few items are subject to the headline rate of 23 percent.

The 6.5 percent rate is levied on books, newspapers, and periodicals; theater admission; hotel accommodation; and certain pharmaceutical products.

The 13 percent rate is levied on foodstuffs; water; certain pharmaceutical products; medical equipment for disabled persons; the transportation of persons; admission to cultural services, with the exception of theater admission; social services and social housing that are not otherwise exempt; renovation and repair work to residential housing; agricultural inputs; restaurants; admission to sporting events; funeral services; medical and dental care; repairs; and domestic care services.

According to Samaras, the troika has called for Greece to add to the list of budget remedies that it has put forward, including the introduction of VAT on medicines, which he has rejected outright.

Thailand Pulls VAT Hike Plan

Thailand's Government has backed away from its plans to raise the value-added tax (VAT) rate late next year, after lawmakers sided with business leaders who said the economy is too fragile.

The Government had said that increased spending was required to boost the economy's prospects, while acknowledging that this would lead to an increased budget deficit in 2015. To counteract higher spending, the Government had proposed raising the VAT rate by 1 percent.

Thailand's headline VAT rate is, in theory, 10 percent. However, a 7 percent rate has been in force since 1999. This 7 percent rate was extended again in July this year, until at least September 2015, on account of civil unrest in the nation and a slowing economy.

Thai media outlets took the Government's announcement to mean that the rate would be increased on top of the introduction of the 10 percent rate from late next year. Instead, it is thought likely that the Government had intended to raise the rate to 8 percent, while extending the waiver from payment of the 10 percent rate, as it has done for more than a decade.

Nevertheless, the Government's plans were quickly retracted, with businesses arguing that the Government should wait until 2016, when the economy is expected to exit a period of stagnant growth and instead post stronger growth rates nearing 4 percent of gross domestic product.

Australia Tackles Bitcoin Enigma At Public Hearing

At a recent public hearing, the Australian Government heard expert witness testimonies on the opportunities for Australia in the area of digital currencies, featuring an in-depth discussion on tax and regulatory issues.

The hearing was intended to inform the preparation of a report, due in March 2015, on a potential revision of Australia's position on the regulation and taxation of virtual currencies, the most prolific of which is Bitcoin. It was convened after the Australian Tax Office (ATO) released in-depth guidance on the tax treatment of such currencies in an August 2014 notice. The ATO decided that transacting with Bitcoin is akin to a barter arrangement, with similar tax consequences. The ATO's view is that Bitcoin is neither money nor a foreign currency, and the supply of Bitcoin is not a financial supply for goods and services tax (GST) purposes. Bitcoin is, however, considered to be an asset for capital gains tax purposes. This classification subjects most transactions involving Bitcoin to Australia's GST, a value-added tax.

In individual comments and during a panel discussion featuring the eight experts invited, the hearing was told that Australia's position, of treating virtual currencies as though it were a commodity, gives rise to double tax issues and makes the Australian industry uncompetitive internationally.

Concern was raised by Australian Senators about a lack of international regulation and consensus on the tax treatment of Bitcoin, with one Senator fearing that exempting virtual currencies in Australia could provide an avenue for more aggressive corporate tax planning, in the absence of an international agreement on taxation and regulation.

Of particular note were the comments of indirect tax expert Andrew Sommer, a Partner at Australian law firm Clayton Utz. Prior to hearing his testimony, the Chair of the hearing recounted a prior conversation with the ATO concerning its tax position.

The Chair said: "Obviously, I spoke to the ATO about this at the start of this process – I want to get this on the record, it is more of a statement than a question, but I think it is fair to put their defense on the record – and their argument is the Australian tax framework was created 20 to 25 years ago and then there was an update period with the GST, which is over a decade ago."

"The argument goes that, when the tax system was being created, none of this was envisaged because it did not exist. The comparison the ATO gave me was that they treat Bitcoin the same way they treat basketball cards or posters – a commodity that is tradeable as opposed to a currency. The defense from the ATO was that people are making the point that this is an issue of regulation – it is not an issue of regulation; it is an issue of policy – and that we, as the regulator in terms of the tax system, will follow the law as the law currently exists."

Addressing Sommer, the Chair said: "I want to get your opinion on this as you are a legal expert: whether we want to treat it differently or not is not the question; we are incapable of doing so because the framework does not allow us to treat it differently – that is the ATO's position."

Sommer said that if the ATO were designing the GST regime for the first time, it would be logical to provide exempt treatment for Bitcoin transactions, as, he said, it is used by consumers as though it were cash. Its use, therefore, should be subject to equal tax consequences, he said.

In exchanges with the Chair, it was pointed out that the purchase of everyday taxable goods for a consideration of Bitcoin, under Australia's current rules, is subject to double taxation – being taxable, in the first instance, on the conversion of fiat currency to

Bitcoin (taxable, despite Bitcoin not being "consumed," Sommer said, likening it to taxing foreign currency exchange transactions, for which commissions are generally the only part of the supply subject to tax), and, second, on the purchase of the good or service for a consideration of Bitcoin.

He contrasted this with the UK's new approach, which since March has been to exempt all but purchases of goods and services in exchange for Bitcoin, treating Bitcoin – and similar virtual currencies – as though it were fiat currency for tax purposes.

Sommer said: "The [ATO is] constrained by the law as it is written. They are mere administrators of the law; they are not an instrument of policy. And so they say: 'We've looked at this definition of money. To us, Bitcoin is outside the definition of money.'" However, he said: "It is not unusual, as you would know, for different people to form a different view in relation to a matter of interpretation of an existing definition."

Asked about the UK's position, Sommer explained that the UK had changed its position through a tax ruling, rather than through a legislative change. He pointed out that there is an argument that the definition of money, as it sits in section 1951 of Australia's GST Act, is capable, on its current terms, of extending to Bitcoin. Sommer said, "I have made that argument and others have made that argument in submission to the Commissioner. The Commissioner has formed the view that that is not the scope of the current definition."

"Initially [HM Revenue & Customs] in the UK tried to treat it as a commodity, which is the current proposed treatment by our revenue authorities. They walked away from that in March this year, and they formed the view that, under the framework of their law, Bitcoin is treated like private money, so it is treated like money."

Later during the panel discussion, other countries' approaches on the taxation of Bitcoin were considered. Concerns were again raised that if Australia adopted an approach not consistent with the rest of the world it could give rise to unforeseen tax base erosion consequences. It was suggested instead by the witnesses that tax was being used to enhance oversight of transactions, given uncertainty by regulators about how to deal with virtual currencies, and they said the key matter should be about devising appropriate regulation for the industry, rather than laboring it with taxation.

On regulation, Perianne Boring, President of the Chamber of Digital Commerce (USA), was asked about the regulatory setup in the US. She told the hearing: "In the US, on the federal level, we have identified about ten federal agencies and departments that somehow have asserted jurisdiction over this technology. I will go through a couple of them. You have the Securities and Exchange Commission that is looking at putting securities regulation and laws on this technology. Then you have the IRS, our taxing agent, which is calling this property. FinCen, the Financial Crimes eEnforcement Network – it is underneath the Treasury – they oversee money laundering, so they regulate money transmission. There is very, very tight regulation on top of those types of activities. They regulate Bitcoin like a currency."

"Then we also have the Commodity Futures Trading Commission, which is looking at this as a commodity. Then we have the intelligence agencies that are looking at this from their own respective views."

She pointed out that the varying treatment of virtual currencies is as a result of the varying aims and mandates of the organizations, but there is not a consistent approach as yet.

Last, Mark Pesce, a technology expert, said: "One of the most interesting conversations that I had at the global dialogue was with Jerry Brito, who works with regulators in the United States. He essentially said that most of the regulators in the United States are waiting for something they called the BitLicense, which are going to be promulgated by the New York state banking regulator sometime in the near future – sometime in the next six months."

He said these discussions, which would set rules on the substantial banking sector in New York, will likely set the benchmark for the adoption of a worldwide regulatory approach. He said: "Now, if they do it well, it will become a prototype for other regulatory domains. If they do it poorly, it will become a prototype of what not to do in other regulatory domains. I think what that starts to become is a conversation that is an international conversation between regulators in financial institutions around the right way to be able to incorporate digital currencies into an economy. I think that that is probably the most important thing. We need to stay involved in that conversation and, where we can, we need to be leading that conversation. I think the most important thing is to stay involved in that conversation because the conversation is going to have impacts throughout the rest of this century."

The hearing was as part of a consultation process, which ran until November 28, 2014. The Senate Standing Committee on Economics received a total of 40 submissions – mostly from digital currency organizations – to feed into its work on a potential revision of Australia's position.

The underlying theme put forward by experts was that, although there is uncertainty concerning the industry and the regulation of such, this is not uncommon for new technology, with Bitcoin being compared to the early days of the internet. Australian lawmakers were warned that the nation would be left behind in the race to innovate in this area if it fails to support the virtual currency industry during its infancy.

The hearing was a rare public debate on the tax treatment of Bitcoin; the ongoing work of the OECD noted that virtual currencies are among the challenges faced by tax authorities in setting tax policies on the digital economy, but its Action 1 report (on the taxation of the digital economy) did not specifically delve into the issue of virtual currencies, instead focusing on the long-running issue of taxing digital supplies to consumers.

International Approval For Patent Box Changes

The OECD and the EU's Code of Conduct Group (CCG) have endorsed a compromise agreement tabled by the UK and Germany concerning the UK Patent Box and the design of similar preferential intellectual property (IP) tax regimes.

The announcement follows an agreement, brokered by Germany with the UK, that the UK would limit its patent box regime, which provides for a preferential 10 percent corporate income tax rate on income from patents. The UK agreed that it would grant this rate only in cases where the patent income is linked to research and development (R&D) activities carried out in the UK.

It has been agreed that the new rules for the UK's Patent Box regime will apply to new participants from June 2016. The new rules will apply fully from June 2021.

The deal will be mirrored by all jurisdictions wishing to offer preferential tax regimes for IP income.

The compromise proposal was presented to the Forum on Harmful Tax Practices (FHTP) at its meeting on November 17–19 and to the CCG on November 20. It considered the OECD's work on agreeing new rules on the level of substantial activities required for a preferential regime to be considered a tax relief that supports real economic activity so as not to be considered "harmful."

The OECD had proposed a number of methods to determine substantial activity. The UK and three other countries had supported the "transfer pricing" method, but a significant majority of OECD-G20 members supported the alternative modified nexus method, which was eventually agreed.

The UK Financial Secretary to the Treasury, David Gauke, said on December 2: "The proposal … will now form the basis of continuing work by the FHTP to determine how the approach will work in practice. As part of the agreement, countries with existing IP regimes must agree to close these to new entrants by June 30, 2016, and will abolish them by June 30, 2021, after which all countries will be required to operate only nexus-compliant regimes."

"The legislative process to introduce changes to existing IP regimes so that continuing IP regimes conform to the re-modified nexus approach will also begin in 2015. In line with the normal tax policy-making process, the Government intends to consult on these changes, once the FHTP has completed work on the detail of the new rules."

He said: "The changes that the Government has secured to the original approach proposed by the OECD will protect the interests of the UK as an excellent location for technology based businesses by retaining a competitive Patent Box regime, which will now align benefits more closely to R&D activity carried out in the UK. As such, the Government is confident that the new regime will continue to incentivize innovation and its commercialization in the UK."

The deal was agreed as part of Action 5 of the OECD's base erosion and profit shifting (BEPS) plan, which deals with countering harmful tax practices, taking into account transparency and the substance of arrangements.

In Budget 2015, the Irish Government announced that it would soon introduce a Knowledge Development Box tax regime, similar to the UK's Patent Box regime, for IP income in 2015, plans for which are to be confirmed in Budget 2016.

Irish Revenue Chasing Unpaid Domicile Levy

The Irish Revenue is investigating 93 cases of suspected non-payment of the EUR200,000 (USD248,744) domicile levy, according to records obtained by state broadcaster RTÉ.

RTÉ's Morning Ireland program obtained the figures through a Freedom of Information request. The documents supplied are said to show that Revenue conducted a compliance drive this year that targeted individuals who were potentially liable for the levy in 2010, 2011, and 2012.

The information shows that, of 256 cases, 93 remain open and are said to concern the tax affairs of 63 individuals.

The domicile levy was introduced in the 2010 Budget. It is charged on an individual who is domiciled in Ireland and whose worldwide income exceeds EUR1m, whose Irish property is worth more than EUR5m, and whose Irish income tax liability in a relevant tax year would otherwise have been less than EUR200,000. The EUR200,000 levy is payable each year, on or before October 31 in the year following the valuation date, on a self-assessment basis.

Failure to pay the levy, or failure to pay it on time, can result in enforced collection. Interest is charged at the rate of 0.0219 percent per day or part of a day.

Revenue told RTÉ that it has collected EUR9.8m since the levy was introduced. In all, 31 individuals have paid the levy to date, with 16 doing so as a result of Revenue's compliance activity.

South Korean Lawmakers Agree 2015 Budget

South Korea's ruling Saenuri Party and the main opposition New Politics Alliance for Democracy (NPAD) agreed the terms of a compromise that led to the approval by the National Assembly of the country's 2015 Budget by the December 2 legal deadline, for the first time in 12 years.

The NPAD has agreed to a KRW2,000 hike (USD1.80) in the excise tax on cigarettes, so that the average price of a packet of cigarettes will increase by 80 percent to KRW4,500. It is expected the price rise will cut the high South Korean smoking rate and provide significant additional revenue for the Government's welfare reforms.

On the other hand, Saenuri has accepted the opposition's request to reduce corporate tax breaks, while the Government will also be able to proceed with its plans for an additional tax on companies that do not spend a minimum percentage of their profits on investments, dividends, and/or wage increases.

In addition, the two parties agreed to extend the individual income tax breaks for purchases on credit cards, but the Government's proposed measure to increase the inheritance tax exemption for heirs taking over shareholdings in family businesses was rejected. It had been proposed that the threshold would rise from KRW300bn (USD269,000) to KRW500bn.

Overall, as lawmakers recognized the need to sustain recovery in the South Korean economy, the Budget passed by the National Assembly contains a 5.5 percent increase in government spending to KRW375.4 trillion next year, up from KRW355.8 trillion in the 2014 Budget. This was only marginally less than the KRW376 trillion originally requested by the Government for next year.

Israeli Budget Plans Collapse With Gov't Coalition

After almost six months of heated debate between Israeli lawmakers, Prime Minister Benjamin Netanyahu has called for the dissolution of Parliament and is due to confirm a date for elections.

On December 2, 2014, Netanyahu broke apart the fractious Coalition Government, after two years of quarreling over numerous issues, the most recent of which was the nation's 2015 Budget, which has now come unstuck. Elections are expected to consolidate the power of Netanyahu's majority Likud Party, and the Budget will now not be passed until the middle of next year at the earliest, with a tentative election date set for mid-March

Yair Lapid, the former Coalition's Finance Minister and leader of minority party Yesh Atid, has, therefore, been unable to see through the introduction of his controversial plans for a value-added tax break for first-time house buyers, which was to benefit few taxpayers given its limited scope.

With many categories of taxpayers excluded, the plans were frequently challenged and were amended four times before the Knesset Finance Committee gave its approval by a slim majority. However, lawmakers rejected the plans at a plenary, and Lapid had threatened to exit the Coalition if his part of the Budget was not approved.

The conditions to secure the zero rate (rather than be subject to the headline rate of 18 percent) were numerous: the applicant must have served in the army (for no less than 18 months, if the applicant is male, or 12 months, if the applicant is female); it was to be open only to couples over the age of 35 with at least one child; it would have had to have been their first purchase for at least two decades; at least one applicant was required to be employed; the house value must not have exceeded ILS1.4m (USD365,000); and the relief was to be available only for houses with a floor space of not more than 140 square meters. Additional last-minute provisions were also proposed for child joint custody cases and for disabled persons.

When appointed, Israel's next Government is expected to draft an interim Budget for 2015 and the Budget for 2016 contemporaneously.

Northern Ireland May Get Corporate Tax Powers

The UK Government has said that it is "well disposed" to the possible devolution of corporation tax rate-setting powers to Northern Ireland, provided that progress can be made in current cross-party talks.

Chancellor George Osborne announced during his Autumn Statement that the UK Government "recognize[s] the strongly held arguments for devolving corporation tax setting powers to Northern Ireland." He explained that the Treasury believes that this is possible, provided that the Northern Ireland Executive can show that it is able to manage the financial implications. If Northern Ireland were able to provide reassurances, the UK Government would introduce legislation before the end of the current Parliament, which is to be dissolved in May 2015.

According to the UK Government, the power to set corporation tax rates could be a powerful tool to help the Executive rebalance the Northern Ireland economy, generate sustainable levels of growth, and drive private sector employment. Northern Ireland shares a border with the Republic of Ireland, which levies a 12.5 percent corporation tax rate – substantially lower than the current UK rate of 21 percent (reducing to 20 percent from April 2015), which is applied in Northern Ireland.

Theresa Villiers, Secretary of State for Northern Ireland, said: "It has taken a significant effort to get to this point and it is positive news that Northern Ireland could be on the brink of getting these powers. [The] Autumn Statement has raised the stakes in the cross-party talks and made it even more vital that the parties do all they can to reach an agreement in the short time we now have. It is vital not to let this opportunity slip away."

Paul Terrington, PwC Regional Chairman in Northern Ireland, commented: "The fact that Westminster is willing to take this step should stimulate an informed debate on what Northern Ireland needs to do to ensure that, if corporation tax is devolved, we get the greatest benefit for the region at the lowest cost to taxpayers and business."

Osborne also announced that an agreement has been reached with the Welsh Government on the full devolution of business rates (property tax). In addition, the UK Government will publish the draft clauses of legislation for the devolution of powers over income tax rates and thresholds to the Scottish Parliament in the new year.

In a December 3 statement, Kevin Kingston, President of Northern Ireland Chamber of Commerce and Industry, said: "[We welcome] today's announcement on the devolution of Corporation Tax powers to the Northern Ireland Executive. The Prime Minister has listened to calls from the business community and all of Northern Ireland's political parties for the devolution of powers, with the outcome now placed firmly on the Northern

Ireland Executive's willingness to cooperate on a number of issues which have challenged them."

"With the powers now sitting firmly in our hands, our politicians must grasp this opportunity whilst using the two years prior to the implementation of the new tax rate to ensure that we maximize the opportunity."

"The crucial point when it comes to the Corporation Tax decision is that Corporation Tax is an investment in the private sector to grow new opportunities and to put new jobs on the ground for all of our communities. The price of doing nothing, of focusing solely on the past and ignoring the opportunity of the future is – for the business community – unthinkable."

The devolution of powers comes on the condition of a *pro rata* reduction in the block grant, money which the UK Government provides to each of its regions to fund their day-to-day operations.

Norway's Commission Recommends Corporate Tax Rate Cut

The Tax Commission, appointed by the Government in March last year to review corporate taxation in Norway in light of international developments, submitted its report on December 2, and proposed a cut in both corporate and individual income tax rates, alongside other adjustments to combat corporate base erosion and profit shifting (BEPS).

The Commission noted that the level of Norway's corporate tax rate has stayed comparatively high when, both at a European level and globally, other countries' rates have been lowered. In 2014, the statutory corporate tax rate was 1.7 percent higher than the OECD average, and 4.4 percent higher than the EU average.

It was therefore recommended that there should be a reduction in the country's corporate tax rate to 20 percent from the current rate of 27 percent (in conjunction with a similar cut in its lowest rate of personal income tax), to dissuade companies from shifting profits out of Norway to more tax-friendly countries and to attract international business and investment, particularly having regard to future years when there will be an oil-sector slowdown.

The Commission provided one package of measures estimated to be approximately revenue-neutral, and another proposal involving tax reductions of NOK15bn (USD2.1bn). Overall, to balance the reduction in corporate tax, it decided that there should be a broadening of the tax base.

However, to generate additional revenue and put a greater emphasis on consumption taxes, it also suggested that a withholding tax on margin-based financial income should be introduced and that value-added tax (VAT) be placed on financial services on which fees are payable. It also recommended a dual-rate VAT, in which the general rate of 25 percent would be retained but the current zero rate and lowest rate would be increased to 15 percent, corresponding to the current rate on food.

In addition, it proposed a net tightening of the tax rules applicable to cross-border activities. For example, with reference to the taxation of cross-border income from shares, it advocated raising the low-tax country definition threshold, from two-thirds to three-quarters of the Norwegian tax level, and levying withholding tax only on shareholders resident in low-tax countries.

Among other measures to prevent BEPS, the Commission noted that Norway should follow up any recommendations concerning transfer pricing and the arm's length principle resulting from the OECD's project, as well as international developments in the area of information exchange for tax purposes, particularly as regards the automatic exchange of information.

It also included a proposal for a withholding tax on royalties and interest; asked the Ministry of Finance to assess whether bareboat vessel charters should be excluded from the Norwegian special tax regime for shipping companies; recommended that companies registered in Norway should always be deemed resident there; and concluded that there should be a statutory general rule to counter tax avoidance.

Given that the report is to be submitted for public consultation in the near future, and that the Government has already presented its Budget for 2015, it is considered that the earliest date for its recommendations to be acted upon would be 2016.

Australian Mineral Exploration Tax Breaks Introduced

The Australian Government has introduced legislation to enact a pre-announced tax offset scheme that will enable junior mineral explorers to use their tax losses for the benefit of their Australian shareholders.

The Exploration Development Incentive (EDI) is aimed at fostering the discovery of new resource deposits. The Government hopes that it will encourage investment in eligible junior exploration companies conducting "greenfields" mineral exploration.

The measure was a Coalition election commitment in 2013, and the Government unveiled details of its plans in May this year. The EDI will allow small mineral exploration companies with no taxable income to provide exploration credits, paid as a refundable tax offset, to their Australian resident shareholders for greenfields mineral exploration.

The EDI is capped at AUD100m (USD83.9m) over the forward estimates period. Exploration credits will be capped at AUD25m for exploration expenditure incurred in 2014/15, AUD35m for expenditure incurred in 2015/16, and AUD40m for expenditure incurred in 2016/17. A modulation process will be used to ensure the cap is not breached.

The incentive will apply from July 1, 2014.

In a joint statement, Finance Minister Mathias Cormann and Industry Minister Ian MacFarlane said: "New mineral discoveries underpin the future of the Australian mining industry. Junior and small miners do most of Australia's greenfields exploration, but changing global market conditions have created challenges and created barriers to new investment and exploration. The Government understands that the mining industry drives our economy through export revenue and by directly employing hundreds of thousands of Australians."

"It's another significant policy the Government has delivered to ensure the resources sector continues to underpin our economy. We scrapped the carbon tax and the mining tax and we're getting rid of the excessive red tape that has burdened the sector," they added.

The Minerals Council of Australia welcomed the legislation's introduction. Deputy Chief Executive John Kunkel commented: "The EDI is a timely and practical commitment to the future of the Australian minerals industry with small Australian exploration companies facing real challenges securing capital. Available to junior companies with no taxable income and to their investors, the EDI addresses the situation whereby junior explorers are unable to access the immediate deduction for exploration expenditure. Importantly, it will allow explorers to leverage additional investment in their companies and to retain existing shareholders."

Puerto Rico's House Approves Oil Tax Hike

Puerto Rico's House of Representatives has approved a controversial 68 percent hike in oil tax to stop a possible worsening of the territory's debt problems, following a stand-off with Governor Alejandro García Padilla, who had threatened to shut down public transport services.

After much negotiation with lawmakers in the House to obtain the required majority, it is planned that the oil excise tax will rise by USD6.25 per barrel, to USD15.50 per barrel, from March 2015.

The increased revenues, worth some USD178m per year, will be used by Puerto Rico's Infrastructure Financing Authority, which is to assume and refinance the debt of the Highways and Transportation Authority, which is in financial difficulty, and support the issue of up to USD2.9bn in bonds.

Implementation of the tax increase will be delayed until March 2015 to give time for the Government and lawmakers to look for other replacement revenue sources that could be less of a burden on families and small businesses. The Senate has yet to approve the relevant legislation.

A joint committee of both Government and Congress representatives is to be formed immediately to assess such alternatives. It is planned that the committee's deliberations will be aided by the Treasury Department's study on a new tax reform framework that is intended to be introduced during the first quarter of next year. It is now expected that the study should be completed before January 31, 2015.

The tax reforms could reduce Puerto Rico's dependence on the collection of direct taxes by, for example, raising individual income tax thresholds and transforming the present sales and use tax into a broad-based value-added tax.

Germany Approves Electric Car Tax Breaks

The German Cabinet on December 3, 2014, approved a raft of measures aimed at supporting carbon emission reduction efforts, including a tax break for electric vehicles purchased as company cars.

The Government aims to have one million electric cars on its roads by 2020, but an advisory body to the Government recently warned that only half of the target number would be achieved unless incentives are offered for electric car purchases.

The package of measures adopted on December 3 also includes tax incentives for the renovation of buildings to make them more energy efficient.

The measures must be approved by Parliament before they can become law.

Germany aims to cut its greenhouse gas emissions by 62–78 million tons by 2020, representing a 40 percent reduction from 1990 levels.

Africa To Benefit From TFA Breakthrough, WTO Chief Says

The Director-General of the World Trade Organization (WTO), Roberto Azevêdo, has said that African nations will benefit in particular from the decision of WTO members to support the agreements at the Bali ministerial, including on the Trade Facilitation Agreement (TFA), which he said would assist their regional integration efforts in a very practical way.

Addressing the African Union Conference of Ministers of Trade on December 4, he said: "Right now I think Africa's potential is unmatched. And I think that trade has a crucial role to play in helping to realize this potential." The Director-General noted that African nations are taking huge strides forward on regional integration. "There is a lot of excellent work going on to lower barriers and streamline procedures so that you can trade with each other more effectively," he said.

However, he pointed out that, as intra-African trade accounts for only a tenth of the continent's total trade, it is critical for African nations to improve regional integration. The TFA will support these efforts "in a very practical way" he said, by introducing binding commitments across all WTO members to expedite the movement, release, and clearance of goods, improve cooperation among WTO members in customs matters, and help developing countries fully implement the Agreement's terms.

It is estimated that the TFA can cut trade costs by almost 14.5 percent for low-income countries, and by 10 percent for high-income countries, adding to reforms – and in particular the proposed Doha Round – to cut tax barriers to trade on a global basis.

He noted that the TFA Facility is now fully operational. This is intended to fulfill the final part of the TFA's mandate – that it should be inclusive for developing countries, by ensuring that they get the help they need to fully reap the full benefits of the TFA.

The members of the WTO adopted the TFA at a meeting of the General Council on November 27, 2014. The agreement must now be ratified by WTO members.

Canada–South Korea FTA To Enter Into Force

Canada and South Korea are on track to bring their free trade agreement (CKFTA) into force on January 1, 2015, after both sides ratified the treaty.

The deal was inked in September 2014. It was ratified by the South Korean National Assembly on December 2, and received Royal Assent in Canada on December 3. Talks were put on hold in 2008 after South Korea maintained an import ban on Canadian beef, but the ban was lifted in January 2013. The terms of the CKFTA were eventually agreed in March of this year.

Upon the CKFTA's entry into force, South Korea will immediately remove duties on 81.9 percent of tariff lines. By the time the agreement has been fully implemented, South Korea will have eliminated duties on 100 percent of Canadian non-agricultural exports and 97 percent of agricultural exports. Canada will remove duties on approximately 99.9 percent of South Korea's exports to the country.

Average South Korean tariffs are three times higher than Canada's, at 13.3 percent compared with 4.3 percent.

The CKFTA is projected to boost Canada's economy by CAD1.7bn (USD1.5bn) and increase merchandise exports to South Korea by 32 percent. Bilateral merchandise trade reached nearly CAD11bn in 2013.

Ed Fast, Canada's International Trade Minister, said: "The [CKFTA], Canada's first with an Asia-Pacific market, will create thousands of new jobs in Canada and provide Canadian businesses and workers with a gateway to Asia. With this latest milestone, Canada and South Korea are on track to bring the agreement into force on January 1, 2015, so that Canadian workers and businesses can access the full range of benefits and opportunities it will provide."

Fast will lead a trade mission to South Korea in February 2015, with the aim of helping Canadian firms make the most of the opportunities the CKFTA will bring.

ARMENIA - ISRAEL

Initialed

Armenia initialed a DTA with Israel following negotiations which took place from November 10 to 13, 2014.

GUERNSEY - AUSTRIA

Into Force

The TIEA signed between Guernsey and Austria entered into force on November 16, 2014.

JERSEY - ROMANIA

Signature

Jersey signed a TIEA with Romania on December 1, 2014.

KYRGYZSTAN - SAUDI ARABIA

Signature

According to preliminary media reports, Kyrgyzstan signed a DTA with Saudi Arabia on December 2, 2014.

UNITED KINGDOM - JAPAN

Into Force

The DTA between the United Kingdom and Japan enters into force on December 12, 2014.

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

THE AMERICAS

US INTERNATIONAL TAX REPORTING AND COMPLIANCE

Bloomberg BNA

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

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

12/15/2014 - 12/16/2014

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

19TH TAXATION OF CORPORATE REORGANIZATION

Federated Press

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

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

1/20/2015 - 1/22/2015

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

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

STEP

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

Chair: Mark Silberfarb (Chapter Chair, STEP OC)

1/22/2015 - 1/24/2015

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

16TH TAX PLANNING FOR THE WEALTHY FAMILY

Federated Press

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

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

1/27/2015 - 1/28/2015

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

INTERNATIONAL TAX ISSUES 2015

Practising Law Institute

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

Chair: Michael A. DiFronzo (PwC)

2/11/2015 - 2/11/2015

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

AMERICAS TRANSFER PRICING SUMMIT 2015

TP Minds

Venue: TBC, Miami, Florida, USA

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

2/19/2015 - 2/20/2015

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

ADVANCED INTERNATIONAL TAX PLANNING

Bloomberg BNA

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

Chair: TBC

2/23/2015 - 2/24/2015

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

THE 4TH OFFSHORE INVESTMENT CONFERENCE PANAMA 2015

Offshore Investment

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

Chair: Derek R. Sambrook (Trust Services)

3/11/2015 - 3/12/2015

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

INTRODUCTION TO US INTERNATIONAL TAX

Bloomberg BNA

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

Chair: TBC

3/16/2015 - 3/17/2015

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

INTERMEDIATE US INTERNATIONAL TAX UPDATE

Bloomberg BNA

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

Chair: TBC

3/18/2015 - 3/20/2015

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

ASIA PACIFIC

THE 3RD OFFSHORE INVESTMENT CONFERENCE SINGAPORE 2015

Offshore Investment

Venue: Raffles, 1 Beach Rd, 189673, Singapore

Chair: Nicholas Jacob (Wragge Lawrence Graham & Co)

1/21/2015 - 1/22/2015

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

INTERNATIONAL CORPORATE TAX PLANNING ASPECTS

IBFD

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

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

4/20/2015 - 4/22/2015

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

CENTRAL AND EASTERN EUROPE

CIS WEALTH MOSCOW 2015

CIS Wealth

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

Key speakers: TBC

2/16/2015 - 2/17/2015

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

WESTERN EUROPE

PRIVATE CLIENT PROPERTY TAXATION 2014

IBC

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

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

1/22/2015 - 1/22/2015

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

EMPLOYMENT TAX PLANNING CONFERENCE 2015

IIR & IBC Financial Events

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

Key Speakers: Patrick Way QC (Field Court Tax Chambers), Teresa Payne (BDO), Nick Wallis (Smith & Williamson), Rosemary Martin (Deloitte), Jenny Wheater (Duane Morris), among numerous others.

1/28/2015 - 1/28/2015

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

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

International Bar Association

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

Key Speakers: TBA

2/9/2015 - 2/10/2015

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

20TH INTERNATIONAL WEALTH TRANSFER PRACTICE LAW CONFERENCE

International Bar Association

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

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

3/2/2015 - 3/3/2015

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

INTERNATIONAL TRANSFER PRICING SUMMIT 2015

TP Minds

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

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

3/10/2015 - 3/11/2015

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

INTERNATIONAL TAX ASPECTS OF CORPORATE TAX PLANNING

IBFD

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

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

3/18/2015 - 3/20/2015

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

SPRING RESIDENTIAL CONFERENCE 2015

Chartered Institute of Taxation

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

Chair: Chris Jones (Chartered Institute of Taxation)

3/27/2015 - 3/29/2015

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

INTERNATIONAL TAX ASPECTS OF MERGERS, ACQUISITIONS AND CORPORATE FINANCE

IBFD

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

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

3/30/2015 - 4/1/2015

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

PRINCIPLES OF INTERNATIONAL TAXATION

IBFD

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

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

4/20/2015 - 4/24/2015

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

INTERNATIONAL TAXATION OF E-COMMERCE

IBFD

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

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

5/11/2015 - 5/13/2015

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

PRINCIPLES OF INTERNATIONAL TAX PLANNING

IBFD

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

Chair: Boyke Baldewsing (IBFD)

6/1/2015 - 6/5/2015

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

INTERNATIONAL TAXATION OF EXPATRIATES

IBFD

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

Key Speakers: TBC

6/10/2015 - 6/12/2015

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

INTERNATIONAL TAX ASPECTS OF PERMANENT ESTABLISHMENTS

IBFD

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

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

6/16/2015 - 6/19/2015

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

INTERNATIONAL TAX SUMMER SCHOOL

IIR & IBC Financial Events

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

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

8/18/2015 - 8/20/2015

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

INTERNATIONAL TAXATION OF BANKS AND FINANCIAL INSTITUTIONS

IBFD

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

Key Speakers: TBC

9/16/2015 - 9/18/2015

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

ASIA PACIFIC

Australia

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

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

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

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

Australia, and if not how much of his income was earned in Australia.

The Tribunal began by looking at the relevant national legislation and interpreting the provision defining "Australian resident." The taxpayer spent his childhood in Australia but as an adult was employed in Vanuatu and, following the divorce of his first wife who lived in Australia, gave up his Australian citizenry in order to become a citizen of Vanuatu at the beginning of the period of time being considered. He remained in contact with his ex-wife and their children and often visited them in Australia, sometimes staying in property that he owned and sometimes staying with his mother-in-law; he also conducted business in Australia. The Tribunal, in considering the common meaning of the word "resided," rejected the Commissioner's argument that the taxpayer resided in both Vanuatu and Australia, despite acknowledging that a person can reside in two different places. During his visits the taxpayer was staying in Australia but not living there because his activity "during the relevant years lacks the permanent, long-term or non-transient quality" that one would associate with residing somewhere, and therefore the Tribunal concluded that the taxpayer was not a resident of Australia during the years in question.

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

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

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

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

The judgment was delivered on November 17, 2014.

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

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

India

The Mumbai Income Tax Appellate Tribunal heard the case of an Indian company which was part of a group offering both international and domestic delivery services. In the report detailing its transactions with an associated enterprise (AE) the company suggested that the prices were at arm's length, having been calculated using the Transactional Net Margin Method (TNMM), but the Transfer Pricing Officer (TPO) believed that the "assessee's margin with the AE and the allocation of costs are not at arm's length" based on a number of factors, including the comparables used to calculate the margin, the allocation of expenses, and the fact that certain deliveries were provided free of charge in both India and the Middle East as part of a reciprocal arrangement with the AE. A transfer pricing adjustment was therefore imposed.

The company approached the Dispute Resolution Panel to argue against the TPO's contention that the transactions had not been undertaken at arm's length, and the subsequent transfer pricing adjustment, but again its arguments were rejected, and so it brought its case before the Tribunal. The company also disputed the imposition of interest on the adjusted amount.

The company stated that although transactions under two of the company's business aspects, express and freight services, had been found to be at arm's length, the TPO had taken issue with the domestic comparable transactions due to the losses incurred from competing with other Indian delivery businesses. The TPO had decided to reject the segregation of transactions between the types of business activity for the sake of the transfer pricing report because he was of the opinion that "the assessee had suffered losses in the Indian operations and from this he inferred that the profits have been shifted to the international transaction with the AEs," which the company disagreed with. The Tribunal sided with the company on the basis that the TPO's reliance on the domestic losses was not in itself a good enough reason to reject the company's segregated report, and to suggest that the transactions had not been made at arm's length.

With regard to the services provided free of charge in the Middle East, the Tribunal accepted the validity of the arrangement between the company and its AE. The unallowed expenses in the company's report were also accepted by the Tribunal, given the accuracy of the company's calculations, and therefore the company's transactions were deemed to have been undertaken at arm's length, and the adjustment was disallowed.

Regarding the consequent imposition of interest, the Tribunal found that interest should be imposed only on the correctly assessed income amount.

The judgment was delivered on November 28, 2014.

http://www.itatonline.in:8080/itat/upload/294771765856287082313$5%5E1REFNO798_Aramexs_India_Private_Limited.pdf

Income Tax Appellate Tribunal: *Aramex India Private Limited v. DCIT (ITA No.798/Mum/2014)*

WESTERN EUROPE

United Kingdom

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

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

The ECJ pointed out that in order to justifiably prevent tax avoidance, measures prescribed under the legislation in dispute must be able to "identify the existence of a wholly artificial arrangement entered into for tax reasons alone," in addition to providing taxpayers the ability to prove with evidence that their arrangement was not only for the sake of avoiding tax. However, in the present case the legislation applied to gains made by close companies without taking into account the intent of the participators, or whether their stake in the company was a controlling one, or for the purposes of investment only. Therefore, there was no method to determine whether tax avoidance was involved or for participators to justify their participation in the event of a tax avoidance accusation.

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

The judgment was delivered on November 13, 2014.

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

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

Dateline December 11, 2014

An "autumn" statement delivered in December? Sounds a bit late to me. Unless you are in the southern hemisphere of course, in which case it could equally well be early. Anyway, I refer here to UK Chancellor George Osborne's Autumn Statement, which used to be a dry summary of the UK fiscal balance sheet, but latterly seems to have morphed into a sort of pre-budget Budget. And with a general election due in May 2015, Osborne must have wanted to ensure that the 2014 Autumn Statement grabbed the attention of voters. To a large degree it has. The most substantial rabbit pulled out of the hat by Osborne was a reform of the absurd stamp duty land tax, which, until midnight on December 3, used to apply under a "slab" system. For example, if you bought a property for over GBP250,000, at which price the rate of stamp duty climbed from 2 percent to 5 percent, you paid 5 percent on the whole amount, not just the portion above GBP250,000. So if your house was worth somewhat above GBP250,000 and you wanted to sell it, good luck with that! It represents a fairly hefty tax cut in the order of nearly GBP1bn a year. And packaged as it was with a series of minor tax concessions for businesses, and small firms in particular, it is clear that the Conservative Party is keen to bring the young and upwardly mobile back into its fold in time for next year's election, putting "clear blue water" between it and the main opposition Labour Party. But yet more evidence of this Government's schizophrenic attitude to taxation emerged from the Autumn Statement, like the 25 percent "diverted profits tax" on company income artificially moved out of the UK to avoid tax. The success of this measure will surely rest on the interpretation of an "artificial arrangement." But I suspect that the Government cares little about that anyway. It is a populist move designed to show the voters and the OECD that it is cracking down on corporate tax avoidance. Nevertheless, the UK's thirst for tax revenues is almost unquenchable at the moment, and yet again we saw a fiscal statement littered with anti-avoidance measures. This is because the Government has spectacularly undershot its target for the deficit, which was supposed to have been eradicated by 2015. That won't happen now until 2020, provided the Conservatives, if re-elected, can oversee the largest squeeze on public spending since the Great Depression (the 1930s one). So while the likes of Greece, Ireland and Spain are talking about an end to austerity, in Britain the austere times might only just be beginning …

"Better late than never" you could say about the UK deficit situation. And you could use the same phrase to describe legislation passed by the US House of Representatives renewing a package of expired tax breaks almost in their entirety. It is something that should have been done a year or more ago before the expiry of the measures at the end of 2013. That they weren't renewed, and haven't been in the meantime, tells you all you need to know about the polarized, paralyzed nature of US politics. Yet, the large majority in favor of a simple one-year extension of most of these tax breaks informs us that both sides can come together when they have to, making the previous period of damaging legislative brinkmanship look so unnecessary. As if complying with the tax code wasn't hard enough for those taxpayers with relatively simple tax affairs, the Internal Revenue Service warned in November that continued delay in enacting a tax extenders package would not only cause heightened uncertainty for those taxpayers who are affected by the expired provisions, but also raise operational and compliance risks that would delay the tax filing season and the processing of individual taxpayer refunds. It has to be said that President Obama has been especially obstinate since the Democrats received a shellacking in the mid-term elections, stubbornly rejecting any Republican proposals out of hand, and slapping down Senate Majority Leader Harry Reid (a Democrat from Nevada) when he began negotiating with the GOP on an extenders' compromise. The indications are that the Senate will probably pass this short-term fix, and, so as not to cause more uncertainty, the President will not wield the veto. But you can virtually guarantee that we'll be watching the same pantomime unfold next year – and possibly well into 2016 – when the extenders expire yet again. It's a habit Washington has to kick.

There are also some bad habits that Italy has to banish to give itself a fighting chance of avoiding a potentially cataclysmic economic crisis. For a start, a substantial swathe of the Italian population has gotten into the habit of thinking that taxation is a voluntary exercise. And the Government continues to spend money it doesn't have. The result is a sticky budget deficit which the Government is struggling to contain, and sovereign debt worth 130 percent of GDP and rising. The economy also has a nasty habit of stalling and then failing to re-start. And it is difficult to see how the Government will break the cycle. Although cultural attitudes are largely responsible for rates of tax evasion in any given country, Italy's tax system seems to provide ample scope for it to take place because (a) it is so complex, and (b) taxes are so high. The recently updated PwC/World Bank ease of paying taxes index puts Italy 141st out of 186 countries. That's only marginally better than Zimbabwe in 143rd place, and slightly worse than Sudan in 139th. Even more damning is that Italy's total tax rate on a mid-sized company, represented by the combination of profit, labor and other taxes, is put at 65.4 percent. Who would want to invest in a country where, after finally figuring out how much tax you owe, it transpires that you must hand over two-thirds of your income to the government? So cutting and simplifying taxes is at least part of the answer to Italy's problems, for this could help to reduce tax evasion and encourage more investment and growth in the Italian economy. But without commensurate spending cuts, Italy's fiscal troubles might just be exacerbated. Prime Minister Matteo Renzi claims to be the one with the answers. But despite his youthful vigor, he is still a politician. Italy's 2015 Budget, recently approved by the lower house, is supposed to be the tonic that saves Italy. The tax cuts contained within it are claimed to be the largest in Italian history, but there's also a bit of clever accounting going on – EUR3bn of the EUR5bn reduction in the regional production tax known as IRAP actually went into effect in April, meaning that strictly speaking the 2015 Budget cuts the tax by EUR2bn. Not so clever is the fact that the Budget includes more borrowing to finance certain items of public expenditure. Slashing spending, if it happens, is only going to increase the chances of fracturing the fragile coalition and losing the support of voters – should Renzi ever get the chance to face them, that is. Unless he is Silvio Berlusconi, the average career of an Italian premier is fleetingly short. Canceling bread and circuses won't help to prolong it.

The Jester